Citation: 2006TCC417
Date: 20061122
Docket: 2004-2146(IT)G

BETWEEN:

JEAN DESMARAIS,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

REASONS FOR JUDGMENT

(Delivered orally from the bench on June 15, 2006
at Montréal, Quebec, and modified for more clarity and precision.)

Archambault J.

[1] The issue in the appeal by Jean Desmarais concerns the qualification of the sum of $350,000 that was paid to him under an employment contract that he entered into on October 29, 2001, with Valeurs mobilières Desjardins (**VMD**). Clause 4.6 of this contract stipulates:

> [TRANSLATION]
>
> 4.6 As well as the above-mentioned commissions, the employer will pay the employee with regard to the clients already represented by the employee (transfer) the lump sum of $350,000 at the pay of November 15, 2001;
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> (Exhibit I-1, tab 13.)

[2] The Minister of National Revenue (the **Minister**) applied section(s) 5 and/or 6 of the *Income Tax Act* (the **Act**) to justify the assessment. It seems that when the assessment was made, the auditor assumed that the $350,000 was a commission for the clients that Mr. Desmarais brought to VMD. At the objection stage, the objections

officer rather considered this sum to be taxable under paragraph 6(3)(*c*) of the Act. Subsection 6(3) provides as follows:

> **6(3) Payments by employer to employee** -- An amount received by one person from another
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> (*a*) during a period while the payee was an officer of, or in the employment of, the payer, or;
>
> (*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.
>
> [Emphasis added.]

[3] I tend to agree with counsel for Mr. Desmarais that it was a new basis for the assessment and that the Minister had the burden of proof as to the facts supporting this new argument. However, the factual evidence that has been offered is more than sufficient to make a decision on whether to apply paragraph 6(3)(*c*)[1] of the Act.

[4] Subsection 6(3) applies if the sum of $350,000 was paid due to an obligation arising from an agreement between VMD and Mr. Desmarais immediately before, during or immediately after Mr. Desmarais was a salaried employee of VMD. The evidence clearly demonstrated that the payment was made during the period when Mr. Desmarais was a salaried employee of VMD and the obligation was created by

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[1] It would have been more conform with the rules of procedural fairness if this reversal of the burden of proof had been mentioned at the commencement of the appeal hearing, rather than in the submissions.

the employment contract itself. The first two conditions of subsection 6(3) have therefore been met.

[5] It now remains to be decided whether the other conditions have also been met. The sum in question is deemed to be remuneration for services that the payee provided as an officer, unless it is established that, regardless of the date when the agreement was entered into or the legal form or effects of this agreement, it is not reasonable to consider this sum as having been received specifically as consideration for accepting the office or entering into the employment contract.

[6] In my opinion, it is reasonable to consider that the $350,000 was paid to Mr. Desmarais as an incentive to sign the employment contract. The reasons justifying this conclusion are largely the same as those used by counsel for the Respondent. First of all, the $350,000 did not represent the proceeds of the sale of goodwill, contrary to what counsel for Mr. Desmarais submitted, with much conviction, to justify his argument that the sum could be attributable to something other than accepting the office.

[7] The events surrounding the negotiation and the performance of the employment contract include several peculiar aspects. The first of them is the rather vague wording of clause 4.6 of the contract: [TRANSLATION] ". . . *the employer shall pay the employee having regard to clients already represented by the employee (transfer).*" After signing this contract, Mr. Desmarais attempted, unsuccessfully, to have VMD specify the extent of the offer that it made him on October 4, 2001. He wanted VMD to recognize that "*the payment of the lump sum amount represents payment for the part of my clientele that it is possible for me to transfer on the date hereof.*" (Exhibit I-1, tab 17). VMD's refusal reveals, in my opinion, the absence of any intention on its part to acquire Mr. Desmarais's client list. On the contrary, it reveals an intention to pay an incentive. Not only did VMD refuse to agree to Mr. Desmarais's request for specification, it acted as an employer that had paid an employment income. Indeed, it prepared a T4 slip on which the $350,000 was described as a commission. It is true that this description is not the one that best reflects the true nature of this sum, but what is the most important, in my opinion, is the fact that VMD did not consider the sum of $350,000 as the purchase price of goodwill.

[8] In addition to these factors, which raise a serious doubt as to the existence of a purchase price for the purchase of goodwill, there is the fact that the employment contract mentions the payment of $350,000 under the heading "Remuneration". This is another indication of the true nature of the $350,000 paid by VMD. If there had

truly been an acquisition of goodwill, normally a separate contract should have been prepared, either a purchase contract or a sales contract, or, at the very least the acquisition should have been dealt with under a separate heading in the employment contract.

[9] There are other factors that support me in my conclusion that the true intention of VMD was not to acquire goodwill. For example, there is no clause in the employment contract that protects VMD against the solicitation of the clients addressed concerned in clause 4.6, i.e. the "clients already represented by the employee" in the case of the departure of Mr. Desmarais. However there is such a clause exists in article 13 of the employment contract with regard to the clients that the institutions of the Mouvement Desjardins could refer to Mr. Desmarais.

[10] I believe that VMD could not really hope to acquire Mr. Desmarais's goodwill because it is recognized in the field that there is a close relationship of trust between an investment advisor and his or her clients, especially if he or she has given them advice over several years. In addition, it would be difficult to prevent a salaried employee from earning a living after leaving the employer and serving the clients who wished to use his or her services. In any case, clients are free to choose their advisor. The retention rate for Mr. Desmarais's clients would not be high if Mr. Desmarais were to leave. The interest for VMD lies in the retention rate of the employee that it hires. Indeed, article 5 of the employment contract provides for total reimbursement of the $350,000 if Mr. Desmarais leaves his employment during his first year of service. Thereafter, the reimbursement is reduced gradually if Mr. Desmarais leaves his employment with VMD over the following four years. If VMD's true intention in paying the $350,000 had been to purchase a goodwill, the clause would only have provided for reimbursement inasmuch as VMD would have lost the clients as a result of Mr. Desmarais's departure.

[11] My analysis of all of the evidence leads me to find that the $350,000 was paid as an incentive for Mr. Desmarais to leave Nesbitt Burns to join VMD and not to acquire Mr. Desmarais's clientele.

[12] It is true that Mr. Desmarais, by going to VMD and accepting the position of branch manager, ceased to be involved with his clients on a daily basis. His role was limited to supervising the many investment advisors joining his team. However, it cannot be said that Mr. Desmarais lost all monetary interest in bringing his clientele with him. On the contrary, during the negotiation of his employment contract with VMD, he made sure that a colleague from Nesbitt Burns, Mr. Bernier, in whom he had great confidence, would join VMD at the same time as him. In fact, it is rather to

Mr. Bernier – and not to VMD – that Mr. Desmarais transferred his clientele, since Mr. Bernier inherited all of the clients who accepted to follow Mr. Desmarais to VMD. In financial compensation for this transfer of clientele, Mr. Bernier paid Mr. Desmarais part of the commissions he received from these clients. This is how Mr. Desmarais described his arrangement with Mr. Bernier: [TRANSLATION] "*Martin Guy Bernier, who is purchasing my clientele, gives me a share of his commissions to purchase my clientele.*"[2] Mr. Bernier even described these payments as dues. This is just another way of paying for the acquisition of a clientele. It is important to add that Mr. Desmarais did not have any other similar agreement with the 23 other investment advisors working on his team.

[13] For these reasons, Mr. Desmarais's appeal is dismissed, with costs to the Respondent.

Signed at Ottawa, Canada, this 22nd day of November 2006.

"Pierre Archambault"

Archambault J.

Translation certified true
on this 24th day of January 2008.

François Brunet, Revisor

[2] Page 42 of the transcript of the examination for discovery, at line 15.

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