Dockets: 2006-3802(IT)G
2006-3801(GST)I

BETWEEN:

DELSO RESTORATION LTD.,

appellant,

and

HER MAJESTY THE QUEEN,

respondent.

Motion heard with the motions of Domenic Eramo
(2006-3600(IT)G) and Natalie Eramo (2006-3599(IT)I)
on August 12, 2009, at Toronto, Ontario.

Before: The Honourable Justice Gaston Jorré

Appearances:

Counsel for the appellant:	A. Christina Tari Leigh Somerville Taylor
Counsel for the respondent:	Bobby Sood

ORDER

Upon motion made by the appellant;

And upon hearing the parties;

In accordance with the attached reasons for order, the motion is dismissed. Costs are in the cause.

Signed at Ottawa, Ontario, this 20th day of September 2011.

"Gaston Jorré"

Jorré J.

Docket: 2006-3600(IT)G

BETWEEN:

DOMENIC ERAMO,

appellant,

and

HER MAJESTY THE QUEEN,

respondent.

Motion heard with the motions of Delso Restoration Ltd. (2006-3802(IT)G and 2006-3801(GST)I) and Natalie Eramo (2006-3599(IT)I) on August 12, 2009, at Toronto, Ontario.

Before: The Honourable Justice Gaston Jorré

Appearances:

Counsel for the appellant:	A. Christina Tari Leigh Somerville Taylor
Counsel for the respondent:	Bobby Sood

ORDER

Upon motion made by the appellant;

And upon hearing the parties;

In accordance with the attached reasons for order, the motion is dismissed. Costs are in the cause.

Signed at Ottawa, Ontario, this 20th day of September 2011.

"Gaston Jorré"

Jorré J.

Docket: 2006-3599(IT)I

BETWEEN:

NATALIE ERAMO,

appellant,

and

HER MAJESTY THE QUEEN,

respondent.

Motion heard with the motions of Delso Restoration Ltd.
(2006-3802(IT)G and 2006-3801(GST)I) and Domenic Eramo
(2006-3600(IT)G) on August 12, 2009, at Toronto, Ontario.

Before: The Honourable Justice Gaston Jorré

Appearances:

Counsel for the appellant:	A. Christina Tari Leigh Somerville Taylor
Counsel for the respondent:	Bobby Sood

ORDER

Upon motion made by the appellant;

And upon hearing the parties;

In accordance with the attached reasons for order, the motion is dismissed. Costs are in the cause.

Signed at Ottawa, Ontario, this 20th day of September 2011.

"Gaston Jorré"

Jorré J.

Citation: 2011 TCC 435
Date: 20110920
Dockets: 2006-3802(IT)G, 2006-3801(GST)I
2006-3600(IT)G
2006-3599(IT)I

BETWEEN:

DELSO RESTORATION LTD.,
DOMENIC ERAMO,
NATALIE ERAMO,

appellants,

and

HER MAJESTY THE QUEEN,

respondent.

REASONS FOR ORDER

Jorré J.

Introduction

[1] The appellants have applied for a determination of questions before trial pursuant to Rule 58 of the *Tax Court of Canada Rules (General Procedure)*, specifically:

(a) Were the assessments of Domenic Eramo and Natalie Eramo in issue in these appeals permitted by subsection 15(1) of the *Income Tax Act* (*Act*), as amended, as alleged by the respondent?
(b) Were the assessments of Mr. and Mrs. Eramo in issue in these appeals permitted by subsection 56(2) of the *Act*, as alleged by the respondent?

[2] Neither of these questions affects the two appeals relating to Delso Restoration Ltd. (Delso), one of which is an income tax appeal and the other a GST appeal.

[3] Throughout the remainder of these reasons, the discussion, unless otherwise noted, relates to the appeals of Mr. and Mrs. Eramo.

Background

[4] Based on the pleadings, the Minister reassessed the appellants' 1995 taxation year, *inter alia*, on the following basis:[1]

(a) Mr. and Mrs. Eramo owned, respectively, 80% and 20% of Nadome Investments Ltd., a company which in turn is the parent corporation of Delso.
(b) Delso paid for various renovations on the home of Mr. and Mrs. Eramo, as well as for landscaping at the home of Mr. Eramo's parents and deducted these costs in computing its expenses.
(c) These expenditures of some $90,000 plus GST were not made for the purpose of producing income.
(d) At the direction of Mr. and Mrs. Eramo, the invoices for the renovation work were issued to Delso and were falsified in an effort to disguise the renovation costs as legitimate business expenses.
(e) The renovation costs were personal and living expenses of Mr. and Mrs. Eramo.
(f) Delso made no adjustments to the shareholder loan accounts.
(g) Neither Mr. nor Mrs. Eramo included any amount in their income in relation to benefits received in respect to the renovations and the landscaping.

[5] The Minister also alleges in the replies that Mr. and Mrs. Eramo failed to include benefits with respect to the renovations and other personal expenditures that were appropriated from, or conferred by, Delso.[2]

[6] The Minister included in the income of Mr. Eramo a benefit equal to 80% of the expenditures and, in the case of Mrs. Eramo a benefit equal to 20% of the expenditures.

[7] In the submissions portions of the replies, the respondent submits that Mr. and Mrs. Eramo received ". . . benefits appropriated from, or conferred by, Delso, but which he [she] failed to include in his [her] income for that year. The Minister correctly reassessed the Appellant's 1995 taxation year to include the . . . unreported benefits in his [her] income, pursuant to subsections 15(1) and 56(2) of the *Act*."[3]

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[1] See paragraph 7 of the reply in Mr. Eramo's appeal and the corresponding paragraph of the reply in Mrs. Eramo's appeal.
[2] *Ibid.* at paragraphs 5 and 6, respectively.
[3] *Ibid.*, at paragraphs 11 and 12, respectively.

[8] The Minister disallowed the deduction of the renovation and landscaping expenditures by Delso.

[9] The four notices of appeal raise a variety of other issues including alleged charter violations and whether the 1995 taxation year was statute barred.

Analysis

Rule 58

[10] Rule 58 says:

> 58(1) A party may apply to the Court,
>
> > (*a*) for the determination, before hearing, of a question of law, a question of fact or a question of mixed law and fact raised by a pleading in a proceeding where the determination of the question may dispose of all or part of the proceeding, substantially shorten the hearing or result in a substantial saving of costs, or
> > (*b*) to strike out a pleading because it discloses no reasonable grounds for appeal or for opposing the appeal,
>
> and the Court may grant judgment accordingly.
>
> (2) No evidence is admissible on an application,
>
> > (*a*) under paragraph (1)(*a*), except with leave of the Court or on consent of the parties, or
> > (*b*) under paragraph (1)(*b*).
>
> (3) The respondent may apply to the Court to have an appeal dismissed on the ground that,
>
> > (*a*) the Court has no jurisdiction over the subject matter of an appeal,
> > (*b*) a condition precedent to instituting a valid appeal has not been met, or
> > (*c*) the appellant is without legal capacity to commence or continue the proceeding,
>
> and the Court may grant judgment accordingly.

[11] The law is well settled that Rule 58 is not intended to provide an easily available right to have the determination of complex and contentious issues and that the rule is discretionary.[4]

[4] See for example *Canada v. Jurchison*, 2001 FCA 126, at paragraph 8.

[12] There is a great deal of authority for the proposition that there must be no dispute as to facts[5] although much of this authority precedes the amendments made in 2004 which added to Rule 58(1)(*a*) the following words: "a question of fact or a question of mixed law and fact".

[13] Given those amendments the existence of a factual dispute cannot be an absolute bar to there being a determination under the rule.[6]

[14] However, the existence of one or more factual disputes will always be relevant to the question whether the determination will substantially shorten the hearing or result in a substantial saving of costs.

[15] Here, I am satisfied that there are significant factual disputes between the parties even if one excludes all the other issues raised by Mr. and Mrs. Eramo apart from those relating to subsections 15(1) and 56(2) of the *Act*. On the pleadings, there are no admissions by Mr. and Mrs. Eramo of the facts assumed or alleged by the Minister in relation to subsections 15(1) and 56(2).[7]

[16] However, in *Canada v. Webster*,[8] Rothstein J.A., speaking for the majority, states at paragraph 5 :

> 5 In *Berneche*, *supra*, at paragraph 7, Mahoney J.A. noted that the requirement that there be no dispute as to any material fact is often stated in terms of an agreement or admission of facts. However, agreement is not a requirement. The Motions Judge may draw a conclusion that there are no material facts in dispute, and such conclusion might be drawn from the entire pleadings of the respondent on the motion, on the assumption that what has been pleaded is true, much as in the case of a motion to strike a statement of claim as disclosing no reasonable cause of action. . . .[9]

[17] Although the motion does not say so explicitly, it is clearly implicit in the grounds set out in the motion[10] as well as the basis on which Mr. and Mrs. Eramo argued the motion[11] that, for the purposes of the motion, the appellants are prepared to accept that the facts alleged in the replies are to be taken as true.

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[5] See for example *McLarty v. Canada*, 2002 FCA 206, at paragraph 7, or *Canada v. Webster*, 2002 FCA 205, at paragraph 8.

[6] Rule 58(2)(*a*) also contemplates the possibility of evidence. I do not have to decide whether the rule, as amended, allows (i) for the possibility of a determination of any kind of fact or (ii) only for the determination of the proper conclusion of fact that is to be determined from other facts which are not disputed.

[7] Indeed, the notices of appeal say very little at all in relation to facts related to subsections 15(1) and 56(2).

[8] See footnote 5.

[9] *Webster* was issued on the same day and by the same panel as *McLarty*, above.

[10] See particularly paragraphs 3 and 4 on page 2 of the motion.

[11] See the appellants' written submissions at Tab 13 of the motion record as well as page 17, line 20, to page 18, line 5, of the transcript.

[18] I will proceed on the basis that Mr. and Mrs. Eramo have, for the purposes of the motion, admitted the allegations and assumptions set out in the replies.

[19] Given the comments quoted from *Webster*, above, I cannot see any reason why the absence of agreement between the parties on the relevant facts would, in itself, preclude a determination of law where one party is prepared to accept, for the purposes of the motion, the allegations made by the other party as is the case here.

[20] However, for reasons that will become apparent below, it is not, in fact, necessary for me to decide this point and I choose not to do so.

[21] If, assuming the allegations of the respondent to be true, the answer to the two proposed questions is "no", then the replies would not disclose any valid basis for the assessments in issue and the disputes might well come to an end.[12]

[22] A key requirement of the rule is that the determination "may dispose of all or part of the proceeding, substantially shorten the hearing or result in a substantial saving of costs". (I shall refer collectively to the words just quoted as "shorten the hearing".)

[23] Consequently for this purpose, it is relevant to ask if it is likely that the determination will shorten the hearing.

[24] In this case, if the answer to either question is "yes", then the litigation will not be materially shorter since it will be necessary to deal with all the evidence relating to the conferring of benefits as well as all the other issues raised in the notices of appeal apart from subsections 15(1) and 56(2) of the *Act*.[13]

[25] Accordingly, to answer the question "Will the determination shorten the hearing?", it is necessary to consider the law on the two proposed questions taking, for the purposes of the motion, the allegations and assumptions in the replies to be true.

[26] I will begin with subsection 56(2).[14]

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[12] Although it was not framed in this manner the motion looks very similar to a motion under Rule 58(1)(*b*) seeking to strike out the reply "because it discloses no reasonable grounds . . . for opposing the appeal". Given my conclusions below, it is unnecessary for me to consider what the consequences are of framing the motion under Rule 58(1)(*a*) instead of (*b*).

[13] If the answer to both questions is "no", then it is likely that it would be unnecessary to deal with that evidence and that the matter would come to an end; however, there may be some other considerations which, in the light of my conclusions below, need not be examined.

[14] Subsection 56(2) reads as follows:

[27] The essence of Mr. and Mrs. Eramo's argument with respect to the subsection 56(2) issue is that, in addition to the four generally accepted requirements for subsection 56(2) to apply, there is a fifth condition.

[28] The four generally accepted conditions are:

> (1) the payment must be to a person other than the reassessed taxpayer;
> (2) the allocation must be at the direction or with the concurrence of the reassessed taxpayer;
> (3) the payment must be for the benefit of the reassessed taxpayer or for the benefit of another person whom the reassessed taxpayer wished to benefit; and
> (4) the payment would have been included in the reassessed taxpayer's income if it had been received by him or her.[15]

[29] Mr. and Mrs. Eramo argue that the fifth condition is that subsection 56(2) can only apply if the benefit conferred is not taxable in the hands of the transferee. Specifically, they submit that subsection 56(2) cannot apply because the contractors are taxable on the payments.

[30] This additional condition is discussed in *Smith v. M.N.R.*[16] where Mahoney J.A. speaking for the Federal Court of Appeal said, at pages 262-263:

> . . . That, however, is not an end to the matter. This Court's decision in *Outerbridge Estate* was rendered after the trial judgment herein. It has added another precondition to the application of subsection 56(2), which seems to me to be relevant in the circumstances.
>
> It was held in *Outerbridge, supra,* at pages 117–18 (D.T.C. 6684),
>
> > that the validity of an assessment under subsection 56(2) of the Act when the taxpayer had himself no entitlement to the payment made or the property transferred is subject to an implied condition, namely that the payee not be subject to tax on the benefit received.
>
> That conclusion, *obiter* in the result, was based on the analysis by Marceau, J.A. that preceded it (C.T.C. 117, D.T.C. 6684).

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(2) A payment or transfer of property made pursuant to the direction of, or with the concurrence of, a taxpayer to some other person for the benefit of the taxpayer or as a benefit that the taxpayer desired to have conferred on the other person . . . shall be included in computing the taxpayer's income to the extent that it would be if the payment or transfer had been made to the taxpayer.

[15] See *Neuman v. M.N.R.*, [1998] 1 S.C.R. 770, at paragraph 32.

[16] [1993] 2 C.T.C. 257.

> It is generally accepted that the provision of subsection 56(2) is rooted in the doctrine of "constructive receipt" and was meant to cover principally cases where a taxpayer seeks to avoid receipt of what in his hands would be income by arranging to have the amount paid to some other person either for his own benefit (for example the extinction of a liability) or for the benefit of that other person [citations omitted]. There is no doubt, however that the wording of the provision does not allow to its being confined to such clear cases of tax-avoidance. The *Bronfman* judgment, which upheld the assessment, under the predecessor of subsection 56(2), of a shareholder of a closely held private company, for corporate gifts made over a number of years to family members, is usually cited as authority for the proposition that it is not a pre-condition to the application of the rule that the individual being taxed have some right or interest in the payment made or the property transferred. The precedent does not appear to me quite compelling, since gifts by a corporation come out of profits to which the shareholders have a prospective right. But the fact is that the language of the provision does not require, for its application, that the taxpayer be initially entitled to the payment or transfer of property made to the third party, only that he would be subject to tax had the payment or transfer been made to him. *It seems to me however, that when the doctrine of constructive receipt is not clearly involved, because the taxpayer had no entitlement to the payment being made or the property being transferred, it is fair to infer that subsection 56(2) may receive application only if the benefit conferred is not directly taxable in the hands of the transferee. Indeed, as I see it, a tax-avoidance provision is subsidiary in nature; it exists to prevent the avoidance of a tax payable on a particular transaction, not simply to double the tax normally due nor to give the taxing authorities an administrative discretion to choose between possible taxpayers.*
>
> [Emphasis added.]

> While I might have distinguished *Bronfman* on further or other grounds, since the benefit to the shareholders of having personal gifts paid for by the company with pre-tax dollars over the shareholders themselves paying for them with after-tax dollars seems transparently clear, I agree with that analysis. Being "subject to tax on the benefit received" means that it is required to be included in the calculation of the recipient's taxable income.

[31] In considering the application of subsection 56(2) it is important to emphasize the third condition: "for the *benefit of the reassessed taxpayer* or for the *benefit of another person* whom the reassessed taxpayer wished to benefit" (emphasis added). The subsection is concerned with the conferring of a benefit on someone.

[32] It is also useful to bear in mind the purpose of subsection 56(2), as explained by the Supreme Court of Canada in *Canada v. McClurg*:[17]

> Subsection 56(2) of the *Income Tax Act*
>
> In attempting to discern the purpose of s. 56(2), it is helpful to refer to the body of jurisprudence dealing with the subsection. A useful starting point is an early case dealing with the predecessor section to s. 56(2): *Miller v. M.N.R.*, 62 D.T.C. 1139 (Ex. Ct.). In that case, Thurlow J., as he then was, in examining s. 16(1) of the Act, made some general comments, at p. 1147, as to the anti-avoidance purpose of the provision which remain relevant today:
>
> > In my opinion, s. 16(1) is intended to cover cases where a taxpayer seeks to avoid receipt of what in his hands would be income by arranging to have the amount received by some other person whom he wishes to benefit or by some other person for his own benefit. The scope of the subsection is not obscure for one does not speak of benefitting a person in the sense of the subsection by making a business contract with him for adequate consideration.
>
> Strayer J. noted, at p. 4, in respect of the *Miller* case:
>
> > Two important qualifications are noted here: the first is that the taxpayer seek "to avoid receipt" of funds, presumably funds that would otherwise be payable to him; and the second is that the concept of payment of a "benefit" is contrasted to payments for adequate consideration.
>
> In my opinion, the views of Thurlow J. and Strayer J. provide a sound foundation for the interpretation of s. 56(2). The subsection obviously is designed to prevent avoidance by the taxpayer, through the direction to a third party, of receipts which he or she otherwise would have obtained. I agree with both Thurlow J. and Strayer J. in their characterization of the purpose of the section and, specifically, I concur with their view that the section reasonably cannot have been intended to cover benefits conferred for adequate consideration in the context of a legitimate business relationship.

[33] In *M.N.R. v. Neuman*,[18] the Federal Court of Appeal stated that there was no general requirement of a fifth condition being met.

[34] The circumstances of *Outerbridge Estate v. Canada*[19] and *Smith* are important.

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[17] [1990] 3 S.C.R. 1020, at page 1051.

[18] [1996] 3 C.T.C. 270, at pages 292-293. In the Supreme Court of Canada decision in *Neuman* (see footnote 15), this comment was noted at paragraph 29; the Supreme Court made no further comment on this point.

[19] [1991] 1 C.T.C. 113 (FCA), also referred to as *Winter v. Canada*.

[35] In *Outerbridge*, Sir Leonard Outerbridge caused a company he controlled to sell shares to his son-in-law for less than their fair market value. The appellant had argued that the son-in-law was taxable on the benefit under subsection 15(1) and that the law was not intended to tax the benefit twice.

[36] While the Court of Appeal found the son-in-law was not taxable under subsection 15(1) because the benefit was conferred on the son-in-law in his capacity as a son-in-law, it accepted the principle that if the son-in-law had received this in his capacity as shareholder then subsection 15(1) would have applied to him and subsection 56(2) would not have applied to Sir Leonard. The Court of Appeal was satisfied that what had been conferred was a benefit.

[37] In *Smith* the facts are somewhat complicated. However, when one goes back to the judgment of Addy J. at trial[20] it is very clear that, with respect to the amounts which the Court of Appeal held to be taxable, there was a finding that these amounts had been received as benefits by the transferee "Holiday 77".[21] That finding was upheld on appeal.

[38] The Court of Appeal also found in *Smith*, at page 263,[22] that the amounts received by the transferee, "Holiday 77", as benefits were taxable. The amounts received by the transferee were not earned by the transferee as consideration for services rendered or goods supplied.

[39] In *Outerbridge* and *Smith*, the payments to the transferees were taxable benefits because the payments were not made in return "for adequate consideration in the context of a legitimate business relationship".[23]

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[20] [1986] 1 C.T.C. 418 (FCTD).
[21] There was no supply of goods or services from "Holiday 77" to "Holiday 80" in relation to the payments in issue.
[22] See footnote 16.
[23] See *McClurg* (footnote 17).

[40] In both *Outerbridge* and *Smith*, the recipient of the payment or the property happened to also be the person on whom a benefit was conferred.[24]

[41] Where the recipient of the payment or the transferred property is simply receiving payment in return for adequate consideration (the supply of goods or services), there is no benefit being conferred on the recipient of the payment.

[42] Those factual circumstances assist in understanding *Smith*, at page 263:[25]

> *. . . subsection 56(2) may receive application only if the benefit conferred is not directly taxable in the hands of the transferee. Indeed, as I see it, a tax-avoidance provision is subsidiary in nature; it exists to prevent the avoidance of a tax payable on a particular transaction, not simply to double the tax normally due nor to give the taxing authorities an administrative discretion to choose between possible taxpayers.*
>
> . . . Being "subject to tax on the benefit received" means that it is required to be included in the calculation of the recipient's taxable income.
>
> [Original italicized. Underlining added.]

The "it" in the second to last line of the preceding quotation is clearly a reference to the word "benefit".

[43] As stated in *McClurg*: "The subsection obviously is designed to prevent avoidance by the taxpayer, through the direction to a third party, of receipts which he or she otherwise would have obtained."[26] If the "fifth condition" in *Outerbridge* and *Smith* were that subsection 56(2) is inapplicable when the recipient of the payment is obliged to include the payment in his income, then the subsection would be largely ineffective.

[44] This is easily illustrated by the following example. "A"[27] causes company "X" to pay company "Y", an electronics store, for the purchase of the television to be delivered to "A". Since "Y" sells the television in the course of its normal business, the receipt would enter into its computation of taxable income and subsection 56(2) would be inapplicable if the correct approach is that subsection 56(2) can have no

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[24] It is worth noting that in *Outerbridge* and, more generally, when someone seeks to provide a benefit to a friend or relative by directing some payment, or property transfer, to that friend or relative by directing, say, a company, to pay, the person making the direction is as much the beneficiary as the friend or relative; this is true both emotionally and financially (insofar as the company pays rather than the person directing the payment).

[25] See footnote 16.

[26] See footnote 17.

[27] Assuming "A" is not a shareholder, an employee, an officer or a director of "X".

application where the recipient is taxable. That would largely defeat the purpose of the subsection as stated by the Supreme Court of Canada in *McClurg*.

[45] Nothing in subsection 56(2) supports such an interpretation. In *Outerbridge* and *Smith* it was unnecessary to distinguish between (i) the recipient of the payment (or transferee of the property) and (ii) the person intended to receive the benefit; in *Outerbridge* and *Smith* they were one and the same person. As a result it was not necessary in those decisions to make a distinction between the recipient and the beneficiary.

[46] However, where the recipient and the beneficiary are different persons when one considers the wording of the subsection and the comments cited above in *McClurg* as to the purpose of the provision, it becomes apparent that the additional condition, the fifth condition, should be restated in circumstances such as this case in the following manner:

1. Where the first four conditions are met,
2. where the taxpayer has no pre-existing entitlement to the payment or property,
3. where a benefit is conferred on a person other than the taxpayer and
4. that benefit is taxable as a benefit in the hands of that other person under some other provision of the *Act*,

then the benefit conferred will only be taxable once, in the hands of the actual recipient of the benefit (that other person). It cannot be taxed a second time under subsection 56(2).

[47] This is entirely consistent with the purpose of subsection 56(2) as set out in *McClurg* above. If a taxpayer buys a gift for his child and pays for the gift with money he appropriated from a corporation he owns, the taxpayer will be taxable on the appropriated funds notwithstanding the fact that the supplier of the gift will be taxable on the sale of the gift to the taxpayer as part of his normal business income.

[48] Similarly, under subsection 56(2) the taxpayer who directs a corporation to buy a gift for his child and send the gift to his child is taxable on the amount spent by the corporation; this liability of the taxpayer is not affected by the fact that the supplier of the gift is taxable on the sale of the gift.[28]

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[28] Where the benefit is for the taxpayer himself, there can be no taxation twice in the absence of a clear statutory intention as a result of paragraph 248(28)(*a*) of the *Act*.

Given that subsection 56(2) is only about benefits conferred without adequate consideration in return (see passage from *McClurg* cited above), it does not appear that there are that many possible situations where the fifth condition could come into play.

[49] This is a very different situation from the situation in *Outerbridge* where, *if* the son-in-law had been taxable in his capacity as a shareholder, then there might[29] have been taxation of the same benefit twice.[30]

[50] In this case, no benefit was conferred on the contractors doing renovations or making improvements to Mr. and Mrs. Eramo's residence, nor was any benefit being conferred on the contractors doing landscaping on the house of Mr. Eramo's parents. The recipients of the benefit were Mr. and Mrs. Eramo as well as Mr. Eramo's parents.

[51] The contractors were simply receiving payments for services supplied in the normal course of business.

[52] Accordingly, to the extent that there is a fifth condition, it does not have application here, given the facts I must assume.

[53] With respect to subsection 56(2), the appellants made a further argument that, on the face of the respondent's pleadings, the fourth condition was not met insofar as the respondent did not plead that the amounts in question would have been included in the income of Mr. and Mrs. Eramo if the amounts had been received by them.

[54] The difficulty with this submission is the following.

[55] For these purposes I must assume that it is not a shareholder benefit[31] nor an employee benefit,[32] both of which would be taxable if that were the nature of what happened. Taking the respondent's allegations as a given, they amount to Mr. and

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[29] I use "might" because one would have to consider whether, if the company had properly decided upon and conferred a shareholder benefit, the third condition was met in the circumstances.

[30] The decision of the Federal Court of Appeal in *Lambert v. Canada*, 2004 FCA 389, is entirely consistent with this; in *Lambert*, a benefit was conferred on "Aviation" and that benefit was not taxable. Similarly, in *Peddle v. The Queen*, 2004 TCC 226, the evidence set out therein shows that the $7,000 payment to "Eagle" ultimately excluded from income by the judgment did not arise from "Eagle" having furnished any consideration to "Riverside", as a result of which the question arose whether the benefit received by "Eagle" was taxable in its hands.

[31] At the hearing there was some debate on how I should read the pleadings and whether I should infer from the replies that the appellants were shareholders. However, I do not need to deal with this point. I do note that in paragraph 6 of Mrs. Eramo's notice of appeal it is alleged that she does not own shares in Delso and is not an officer of Delso, which allegation is denied by in the respondent's reply. In the case of Mr. Eramo, he alleges at paragraph 4 of the notice of appeal that he is an officer of Delso, which allegation is admitted by the respondent; there is no allegation by Mr. Eramo that he is not a shareholder.

[32] The appellants do not allege that the amounts in issue are employee (or officer) benefits, something they would have to allege and demonstrate at trial. Furthermore, that would be inconsistent with the respondent's allegation in the replies that the invoices were falsified to make them look like legitimate business expenses.

Mrs. Eramo having indirectly appropriated over $90,000 from Delso to their benefit[33] by causing Delso to pay for the renovations and landscaping.

[56] For the purposes of the fourth condition one has to analyze the situation as if Mr. and Mrs. Eramo had received the $90,000 themselves instead of the funds being paid to contractors.

[57] Had Mr. and Mrs. Eramo received the $90,000 it could not have been the reimbursement of a loan or a return of share capital, nor could it have been a gain from the disposition of something to the company.[34]

[58] It would purely and simply have been an appropriation to themselves directly of corporate assets to which they had no legal right.

[59] Delso, like any companies, is a separate legal entity; the fact that Mr. and Mrs. Eramo may own Delso directly or indirectly does not mean that they have any right to simply take any asset of the corporation. For them to validly acquire any corporate assets there must be a valid corporate decision which results in a transfer of the assets.

[60] For example there must be a corporate decision to effect a return of capital, the payment of dividends, a loan to someone or the payment of bonuses to employees, etc. Such decisions are normally recorded in some way and show up in the corporate records. For example, a loan to a shareholder will be recorded in a shareholder loan account.

[61] Here, based on the allegations which I must assume for these purposes, there is nothing like that. There are allegedly false invoices to disguise the purpose of the payments. Even if the appellants are officers of the corporation, given the obligations that they have to the corporation in corporate law, they could not be validly acting on behalf of the corporation in making payments justified with false invoices that hide the fact of their benefiting from the payments.

[62] As a result, if the appellants appropriated the $90,000 directly to themselves in such circumstances they could not be doing so in any capacity as officers, employees or shareholders; they would be doing so in their capacity as individuals without the company having validly authorized such a payment from a corporate law perspective.

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[33] Or the benefit of Mr. Eramo's parents.

[34] Not only would these possibilities have to be alleged and proven by the appellants but they are clearly inconsistent with the respondent's allegations, notably those of falsified invoices to hide the actual use of the payments.

[63] Such an appropriation of property to which a person has no legal right is income and is taxable. The fact that they may be under legal obligation to account for the income to the corporation does not change the fact that the appropriation has the quality of income in the hands of Mr. and Mrs. Eramo.[35]

[64] As a result the allegations in the replies provide sufficient facts to support the fourth condition.

[65] Thus, the answer to the second question is: Yes, subsection 56(2) does form a basis for the assessments, on the assumption that the allegations in the replies are true.

[66] Consequently, the proposed determinations are unlikely to significantly shorten the hearing.

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[35] On the alleged facts there is an organized activity involved in appropriating the $90,000 amount to Mr. and Mrs. Eramo's benefit. They had to cause the company to contract for the work, make the necessary payments and falsify the invoices. Such organized activity constitutes at least an adventure in the nature of trade and is taxable as such.

While the context is different, the taxability is not different in principle from that where an employee obtains funds to which he has no legal right from a corporation such as in *The Queen v. Poynton*, [1972] C.T.C. 411 (Ontario Court of Appeal). From *Poynton* it is clear that, even if there is an obligation to account for the funds, appropriation of the funds still has the quality of income. Given the separate juridical personality of Delso, the fact of Mr. and Mrs. Eramo being indirect owners, as I indicated above, does not change this.

I note that it is quite clear from *Poynton* that the taxability of funds obtained through a conscious effort to obtain funds without a legal basis from a company is in no way dependent on specific provisions relating to employee, officer, director or shareholder benefits. See *Poynton*, at pages 419-420:

> I am of the opinion that there is no difference between money and money's worth in calculating income. They are both benefits and fall within the language of sections 3 and 5 of the Act, being benefits received or enjoyed by the respondent in respect of, in the course of, or by virtue of his office or employment. I do not believe the language to be restricted to benefits that are related to the office or employment in the sense that they represent a form of remuneration for services rendered. *If it is a material acquisition which confers an economic benefit on the taxpayer and does not constitute an exemption, eg loan or gift, then it is within the all-embracing definition of section 3.*
>
> In view of the above finding I do not consider it necessary to refer in detail to paragraph 8(1)(*b*) and subsection 137(2). These provisions would appear to refer to those situations in which the taxpayer obtains a benefit with the knowledge and consent of the donor-employer and would have no application in the present factual situation. *The benefits sought to be taxed did not accrue to Poynton nor were they conferred upon or received by him qua director, qua officer or qua shareholder but qua thief.*
>
> [Emphasis added.]

The emphasized passages show that the liability for tax arose apart from Poynton's employment and apart from his being a director.

The principle does not require that there be theft; it is equally applicable if something is taken through organized effort in the absence of a valid legal right to do so.

On the facts I must assume, the appropriation here may well be taxable even in the absence of subsection 56(2), but since that question was not before me, I need not deal with it.

[67] In the circumstances, given this conclusion it is unnecessary for me to consider the first question.[36]

Conclusion

[68] Accordingly, it is not appropriate to order a determination and the motion will be dismissed.

[69] Costs will be in the cause.

Signed at Ottawa, Ontario, this 20th day of September 2011.

"Gaston Jorré"

Jorré J.

[36] It is also unnecessary for me to consider a number of matters raised. For example, there was an issue at the start of the hearing as to whether the parties had agreed among themselves that I could make the determination without first deciding whether there should be a determination. The appellants were of the view that there was such an agreement; the respondent was not. Given my conclusion it does not matter.

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PLACE OF HEARING:	Toronto, Ontario
DATE OF HEARING:	August 12, 2009
REASONS FOR ORDER BY:	The Honourable Justice Gaston Jorré
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