Docket: 2018-1659(EI)

BETWEEN:

SLOW PUB LTD.,

Appellant,

and

THE MINISTER OF NATIONAL REVENUE,

Respondent.

Appeal heard on May 10, 2019, at Regina, Saskatchewan

Before: The Honourable Justice Susan Wong

Appearances:

Agent for the Appellant:	Adam Sperling
Counsel for the Respondent:	Anne Jinnouchi
	Nicole Sample (student-at-law)

JUDGMENT

The appeal pursuant to subsection 103(1) of the *Employment Insurance Act* is allowed and the Minister of National Revenue's April 19, 2018 decision is vacated, on the basis that John Zaremba was not engaged in insurable employment with the Appellant during the period from January 1, 2017 to October 23, 2017.

Signed at Edmonton, Alberta, this 31st day of October 2019.

"Susan Wong"

Wong J.

Citation: 2019 TCC 247
Date: 20191031
Docket: 2018-1659(EI)

BETWEEN:

SLOW PUB LTD.,

Appellant,

and

THE MINISTER OF NATIONAL REVENUE,

Respondent.

REASONS FOR JUDGMENT

Wong J.

Introduction

[1] The Appellant Slow Pub Ltd. appeals the April 19, 2018 decision of the Minister of National Revenue (the "Minister") in which she confirmed a ruling that John Zaremba was an employee of the Appellant and engaged in insurable employment within the meaning of paragraph 5(1)(a) of the *Employment Insurance Act* during the period from January 1 to October 23, 2017 (the "Period").

[2] The following witnesses testified on behalf of the Appellant: Adam Sperling (President of the Appellant), Meagan O'Flanagan (VP Marketing for Cansoft Technologies), and Kazi Mamun (CEO of Cansoft Technologies). The Respondent did not call any witnesses and Mr. Zaremba did not intervene in this appeal.

Issue

[3] The issue is whether Mr. Zaremba was engaged in insurable employment with the Appellant during the Period. The Appellant says that during the Period, Mr. Zaremba was an owner as well as Mr. Sperling's business partner and therefore, not its employee.

Test

[4] In *671122 Ontario Ltd. v. Sagaz Industries Canada Inc.*, 2001 SCC 59, [2001] 2 SCR 983, at paras. 46 and 47, the Supreme Court of Canada stated that there is no universal test to determine whether a person is an employee versus an independent contractor and that the "central question is whether the person who has been engaged to perform the services is performing them in business on his own account." The Court then referred to the non-exhaustive list of factors to be considered:

> [47] … In making this determination, the level of control the employer has over the worker's activities will always be a factor. However, other factors to consider include whether the worker provides his or her own equipment, whether the worker hires his or her own helpers, the degree of financial risk taken by the worker, the degree of responsibility for investment and management held by the worker, and the worker's opportunity for profit in the performance of his or her tasks.

[5] In *1392644 Ontario Inc. o/a Connor Homes v. The Minister of National Revenue*, 2013 FCA 85, [2013] FCJ No. 327, at paras. 38 to 42, the Federal Court of Appeal considered the weight to be given to the parties' intention in determining whether a worker is an employee (contract of service) or an independent contractor (contract for services). The Court concluded that the inquiry is a two-step process, i.e. first, ascertain the subjective intent of the parties and second, determine whether an objective reality supports their subjective intent. The Court also stated that the central question remains as set out above in *Sagaz*.

[6] The parties' subjective intent is not determinative of their relationship and their intent must be consistent with the objective reality, i.e. what the parties say (or believe) their relationship to be only matters if the facts support what they say (or believe). In this regard, the Federal Court of Appeal in *Connor Homes* stated that:

> [37] … [T]he determination of whether a particular relationship is one of employee or of independent contractor cannot simply be left to be decided at the sole subjective discretion of the parties. Consequently, the legal status of independent contractor or of employee is not determined solely on the basis of the parties'[sp] declaration as to their intent. That determination must also be grounded in a verifiable objective reality.

[7] In the present appeal, the question is only whether Mr. Zaremba was an employee and not whether he was an independent contractor. The same test applies except that the court need not reach a conclusion about independent contractor status.

A. Intention

[8] The Appellant was incorporated under the name "Slow Pub Ltd." on March 23, 2011 and changed its name to "Sperling Silver Distilleries Ltd." on April 26, 2018 [Exhibit A-4, Saskatchewan Corporate Registry Profile Report]. The Appellant's directors and majority shareholders are Mr. Sperling and Alla Sidorenko, who also hold the only voting shares.

[9] The Appellant initially operated as a brew pub and sports bar, and added a distillery operation in 2012.

[10] Mr. Sperling testified that he met Mr. Zaremba in about 2002 because Mr. Zaremba's wife worked for Mr. Sperling. Mr. Sperling stated that he began working with Mr. Zaremba in about 2010, when Mr. Zaremba lost his crepe business and asked Mr. Sperling for help. Mr. Sperling stated that he loaned some money to Mr. Zaremba and gave him a job as a wine person in a local restaurant.

[11] Mr. Sperling testified that when the Appellant commenced operations in 2011, he asked Mr. Zaremba to work for the Appellant as a brewmaster and general manager. Mr. Zaremba did so, beginning in April 2011 [Reply to the Notice of Appeal, paragraph 7(g)].

[12] Mr. Zaremba entered into written employment agreements with the Appellant on April 1, 2011 and October 10, 2015 [Reply to the Notice of Appeal, paragraph 7(i)]. The October 2015 employment agreement [Exhibit R-1] provided for the following, among other things:

a) Mr. Zaremba's position was "Brewmaster, Distiller/General Manager" [paragraph 1A of the agreement];

b) Mr. Zaremba was expected to work at least 50 hours per week and to be on duty for statutory holidays [paragraph 2B of the agreement];

c) the Appellant would pay Mr. Zaremba an annual salary of $60,000 plus profit-sharing of 1.5% of annual net profits excluding unsold inventory [paragraph 4A of the agreement];

d) 21 days of paid vacation per year [paragraph 15B of the agreement]; and

e) there was no specified term of employment [paragraph 3 of the agreement].

[13] The October 2015 employment agreement also had a section entitled "Exclusivity and Non-Competition" which provided for the following, among other things:

a) Mr. Zaremba would provide his services exclusively to the Appellant and would not provide those services to anyone else engaged in a similar business [paragraph 7A of the agreement];

b) Mr. Zaremba would not have business commitments or obligations in direct competition with the Appellant's operations, prior to or after signing the employment agreement [paragraph 7C of the agreement]; and

c) this section would remain in effect for two years after the termination of Mr. Zaremba's employment for any reason [paragraph 9 of the agreement].

[14] Mr. Sperling stated that in 2016, the Appellant's business operations began to grow so he offered Mr. Zaremba an opportunity to buy shares in the Appellant. Mr. Sperling stated that becoming a shareholder would give Mr. Zaremba the chance to be a business partner, be paid in dividends rather than salary, and to have his income grow as the Appellant became more successful. Mr. Sperling also testified that Mr. Zaremba had the option of receiving independent legal and accounting advice prior to purchasing the shares, and that he chose to use the Appellant's lawyer and accountant instead.

[15] On April 30, 2016, Mr. Zaremba entered into a written share purchase agreement with the Appellant [Exhibit A-3] which provided for the following, among other things:

a) Mr. Zaremba would purchase 250 Class "C" (non-voting) shares for $83,332.50 [paragraphs 1 and 2 of the agreement];

b) the purchase price consisted of a cash payment in the amount of $50,000 plus an equity allotment of $33,332.50. The equity allotment represented compensation by the Appellant to Mr. Zaremba for past services [paragraph 4 of the agreement]; and

c) Mr. Zaremba would purchase one-third of the 250 shares each year over the three-year period from 2017 to 2019. The cash payment and equity allotment would be applied in equal thirds across the same three-year period [paragraph 4 of the agreement].

[16] Mr. Sperling stated that Mr. Zaremba did not have enough cash to purchase the shares so the Appellant financed his purchase and Mr. Zaremba was expected to reimburse the Appellant. Despite that the share purchase agreement provided for Mr. Zaremba to purchase the 250 shares over three years, the Appellant issued an April 30, 2016 share certificate to him for the entire allotment [Exhibit A-4]. A Saskatchewan Corporate Registry Profile Report dated January 13, 2017 [Exhibit A-4] shows that Mr. Zaremba held his full allotment of 250 non-voting shares in the Appellant.

[17] Mr. Sperling testified that the change in the relationship from employee to business partner was done by verbal agreement. He stated that Mr. Zaremba then began to receive dividends instead of salary. Copies of Mr. Zaremba's paystubs for the period from March 1, 2017 to October 31, 2017 [Exhibit A-2] show the following things:

a) year-to-date totals as of March 1, 2017 being:

    i. source deductions in the amounts of $233.06, $81.50, and $1,000.18 for CPP, EI, and income tax, respectively;

    ii. vacation pay in the amount of $283.02;

    iii. $583.34 in bonuses;

b) from March to October, the above year-to-date totals did not change;

c) from March to October, he received $2,500 gross twice a month and these amounts were recorded as dividends. Mr. Sperling testified that these dividend payments were based on Mr. Zaremba holding all 250 shares even though they were not fully paid for. Mr. Sperling also stated that he himself received the same amount in dividends twice a month;

d) from March to October, no amounts were paid to him and recorded as salary;

e) from April to September, $1,500 was deducted from his paycheque once a month and recorded as a loan payment;

f) from April to October, interest ranging from $242.50 to $300.00 was deducted from his paycheque once a month;

g) from March to October, $50 was deducted from his paycheque and recorded as group insurance; and

h) with respect to the final pay period, the dividend and loan amounts were prorated to reflect his resignation on October 23rd.

[18] Mr. Sperling testified that with the share purchase, they verbally agreed that Mr. Zaremba's status would change from employee to business partner. Mr. Sperling also stated that another individual was then hired to replace Mr. Zaremba as manager. Mr. Sperling stated that the new arrangements were intended to free Mr. Zaremba's time in order to promote the Appellant's products.

[19] In contrast to Mr. Sperling's testimony, he signed three documents during or after the Period which confirmed, accepted, or stated that Mr. Zaremba was the Appellant's employee. They were as follows:

a) a January 12, 2017 letter in which he confirms that Mr. Zaremba commenced employment on April 1, 2011, his base annual salary was $60,000, and his current position was general manager/distiller [Exhibit R-2]. In cross-examination, Mr. Sperling stated that this letter was prepared by Mr. Zaremba for the purpose of borrowing money to finance his share purchase;

b) Mr. Zaremba's undated resignation letter in which he advises that he is resigning from his position as sales representative effective October 23, 2017 [Exhibit R-3]. In cross-examination, Mr. Sperling stated that he signed this letter to acknowledge Mr. Zaremba's resignation and not his employment status; and

c) an undated Resignation and Mutual Release which refers to Mr. Zaremba's October 23, 2017 resignation, the employment contract, and states that Mr. Zaremba agrees not to compete against the Appellant in Saskatchewan for one year [Exhibit R-4]. In cross-examination, Mr. Sperling testified that the agreement was necessary because Mr. Zaremba had corporate knowledge about the Appellant.

[20] Mr. Sperling testified that at the time of Mr. Zaremba's departure, the Appellant agreed to purchase his shares for $6,000 less $4,600 already paid by Mr. Sperling, for a net payment of $1,400 [Exhibit A-1].

Analysis of intention

[21] Credibility is crucial when the evidence is conflicting. This Court did not have an opportunity to evaluate Mr. Zaremba's credibility because he did not intervene and was not called as a witness by the Respondent.

[22] I found Mr. Sperling to be a credible witness. However, his oral testimony about the parties' intentions was clouded by the parties' actions, including the creation and signing of Exhibits R-2 to R-4 described above.

[23] I also find that the Appellant and Mr. Zaremba conflated the concepts of owner, shareholder, and employee such that it is impossible for this Court to find clear evidence of their subjective intent.

[24] For example, the Resignation and Mutual Release [Exhibit R-4] referred to the employment agreement for authority but imposed a one-year non-competition covenant which was not from the employment agreement.

[25] As another example, the February 13, 2018 letter from the Appellant to the Minister [Exhibit R-5] refers to Mr. Zaremba in several different capacities and seems to imply that a shareholder cannot be an employee, which is not correct. In fact, paragraph 5(2)(b) of the *Employment Insurance Act* excludes employment from insurability only if an employee controls more than 40 percent of the voting shares of the corporate employer. In the present case, Mr. Zaremba held no voting shares in the Appellant so he is not precluded from being an employee.

[26] On the other hand, Mr. Zaremba's remuneration changed from salary to dividends after becoming a shareholder and the Appellant hired someone to replace him as manager. Mr. Zaremba also received advice from the Appellant's accountant and lawyer before entering into the share purchase agreement. Therefore, he understood or should have understood that there was an impending change in his relationship with the Appellant. However, when he prepared the January 12, 2017 letter [Exhibit R-2] to secure financing, he described his relationship with the Appellant as one of continuous employment since April 2011.

[27] It is sufficiently clear from the available evidence that the Appellant and Mr. Zaremba either did not share a common intention or they did not have the same intention at the same time.

B. <u>Objective reality of the parties' conduct</u>

[28] To answer the central question of whether Mr. Zaremba was an employee, I now turn to the second step of the two-part inquiry, i.e. a determination of the objective reality of the parties' conduct based on the relevant factors referred to in *Sagaz*.

Control

[29] In *Wolf v. The Queen*, 2002 FCA 96, 2002 DTC 6853 at para. 74, the Federal Court of Appeal said that:

> [74] The control test, as it is commonly referred to, purports to examine who controls the work and how, when and where it is to be done. In theory, if the worker has complete control over the performance of his work once it has been assigned to him, this factor might qualify the worker as an independent contractor. On the other hand, if the employer controls in fact the performance of the work or has the power of controlling the way the employee performs his duties (*Gallant v. Canada (Department of National Revenue*) (F.C.A.), [1986] F.C.J. No. 330 (Q.L.), the worker will be considered an employee.

[30] At paragraph 75 of *Wolf*, the Court noted that in the case of skilled workers such as pilots and doctors, the control test can be inadequate because little supervision or control can be exercised over the way in which the work is done.

[31] Mr. Zaremba's roles as distiller, brewmaster, and sales representative are skilled services which likely did not require much regular or direct supervision. Based on Mr. Zaremba's resignation letter [Exhibit R-3] and Mr. Sperling's testimony, it appears that during the Period, Mr. Zaremba worked primarily in sales, i.e. promoting the Appellant's products.

[32] I accept Mr. Sperling's testimony that Mr. Zaremba made his own schedule. I do not believe that the Appellant had the power to control the way he performed his duties and simply refrained from using that power.

[33] For example, Ms. O'Flanagan testified that in the summer of 2017, she sold advertising for a local magazine and contacted Mr. Sperling in that regard. She stated that he referred her to Mr. Zaremba, and that she understood him to be Mr. Sperling's business partner. She stated that she and Mr. Sperling each attempted to set up a meeting with Mr. Zaremba, but he did not show up at either meeting. She testified that she ultimately sold the advertising to the Appellant without involving him.

[34] As another example, Mr. Mamun testified that he met with Mr. Sperling three or four times to discuss digital marketing. He recalled that during their first meeting to discuss the Appellant's website, they were unable to reach a conclusion because Mr. Sperling had a business partner who was absent from the meeting. In cross-examination, Mr. Mamun stated that he understood that Mr. Sperling needed to discuss things with Mr. Zaremba before making a decision. He also stated that he ultimately never met Mr. Zaremba and dealt only with Mr. Sperling.

[35] While what Mr. Sperling said to Ms. O'Flanagan and Mr. Mamun is hearsay, their respective understanding of what they heard is not. They both understood from their respective conversations that Mr. Sperling had a business partner and they both experienced a delay in concluding their business dealings with the Appellant because Mr. Sperling's business partner was either absent or unreachable.

[36] These circumstances do not suggest the actions of a skilled employee who requires minimal supervision. Rather, they suggest the actions of an individual who does not fear reprisal, termination, or other consequences as a result of missing business meetings.

[37] Therefore, control was not exercised or exercisable over Mr. Zaremba and this factor favors a finding that he was not an employee during the Period.

Who provided the equipment?

[38] The Appellant did not challenge the Minister's assumptions in the Reply to the Notice of Appeal with respect to equipment [subparagraphs 7(ss) and (tt) of the Reply]. To carry out his functions as brewmaster, distiller, and sales representative, the Appellant provided distilling equipment such as hydrometers, mash tuns, stills, and fermenters as well as office equipment and supplies such as computers, fax, and printers.

[39] I would expect Mr. Zaremba to use the Appellant's equipment regardless of whether he was an employee or a business partner. Therefore, I find this factor to be neutral.

Opportunity for profit/Degree of financial risk taken

[40] In cross-examination, Mr. Sperling testified that the annual fixed dividend of $60,000 (i.e. $2,500 twice a month) represented dividends on Mr. Zaremba's

allotment of 250 shares, even though Mr. Zaremba had not paid for them in full yet. In the same cross-examination, he stated that the amount of the dividend was not based on a particular calculation nor was it connected to the number of shares owned.

[41] The payments of $2,500 to Mr. Zaremba were recorded as dividends by the Appellant and this characterization was accepted by Mr. Zaremba, either because he acknowledged the change in their relationship or because he simply wished to receive a larger cheque without source deductions taken. However, there was no opportunity for this Court to hear his explanation and assess his credibility in this regard.

[42] Based on the share purchase, there would be an opportunity for profit. In cross-examination, Mr. Sperling stated that Mr. Zaremba was assuming the Appellant's risk and could potentially receive less in dividends in the future. However, his statement was purely speculative at this point and in fact, the fixed dividend insulated Mr. Zaremba from economic fluctuations and lowered his degree of financial risk.

[43] Counsel for the Respondent submitted that the Appellant's retained earnings were negative during the Period [subparagraph 7(hhh) of the Reply] and it would have been irresponsible for the Appellant to pay dividends in these circumstances.

[44] A corporation's decision to pay dividends is not based solely on its retained earnings. Section 113 of *The Companies Act*, RSS 1978, c. C-23 says that:

> **113**. The directors shall not declare or pay a dividend when the company is insolvent, or a dividend, the payment of which renders the company insolvent or diminishes its capital.

[45] There was no evidence to suggest that the circumstances set out in section 113 existed during the Period and therefore, no basis to conclude that the Appellant could not pay the dividend in question.

[46] Based on the opportunity for profit but the limited financial risk, I find this factor to be neutral.

Conclusion

[47] I have weighed the relevant factors and conclude that Mr. Zaremba was not an employee during the Period. I would have difficulty finding what he in fact was, without more direct evidence in that regard. As stated earlier, I am of the view that the parties conflated the concepts of owner, shareholder, and employee and at different times, each party relied on whichever concept best suited their needs at that point.

[48] The Minister of National Revenue's April 19, 2018 decision is vacated, on the basis that Mr. Zaremba was not engaged in insurable employment during the Period.

Signed at Edmonton, Alberta, this 31st day of October 2019.

"Susan Wong"

Wong J.

CITATION:	2019 TCC 247
COURT FILE NO.:	2018-1659(EI)
STYLE OF CAUSE:	SLOW PUB LTD. and M.N.R.
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