Buying Commissions Non-Dutiable in CITT Case

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On February 11, 2004, the Canadian International Trade Tribunal (CITT) released its decision in *Browns Shoe Shops Inc. v CCRA.*[1] The CITT found in favour of the importer by excluding buying agent commissions from the value for duty (VFD) of imported footwear determined under the transaction value method. This decision confirms a recent trend in the case law, which has examined the dutiability of purported buying agent commissions. The CITT and Federal Court have looked at all the relevant factors to determine whether the true nature of the relationship between the non-resident and the importer is one of buying agent-principal, or something else, such as foreign vendor-purchaser of the goods. This decision confirms a broader trend in the jurisprudence, settled by the Supreme Court of Canada. According to this jurisprudence, absent a sham, the nature of the underlying legal transactions, not the "economic realities," will govern in determining the tax/customs consequences.[2]

In accordance with subparagraph 48(5)(a)(i) of the *Customs Act*, the import price of goods sold for export to Canada shall be adjusted by adding to the price any commissions or brokerage fees paid by the importer (to the extent not already included in the import price). However, this required adjustment does not apply to "fees paid or payable by the purchaser to his agent for the service of representing the purchaser abroad in respect of the sale." The "buying commission" jurisprudence has focused on this quoted exception to subparagraph 48(5)(a)(i).

A *bona fide* buying agent representing the purchaser abroad connects the purchaser with the foreign vendor. In his capacity as a *bona fide* buying agent, the agent may approve samples, negotiate sales prices on the purchaser's behalf, place orders for the purchaser, and advise as to delivery schedule, among other functions.

In *Browns Shoe*, the importer purportedly paid buying commissions to Krasnow Enterprises Ltd. (Krasnow) to represent the importer abroad as its buying agent for the purchase and importation of Aquatalia footwear. Krasnow wore another hat as "purchaser/importer and distributor of the Aquatalia footwear in its own right." On this latter basis, the CCRA argued that Krasnow exceeded its purported authority as a buying agent for the importer, Browns Shoe Shops Inc. (Browns), and, in effect, entered into a vendor/purchaser relationship with Browns.

The CITT rejected the CCRA's argument in this regard. Browns knew that Krasnow wore two hats. However, Browns also knew that it benefited economically from reduced purchase prices because of the increased volumes and purchasing power of acquiring the imported footwear through Krasnow as its agent. There was no evidence of a conflict of interest, or that Krasnow failed to fulfil its fiduciary obligation to act in the best interests of Browns. Browns adduced evidence that it acquired the Aquatalia footwear directly from Italian factories (vendors). There was nothing to indicate that Browns had relinquished control or authority over the powers of its agent, Krasnow, such that if it had expressed dissatisfaction with Krasnow's choice of manufacturers, it could not have chosen another one.

Browns Shoe followed a recent line of cases, which had found in favour of the importer based on agency law. This recent line of cases has rejected CCRA's challenges as to the existence of a *bona fide* buying agency relationship based on the application of economic realities or indicators. We will briefly discuss some of these cases below.

In *Utex Corporation v The Deputy Minister of National Revenue*,[3] the Federal Court of Appeal reversed the decision of the CITT. The CITT found that certain amounts allegedly paid as commissions to a foreign representative of the purchaser had to be added to the import price. The foreign representative, Fabco Trading Corp. (Fabco), relied on the activities of a related person, Corin International (HK) Ltd. (Corin), to represent the purchaser/importer, Utex Corporation (Utex) abroad. Corin received commissions from Chinese factories with which Utex was doing business. The CITT found that Fabco could only be Utex's *bona fide* buying agent, if Fabco always acts in the best interests of Utex and has no conflicting duties or loyalties. The CITT found otherwise.

The Federal Court of Appeal found

Commissions, *cont'd on pg.5*

Commissions, cont'd from pg.2

no evidence that Fabco failed in any respects to act in the best interests of Utex. Even if Fabco had failed in such respects, "that by itself would not be sufficient to establish that the fees paid to Fabco are outside the exception set out in subparagraph 48(5)(a)(i) of the Act as fees paid to the agent of a purchaser for the service of representing the purchaser abroad in respect of the sale." In other words, the buying agent may have simply failed to fulfil its fiduciary obligations as a buying agent to act in the best interests of its principal.

The CITT has accepted that a person can act as a *bona fide* buying agent where the buying agent is a trademark holder in relation to the imported goods, the designer and distributor of the goods in the U.S., acts for more than one purchaser, or is much larger than the purchaser.[4]

The CCRA has attempted to assess import duties on legitimate buying agency commissions payable for representing a purchaser abroad based on irrelevant economic considerations, such as the size of the buying agent in relation to the purchaser/importer. Another largely irrelevant economic consideration is that the buying agent may wear more than just the one hat as buying agent. It may own the trademarks under which the imported products are distributed and sold and may, in fact, act as a purchaser and distributor of the goods in its own right. None of these considerations necessarily undermine the fact that this person represents a purchaser/importer abroad as a buying agent to connect the purchaser/importer with the foreign vendor. Among the relevant considerations are whether the foreign person takes ownership of the goods sold to the purchaser/importer or assumes any risk for the purchase price payable for the imported goods. The nature of their legal relationship, based on relevant legal considerations, determines whether a true buying agency relationship exists. All in all, another "nail in the coffin" for the "economic realities" approach, despite numerous earnest attempts by the CCRA to resurrect the corpse.

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