Docket: 2007-561(GST)G

BETWEEN:

SERGE TRAJKOVICH,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on May 1 and 2, 2008, at Toronto, Ontario

Before: The Honourable Justice L.M. Little

Appearances:

Counsel for the Appellant:	David B. Hamilton
Counsel for the Respondent:	Suzanne M. Bruce

JUDGMENT

The appeal from the assessment made under the *Excise Tax Act*, notice of which is dated October 14, 2005 and bears number A106415 for the period from December 1, 2001 to August 7, 2002 is allowed, with costs, in accordance with the attached Reasons for Judgment.

Signed at Vancouver, British Columbia, this 11th day of July, 2008.

"L.M. Little"

Little J.

Citation: 2008 TCC 402
Date: 20080711
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BETWEEN:

SERGE TRAJKOVICH,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Little J.

A. Facts

[1] A company by the name of 4225317 Manitoba Limited was incorporated under the laws of the province of Manitoba on June 19, 2000.

[2] The Corporation carried on business as Image Colour 2000.

[3] The Corporation was involved in the commercial printing industry, primarily printing promotional materials and the manufacturing of plates and films for use by printers. The Corporation became part of the Imaginex Group of Companies.

[4] On or about June 19, 2000 the Appellant, Marvin Kass and Emilio Mazzona were elected Directors of the Corporation.

[5] On or about July 5, 2001 Marvin Kass ceased to be a Director of the Corporation.

[6] On or about November 1, 2001 Emilio Mazzona ceased to be a Director of the Corporation.

[7] On or about May 10, 2002, the Appellant, being the sole shareholder of the Corporation, elected himself to be the sole director of the Corporation for the ensuing year.

[8] The parties agree that at all relevant times the Appellant was a director of the Corporation.

[9] The Corporation was a registrant for Goods and Services Tax ("GST") under the *Excise Tax Act* (the "*Act*").

[10] The Minister of National Revenue (the "Minister") maintains that the Corporation failed to remit to the Receiver General GST in the amount of $51,313.41 for the period December 1, 2001 to August 7, 2002.

[11] On or about August 7, 2002 the Ontario Superior Court of Justice ordered that the Corporation be placed in receivership.

[12] On or about December 20, 2002 the Receiver filed for bankruptcy on behalf of the Corporation.

[13] On or about September 7, 2004 the Minister filed with the Receiver an amended proof of claim as an unsecured creditor in the amount of $51,313.41.

[14] On October 14, 2005 the Minister issued a Notice of Assessment against the Appellant for GST in the amount of $51,313.41. The GST in issue represents the unremitted GST owing by the Corporation for the specified periods:

Reporting Period	**Net GST**	**Interest**	**Penalty**	**Total**
Dec. 1, 2001 to Feb. 28, 2002	$19,219.58	$316.59	$794.88	$20,331.05
Mar. 1, 2002 to May 31, 2002	$21,521.19	$244.75	$616.91	$22,382.85
June 1, 2002 to Aug. 7, 2002	$8,441.08	$45.00	$113.43	$8,599.51
Total	$49,181.85	$606.34	$1,525.22	$51,313.41

B. Issue

[15] The issue is whether the Appellant is liable under subsection 323(1) of the *Act* for the failure of the Corporation to remit GST in the amount of $51,313.41.

C. Analysis and Decision

[16] Section 323 of the *Excise Tax Act* reads as follows:

> **323.** (1) **Liability of directors -** Where a corporation fails to remit an amount of net tax as required under subsection 228(2) or (2.3), the directors of the corporation at the time the corporation was required to remit the amount are jointly and severally liable, together with the corporation, to pay that amount and any interest thereon or penalties relating thereto.
>
> (2) **Limitations** - A director of a corporation is not liable under subsection (1) unless
>
> > (a) a certificate for the amount of the corporation's liability referred to in that subsection has been registered in the Federal Court under section 316 and execution for that amount has been returned unsatisfied in whole or in part;
> >
> > (b) the corporation has commenced liquidation or dissolution proceedings or has been dissolved and a claim for the amount of the corporation's liability referred to in subsection (1) has been proved within six months after the earlier of the date of commencement of the proceedings and the date of dissolution; or
> >
> > (c) the corporation has made an assignment or a bankruptcy order has been made against it under the *Bankruptcy and Insolvency Act* and a claim for the amount of the corporation's liability referred to in subsection (1) has been proved within six months after the date of the assignment or bankruptcy order.
>
> (3) **Diligence -** A director of a corporation is not liable for a failure under subsection (1) where the director exercised the degree of care, diligence and skill to prevent the failure that a reasonably prudent person would have exercised in comparable circumstances.
>
> (4) **Assessment -** The Minister may assess any person for any amount payable by the person under this section and, where the Minister sends a notice of assessment, sections 296 to 311 apply, with such modifications as the circumstances require.
>
> (5) **Time Limit -** An assessment under subsection (4) of any amount payable by a person who is a director of a corporation shall not be made more than two years after the person last ceased to be a director of the corporation.

> (6) **Amount recoverable -** Where execution referred to in paragraph (2)(*a*) has issued, the amount recoverable from a director is the amount remaining unsatisfied after execution.
>
> (7) **Preference -** Where a director of a corporation pays an amount in respect of a corporation's liability referred to in subsection (1) that is proved in liquidation, dissolution or bankruptcy proceedings, the director is entitled to any preference that Her Majesty in right of Canada would have been entitled to had the amount not been so paid and, where a certificate that relates to the amount has been registered, the director is entitled to an assignment of the certificate to the extent of the director's payment, which assignment the Minister is empowered to make.
>
> (8) **Contribution -** A director who satisfies a claim under this section is entitled to contribution from the other directors who were liable for the claim.

[17] Counsel for the Appellant agreed that the Appellant was a director of the Corporation at the relevant time. However, Counsel for the Appellant maintains that the Appellant was effectively removed from the normal operations of a director.

[18] In support of his position Counsel for the Appellant maintains that as a result of a refinancing of the Imaginex Group of Companies, the Appellant was stripped of any ability to control the financial affairs of the Corporation.

[19] The argument of Counsel for the Appellant may be summarized as follows:

(1) After the refinancing carried out by the Laurentian Bank of Canada, RoyNat and the Business Development Bank of Canada ("BDC") the Appellant had no authority to force or compel the Corporation to pay GST.

(2) The Appellant was a Director of the Corporation in name only. RoyNat and BDC had appointed Richard Parkinson, Chartered Accountant, as the Chief Financial Officer. All decisions as to which accounts payable by the Corporation should be paid were made by RoyNat, BDC and Mr. Parkinson.

(Note: An examination of the Agreement prepared by the Laurentian Bank of Canada (see Exhibit A-1, Tab 3) and the agreement prepared by RoyNat Capital (see Exhibit A-1, Tab 5, pages 3 and 4) contain severe restrictions on what the Corporation and its management could do in the future.)

(3) By letter dated January 7, 2002, Laurentian Bank of Canada indicated that it was providing a new term loan of $40,000 to cover the Bank's solicitor's expenses and monitor expenses (Mr. Bob Cumming) (see Exhibit A-1, Tab 6). (Note – Richard Parkinson signed this letter as the CFO of Imaginex Incorporated.)

(4) On February 14, 2002, Richard Parkinson specifically instructed the Appellant not to involve himself in the financial affairs of the Imaginex Group of Companies. Mr Parkinson prepared a Notice which reads as follows:

> "I PROMISE TO BUGGER OUT OF FINANCE"
>
> Signed "S. Trajkovich"
>
> Date February 14, 2002
>
> (see Exhibit A-1, Tab 7)

The evidence was that this Notice was signed by the Appellant and placed by Mr. Parkinson on his wall behind his chair.

(5) The Appellant did not have the authority to issue a cheque on behalf of the Corporation on the basis of his signature alone.

(6) All cheques issued to pay the liabilities of the Corporation were issued by Richard Parkinson, the CFO, and/or Gary Hill, a Chartered Accountant employed by the Corporation.

(7) The new equity parties, RoyNat, BDC and Richard Parkinson controlled approximately 65% of the voting shares of the Corporation.

(8) The Appellant was demoted to a sales function. The Appellant's job description was "Direct Sales, Mississauga and Indirect Sales, Toronto and Winnipeg".

(9) The control of payables was outside the authority or control of the Appellant. In support of his position that the Appellant was not involved or responsible for the payables, Counsel for the Appellant referred to an e-mail from Gary Hill, Chartered Accountant in Toronto, to Marilyn McClay in Winnipeg dated May 17, 2002. The e-mail from Mr. Hill reads as follows:

> Subject: Re: GST

> GST – That will do.
>
> That is, A) Currently – we to cover Vision's chq for 6,500 released but hold back on any further payments by Image Color.
>
> B) Plan – unless cash position improves, pls. hold off on making further payments for GST until at least mid-August.
>
> - please file GST returns by their due dates, but note on your returns that we will catch up on delayed …
>
> (underlining added)

(10) Note - This instruction from Gary Hill not to pay GST for the Corporation was not conveyed to the Appellant until July 5, 2002 when he received an e-mail from Marilyn (see Exhibit A-1, Tab 25).

(11) Counsel for the Appellant stated in his argument that the Appellant was "ostracized" from the management of the Corporation.

[20] In support of his position that the Appellant was excluded from the management of the Corporation and should not be responsible for the GST liability of the Corporation, Counsel for the Appellant referred to the following Court decisions:

Mosier v. The Queen, [2001] G.S.T.C. 124;
DiLorenzo v. The Queen, [2001] G.S.T.C. 67; and
Worrell v. The Queen, 98 DTC 1783.

[21] In *Worrell v. The Queen*, my colleague Justice McArthur was considering the liability of the taxpayer under section 323 of the *Excise Tax Act*. Justice McArthur said at paragraph [10]:

> [10] The primary submission was that the Appellants, as directors of Abel, did not have the freedom of choice to govern the corporation and prevent the failures to remit. Second, the bulk of the GST owing by Abel for which the Minister of National Revenue (the "Minister") is holding the directors liable was never collected by Abel, never came under the dominion of the directors and never was impressed with a trust. The Appellants submit that it is inappropriate that they be held vicariously liable for these amounts.

[22] Justice McArthur said at paragraphs [16], [17] and [22]:

> [16] The facts support the finding that from October 18, 1993 until the bankruptcy on April 28, 1994, it was the bank, and not the directors, that controlled the finances of Abel. This restriction on the directors' freedom of choice is sufficient to relieve the Appellants of personal liability for both the payroll assessment and the GST assessment. The Appellants did not have the freedom of choice to govern the corporation and prevent the failures to remit, in respect of both the payroll assessments and GST assessments.
>
> [17] The Federal Court of Appeal has recently examined the nature of the due diligence defence in *Soper* (*supra*). A necessary pre-condition for imposition of personal liability is that the directors must have the necessary freedom of choice such that the corporation is freely acting through its board of directors. In *Champeval* (*supra*), under circumstances similar to those of the Appellants, Couture, C.J.T.C. found that where the failure of the corporation results from factors outside the control of the director, the director is relieved of personal liability. *McMartin* (*supra*) is another case where a bank dictated which cheques would be honoured and which would not. Bell, J. held in favour of the Appellant. (emphasis added)
>
> [22] The Appellants did not have the freedom of choice to prevent the failures to remit in respect to both the income tax and GST assessments.

[23] The Minister appealed the decision of the Tax Court in *Worrell* to the Federal Court of Appeal.

[24] The Federal Court of Appeal upheld the decision of Justice McArthur in a reported decision under the issue of *The Attorney General of Canada v. Lynda McKinnon, Ronald LaPointe and Brad Worrell*, 2000 DTC 6593.

[25] In the decision of the Federal Court of Appeal Justice Rothstein said:

> … I wish to emphasize that whether the due diligence defence will be successful is fact-driven in each case, i.e. always comparing what the directors did to prevent the failure with what a reasonably prudent person would have done in comparable circumstances. I agree with Evans J.A. that the due diligence defence is established on the facts of this case. …
>
> Evans J.A. had stated at paragraph 77 of his reasons (at page 6604):
>
> Given the limitations placed upon them by the bank's *de facto* control of the company's finances, I am satisfied that, on the facts of this case, the directors exercised the degree of care, diligence and skill to prevent failures to remit that would have been shown by a reasonably prudent person in comparable circumstances. …

(underlining added)

[26] Counsel for the Appellant also referred to the decision of Associate Chief Justice Bowman (as he then was) in *Mosier v. The Queen*. This case also dealt with a situation where a taxpayer was assessed for the tax liability of a corporation of which he was a director. Associate Chief Justice Bowman said:

> [32] One fact stands out like a sore thumb. The bank had the company's finances sewn up as tight as a drum. In addition to scooping as much of the cash as it wanted when it came into the cash room, it had an absolute power to veto the payment of any cheques that were issued. The appellant worked out with the CCRA a payment of $2,400 per week to clear up the arrears of tax. On one occasion he persuaded the bank to allow a somewhat larger cheque to the CCRA by threatening to walk away from the whole business. The bank wanted him around because if he succeeded in keeping the business afloat or, better still, if he bought the business - a prospect that was always in the wind but never came to fruition until TRS went bankrupt - the bank's chances of getting paid were enhanced. Apart from this small amount of leverage the appellant was powerless to ensure that CCRA would get paid. He had to perform a delicate balancing act with predators snapping at him from all sides - the bank, the suppliers, the other creditors, the union and the employees. If he failed the company would go under and everyone would have lost, including the CCRA and the 600 employees.
>
> [33] One has to ask: what could he have done that he did not do? The answer is absolutely nothing. The case is in some ways reminiscent of *Holmes v. R.*, [2000] 3 C.T.C. 2235, where the directors were unable to ensure that the CCRA be paid because the company's finances were completely controlled by their supplier.
>
> …
>
> I find as a fact that there is nothing that Mr. and Mrs. Holmes could reasonably have done to prevent the failure. They struck me as decent, honourable people who did all they could to ensure that the corporate obligations were fulfilled, but the economic circumstances rendered that impossible.
>
> [34] This approach is one that I have followed in other cases and one that is, I believe, consistent with the series of cases in the Federal Court of Appeal which have invariably modified the more stringent standards applied in this court. The cases in the Federal Court of Appeal to which I am referring are *The Queen v. Corsano et al.* (*supra*), *Worrell v. R.*, [2000] G.S.T.C. 91, *Smith v. The Queen*, 2001 D.T.C. 5226, *Cameron v. The Queen*, 2001 D.T.C. 5405, and *Soper v. The Queen*, 97 D.T.C. 5407.
>
> [35] I need not quote from them. They stand for the proposition that section 227.1 of the *Income Tax Act* and subsection 323(3) of the *Excise Tax Act* require only that

> directors act reasonably. They do not demand the impossible. I have no hesitation in following that approach.
>
> [39] For all the above reasons and notwithstanding Mr. Bornstein's usual thorough and skilful presentation of the Crown's case the appeal is allowed with costs and the assessment made under section 323 of the *Excise Tax Act* is vacated.

[27] Counsel for the Respondent suggested that the *Worrell* decision and the *Mosier* decision relied upon by the Appellant could be distinguished on the facts. In connection with "distinguishing the cases," I am reminded of the following comment made by Justice Evans in *The Attorney General of Canada v. McKinnon, LaPointe and Worrell* in 2000 DTC 6593. Justice Evans said at paragraphs 23 and 24:

> [23] In the absence of a developed analytical framework, cases are readily distinguishable on their facts, even when those facts, including the facts in the instant appeal, conform to a recurring general pattern. Inevitably, but without express advertence, some decisions exhibit a relatively strict approach to subsection 227.1(3), while others, including the decision under appeal here, adopt a view more favourable to the director.
>
> [24] Nonetheless, amid this wilderness of single instances some general guidance on section 227.1 is available, most notably from this Court in *Soper v. Canada*, [1998] 1 F.C. 124 (C.A.). First, writing for the majority in *Soper, supra*, Robertson J.A. (at paragraph 11) put subsection 227.1(3) into context by explaining its rationale: …

[28] I believe that Justice Rothstein and Justice Evans have correctly applied the test for the application of section 323 of the *Act* in their Reasons for Judgment in *McKinnon*, *LaPointe* and *Worrell.*

[29] Based on the evidence before me, I find as a fact that there is nothing that the Appellant could reasonably have done to prevent the failure of the Corporation paying the GST.

[30] I have also concluded that the Appellant carried out the necessary due diligence that a reasonable person would do in similar circumstances. He is therefore protected by the due diligence defence contained in section 323 of the *Act*.

[31] The appeal is allowed with costs.

Signed at Vancouver, British Colombia, this 11th day of July 2008.

"L.M. Little"

Little J.

CITATION:	2008 TCC 402
COURT FILE NO.:	2007-561(GST)G
STYLE OF CAUSE:	SERGE TRAJKOVICH AND HER MAJESTY THE QUEEN.
PLACE OF HEARING:	Toronto, Canada
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REASONS FOR JUDGMENT BY:	The Honourable Justice L.M. Little
DATE OF JUDGMENT:	July 11, 2008

APPEARANCES:

Counsel for the Appellant:	David B. Hamilton
Counsel for the Respondent:	Suzanne M. Bruce

COUNSEL OF RECORD:

For the Appellant:

Name:	David B. Hamilton
Firm:	David Bruce Hamilton, Toronto, Ontario

For the Respondent:	John H. Sims, Q.C. Deputy Attorney General of Canada Ottawa, Canada