Canadian International Trade Tribunal
Tribunal canadien du commerce extérieur

CANADIAN INTERNATIONAL TRADE TRIBUNAL

Appeals

DECISION AND REASONS

Appeal AP-2021-004

Centric Brands d.b.a. KHQ Investments LLC

v.

President of the Canada Border Services Agency

Decision and reasons issued
Thursday, May 23, 2023

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IN THE MATTER OF an appeal heard on June 7, 2022, pursuant to section 67 of the *Customs Act*;

AND IN THE MATTER OF a decision of the President of the Canada Border Services Agency made pursuant to subsection 60(4) of the *Customs Act* and dated March 15, 2021, with respect to a request for re-determination.

BETWEEN

CENTRIC BRANDS D.B.A. KHQ INVESTMENTS LLC **Appellant**

AND

THE PRESIDENT OF THE CANADA BORDER SERVICES AGENCY **Respondent**

DECISION

The appeal is allowed.

The matter is returned to the Canada Border Services Agency for reappraisal of the value for duty of the goods in issue in a manner consistent with the reasons for this decision.

Peter Burn

Peter Burn
Presiding Member

Place of Hearing:	Via videoconference
Date of Hearing:	June 7, 2022
Tribunal Panel:	Peter Burn, Presiding Member
Tribunal Secretariat Staff:	Kirsten Goodwin, Counsel Morgan Oda, Registrar Officer Stephanie Blondeau, Registrar Officer

PARTICIPANTS:

Appellant	**Counsel/Representatives**
Centric Brands d.b.a. KHQ Investments LLC	Michael Kaylor Lawrence N. James
Respondent	**Counsel/Representatives**
President of the Canada Border Services Agency	Aman Owais Brooklynne Eeuwes

WITNESSES:

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STATEMENT OF REASONS

INTRODUCTION

[1] Centric Brands d.b.a. KHQ Investments LLC (KHQ) appeals, pursuant to subsection 67(1) of the *Customs Act* (the Act),[1] a value for duty re-determination decision made by the President of the Canada Border Services Agency (CBSA) under subsection 60(4) of the Act.

[2] The main issue is, in appraising the deductive value of the imported goods in issue pursuant to subsection 51(1) of the Act, whether certain profit can be deducted in adjusting the unit price of the goods under subparagraph 51(4)(a)(ii) of the Act.

BACKGROUND AND PROCEDURAL HISTORY

[3] KHQ is based in the United States. Between 2014 and 2018, it imported children's clothing and accessories into Canada. It issued purchase orders to overseas vendors in response to orders placed by Costco Wholesale Canada Ltd. (Costco Canada) via order confirmation sheets. The order confirmation sheets were not purchase orders and did not commit Costco Canada to purchase the goods.

[4] Overseas vendors shipped the goods to KHQ at a third-party logistics facility in Vancouver, British Columbia, or in Toronto, Ontario. KHQ was the importer of record and held title to the goods when they were imported into Canada. KHQ was not a resident of Canada, nor did it have a permanent establishment in Canada.

[5] After the goods entered the third-party logistics facility, Costco Canada issued purchase orders for its desired quantity of goods. Any remaining balance of goods stayed in the facility. No work was done on the goods in Canada, and the goods were generally sold to Costco Canada within 90 days of importation. If Costco Canada did not purchase some or all of the goods, KHQ disposed of them (e.g., by destroying damaged goods).[2] KHQ's invoices for the goods identify Costco Canada as the "bill-to-party".[3] The invoices were sent to, and paid in U.S. dollars by, Costco Canada's U.S. parent corporation (Costco USA).[4] The transactions were accounted for in KHQ's accounts, with the resulting profits taxable in the United States.

[6] In June 2016, the CBSA initiated a trade compliance verification of goods imported by KHQ between April 1, 2015, and March 31, 2016. The CBSA issued its verification final report in October 2017, which included re-determining the goods' value for duty using the transaction value method (TVM) under section 48 of the Act.[5]

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1 R.S.C., 1985, c. 1 (2nd Supp.).
2 Exhibit AP-2021-004-07 at para. 13; *Transcript of Public Hearing* at 15–16.
3 Exhibit AP-2021-004-11.A (protected) at 10–37.
4 *Transcript of Public Hearing* at 28; Exhibit AP-2021-004-11 at para. 2.
5 Exhibit AP-2021-004-11 at para. 8; Exhibit AP-2021-004-11.A (protected) at 45–50.

[7] In June 2018, KHQ asked the CBSA to re-determine the value for duty. KHQ argued that the TVM did not apply. In September 2020, the CBSA asked KHQ for information to enable calculating the value for duty using alternate methods of appraisal including the TVM for identical goods under section 49 of the Act, the TVM for similar goods under section 50 of the Act, and the deductive value method (DVM) under section 51 of the Act.[6] Regarding the DVM, the CBSA communicated that certain profit as identified by KHQ (viewed by the CBSA as "profit incurred outside of Canada") was not deductible.[7] KHQ did not submit additional information substantiating the profit.[8]

[8] In March 2021, the CBSA issued its re-determination decision under subsection 60(4) of the Act.[9] The CBSA determined that the TVM did not apply.[10] In the absence of additional information regarding the profit in issue, the CBSA decided to apply the DVM in a flexible manner under section 53 of the Act.[11]

[9] KHQ filed its appeal on June 10, 2021. The Tribunal held a videoconference hearing with the parties on June 7, 2022.

LEGAL FRAMEWORK

[10] Canada values imported goods pursuant to the Act, which enacts into Canadian domestic law, among other things, the rules found in the World Trade Organization's Customs Valuation Agreement (formally known as the Agreement on Implementation of Article VII of the General Agreement on Tariffs and Trade 1944). The determined value for duty also serves as the basis for the application of value-added taxes on imported goods, such as the harmonized sales tax (though unlike the value for duty, the sales tax base on imported goods includes not only the value for duty but also the amount of the duty and excise tax if applicable).

[11] The Act allows the value for duty to be established using one of six methods. Section 46 of the Act requires the value for duty of imported goods to be determined in accordance with the valuation methods set out in sections 47 to 55. The methods must be considered in the order set out in section 47.

[12] Sections 47 and 48 provide that the first (and preferred) valuation method is the TVM, which is followed by two TVM-based subsidiary bases of appraisal (the two being transactions involving identical or similar goods). The parties submit, and the Tribunal agrees, that these three methods of appraisal do not apply to the goods in issue because the sales between KHQ and Costco Canada do not constitute sales for export, which is a precondition for applying the TVM.[12]

[13] Paragraph 47(2)(c) of the Act provides that the next (i.e., fourth) valuation method is the DVM, which seeks to arrive at a value for the good at the point of entry into Canada by deducting

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6 Exhibit AP-2021-004-07 at 45.
7 *Ibid.* at 46–47.
8 *Ibid.*; *Transcript of In Camera Hearing* at 89–90.
9 Exhibit AP-2021-004-01 at 8–17; Exhibit AP-2021-004-07 at 41–48.
10 Exhibit AP-2021-004-01 at 11; Exhibit AP-2021-004-07 at 42.
11 Exhibit AP-2021-004-01 at 11; Exhibit AP-2021-004-07 at 47.
12 *Cherry Stix Ltd. v. President of the Canada Border Services Agency* (10 May 2010), AP-2008-028 (CITT) at para. 35.

from the selling price per unit certain costs incurred *subsequent to* entry into Canada. The DVM is applied in accordance with section 51 as follows:

> **Deductive value as value for duty**
>
> **51 (1)** Subject to subsections (5) and 47(3), where the value for duty of goods is not appraised under sections 48 to 50, the value for duty of the goods is the deductive value of the goods if it can be determined.
>
> **Determination of deductive value**
>
> **(2)** The deductive value of goods being appraised is
>
> > **(a)** where the goods being appraised, identical goods or similar goods are sold in Canada in the condition in which they were imported at the same or substantially the same time as the time of importation of the goods being appraised, the price per unit, determined in accordance with subsection (3) and adjusted in accordance with subsection (4), at which the greatest number of units of the goods being appraised, identical goods or similar goods are so sold;
> >
> > **(b)** where the goods being appraised, identical goods or similar goods are not sold in Canada in the circumstances described in paragraph (a) but are sold in Canada in the condition in which they were imported before the expiration of ninety days after the time of importation of the goods being appraised, the price per unit, determined in accordance with subsection (3) and adjusted in accordance with subsection (4), at which the greatest number of units of the goods being appraised, identical goods or similar goods are so sold at the earliest date after the time of importation of the goods being appraised; or
> >
> > **(c)** where the goods being appraised, identical goods or similar goods are not sold in Canada in the circumstances described in paragraph (a) or (b) but the goods being appraised, after being assembled, packaged or further processed in Canada, are sold in Canada before the expiration of one hundred and eighty days after the time of importation thereof and the importer of the goods being appraised requests that this paragraph be applied in the determination of the value for duty of those goods, the price per unit, determined in accordance with subsection (3) and adjusted in accordance with subsection (4), at which the greatest number of units of the goods being appraised are so sold.
>
> **Price per unit**
>
> **(3)** For the purposes of subsection (2), the price per unit, in respect of goods being appraised, identical goods or similar goods, shall be determined by ascertaining the unit price, in respect of sales of the goods at the first trade level after importation thereof to persons who
>
> > **(a)** are not related to the persons from whom they buy the goods at the time the goods are sold to them, and
> >
> > **(b)** have not supplied, directly or indirectly, free of charge or at a reduced cost for use in connection with the production and sale for export of the goods any of the goods or services referred to in subparagraph 48(5)(a)(iii),

at which the greatest number of units of the goods is sold where, in the opinion of the Minister or any person authorized by him, a sufficient number of such sales have been made to permit a determination of the price per unit of the goods.

Adjustment of price per unit

(4) For the purposes of subsection (2), the price per unit, in respect of goods being appraised, identical goods or similar goods, shall be adjusted by deducting therefrom an amount equal to the aggregate of

(a) an amount, determined in the manner prescribed, equal to

(i) the amount of commission generally earned on a unit basis, or

(ii) the amount for profit and general expenses, including all costs of marketing the goods, considered together as a whole, that is generally reflected on a unit basis

in connection with sales in Canada of goods of the same class or kind as those goods,

(b) the costs, charges and expenses in respect of the transportation and insurance of the goods within Canada and the costs, charges and expenses associated therewith that are generally incurred in connection with sales in Canada of the goods being appraised, identical goods or similar goods, to the extent that an amount for such costs, charges and expenses is not deducted in respect of general expenses under paragraph (a),

(c) the costs, charges and expenses referred to in subparagraph 48(5)(b)(i), incurred in respect of the goods, to the extent that an amount for such costs, charges and expenses is not deducted in respect of general expenses under paragraph (a),

(d) any duties and taxes referred to in clause 48(5)(b)(ii)(B) in respect of the goods, to the extent that an amount for such duties and taxes is not deducted in respect of general expenses under paragraph (a), and

(e) where paragraph (2)(c) applies, the amount of the value added to the goods that is attributable to the assembly, packaging or further processing in Canada of the goods.

Rejection of deductive value

(5) Where there is not sufficient information to determine an amount referred to in paragraph (4)(e) in respect of any goods being appraised, the value for duty of the goods shall not be appraised under paragraph (2)(c).

Definition of *time of importation*

(6) In this section, ***time of importation*** means

(a) in respect of goods other than those to which paragraph 32(2)(b) applies, the date on which an officer authorizes the release of the goods under this Act or the date on which their release is authorized by any prescribed means; and

(b) in respect of goods to which paragraph 32(2)(b) applies, the date on which the goods are received at the place of business of the importer, owner or consignee.

[14] The DVM is applied in accordance with the *Valuation for Duty Regulations* (Regulations).[13] Section 5 reads as follows:

> **5 (1)** For the purposes of paragraph 51(4)(a) of the Act, an amount equal to the amount of commission or the amount for profit and general expenses, as referred to therein in respect of the appraisal of imported goods, shall be calculated on a percentage basis and determined from sufficient information that is prepared in a manner consistent with generally accepted accounting principles and, subject to subsection (2), is supplied by or on behalf of the importer of the goods being appraised.
>
> **(2)** Where the amount determined from sufficient information supplied by or on behalf of an importer pursuant to subsection (1) is not consistent with the amount generally earned or reflected in connection with sales in Canada by importers who deal with vendors in a manner consistent with that of persons who are not related to each other, the sufficient information shall be based on an examination of sales in Canada
>
> > **(a)** of the narrowest group or range of goods of the same class or kind as the goods being appraised, including the goods being appraised;
> >
> > **(b)** by importers dealing with vendors in a manner consistent with that of persons who are not related to each other; and
> >
> > **(c)** from which sufficient information can be obtained.

[15] As noted earlier, the DVM is the fourth of the six alternative methods of valuation for duty. If the value for duty cannot be determined using the DVM, the fifth approach is the computed value method (CVM), which involves constructing a value by aggregating the various costs described in section 52 of the Act. If the CVM cannot be applied, the residual method under section 53 provides for a flexible application of one of the methods set out in sections 48 to 52.

ANALYSIS

[16] The first step in the analysis is to identify the applicable method of appraisal. Both parties submit that the DVM applies. For the reasons below, the Tribunal agrees. The second step is to determine whether the DVM approach allows certain profit to be deducted in adjusting the unit price of the goods in issue under paragraph 51(4)(a) of the Act.

The DVM is the applicable valuation methodology

[17] The Tribunal has found above that neither the primary TVM nor the subsidiary TVM-based methods of appraisal apply. The next valuation method is the DVM, set out in section 51 of the Act. The DVM estimates the value of goods at the time they were imported by deducting certain costs incurred in Canada after importation. Pursuant to subsection 51(2), the value of goods sold in Canada after importation is based on the price per unit (PPU) established in accordance with subsection 51(3) and adjusted in accordance with subsection 51(4).

[18] Uncontested evidence shows that the goods in issue were sold to Costco Canada in the condition in which they were imported, and the sales were generally within 90 days of importation, in accordance with paragraph 51(2)(b) of the Act. Regarding subsection 51(3), there is evidence on

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[13] SOR/86-792.

the record showing sales of the goods in issue at the first trade level after importation as between KHQ and Costco Canada as unrelated parties. There is no evidence that Costco Canada supplied any goods or services for use in connection with the production and sale for export of the goods in issue. Neither party submits that a PPU cannot be determined under subsection 51(3). While the parties disagree on whether certain profit can be deducted from the PPU under subsection 51(4), there is no dispute that adjustments to the PPU can be made under that provision, and the parties agree that the DVM applies.

[19] On the basis of the evidence and the parties' agreement, the Tribunal finds that the DVM is the applicable appraisal method.

Profit earned in Canada is deductible in adjusting the unit price of the goods in issue

[20] Subsection 51(4) of the Act requires the PPU of imported goods to be adjusted by making certain deductions. The main issue in this appeal is whether profit arising from KHQ's sales to Costco Canada may be deducted in adjusting the PPU under subparagraph 51(4)(a)(ii).[14] The parties do not agree on whether KHQ's claimed profit was "in connection with sales in Canada" and can therefore be deducted from the PPU under subparagraph 51(4)(a)(ii).

[21] KHQ submits that there was only one profit earned on the sales to Costco Canada. As such, that profit was earned in connection with sales in Canada, irrespective of whether KHQ was a non-resident importer and whether invoicing and payment for the goods was completed in the United States. KHQ submits that, "[s]imply stated, it suffices that there be a nexus between the sale in Canada and the profit earned on that sale."[15]

[22] The CBSA submits that the deductions for profit permitted under subsection 51(4) of the Act are limited to profit made in Canada. According to the CBSA, the profit in issue was not earned in Canada, but rather in the United States, because KHQ invoiced Costco Canada at a Costco USA address, KHQ received payment from Costco USA in the United States, and the profit was taxable only in the United States. The CBSA therefore contends that the profit is "foreign profit" that does not constitute profit in connection with sales in Canada and cannot be deducted under subparagraph 51(4)(a)(ii). The CBSA also argues that, because KHQ did not provide supporting documentation for its claimed deduction for profit, it waived its potential entitlement to that deduction.[16]

[23] The Tribunal begins its analysis by interpreting paragraph 51(4)(a) of the Act, with particular focus on the words emphasized below:

> **51(4)** For the purposes of subsection (2), the price per unit, in respect of goods being appraised, identical goods or similar goods, shall be adjusted by deducting therefrom an amount equal to the aggregate of

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14 KHQ confirmed that its appeal is limited to the deductibility of profit only. *Transcript of Public Hearing* at 34, 41.

15 Exhibit AP-2021-004-07 at para. 51.

16 The CBSA also asks the Tribunal to find that the CBSA does not need to apply the flexible DVM solely because an importer refuses to cooperate with its obligations under the Act. The Tribunal considers that it is not necessary to address that request in the circumstances of this appeal.

> **(a)** an amount, determined in the manner prescribed, equal to
>
> > **(i)** the amount of commission generally earned on a unit basis, or
> >
> > **(ii)** *the amount for profit* and general expenses, including all costs of marketing the goods, considered together as a whole, that is generally reflected on a unit basis
>
> *in connection with sales in Canada* of goods of the same class or kind as those goods,
>
> [Emphasis added]

[24] Statutory interpretation principles require reading the words of a legislative provision "in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament".[17] When "the words of a statutory provision are precise and unequivocal, the ordinary meaning of the words will play a dominant role in the interpretive process".[18] While the purpose and context of the legislation are still examined,[19] they are "not a licence to overlook legislative text that is genuinely clear and unambiguous. Nor can the purpose of the legislation be used to extend the meaning of a legislative provision beyond what its plain, unambiguous words will allow."[20] It is well established that "courts should be reluctant to embrace unexpressed notions of policy or principle in the guise of statutory interpretation."[21]

[25] Subsection 51(4) of the Act requires the PPU to be adjusted by deducting an amount equal to the aggregate of amounts determined in accordance with paragraphs 51(4)(a) to (e). The relevant provision in this appeal is subparagraph 51(4)(a)(ii), which provides for deducting "the amount for profit … in connection with sales in Canada …".

[26] On their face, these words are clear, unambiguous, and can be defined as follows: "amount" is "a quantity, the total of a thing or things in number, size, value, extent, etc.";[22] "profit" is "financial gain; excess of returns over outlay";[23] "connection" is "the state of being connected";[24] "connect" can be defined as "join";[25] and "sale" is "the exchange of a commodity for money etc.".[26] None of these definitions include a geographical component. However, "sales" (i.e., "the exchange of a commodity for money") is qualified by the words "in Canada".

[27] The next step in the analysis is to interpret these words in their entire context. The Tribunal has said previously that the purpose of the sequentially applied valuation methods in the Act is to

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17 *Canada (Attorney General) v. Burke*, 2022 FCA 44 [*Burke*] at para. 32, citing *Canada Trustco Mortgage Co. v. Canada*, 2005 SCC 54 [*Canada Trustco*] at para. 10.

18 *Burke* at para. 33, citing *Canada Trustco* at para. 10.

19 *Hillier v. Canada (Attorney General)*, 2019 FCA 44 [*Hillier*] at para. 24.

20 *Hillier* at para. 25, citing *Canada v. Cheema*, 2018 FCA 45 at paras. 74–75.

21 *65302 British Columbia Ltd. v. Canada*, [1999] 3 SCR 804 at para. 51. See also *AAi. FosterGrant of Canada Co. v. Canada (Commissioner of the Canada Customs and Revenue Agency)*, 2004 FCA 259 at para. 20, citing *Shell Canada Ltd. v. Canada*, [1999] 3 S.C.R. 622 at paras. 40, 43.

22 *The Canadian Oxford Dictionary*, 2nd ed., *s.v.* "amount".

23 *The Canadian Oxford Dictionary*, 2nd ed., *s.v.* "profit".

24 *The Canadian Oxford Dictionary*, 2nd ed., *s.v.* "connection".

25 *The Canadian Oxford Dictionary*, 2nd ed., *s.v.* "connect".

26 *The Canadian Oxford Dictionary*, 2nd ed., *s.v.* "sale".

capture different scenarios under which goods are imported into Canada.[27] Calculations under different valuation methods should produce approximately the same value for duty.[28] The Tribunal has stated that "the valuation methods, apart from the transaction value method, seek to *approximate* an arm's-length transaction between two unrelated parties" [emphasis in original].[29]

[28] The purpose of the DVM is to estimate the value of goods at the time they were imported by deducting certain amounts connected with the sales in Canada that were incurred subsequent to importation.[30] Reading subparagraph 51(4)(a)(ii) of the Act in this context supports a conclusion that the PPU can be adjusted by deducting the amount of profit that was linked or joined (i.e., connected) with selling imported goods in Canada, as part of estimating the value of those goods at the time they were imported. This is consistent with the Tribunal's decision in *Armstrong Bros. Tool Co. v. The Deputy Minister of National Revenue* (*Armstrong*), which states the following:[31]

> In understanding the meaning of the expression "in connection with sales in Canada," the Tribunal had regard to the greater context within which this expression is contained, as well as the object and intention of Parliament in providing an adjustment to the price per unit of goods. The Tribunal is of the view that the adjustments to the price per unit provided by subsection 51(4) are "to deduct the *markup which is usually added in [Canada], so as to reduce the selling price to a value which can properly be said to have applied at the stage of importation, rather than at the later stage of resale.*" In the Tribunal's view, that *deduction for markup is limited to profits earned* and expenses incurred *in Canada*. This way, *the price per unit of the goods is reduced to a reasonable approximation of their value at the time of importation*.
>
> It is clear from a reading of section 51 that the focus of the deductive value method for determining value for duty is on the "sales of ... goods at the first trade level after importation." It is from this transaction that the predominant price per unit is determined and adjustments made therefrom. In the Tribunal's view, therefore, *the adjustments allowed under subsection 51(4) relate to markups reasonably made to account for profits* and expenses *on this transaction*. Thus, *for there to be a "connection with sales in Canada," the profits* and expenses *must have occurred in Canada just as the transaction occurred in Canada*. That being said, although an expense was incurred in Canada, it may have been paid from abroad.
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> [Footnote omitted, emphasis added]

[29] While the parties' arguments align with aspects of the Tribunal's interpretative analysis in *Armstrong*, they diverge on others. KHQ argues that interpreting "in connection with" to require profit to be "earned in Canada" is an unduly narrow and therefore improper reading of the legislation.

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27 *Tootsie Roll of Canada Ltd. v. The Deputy Minister of National Revenue* (16 September 1997), AP-96-114 (CITT) [*Tootsie Roll*] at 4; *Pier 1 Imports (U.S.), Inc. v. President of the Canada Border Services Agency* (16 December 2021), AP-2019-047 (CITT) [*Pier 1 Imports*] at para. 17. See also *Bluestein Enterprises Inc. v. President of the Canada Border Services Agency* (31 March 2014), AP-2013-028 (CITT) [*Bluestein Enterprises*] at para. 49.

28 *Tootsie Roll* at 4; *Pier 1 Imports* at para. 17. See also *Bluestein Enterprises* at para. 49.

29 *Pier 1 Imports* at para. 17.

30 *Pier 1 Imports (U.S.), Inc. v. President of the Canada Border Services Agency* (2 September 2021), AP-2019-047 (CITT) at para. 21; *Bluestein Enterprises* at note 27.

31 (15 August 1997), AP-96-105 (CITT) at 6–7, affirmed by the Federal Court of Appeal on June 22, 1999 (A-818-97).

The CBSA argues that *Armstrong* stands for the proposition that "profit … in connection with sales in Canada" means that profit accounted for outside Canada, where the sales in issue were invoiced and paid for outside Canada, is not deductible for DVM purposes because such profit is "foreign profit" that was not "earned" or "made" in Canada. Furthermore, the CBSA argues that allowing profit booked outside Canada to be deducted from the PPU under subparagraph 51(4)(a)(ii) of the Act would be inconsistent with the purpose of the Act and frustrate parliamentary intent as reflected therein.

[30] The positions taken by the parties are perhaps not surprising, given that they respectively seek to optimize and minimize the deduction for profit and hence minimize and optimize the value for duty (and sales tax). However, both parties appear to have misconstrued the interpretative analysis in *Armstrong*. Indeed, the Tribunal believes that both positions are inconsistent with the purpose of the Act.

[31] The fundamental policy objective of the Act's multiple methods of valuation is to improve the chances of producing a value for duty that approximates the value that would be produced in an arm's-length transaction between unrelated parties (the first and preferred method of valuation when available). In an arm's length import transaction under the TVM, the value for duty invariably includes a markup for costs incurred *prior* to importation, though not for a markup applied after importation to cover costs incurred in Canada. The positions promoted by both the CBSA and KHQ would fail to meet this fundamental objective. KHQ is essentially arguing that profit covering all costs incurred both in Canada *and* elsewhere prior to importation should be deductible for DVM purposes as profits earned in Canada, while the CBSA is arguing that *no* profit *is* deductible if the profit is accounted for outside Canada in the foreign parent's books, even when profit and expenses have occurred in Canada.

[32] Contrary to the assertion of KHQ, *Armstrong* does not stand for the proposition that a mere nexus between the sale in Canada and the profit booked on that sale is sufficient to allow all the profit accounted for outside Canada by KHQ to be deductible for DVM purposes as "profits earned in Canada". On the other hand, and contrary to the position argued by the CBSA, neither does *Armstrong* stand for the proposition that the mere invoicing and accounting in the United States of sales occurring in Canada causes the profit on such sales to be profit entirely earned in the United States, and not at least partially earned in Canada or in connection with sales in Canada.[32]

[33] The Tribunal in *Armstrong* stated that the "deduction for markup is limited to profits earned … in Canada." The Tribunal also stated that adjustments under subsection 51(4) of the Act relate to markups made to account for profit "on" sales transactions in Canada. The Tribunal further stated that, to be deductible, profit had to have "occurred" in Canada. Finally, the Tribunal held that only profits "*incurred* in Canada, that were in connection with the sales in Canada, are allowed" [emphasis added].[33] When the Tribunal's interpretation in *Armstrong* is considered as a whole, "earned" in Canada is simply one characterization of the Tribunal's view that the PPU can be adjusted for DVM purposes by deducting costs incurred in Canada and an appropriate share of the profit so that the selling price in Canada is reduced to a value which can properly be said to have

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32 In *Armstrong*, the Tribunal was unable to evaluate the profit (and expenses) claimed by the appellant and returned the matter to the respondent for reappraisal; *Armstrong* at 9, affirmed by the Federal Court of Appeal on June 22, 1999 (A-818-97).

33 *Armstrong* at 2, affirmed by the Federal Court of Appeal on June 22, 1999 (A-818-97).

applied at the stage of importation, rather than at the later stage of resale or at an earlier stage prior to entry into Canada.

[34] Deductions for profit permitted under subsection 51(4) of the Act are limited to the amount of profit earned in Canada. The amount of profit earned in Canada is not necessarily the same as the markup applied in Canada. The amount of the profit deductible for DVM purposes should reflect the share of the total costs incurred in the production, delivery and sale of the good that is reasonably connected to the sales in Canada. It is the job of the CBSA to appraise whether any portion of the profit is rightfully attributable to costs incurred and profit earned outside Canada prior to importation into Canada.

[35] The CBSA also argues that subparagraph 51(4)(a)(ii) of the Act should be interpreted in a manner consistent with the Convention Between Canada and the United States of America with Respect to Taxes on Income and on Capital (Convention).[34] Article VII of the Convention provides that business profits of residents of Canada and the United States are taxable in the country where they are resident, unless they carry on business through a permanent establishment in the other country, in which case certain profits may be attributed to that permanent establishment. Thus, interpreting subparagraph 51(4)(a)(ii) in accordance with the Convention means that, if there is no permanent establishment in Canada, U.S.-based non-resident importers like KHQ could never have deductible profit arising from sales in Canada. Although the Tribunal recognizes that taxation agreements, legislation and jurisprudence may be useful interpretative aids in some circumstances, it is not necessary for the Tribunal to consider the Convention in interpreting subparagraph 51(4)(a)(ii). First, the provision is clear and unambiguous, and the context for interpreting the provision arises from the Act itself (as the Tribunal explains above). Second, the Convention addresses tax evasion and double taxation as between Canada and the United States, and the link between business profits and residence and permanent establishments in Article VII reflects that context. The DVM method of appraisal under the Act does not include residency nor permanent establishment requirements, and the Tribunal sees no basis for essentially reading them into subparagraph 51(4)(a)(ii).

[36] The CBSA further argues that allowing the deduction for profit recorded in books and records maintained outside Canada "would make determining the value for duty for non-resident importers potentially unworkable, since CBSA has no power to enter foreign premises to verify the information or compare the profits declared to foreign jurisdiction income tax filings." This claim is untenable. The CBSA is a sophisticated organization that routinely conducts detailed verifications and audits of resident and non-resident import documentation (and encourages U.S.-based companies to become members of its Non-Resident Importers Program). In any event, nothing in subsection 51(4) of the Act requires prohibiting the deduction for profit simply because the records are maintained outside Canada, particularly when such records are at least potentially verifiable. To the extent that the CBSA is again advancing an interpretation in pursuit of a CBSA objective despite the clear and unambiguous language in subparagraph 51(4)(a)(ii), the Tribunal reiterates that it is reluctant to embrace the CBSA's expressed notions of policy and principle in the guise of statutory interpretation.[35]

[37] The CBSA also argues that interpreting subparagraph 51(4)(a)(ii) of the Act to allow "foreign" profit to be deducted from the PPU would distort the value for duty in relation to the other

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34 *Canada–United States Tax Convention Act, 1984*, S.C. 1984, c. 20, Schedule I.

35 *Hillier* at para. 25, citing *Canada v. Cheema*, 2018 FCA 45 at paras. 74–75; *65302 British Columbia Ltd. v. Canada*, [1999] 3 SCR 804 at para. 51.

valuation methods prescribed in the Act, contrary to estimating the value for duty under the DVM in a manner that approximates the value for duty that would be achieved under the other methods.[36] To support this argument, the CBSA provided hypothetical valuation scenarios for comparison.[37] The Tribunal was not persuaded by the hypothetical scenarios, though it does appreciate the danger of distortion if it were to agree with the position espoused by KHQ. However, the Tribunal also recognizes the distortions that could arise if it agreed with the CBSA that profit earned in Canada could become nondeductible "foreign profit" for purposes of the DVM merely through being invoiced and accounted for outside Canada.

[38] Finally, the CBSA argues that, by failing to provide supporting documentation for its claimed deduction for profit, KHQ waived its potential entitlement to that deduction. In the unique circumstances of this appeal, the Tribunal disagrees. The CBSA decided that, in advance of receiving supporting documentation from KHQ regarding its profit, the profit in issue was not deductible. Having made that decision, the CBSA advised KHQ that the profit was not deductible. In response to the CBSA's clear direction that it would not deduct the profit, KHQ did not submit supporting documentation. The CBSA effectively induced KHQ's response. If the CBSA had not made and communicated its decision to KHQ before receiving supporting documentation, and KHQ refused to provide the documentation, that might be another matter, but that is not the case here.

[39] Ultimately, in the course of this appeal KHQ provided a breakdown of annual sales to Costco Canada, which includes brand names, product categories, amounts for selling prices per unit, and amounts for profit per unit.[38] The CBSA does not contest the submission of this information *per se*; it is well established that appeals under section 67 of the Act are conducted *de novo*, and the record may be supplemented with new evidence.[39] However, the CBSA submits that the evidence on the record, specifically the new information, is not sufficiently detailed and the CBSA would require further information to properly calculate the value for duty using the DVM. Given the CBSA's request that if the Tribunal finds that the profit in issue is deductible the Tribunal should return the matter to the CBSA for re-determination, the Tribunal did not seek additional information from KHQ in this appeal. The parties generally agree that sufficient information exists.[40]

[40] The Tribunal believes that the interpretation of the Act laid out in this decision reflects the language and purpose of the existing legislation. It minimizes the dangers of unfair distortions between alternative valuation methods, protects against a potential erosion of the value-added sales tax base, and respects the basic principles underpinning World Trade Organization rules.

[41] The Tribunal finds that at least a portion of KHQ's profit, and perhaps all, was connected to sales in Canada in the manner set out in subparagraph 51(4)(a)(ii) of the Act. What must now be appraised is the amount of the profit booked by KHQ that is deductible for DVM valuation purposes,

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36 *Tootsie Roll* at 4; *Pier 1 Imports* at para. 17. See also *Bluestein Enterprises* at para. 49.

37 Exhibit AP-2021-004-11.A (protected) at 115–118.

38 Exhibit AP-2021-004-07.A (protected) at 66–73.

39 *Canada (Attorney General) v. Best Buy Canada Ltd.*, 2021 FCA 161 at para. 43; *Instant Brands Inc. v. President of the Canada Border Services Agency* (26 March 2021), AP-2019-039 (CITT) at para. 45.

40 Subsection 45(1) of the Act provides that "***sufficient information***, in respect of the determination of any amount, difference or adjustment, means objective and quantifiable information that establishes the accuracy of the amount, difference or adjustment". Section 5 of the Regulations provides that, "[f]or the purposes of paragraph 51(4)(a) of the Act, an amount equal to the amount of commission or the amount for profit and general expenses, as referred to therein in respect of the appraisal of imported goods, shall be calculated on a percentage basis and determined from sufficient information …".

so that the selling price in Canada is reduced to a value which can reasonably be said to have applied at the stage of importation.

DECISION

[42] The appeal is allowed.

[43] The matter is returned to the respondent for reappraisal of the value for duty of the goods in issue in a manner consistent with the reasons for this decision.

Peter Burn

Peter Burn
Presiding Member