Date: 20070111

Docket: A-263-06

Citation: 2007 FCA 16

CORAM: **DÉCARY J.A.**
NOËL J.A.
PELLETIER J.A.

BETWEEN:

LOUIS MORISSETTE

Appellant

and

HER MAJESTY THE QUEEN

Respondent

Hearing held at Montréal, Quebec, on January 8, 2007.

Judgment delivered at Montréal, Quebec, on January 11, 2007.

REASONS FOR JUDGMENT OF THE COURT BY: NOËL J.A.

CONCURRED IN BY: DÉCARY J.A.
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REASONS FOR JUDGMENT

NOËL J.A.

[1] This is an appeal from a decision rendered by the Madam Justice Lamarre Proulx of the Tax Court of Canada (2006 TCC 284), upholding the assessment issued by the Minister of National Revenue (the Minister) for taxation year 2002 in respect of the appellant on the basis that the amount of $20,000 he received on termination of his employment constituted severance pay taxable

as employment income under subsection 6(3) of the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) (ITA).

[2] According to the appellant, however, the payment in question constituted consideration for the sale of clientele and gave rise to a capital gain in his hands.

Background

[3] The appellant worked for Laurentian Bank Securities (LBS) as an investment advisor from January 2000 to October 2002, at which point LBS terminated their relationship by reason of non-performance. Lamarre Proulx J. found that theirs was a employer-employee relationship, and that aspect of her decision is not challenged in the appeal.

[4] The agreement that terminated the employment and pursuant to which the payment was made (hereinafter the "termination agreement") reads as follows:

> [TRANSLATION]
>
> 1. Your employment shall cease as of October 16, 2002.
>
> 2. We shall pay you $20,000, minus all deductions that apply, as compensation, plus an additional $5,000 in six (6) months, if LBS has retained at least 75% of your managed assets.
>
> 3. The amounts owing to you as of the date of your termination shall be paid to you.
>
> 4. This offer shall expire on October 24, 2002.
>
> 5. It is understood and agreed that you shall keep the terms and conditions of this agreement completely confidential and that you shall not subsequently disclose information concerning the payments made or the terms and conditions of this agreement to anyone, except to your family, legal counsel, accountants or professional advisers, provided that they undertake to keep this information confidential and not disclose it to anyone.

> 6. It is understood and agreed that you shall not solicit your clients, directly or indirectly or in any way whatsoever, and you agree that such solicitation would cause a serious prejudice to LBS if this commitment were not respected. Therefore, we could, in such a case, not only claim damages from you, but also take any other action, through the courts or otherwise, including by way of injunction, to enforce compliance with the present agreement.
>
> 7. Your acceptance of this agreement, confirmed by your signature, is in total, full and final settlement of all claims or complaints that you have or might have against Laurentian Bank Securities and its mandataries, trustees or other representatives, regardless of the nature of such claims or complaints, including any claims for damages, salary, vacation pay, incentive pay, benefits, pay in lieu of notice, severance pay, or any other benefit related to your employment with Laurentian Bank Securities, and any legal recourse that you might have against them shall consequently be barred.
>
> 8. The present agreement constitutes a transaction within the meaning of articles articles 2631 *et seq.* of the Civil Code of Québec. [my emphasis]

[5] The amounts of $20,000 and $5,000 referred to in clause 2 of the termination agreement were paid out in 2002 and 2003 respectively, and in each case, LBS issued a T4A slip, making the appropriate deductions at source.

[6] On the appellant's income tax returns filed for the two years in question, he reported the payments as having been received in consideration for disposing of his interest in the clientele that was under his management while employed with LBS.

[7] The Minister, however, considered that the two payments were remuneration received "in consideration or partial consideration" for a non-solicitation covenant within the meaning of paragraph 6(3)(*e*) of the ITA:

(3) An amount received by one person from another	(3) La somme qu'une personne a reçue d'une autre personne:
(*a*) during a period while the payee was an officer of, or in the employment of, the payer, or	*a*) soit pendant une période où le bénéficiaire était un cadre du payeur ou un employé de ce

(*b*) on account, in lieu of payment or in satisfaction of an obligation arising out of an agreement made by the payer with the payee immediately prior to, during or immediately after a period that the payee was an officer of, or in the employment of, the payer,

shall be deemed, for the purposes of section 5, to be remuneration for the payee's services rendered as an officer or during the period of employment, unless it is established that, irrespective of when the agreement, if any, under which the amount was received was made or the form or legal effect thereof, it cannot reasonably be regarded as having been received

(*c*) as consideration or partial consideration for accepting the office or entering into the contract of employment,

(*d*) as remuneration or partial remuneration for services as an officer or under the contract of employment, or

(*e*) in consideration or partial consideration for a covenant with reference to what the officer or employee is, or is not, to do before or after the termination of the employment.

dernier;

b) soit au titre ou en paiement intégral ou partiel d'une obligation découlant d'une convention intervenue entre le payeur et le bénéficiaire immédiatement avant, pendant ou immédiatement après une période où ce bénéficiaire était un cadre du payeur ou un employé de ce dernier,

est réputée être, pour l'application de l'article 5, une rémunération des services que le bénéficiaire a rendus à titre de cadre ou pendant sa période d'emploi, sauf s'il est établi que, indépendamment de la date où a été conclue l'éventuelle convention en vertu de laquelle cette somme a été reçue ou de la forme ou des effets juridiques de cette convention, il n'est pas raisonnable de considérer cette somme comme ayant été reçue, selon le cas:

c) à titre de contrepartie totale ou partielle de l'acceptation de la charge ou de la conclusion du contrat d'emploi;

d) à titre de rémunération totale ou partielle des services rendus comme cadre ou conformément au contrat d'emploi;

e) à titre de contrepartie totale ou partielle d'un engagement prévoyant ce que le cadre ou l'employé doit faire, ou ne peut faire, avant ou après la cessation de l'emploi.

[my emphasis]

[8] In response to the appeal filed by the appellant before the Tax Court of Canada, Lamarre Proulx J. ruled that the sum of $20,000 constituted severance pay and that it was taxable as

such. However, she ruled that the amount of $5,000 was paid “in respect of a certain right of the appellant in his clientele” and allowed the appeal for the 2003 taxation year.

[9] The appellant is appealing that part of the judgment which upheld the taxation of the $20,000 he received during taxation year 2002. The Crown, while stating that it disagrees with the decision rendered in respect of 2003, did not appeal from it.

[10] In support of his appeal, the appellant argues that Lamarre Proulx J. made a palpable error in her assessment of the evidence, which, according to him, unequivocally demonstrate that he was not entitled to severance pay of $20,000 when he lost his employment and that the only possible explanation for the amount that was paid to him is the value for LBS of the clientele that he agreed to relinquish pursuant to the termination agreement.

[11] In that regard, the appellant refers to the testimony of the employer’s representative and to his own testimony, which establish that the amounts totalling $25,000 were calculated on the basis of the value of the assets under his management ($8,103,829) and the commissions generated thereby. Thus, a value of $3,000 was assigned to each million dollars of assets under his management, for an approximate total of $25,000. That amount was paid to him in two installments.

Analysis and Decision

[12] Like the appellant, I find it difficult to reconcile the evidence adduced before the Tax Court of Canada with Lamarre Proulx J.’s finding that the $20,000 was somehow received as severance

pay. Indeed, the appellant was employed by LBS for only a short time, and a severance allowance of that scale would not have been warranted by the meagre revenue he generated.

[13] Furthermore, the evidence reveals unequivocally that the amounts received under the termination agreement were arrived at by a calculation of the value of assets that the appellant was managing and their future revenue potential. I must therefore rule that Lamarre Proulx J.'s characterization of the amount in question as "severance pay" is incorrect.

[14] The foregoing notwithstanding, the appeal cannot succeed.

[15] Indeed, the underlying presumption of the assessments issued in 2002 and 2003 is that the amounts paid to the appellant constitute consideration or partial consideration for his covenant not to solicit the clients that were under his management (Reply to Notice of Appeal, para. 18(*f*)(*i*)). Under paragraph 6(3)(*e*), such amounts are deemed to be employment income. Accordingly, to succeed, the appellant needed to show that the amounts in question could not reasonably be considered as having been received in consideration or partial consideration for that covenant.

[16] However, that is not easy to show in the case at bar, notably because the non-solicitation covenant is at the very heart of the termination agreement, which makes no mention of any sale of assets. Moreover, the formula for calculating the amounts paid to the appellant on an asset-value and revenue-potential basis is wholly consistent with the analysis that had to be done to determine the value of the non-solicitation covenant entered into by the appellant.

[17] The appellant submits that, despite the wording of the agreement, the clear and common intent of the parties was to carry out a sale of assets. That is far from clear, especially from the perspective of the employer, which obtained everything it was seeking through the non-solicitation clause without having to purchase assets from the appellant.

[18] There is no doubt that by entering into the covenant as he did, the appellant was relinquishing the clientele he considered as being "his"; but even assuming that the clients were in fact "his" (the evidence does not reveal where their loyalties actually lay), the legislation provides that such a covenant, when exchanged for cash in the context of an employment termination, gives rise to employment income.

[19] I find therefore that the evidence adduced in the Tax Court of Canada does not rebut the Minister's presumption that the amount in queston was paid out in consideration or partial consideration for the non-solicitation covenant and, as such, was taxable as employment income.

[20] For these reasons, I would dismiss the appeal, but without costs, as I make this determination on the basis of reasoning that is different from—in fact, contrary to—the reasoning used in first instance.

"Marc Noël"

Judge

"I concur.
Robert Décary, J.A."

"I concur.
Denis Pelletier, J.A."

Certified true translation
François Brunet, LLB, BCL

FEDERAL COURT OF APPEAL

SOLICITORS OF RECORD

DOCKET:	A-263-06
APPEAL FROM A JUDGEMENT OF THE HONOURABLE MADAM JUSTICE LOUISE LAMARRE-PROULX OF THE TAX COURT OF CANADA	
STYLE OF CAUSE:	LOUIS MORISSETTE v. SA MAJESTÉ LA REINE
PLACE OF HEARING:	Montréal, Quebec
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CONCURRED IN BY:	DÉCARY J.A. PELLETIER J.A.
DATED:	January 11, 2007

APPEARANCES:

Louis Morissette	FOR HIMSELF
Mounes Ayadi	FOR THE RESONDENT

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