

Docket: 2005-859(EI)

BETWEEN:

MICHEL DESMARAIS,

Appellant,

and

THE MINISTER OF NATIONAL REVENUE,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on common evidence with the appeal of *Pierre Desmarais*
(2005-860(EI)) on March 28, 2006, at Québec, Quebec

Before: The Honourable S.J. Savoie, Deputy Judge

Appearances:

Counsel for the Appellant: Normand Drolet

Counsel for the Respondent: Marie-Claude Landry

JUDGMENT

The appeal is dismissed and the decision by the Minister is confirmed in accordance with the attached Reasons for Judgment.

Signed at Grand-Barachois (New Brunswick), on this 30th day of June 2006.

“S.J. Savoie”

Savoie D.J.

Translation certified true
on this 11th day of December 2006.
Gibson Boyd, Translator

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Citation: 2006TCC329
Date: 20060630
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MICHEL DESMARAIS,

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Docket: 2005-860(EI)

PIERRE DESMARAIS,

Appellant,

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THE MINISTER OF NATIONAL REVENUE,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

REASONS FOR JUDGMENT

Deputy Judge Savoie

[1] These appeals were heard on common evidence at Québec, Quebec, on March 28, 2006.

[2] These are appeals against the decisions of the Minister of National Revenue (the “Minister”) dated November 25, 2004. The Appellants’ period at issue spans

from January 1, 2003 to August 16, 2004. At the heart of the issue is the work performed by the brothers Michel and Pierre Desmarais for the corporation Quincaillerie Hors Série Inc., the Payer, of which they were also shareholders and directors.

[3] The Minister determined that the Appellants were employed by the Payer under a contract of service, relying on the following presumed facts:

- 5.(a) The Payer, incorporated on July 28, 1987, operates a family hardware store;
- (b) The Payer operates its business year round and specializes in the sale of decorative and architectural hardware (locks, doorknobs, etc.);
- (c) The Appellant [Pierre Desmarais] has been providing services to the Payer since 1987; the Appellant [Michel Desmarais] since 1988;
- (d) As well as employing the Appellant and his brother (shareholder), the Payer also employs a reception clerk and a casual worker;
- (e) The main duties of the Appellant [Pierre Desmarais] can be summarized as follows:
 - serve clients, both on the telephone and in the store,
 - look after purchasing, promotion and advertising,
 - attend exhibitions, etc.

The main duties of the Appellant [Michel Desmarais] can be summarized as follows:

- serve clients, both on the telephone and in the store,
 - look after purchasing and inventory,
 - find new products
 - meet with suppliers
 - prepare deposits, etc.
- (f) The Appellant had a variable work schedule depending on the needs of the Payer, who did not record his hours;
 - (g) He generally worked from Monday to Wednesday, from 8:30 a.m. to 5:30 p.m., Thursdays and Fridays from 8:30 a.m. to 9:00 p.m. and, alternating with his brother, Saturdays from 9:00 a.m. to 5:00 p.m.;
 - (h) Despite a varying schedule, the Appellant worked 48 hours per week on average;

- (i) One of the shareholders, the Appellant or his brother, always had to be present at the store; the Appellant had to notify his brother when he had to leave the store;
- (j) To accomplish these tasks, the Appellant used all the Payer's supplies and equipment;
- (k) When he had to use his car for work, he used the Payer's credit card;
- (l) The Appellant received \$900 every two weeks and an annual bonus, leaving him with a total of \$40,000;
- (m) He was paid by cheques, cashed regularly.

[4] The Appellants and the Payer are related persons under the meaning of the *Income Tax Act* because:

- 6.(a) The voting shareholders of the Payer were
 - the Appellant, Michel Desmarais, with 35% of the shares;
 - The Appellant, Pierre Desmarais, with 40% of the shares,
 - Claude Dupéré, spouse of the Appellant, Pierre Desmarais, with 25% of the shares;
- (b) The Appellants are members of a related group that controls the Payer.

[5] The Minister determined that the Appellant and the Payer were deemed to be at arm's length in the context of this employment because he was satisfied that it was reasonable to conclude that the Appellant and the Payer would have entered into a substantially similar contract of employment if they had been dealing with each other at arm's length, given the following circumstances, which are the same in both cases:

- 7.(a) The Appellant received compensation of \$450 per week plus an annual bonus, for a reasonable total of \$40,000 per year;
- (b) The Appellant worked year-round for the Payer;

- (c) The Appellant worked roughly 48 hours per week, used the Payer's equipment and supplies and did not, as employee of the Payer assume any risk of loss;
- (d) The Appellant's duties and responsibilities were necessary for the proper operation of the Payer's business.

[6] The Appellants have admitted the Minister's presumed facts except for those stated in subparagraphs 5(d), (e) and (g) to (k) and subparagraph 7(c).

[7] It has been established that the Payer also hired two students as sales representatives during the summer season.

[8] Besides the Appellants' duties recognized by the Minister, the Appellants also mentioned others at the hearing, such as the marketing of some 3,000 products that they carefully selected to protect their particular niche since they cannot compete with the large players in this industry, such as Rona, for example. With this objective in mind, they rent spaces at different home shows where they advertise their various products.

[9] The two Appellants did not count their work hours. At the store, they were present and on duty approximately 55 to 60 hours per week. In addition, they often worked evenings, weekends and holidays. The Appellants received no compensation for overtime hours worked. They used the Payer's credit card when using their car to meet clients or to take part in exhibitions.

[10] They were both solidarily liable for the Payer's loans and its \$20,000.00 line of credit. The Appellants met at the Payer's annual meeting, along with their accountant. Yet they discussed the Payer's business every day.

[11] The Appellants, as the Payer's shareholders, voted on their bonus, which was not automatic, but rather depended on the profitability of the business.

[12] It remains to be determined if the Appellants' employment is excluded from insurable employment.

[13] Since the Appellants were related to a group that controlled the Payer, the Minister determined that these people were not at arm's length, as prescribed by the *Income Tax Act*, in subparagraph 251(2)(b)(iii) reproduced below:

251(2) Definition of “related persons”. For the purpose of this Act, "related persons", or persons related to each other, are:

...

(b) a corporation and:

...

(iii) any person related to a person described in subparagraph 251(2)(b)(i) or 251(2)(b)(ii);

...

[14] In accordance with the preceding, the Minister maintains that the Appellants' employment is excluded under paragraph 5(2)(i) of the *Employment Insurance Act*, (the “Act”), reproduced below:

(2) Insurable employment does not include:

...

(i) employment if the employer and employee are not dealing with each other at arm's length.

[15] Thus the Minister has the discretion to determine in accordance with the mandate conferred by the legislation under paragraph 5(3)(b) whether non-related persons would have entered into a substantially similar contract if they were dealing with each other at arms length. This paragraph is reproduced below:

(3) For the purposes of paragraph (2)(i),

...

(b) if the employer is, within the meaning of that Act, related to the employee, they are deemed to deal with each other at arm's length if the Minister of National Revenue is satisfied that, having regard to all the circumstances of the employment, including the remuneration paid, the terms and conditions, the duration and the nature and importance of the work performed, it is reasonable to conclude that they would have entered into a substantially similar contract of employment if they had been dealing with each other at arm's length.

[16] The Minister therefore proceeded to analyze the Appellants' employment according to paragraph 5(3)(b) of the Act.

REMUNERATION

[17] Exhibit I-2, filed at the hearing, was prepared by the Minister of Human Resources and Skills Development Canada. This document establishes that the salary paid to the Appellants, including their bonus, is within the average of those paid in this type of business for similar work.

[18] The Appellants received a fixed salary of \$900.00 gross every two weeks, or \$450.00 per week for a work week sometimes reaching 60 weeks or more. They received a bonus that was awarded depending on the Payer's financial condition.

[19] Tardif J. of this Court addressed a similar case in the judgment *Industries J.S.P. Inc. v. Canada (Minister of National Revenue – M.N.R.)*, [1999] T.C.J. No. 423, and stated after his analysis:

Contributing to and being a partner in the management, administration or development of a business, particularly a small business, means that a person's job description is strongly marked by responsibilities characteristic of those often fulfilled by actual business owners or persons holding more than 40 per cent of the voting shares in the company employing them. In other words, in assessing remuneration, at this level of responsibility, caution must be exercised when a comparison is made with the salaries of third parties; often there are advantages that offset the lower salaries.

This led him to conclude that the employment of these members of the same family, therefore not at arm's length, was not excluded from insurable employment.

DURATION OF EMPLOYMENT

[20] The Appellants worked year round and full-time for the Payer, one since 1987 and the other since 1988.

TERMS AND CONDITIONS OF EMPLOYMENT

[21] Let us not forget that the Appellants acted not only as workers for the Payer, but also as shareholders and directors. The evidence has demonstrated that they put all their energy into the business, by not counting their hours, but also by accepting their respective status of minority shareholders, subject to the Payer's power, exercised by the voice of the board of directors, of which they were members and held the majority of shares.

[22] The Appellants, in their duties, their work and their administrative responsibilities, had the latitude to act as shareholders and could make the decisions necessary to ensure the proper operation of the business individually, in the other Appellant's absence, but they regularly communicated and consulted with one another on the Payer's affairs, like something of an informal board of directors. Nearly all the necessary equipment was supplied by the Payer, except for their car. They were both solidarily liable for the Payer's line of credit of \$20,000.00.

[23] It has not been proven that other shareholders, at arm's length, would not have entered into a substantially similar contract with the Payer, occupying a similar position.

NATURE AND IMPORTANCE OF THE WORK

[24] It has been determined that the Appellants' work was essential for the proper operation of the business. Indeed, without them, the business would not exist.

[25] This Court analyzed the facts, in the instant case, in light of the legislation cited above. This Court also examined how the Minister carried out his mandate under the legislation. The Federal Court of Appeal has described the mandate of the Minister and this Court in *Légaré v. Canada (Minister of National Revenue – M.N.R.)* [1999] F.C.J. No. 878, reviewing the Minister's decision, in which Marceau J.A. held the following at paragraph 4:

The Act requires the Minister to make a determination based on his own conviction drawn from a review of the file. The wording used introduces a form of subjective element, and while this has been called a discretionary power of the Minister, this characterization should not obscure the fact that the exercise of this power must clearly be completely and exclusively based on an objective appreciation of known or inferred facts. And the Minister's determination is subject to review. In fact, the Act confers the power of review on the Tax Court of Canada on the basis of what is discovered in an inquiry carried out in the presence of all interested parties. The Court is not mandated to make the same kind of determination as the Minister and thus cannot purely and simply substitute its assessment for that of the Minister: that falls under the Minister's so-called discretionary power. However, the Court must verify whether the facts inferred or relied on by the Minister are real and were correctly assessed having regard to the context in which they occurred, and after doing so, it must decide whether the conclusion with which the Minister was "satisfied" still seems reasonable.

[26] Having studied this case, this Court must conclude that the Minister carried out his mandate as prescribed by the legislation and the case law.

[27] Moreover, I must find that the facts inferred or relied on by the Minister are real and were correctly assessed having regard to the context in which they occurred. In my opinion, the conclusion with which the Minister was "satisfied" still seems reasonable to me.

[28] Consequently, the appeals are dismissed and the Minister's decisions are confirmed.

Signed at Grand-Barachois (New Brunswick), this 30th day of June 2006.

“S.J. Savoie”

Savoie D.J.

Translation certified true
on this 11th day of December 2006.
Gibson Boyd, Translator

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DOCKET: 2005-859(EI), 2005-860(EI)

STYLE OF CAUSE: Michel Desmarais and M.N.R. and
Pierre Desmarais and M.N.R.

PLACE OF HEARING: Québec, Quebec

DATE OF HEARING: March 28, 2006

REASONS FOR JUDGMENT BY: The Honourable S.J. Savoie,
Deputy Judge

DATE OF JUDGMENT: June 30, 2006

APPEARANCES:

For the Appellants: Normand Drolet

For the Respondent: Marie-Claude Landry

SOLLICITORS OF RECORD:

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