

Docket: 2008-515(IT)G

BETWEEN:

KOMUTEL INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

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Appeal heard on June 5, 2009, at Quebec City, Quebec.

Before: The Honourable Justice Alain Tardif

Appearances:

Counsel for the Appellant: Jean-François Bertrand  
Counsel for the Respondent: Anne Poirier

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**JUGEMENT**

The appeal of the reassessment made under the *Income Tax Act* for the year ending March 31, 2005, is allowed, in accordance with the attached Reasons for Judgment, with costs to the appellant.

Signed at Ottawa, Canada, this 15th day of June 2010.

“Alain Tardif”

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Tardif J.

Translation certified true  
on this 10th day of November 2010.

Erich Klein, Revisor

Citation: 2010 TCC 284  
Date: 20100615  
Docket: 2008-515(IT)G

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### **REASONS FOR JUDGMENT**

Tardif J.

[1] This is an appeal of an assessment that was confirmed on November 15, 2007. The issues are as follows:

For the 2005 taxation year, did the Minister correctly add \$100,937 to the appellant's income as settlement of a commercial obligation, in accordance with subsection 80(13) of the Act?

For the 2006 taxation year, did the Minister correctly change the refundable investment tax credit to \$39,417 in accordance with subsection 127.1(1) of the Act?

[2] In making the assessment under appeal, the respondent relied on the following facts:

[TRANSLATION]

- a) The company Groupe Capital Vision Inc. ("Capital Vision") was incorporated on July 7, 2000, under Part IA of the Quebec *Companies Act*.
- b) Benoît Beaudin was the president, director and shareholder of Capital Vision.
- c) Capital Vision has never filed an income tax return.

- d) Richard Poulin was a shareholder of the company 9098-5854 Québec Inc. (“9098-5854”), incorporated on December 4, 2000, under Part IA of the *Quebec Companies Act*.
- e) According to the Enterprise Register, 9098-5854 specializes in software development.
- f) Richard Poulin had an assistive technology product for Web/Internet customer service and was looking for financial partners.
- g) Capital Vision was willing and had the capital to invest in technology.
- h) On April 4, 2001, Capital Vision, represented by its president, Benoît Beaudin, and Richard Poulin, an independent contractor, signed an agreement that included the following provisions:
- i) a contract of employment for Richard Poulin under the terms of the agreement;
  - ii) an undertaking from Capital Vision to create a business (and incorporate it under federal law for this purpose) with 51 per cent of the common voting shares to be held by Capital Vision and 49 per cent by Richard Poulin, and 49 per cent of non-voting preferred shares to be held by Capital Vision and 51 per cent by Richard Poulin;
  - iii) an investment of \$350,000 by Capital Vision, namely,
    - A \$200,000 initial investment in the business according to a timetable extending from April to September 2001;
    - \$100,000 paid to the company to be incorporated, in the form of advances reimbursable from profits; and
    - \$50,000 paid in cash to Richard Poulin, on terms to be established.
- i) On April 23, 2001, the company B2C Web Support Inc. (“B2C”) was incorporated federally under the *Canada Business Corporations Act*.
- j) B2C’s articles of incorporation provide for various classes of shares:

CLASS	
“A”	Voting and participating (subject to, among other things, pre-emptive rights attaching to the other classes of shares) and exchangeable for Class C shares under certain conditions.
“B”	Non-voting and non-participating.
“C”	Non-voting, entitling the holder to a preferred dividend on classes A, D and E, redeemable by the

	company at the holder's option under certain conditions, with the possibility of being bought over the counter by the company.
"D"	Voting and entitling the holder to a preferred dividend on classes A and E.
"E"	Non-voting and entitling the holder to a preferred dividend on Class A, but after classes C and D.

- k) B2C's articles of incorporation state that no shares of the capital stock may be transferred without the consent of the majority of the directors or the majority of the shareholders.
- l) The company's minutes book, the declaration of registration dated July 16, 2001, and the annual returns filed for 2002, 2003, 2004 and 2005 with the Enterprise Registrar show that Richard Poulin is the sole director and shareholder of B2C.
- m) According to Corporations Canada's information, Richard Poulin was also the sole director and shareholder of B2C.
- n) According to the computerized reports of the Canada Revenue Agency (CORTAX) for the taxation years ending March 31, 2002, 2003, 2004 and 2005, B2C's income tax returns indicated that Richard Poulin held 100 per cent of the common shares and, as of the year 2004, 100 per cent of the preferred shares.
- o) B2C's share register does not mention the issuance of any non-voting Class C shares, or of any other shares of Class A or any other class.
- p) B2C's minutes book does not contain any resolutions of the director regarding the issuance of Class C shares or any other class of shares.
- q) B2C has not issued any share certificates.
- r) The notes to B2C's financial statements for the years ending March 31, 2002, and March 31, 2003, show that there were 100 Class A shares issued and paid for, and 350,000 Class C shares were apparently issued.
- s) Of these 350,000 Class C shares, 193,532 were purchased for \$1 each on March 31, 2002, and 233,532 were purchased for \$1 each on March 31, 2003.
- t) The FF-1 sheet comparing the capital stock on March 31, 2004, with the capital stock on March 31, 2003, indicates that Richard Poulin held 350,000 Class C (ordinary) shares on March 31, 2003.
- u) The chartered accountants' office that had prepared the financial statements for the years ending March 31, 2002 and 2003, stated in the notice to reader that no audit or review of the balance sheet and the statement of income and expenses had been

carried out, and that no other measures had been taken to ensure the accuracy and completeness of the information provided by B2C's management.

- v) No external audit was carried out of B2C's financial statements for the fiscal years ending March 31, 2004, and March 31, 2005.
- w) On May 15, 2004, Benoît Beaudin, Capital Vision and Fiducie MGT gave Richard Poulin, B2C and 9098-5854 Québec Inc. a full and final acquittance in consideration of \$5,000 payable to Benoît Beaudin in five instalments between April 15 and August 15, 2005.
- x) This acquittance covered the extinction or performance of recipients' obligations under the terms of any investment project agreed to orally or in writing between the parties.
- y) On October 17, 2005, the company B2C changed its name to Komutel Inc., the appellant.
- z) In an initial meeting with the Agency's auditor on May 3, 2005, Richard Poulin stated the following:
  - Capital Vision had invested \$250,000 over the first three years in exchange for B2C shares.
  - Benoît Beaudin had been paid \$5,000 for the redemption of the shares held by Capital Vision.
- aa) In a second meeting with the Agency's auditor on May 6, 2005, Richard Poulin stated the following:
  - He had redeemed the 350,000 Class C shares that Capital Vision held in B2C for \$5,000.
  - Payment had been made to Benoît Beaudin by a cheque for \$5,000 issued by B2C.
- bb) In a third meeting with the Agency's auditor on June 16, 2005, Richard Poulin stated the following:
  - Capital Vision had actually loaned \$350,000 to B2C.
- cc) In a fourth meeting with the Agency's auditor on October 4, 2005, Richard Poulin stated the following:
  - No document regarding Capital Vision's \$350,000 investment was signed following the initial agreement of April 4, 2001, and he was unable to confirm whether it was a loan or capital stock.
  - B2C had not issued any share certificates to Capital Vision.

- He was unable to confirm how and by whom the \$5,000 for acquittance was paid to Benoît Beaudin in order to terminate the partnership.
- dd) On January 11, 2006, Benoît Beaudin signed a letter stating that all of the money invested in B2C had been so invested in exchange for 51 per cent of the common shares and that he authorized Capital Vision's management to transfer the share certificates to Richard Poulin's account as consideration for the redemption of May 15, 2004.
- ee) No share certificates of any class whatsoever were transferred between Capital Vision and Richard Poulin.
- ff) Capital Vision was struck off the enterprise register on June 16, 2006, by the Quebec Enterprise Registrar.
- gg) B2C never repaid to Capital Vision the \$350,000 loan.
- hh) The money paid to B2C by Capital Vision totalled \$363,932, representing the \$350,000 loan, plus a \$130,500 advance minus a \$116,568 subscription receivable.

[3] The facts set out in the reply to the notice of appeal are substantially the same as those revealed by the evidence. In short, the evidence showed that Mr. Poulin and Mr. Beaudin had met in the course of an attempt to obtain financing.

[4] Mr. Poulin said that after the presentation of his project, he was surprised by the interest and, above all, eagerness of the group led by Mr. Beaudin to invest over \$300,000.

[5] Mr. Poulin was aware that his financial limitations prevented him from successfully carrying out his project alone; he explained that he could not be too demanding regarding the control of the company and had therefore agreed to hand control over to Mr. Beaudin's group.

[6] The parties then agreed in writing to the approach that would be taken and the form that the financial contributions were to take. It was a bare-bones agreement with some potentially confusing points, given the lack of detail and clarification on several aspects.

[7] Early on, Mr. Poulin became disabused of his regarding cooperation with Mr. Beaudin and his group. He became more worried still on receiving calls from putative shareholders with unrealistic expectations.

[8] Mr. Poulin became increasingly worried, to the point of becoming suspicious and mistrustful of Mr. Beaudin and his group. He feared losing control of the business. Thus, Mr. Poulin hesitated and repeatedly postponed signing the draft share-transfer agreement that Mr. Beaudin had prepared and submitted.

[9] In the context of a now rather strained relationship between the investing group's leader and the project's initiator, the documentary and regulatory aspects were so badly neglected as to give rise to confusion and ambiguity, so much so that the interested parties, Mr. Poulin and Mr. Beaudin, had substantially different interpretations of the situation, according to their testimony.

[10] This was the context or background at the time of the audit and the drafting of the reply to the notice of appeal.

[11] In his testimony, Mr. Poulin stated that he had lacked discipline when it came to management, that he had lacked knowledge, and that he had also had problems communicating with Mr. Beaudin. He stated as well that there had been several changes because the development of the project did not correspond to his initial vision or to his expectations. He repeated that adjustments had had to be made a number of times.

[12] In May 2004, when the business was still at the developmental stage, the two men decided to terminate their business relationship. Mr. Poulin was as mistrustful and worried as ever, especially since he was still receiving calls from people who had been misinformed about the file.

[13] It is important to note at the outset that the terms of the agreement on the management of the initial investments are not all clear and precise, particularly those relating to the consideration for the funds invested. The contents of the agreement were reproduced in paragraphs h i) to iii) of the reply to the notice of appeal, at page 2 of these reasons.



[14] Even though the project's progress had failed to meet expectations, the parties made no changes to the agreement prior to breaking off their relationship.

[15] This breaking off was sealed by a document that reads as follows:

[TRANSLATION]

**FULL AND FINAL  
ACQUITTANCE**

**BY: Benoît Beaudin**, domiciled and residing at 1558 Antoine-Daniel Street, Boisbriand, Quebec, J7G 3B5;

**Groupe Capital Vision Inc.**, a duly incorporated company having its head office at 1200 Chomedy Boulevard, Laval, Quebec, H7V 3Z3, and represented herein by its mandatary, Benoît Beaudin, duly authorized for the purposes of this acquittance;

**Fiducie MGT**, 1558 Antoine-Daniel Street, Boisbriand, Quebec, J7G 3B5, and represented herein by the trustee Benoît Beaudin, acting as its duly authorized mandatary for the purposes of this acquittance; (hereafter collectively referred to as the "**Creditor**")

**FOR THE BENEFIT OF:**

**Richard Poulin**, domiciled and residing at 747 161st Street, St-Georges de Beauce, Quebec, G5Y 7V9

**B 2 C WEB SUPPORT Inc.** (Innocom), a duly incorporated company having its head office at 11505 1st Avenue, Suite 470, St-Georges de Beauce, Quebec, G5Y 7X3, and represented herein by its mandatary, Richard Poulin, duly authorized for the purposes of this acquittance;

90985854 CANADA INC. (Innocom) a duly incorporated company having its head office at 11505 1st Avenue, Suite 470, St-Georges de Beauce, Quebec, G5Y 7X3, and represented herein by its mandatary Richard Poulin, duly authorized for the purposes of this acquittance; (hereafter collectively referred to as the "Recipient")

**FOR GOOD AND VALUABLE CONSIDERATION**, which each of the undersigned acknowledges having duly received, we, the undersigned, agree as follows:

The Creditor, Benoît Beaudin, Groupe Capital Vision Inc. and Fiducie MGT, and all other entities related to or affiliated with Benoît Beaudin, Groupe Capital Vision Inc. and Fiducie MGT, hereby acknowledge and confirm the extinction and/or

performance of each and every one of the Recipient's obligations to them under any investment project or verbal or written agreement between the parties, and hereby release by the Recipient from all obligations under any investment project or verbal or written agreement between the parties.

#### **PAYMENT OF THE CONSIDERATION**

The acquittance is granted in consideration of the following:

FIVE THOUSAND DOLLARS (\$5,000.00), to be by means of five bank cheques made out to Benoît Beaudin, commencing April 15, 2005, and continuing to August 15, 2005.

Accordingly, for good and valuable consideration, the Creditor, Benoît Beaudin, Groupe Capital Vision Inc. and Fiducie MGT, and all other entities related to or affiliated with Benoît Beaudin, Groupe Capital Vision Inc. and Fiducie MGT, hereby grant full, final and definitive acquittance to the Recipient or the Recipient's directors, officers, shareholders or employees, in their capacity as directors, officers, shareholders or employees or otherwise, with respect to all rights, claims, actions, demands, rights of action, damages, and claims of any nature whatsoever, past, present or future, that the Creditor, Benoît Beaudin, Groupe Capital Vision Inc. and Fiducie MGT, and all other entities related to or affiliated with Benoît Beaudin, Groupe Capital Vision Inc. and Fiducie MGT, have or could claim to have against the Recipient in relation to any investment project, investment, or verbal or written agreement.

This acquittance constitutes a transaction within the meaning of article 2631 of the *Civil Code of Québec*.

IN WITNESS WHEREOF, the parties have signed this acquittance on the 15th day of May 2004.

[16] During the audit, the auditor noticed several discrepancies and ambiguities. He concluded that the documentary evidence was either incomplete or deficient.

[17] The minutes book and financial statements, far from clarifying the situation, confirm instead that there was so much confusion regarding the file that neither the appellant nor the respondent could rely on these documents to support their respective positions, which were based mainly on interpretations and extrapolations.

[18] Given the poor quality of the documentary evidence available, the Canada Revenue Agency characterized the capital contributions of Mr. Beaudin's group as loans rather than shareholders' participation in a new company run by Richard Poulin.

[19] Consequently, an assessment was made in which the loss at issue was characterized as a loss resulting from the partial forgiveness of a loan rather than a loss resulting from a sale of shares, since the investor had accepted a consideration that was less than the amount invested.

[20] Thus, the respondent relied on the assumption that it was not a capital loss but, rather, a forgiveness of debt, which therefore generated income for the recipient taxpayer under section 80 of the *Income Tax Act* (ITA), all of which had, in addition, direct consequences on the computation of the research and development tax credits claimed.

[21] It is important to note at the outset that an assessment must be made on the basis of actual and verifiable facts, not possible and probable scenarios desired by the taxpayer or taxpayers concerned.

[22] This is an important principle that must be upheld, otherwise, a person could, in order to make a more advantageous choice from a tax standpoint, rely on a confused and ambiguous situation that was unsupported by written evidence and that could lead to various interpretations when facts unknown at the closing of the transaction are revealed. In other words, retroactive tax planning is obviously unacceptable.

[23] Maintaining and/or fostering ambiguity in order to be able to obtain a tax benefit later is therefore very risky, if not dangerous. Indeed, such recklessness may often lead to outcomes that are more penalizing than beneficial.

[24] In this case, the evidence is very clear on one point. A number of the usual documents are missing, while other relevant documents are incomplete or so confusing that all of the hypotheses put forward by the parties are plausible.

[25] The appellant first called Mr. Beaudin, who described himself as a financial broker. He stated that he was convinced that his agreement with Mr. Poulin provided for, among other things, an investment in the form of common shares in the capital stock of the company to be created by Mr. Poulin. This interpretation is supported, moreover by some of Mr. Poulin's statements, in particular his explanation that his personal financial situation prevented him from being too independent and demanding.

[26] Mr. Beaudin claimed that he had recently learned that his group had actually invested in preferred shares. His testimony revealed that he was a slightly mysterious individual whose behaviour had caused Mr. Poulin to be worried and even somewhat mistrustful.

[27] As for Mr. Poulin, he stated that the company run by Mr. Beaudin had indeed invested a little over the \$350,000 provided for by the agreement.

[28] A sum of \$200,000 was allegedly invested in preferred stock through a series of payments that in fact did not follow the established timetable. This was allegedly a temporary, not to say transitory, situation.

[29] The shares were eventually to be converted into common shares, following the conclusion of a shareholders' agreement allowing Mr. Poulin to keep control of the company. The agreement was never signed for various reasons, including certain concerns Mr. Poulin had.

[30] The \$100,000 loan amount provided for by the agreement was not paid, given the company's difficulties. According to Mr. Poulin, that amount, like the \$50,000 provided for by the agreement that was to be used to pay his salary, had been invested in the company, also in the form of preferred stock.

[31] Mr. Poulin stated that he had run the business as best he could given the knowledge he had, which he himself considered inadequate. He explained that he had always been aware of the importance of Mr. Beaudin's contribution and that he had felt indebted to him. Nevertheless, Mr. Beaudin's behaviour and the calls from people from his investment group had worried Mr. Poulin.

[32] Moreover, the breaking off of his relationship with Mr. Beaudin took place after Mr. Poulin began receiving telephone calls from people claiming to have made investments in a manner that was not totally in line with reality. In fact, this was part of the reason, he said, for the company's subsequent name change.

[33] Mr. Poulin also explained that he himself had drafted the document attesting the definitive breakup with Mr. Beaudin, using a loan acquittance template, the object of it all being pay off Mr. Beaudin by means of five payments of \$1,000.

[34] Only the auditor, Éric Laplante, testified in support of the respondent's evidence. His testimony, as well as his observations, appear to me to summarize very aptly the assumptions of fact in paragraphs a) to hh) inclusive of the reply to the notice of appeal, which are reproduced at pages 1, 2, 3, 4 and 5 of these Reasons for Judgment.

[35] Mr. Laplante stated that he had also relied on the document entitled [TRANSLATION] "Full and Final Acquittance", attesting the breakup of Mr. Poulin's and Mr. Beaudin's relationship. He stressed the fact that it made no mention of shares, but contained rather the terms [TRANSLATION] "creditor" and [TRANSLATION] "investment project". He also noted that the financial statements dated March 31, 2003, are based on data that were not audited by the accounting firm that had prepared those statements.

[36] Called on by the respondent to explain the discrepancy between the financial statements, which indicate that \$156,468 in preferred shares had been issued and paid for, and the income tax returns, which show that Mr. Poulin was the taxpayer's sole shareholder, Mr. Laplante conceded that [TRANSLATION] "this is the only point that mentioned a second shareholder".

[37] In cross-examination, Mr. Laplante stated that, in the financial statements from the years 2002 to 2004, he had found no trace of the \$100,000 loan provided for in the agreement, or of any documents attesting the existence of such a loan, or of any agreements providing for the payment of interest, or of amounts due as interest, and this despite his acknowledgment that Mr. Poulin, who at the time had referred him to his accountant, had been cooperative.

[38] I think it would be useful to reproduce an excerpt of one of the important documents at the core of this dispute. The agreement entered into following the one relating to the initial investment reads as follows:

[TRANSLATION]

A total investment of \$350,000.00 will be made under the following terms:

- A \$200,000.00 initial investment in the business according the following timetable . . .
- \$100,000.00 paid to the company in the form of advances reimbursable from profits
- \$50,000.00 in cash paid to Richard Poulin, on terms to be established.

[39] The first and third undertakings are rather poorly defined, since the form that the \$200,000 investment is to take is not indicated; as for the terms regarding the \$50,000 payment, it was agreed that the money was to go to Mr. Poulin personally, not the company to be created. That it was the appellant that received that amount supports Mr. Poulin's testimony that changes were made to the agreement along the way.

[40] The respondent invoked the absence of any resolutions on the issuance of shares, but her position contains an implicit admission, as the necessity of a resolution is not specific or exclusive to the issuance of shares. A resolution would have also been appropriate in the case of a loan. Indeed, the company would have had to accept the loan, for loans are also contracts arising from the exchange of consents.

[41] The financial statements for March 31, 2002, 2003 and 2004, recorded sums of \$193,532, \$233,532 and \$350,000 respectively, in association with the words [TRANSLATION] "issued and paid – Class C shares". It is true that this is not the best evidence of shares having been issued. However, it is fair to consider such information to be at least a commencement of proof.

[42] On the one hand, it is clear that things did not proceed as had been expected; on the other hand, it was expressly provided for in the financial undertakings that clarification or modification might be necessary with regard to the treatment of the initial investments, given the uncertainties that existed even at the time that the first agreement was concluded.

[43] One thing is sure: neither the agreement creating the partnership between Mr. Beaudin and the company to be established for the purpose of developing Mr. Poulin's project nor the document attesting his good faith is a model of clarity.

[44] Between the beginning and end of the business relationship between Mr. Poulin and the group led by Mr. Beaudin, the company produced financial statements. While these financial statements do not satisfactorily support either the appellant's position or the respondent's, it is possible to find therein at least one indicator supporting the appellant's position.

[45] I refer in particular to the fact that there is no indication of a loan. Had the financial statements mentioned such a loan, there would obviously have been a paper trail, especially since the period during which these statements were prepared corresponds to the period during which the initial investments were made.

[46] However, there is absolutely no evidence on this point, which thus creates a kind of presumption, albeit not a formally stated one, that the contribution agreed to by Mr. Beaudin's group was not disputed.

[47] The respondent concluded that this was a partial forgiveness of a commercial liability, in particular because shares could not have been involved, as the formalities required for issuing shares were either non-existent or insufficient.

[48] In other words, the respondent seems to be alleging that the contribution is simply a loan, since the formalities for issuing shares were not observed or respected.

[49] If it is a loan, although fewer, less strict formalities are required in order to attest its validity, there should have been a certain minimum of formalities, including those relating to the term and the interest rate applicable. There were no such formalities here.

[50] In this regard, I note that the respondent made certain allusions to the fact that the parties were run by businessmen. Is it plausible that businessmen would forget to specify the term or interest rate of a loan? The answer is obvious.

[51] The argument that this was a \$350,000 commercial liability because there was an agreement between two companies represented by experienced businessmen who were not related is not serious and can be explained as essentially the result of a desperate search to find a basis for a hypothesis that is somewhat odd on its face.

[52] As for the acquittance document, the respondent refers to it merely to show that Mr. Beaudin is a seasoned businessman.

[53] The respondent submitted that an acquittance document that mentions a [TRANSLATION] “creditor” and [TRANSLATION] “investment project” and makes no reference to shares would support the theory that a loan had been made to the appellant. This argument is preposterous and, moreover, was not pursued at the oral argument stage.

[54] This is also the case with the various undertakings regarding dates that were not fulfilled. Any type of undertaking can be modified with the consent of all the parties.

[55] A change agreed to by the parties is perfectly legitimate as long as it does not involve retroactive tax planning.

[56] Lastly, Mr. Poulin’s fear of losing control of the company is completely irrelevant, as there are an infinite number of ways to attach conditions, benefits or privileges to shares and create several classes of shares.

[57] The financial statements for March 31, 2002, 2003 and 2004, are dated August 12, 2002, September 9, 2003, and July 9, 2004, respectively. Neither the date on which they were prepared nor their contents were called into question. The financial statements for 2004, indicating an amount of \$350,000 accompanied by the note [TRANSLATION] “Issued and paid – Class ‘C’ shares”, were prepared by a third party. Again, this is not the best evidence, but it is at least a commencement of proof, an indicator of a scenario more consistent with the argument of the appellant than that of the respondent. In any event, this one point alone has greater validity than those put forward by the respondent, which are essentially based on the auditor’s fertile imagination.



[58] The financial statements were disregarded, given that they were unaudited. However, there is no evidence that they were not reliable or credible.

[59] These financial statements contain nothing to support the respondent's argument, but they do reveal some indicators supporting the appellant's position.

[60] The auditor attached great importance to the contents of the agreement, so much so, in fact, that he said he had been given what he judged to be four different versions, and he implied that he consequently no longer believed Mr. Poulin. However, an analysis of what he considered to be different, if not contradictory, versions, does not support such a conclusion. What is certain is that the agreement cannot be excluded from the evidence on the basis of that analysis.

[61] The auditor's testimony confirms the impression of confusion left by the file. However, if the appellant's intention had been to foster confusion for its own benefit, the appellant would have at least tried to give explanations pointing in the direction it desired, but this was not the case.

[62] The auditor gave such great weight to the fact that Mr. Poulin had given different versions of the evidence that he concluded that Mr. Poulin was not particularly credible and that a large part of his testimony had to be disregarded.

[63] What the auditor considered to be contradictory versions is rather a demonstration of the ambiguity of the situation and the obvious candour of Mr. Poulin, who himself did not know how the file would evolve, his sole concern having been to pursue and maintain control of the project that he had created.

[64] The auditor, asserting that the existence of preferred shares suggested the presence of another shareholder, stated that these documents were the only ones supporting such a conclusion. All the same, he had noted that Schedule 50 to the 2004 tax return also showed the existence of these shares, although they were in Mr. Poulin's name. Having recognized that the \$350,000 had not come from Mr. Poulin, the respondent could have seen therein an indicator corroborating the 2004 financial statements.

[65] It is true that all assessments must be made on the basis of facts that existed during the period covered by the assessment, not on the basis of hypotheses or wishes that do not correspond to reality. It is true that any retroactive planning must be rejected. Everyone must assume the consequences of his or her actions in tax matters, and this frequently gives rise to results which are neither desired nor hoped for by those involved. Moreover, anyone who is assessed bears the burden of proof. Nevertheless, such statements must not be used as the only foundation for an assessment. The respondent cannot make an assessment on the basis of questionable, uncertain or incomplete facts, on the pretext that the appellant bears the burden of proof. The respondent must provide a certain minimum of reasonable justification.

[66] Here, Mr. Poulin set up a project related to information technology. He could not afford to develop his project himself. Information technology is a very popular field that attracts investors. There is a host of “get rich quick” stories in that field, and new ideas rapidly fuel investors’ speculative hopes.

[67] Mr. Poulin met Mr. Beaudin, who headed a group of investors. Mr. Poulin gave a presentation concerning his project and its possibilities. Very quickly, within hours, he received a positive response beyond all his expectations: a formal undertaking to invest \$350,000.

[68] Extremely happy and very surprised, he was nevertheless aware that he would now have to form a partnership with others. He wanted to lead the project, but the funds required for its development were supplied by third parties. He assessed the situation, in particular with respect to control of the project. The parties entered into a written agreement whose contents were vague but reflective of a certain degree of mutual trust.

[69] Things subsequently advanced somewhat chaotically, and Mr. Poulin became disillusioned to the point that the parties had to agree to break off their relationship upon five payments of \$1,000, that is, \$5,000 in total, although the amounts laid out had been in the order of \$350,000.

[70] What was to have been the consideration for the \$350,000 investment? There are two possibilities: a loan or a certain number of shares to which various rights could be attached.

[71] We must place ourselves in the context of the birth of the project. At that point, the idea was at the embryonic stage, potentially very promising, but hypothetical and speculative.

[72] The investors knew neither the promoter nor the company, but they obviously wanted to participate in this promising project and reap the profits it would yield.

[73] This scenario clearly presupposes the issuance of some number of shares to which various rights may be attached, but it excludes all scenarios of initial investments in the form of loans, since the evidence shows that, in the present case, it was in essence a speculative project.

[74] This is not public money for the creation of jobs, where a return on the investment is not the priority, nor is it a philanthropic venture or short-term support. This is essentially a commercial project in which, on the one hand, there are businessmen willing to take great risks in exchange for an exceptional return, which is obviously not a characteristic of a loan under circumstances considered to be very risky.

[75] These are the inescapable facts revealed by the evidence. At this point, is it possible that one or more intelligent people would have committed to such a venture by making an interest-free loan? It is all the same doubtful given that there is no note or document supporting such an interpretation. To pose the question is sufficient to conclude without hesitation that the answer is no.

[76] Months passed, the project progressed very slowly, and the financial situation was disappointing. It is possible that the investors, with the promoter's consent, agreed to have part of the money invested presently retroactively as a loan? Again, the question answers itself: relatively reasonable people would not have contemplated such a scenario unless their goal had been completely unrelated to any return.

[77] Except in the case of governments and certain paragovernmental entities, I have trouble imagining that an investor looking for exceptional returns would agree

to loan money to a prospective debtor who was not financially sound, without attaching a very high interest rate to the loan.

[78] Here, while the project might have been promising despite its speculative nature, it was plainly not likely to interest a lender.

[79] On the contrary, the project was still in its early stages. True, it perhaps showed promise, but offered no prospect of short-term or even medium-term, profitability. The group led by Mr. Beaudin was in no way charitable or philanthropic. It was looking to obtain the greatest return possible as quickly as possible.

[80] If this were a loan, the lenders would certainly have set an interest rate, but there is no evidence in this regard.

[81] The appellant submitted evidence of which only the verbal aspect is coherent. Generally, in matters of evidence, it is in the nature of things to validate and corroborate verbal explanations using documentary evidence. However, the documentary evidence here is deficient, incomplete and confused.

[82] It fails to meet basic requirements and simply does not respect certain formalities for the incorporation of a company, in particular as regards the issuance of shares, the declaration and the financial statements.

[83] Nonetheless, this evidence has the virtue of being reasonable and probable. A conclusion does not depend solely on the number of flaws or shortcomings found; it must have at least some degree of reasonableness.

[84] Faced with such chaos in the documents, the auditor became decidedly suspicious and sought to document certain points in order to make an assessment.

[85] On the grounds that the documentary evidence was of very poor quality and that the explanations obtained regarding the company's organizational development (the initial agreement and the change of heart regarding the nature of the shares, different versions, etc.) were often incoherent, the auditor concluded that the amount

at issue was a loan and that there was enough evidence in support of his finding to justify the assessment under appeal.

[86] The auditor focussed mainly on the words used, which, however, in no way validated the conclusion drawn. He noted that there was insufficient written evidence and that the written evidence available was confusing, and he concluded, quite rightly, that this file was plagued by rather generalized confusion. He also raised some irregularities regarding compliance with formalities. However, there was insufficient evidence to establish the existence of a commercial liability that could trigger the application of section 80 of the ITA.

[87] The word liability was indeed used, but I do not think that this is enough to support the Agency's conclusion, especially since that would contradict everything revealed by the context and the evidence, which is rather circumstantial here.

[88] I do not think that incoherence, deficiency and insufficiency should be rewarded; generally, one does the opposite in such cases.

[89] I am of the opinion that the evidence here is clear on some points. I note in particular the following facts: a potentially promising project; investors showing interest very quickly; project advancing chaotically and contrary to expectations; generalized confusion; and lacunae, deficiencies and irregularities in the issuance of shares. Underlying all of this is the fact that the principal party concerned was acting in good faith. He believed in his project and wanted to succeed. These facts are demonstrated by Mr. Poulin's cooperation with the auditor.

[90] In conclusion, I am of the view that, through the oral evidence and a commencement of proof or bits of information revealed by the documentary evidence, the appellant has established on a balance of probabilities that the capital at issue was invested in the form of shares, and not as loans as the Agency contends.

[91] The respondent's argument is based on evidence that is insufficient and on hypotheses that do not pass the test of reasonableness. Consequently, these are excluded.

[92] The appeal is therefore allowed, and the file will be referred back to the Agency for reassessment on the basis that the amounts received by the appellant were contributions by its shareholders, not loans. Costs are awarded to the appellant.

Signed at Ottawa, Canada, this 15th day of June 2010.

“Alain Tardif”

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Tardif J.

Translation certified true  
on this 10th day of November 2010.

Erich Klein, Revisor

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