Docket: 2009-1785(IT)G

BETWEEN:

RNC MÉDIA INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on October 18, 2010, at Montréal, Quebec

Before: The Honourable Justice Paul Bédard

Appearances:

Counsel for the appellant:	Dominic C. Belley
Counsel for the respondent:	Claude Lamoureux
	Nathalie Labbé

JUDGMENT

The appeal from the reassessment made pursuant to the *Income Tax Act* for the taxation year ending August 31, 2003, is allowed with costs, in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Canada, this 16th day of February 2011.

"Paul Bédard"

Bédard J.

Translation certified true
on this 15th day of April 2011.

François Brunet, Revisor

Citation: 2011 TCC 92
Date: 20110216
Docket: 2009-1785(IT)G

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RNC MÉDIA INC.,

Appellant,

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REASONS FOR JUDGMENT

Bédard J.

[1] This is an appeal by the appellant, RNC Média Inc., formerly Radio Nord Communications Inc., from an assessment made on April 18, 2007, by the Minister of National Revenue (the Minister), pursuant to the *Income Tax Act* (the Act) for its taxation year ending August 31, 2003. A notice of objection was duly produced on July 12, 2007. The assessment was amended on February 26, 2009. The total amount in question is less than $50,000 (Category A).

[2] On February 15, 2001, the appellant dismissed its President and Chief Operating Officer, Gilles Poulin. The appellant paid Mr. Poulin $135,843 in the context of his dismissal. The appellant deducted $135,843 from its income calculation for the 2003 taxation year. The appellant claims it was entitled to deduct the amount of $135,843 in the calculation of its income because it paid Mr. Poulin compensation for the services he had rendered. Moreover, in the assessment made on April 18, 2007, and amended on February 26, 2009, the Minister disallowed the expense the appellant deducted as a benefit for services rendered. The Minister considered that this amount had been used to purchase the 75 shares Mr. Poulin held in the capital stock of the appellant and which resulted in a deemed dividend pursuant to subsection 84(3) of the Act. In this case, only one issue is raised: did the appellant

pay Mr. Poulin $135,843 to purchase its own shares that he held, or as a benefit for services rendered?

[3] Martin Leblanc, tax specialist with the firm Samson, Bélair (the appellant's external auditor) and Pierre Brosseau, Chair of the appellant's board of directors, testified in support of the appellant's position. Only Mr. Poulin testified in support of the respondent's position.

Background

[4] The appellant has been operating in the telecommunications sector for more than 50 years. It began its activities by operating radio stations in northwest Quebec. It has since acquired many radio stations and some regional television stations.

[5] Until February 15, 2001, Mr. Poulin worked as the appellant's President and Chief Operating Officer. He was responsible for the activities of all its radio and television units. During his 24 years of service, Mr. Poulin held the positions of Director General, Vice-President of Development, Executive Vice-President, President and Director General, and President and Chief Operating Officer (as of 1998) for the appellant. Starting in 1982, he took on the role of director and officer as president. In 1987, he became a shareholder of the appellant. He held 2,575 ordinary shares, for 5% of the appellant's capital stock.

[6] On March 19, 1998, the appellant entered into a contract of employment with Mr. Poulin (Exhibit A-1, Tab 10) to retain his services as president and Chief Operating Officer. The contract came into force on September 1, 1997. When the contract was signed, and when Mr. Poulin was dismissed, the appellant was represented by Pierre Brosseau, a lawyer by training who was a consultant for Groupe Radio-Nord Inc. and Radio-Nord Communications Inc. in 1996 and President and Chief Executive Officer of Groupe Radio-Nord Inc. in 1997, in which he held 50% of shares as of the fall of 2000.

[7] A specific agreement on Mr. Poulin's profit sharing in the appellant's capital stock (the Agreement) was entered into on March 19, 1998 (Exhibit I-1, Tab 1). The effective date of the Agreement is September 1, 1997. Article 1 of the Agreement stipulates:

> [TRANSLATION]
> ARTICLE 1 – CAPITAL PROFIT SHARING

1.1. Considering that the Intervenor shall proceed with a corporate reorganization as a "freeze", the President and COO shall subscribe to 75 of the 1,000 voting and participating shares to be issued by the Company after the "freeze", representing the only participating shares that will be in circulation, for consideration of $1.00 per share payable in cash, or for a similar fraction of a different number of equally voting and participating shares.

1.2. In the case where the President and COO does not remain employed by Radio Nord Inc. for a period of 3 years as of the Effective Date, he shall return to the Company or to persons determined by the Company's board of directors 25 of the voting and participating shares he holds for consideration of $1.00 each payable upon request. The balance of 50 shares shall be treated in the same manner as the case where the President and COO remains employed by the Company for a minimum period of 3 years.

1.3. In the case where the President and COO remains employed by the Company for 3 years as of the Effective Date, the Company or persons designated by its board of directors, shall proceed with the purchase or redemption of the shares in circulation for their book value during the Company's last fiscal year settled by the Company's auditors and payable in the 30 days following the board of directors meeting approving the financial statements of the preceding fiscal year.

1.4. For the purposes of ensuring the execution of each party's obligations under this paragraph, the share certificates for the Company subscribed by the President and COO shall be remitted to a depositary-agent that will be the law firm Lapointe, Rosenstein and whose mandate shall be as follows:

1. hold the above-noted share certificates duly endorsed by the Company (or eventually the Intervenor);

2. remit the above-noted share certificates or any portion thereof to their owner according to the provisions set out in these presents;

3. in case of dispute between the parties, hold the shares until final judgment, provided always that:

    a. the depositary-agent shall only be responsible for its acts done or made in bad faith,
    b. shall be released from any obligation if it acts in accordance with an opinion from a Quebec law firm of at least 20 lawyers in a partnership,
    c. may resign from its duties simply with a 15-day notice or be replaced upon consent by the parties,
    d. shall not be responsible for ensuring the execution of the respective obligations of the parties and may require any indemnity guarantee it deems sufficient.

> All of the depositary-agent's fees shall be assumed in equal parts by the Company and/or Intervenor on one hand, and by the President and COO on the other.

[8] Mr. Poulin submits that he subscribed to 75 ordinary Class "C" shares in the appellant for consideration of $0.10 per share and he paid the amount of the subscription by cheque payable to the appellant for $7.50 on August 15, 2000. I immediately note that the appellant's financial statements (see Exhibit A-1, Tab 2, Page 99, note 10) for its fiscal year ending August 25, 2002, indicate that the appellant's shares subscribed to by Mr. Poulin were not issued. One could also deduce from these financial statements that the appellant cashed the $7.50 cheque at some point because there is an entry for $8 ($7.50 rounded to $8) under the heading [TRANSLATION] "other subscribed shares" dated August 25, 2002. On this, I immediately note that the appellant submits that while the 75 ordinary Class C shares of its capital stock had been subscribed by Mr. Poulin, they were never issued. The respondent submits that these shares were issued, hence the present litigation.

[9] On February 15, 2001, Pierre Brosseau sent a letter to Mr. Poulin (Exhibit I-1, Tab 3) in which the appellant advised him that he was dismissed following the company's reorganization. This letter was accompanied by the text of a transaction and discharge that stated the various benefits granted by the appellant to terminate its relationship with Mr. Poulin. The appellant had granted Mr. Poulin 6 days to communicate his consent to such an agreement. The second "whereas" of this agreement stipulates:

> [TRANSLATION]
> Whereas Mr. Poulin subscribed to seventy-five (75) voting and participating shares of RNCI pursuant to a capital profit-sharing agreement entered into on March 19, 1998;
>
> (emphasis added)

In regard to the 75 shares with voting and participation rights to which Mr. Poulin subscribed, the appellant offered, under paragraph 2.4 of this agreement that: [TRANSLATION] "RNCI buy back the 75 voting and participating shares of capital stock in RNCI acquired by Mr. Poulin pursuant to the capital profit-sharing agreement entered into by the parties on March 19, 1998, and pay Mr. Poulin, in consideration of the said redemption, the amount of $59,193." Mr. Poulin rejected the appellant's transaction proposal.

[10] On June 21, 2001, Mr. Poulin brought legal action against the appellant to have his rights recognized under the terms of the Agreement (Exhibit I-1, Tab 1). The initial case included a declaratory component and for passation of title regarding the 75 ordinary Class "C" shares to which he subscribed. On this, paragraphs 45 and 46 of the Re-Amended Statement and Retraxit are worth citing (see Exhibit I-1, Tab 4). They state:

> [TRANSLATION]
> 45 Also, the applicant is asking this court to declare whether, in fact, he or the defendant company, could, after his contract for employment was extended for two years on February 15, 2001, require the sale, purchase or redemption of his shares;
>
> 46 In the affirmative, the applicant asks for the transfer of titles, for the price to be determined by this honourable Court, submitting that the fair market value of his shares is $3,000,000 and their book value is not $59,193 as proposed by the defendant company, but rather $279,127.00… In support of these claims, the applicant submitted an expert accounting report (Exhibit P-36)…

[11] Further to this initial litigation, as a settlement offer on August 22, 2002, the appellant paid Mr. Poulin compensation of $468,986. On reading the letter by counsel Alain Gascon (Exhibit I-1, Tab 7), who represented the appellant during this case, to which cheques totalling $468,986 were enclosed, it can be seen that a cheque for $67,880.37 was drawn on the appellant's bank account payable to Mr. Poulin in regard to the 75 ordinary Class "C" shares. The text of this letter can be usefully reproduced. It states:

> [TRANSLATION]
> SHARE REDEMPTION: $59,193.00
> DIVIDENDS: $69,559.00

Cheque no. 003987	Payable to Gilles Poulin Share redemption: $59,193.00 (Value of the 75 non-issued ordinary shares) Dividends: $69,559.00 Gross total: $128,752.00 Less tax deductions - 60 871.63	$67,880.37

[Emphasis added]

[12] As to the initial litigation, an amendment took place so that the August 22, 2002, payment of $468,986 (see Exhibit I-1, Tab 4) could be taken into consideration. Considering the $59,193 received by Mr. Poulin for the 75 subscribed ordinary Class "C" shares after his initial legal case was brought, Mr. Poulin asked, in the amended case, for a judgment on the balance, submitting that the value of his shares was $279,127 and not $59,193.

[13] On August 28, 2003, Justice Nicole Morneau of the Superior Court of Québec rendered the following decision regarding the 75 ordinary Class "C" shares in the appellant to which Mr. Poulin subscribed (see Exhibit A-1, Tab 6, page 14):

> [TRANSLATION]
> …
>
> **DETERMINES** the value of the applicant's 75 ordinary shares in Radio Nord Communications Inc. to be $195,036.00, as of August 31, 2000;
>
> **ORDERS** the defendant to pay the applicant $135,843.00 for the balance of its shares with interest at the legal rate and additional indemnity as provided under article 1619 Cr.C.Q. on the amount of $195,036.00 from February 2001 to August 22, 2002, and on the balance of $135,843.00 as of August 23, 2002;
>
> **DECLARES** good and valid the tender and payment of the applicant's shares to the defendant and orders their transfer to the defendant for payment of the price established above;
>
> …

[14] Moreover, the evidence showed that:

a. The regulation (Special Regulation No. 29) modifying the appellant's status and in particular giving effect to the freeze proposed by the appellant in the Agreement and to create a Class "C" ordinary shares class was adopted on August 9, 2000 (see Exhibit A-1), Tab 14, pages 159-160). The statute modification certificate was submitted to the Inspecteur général des institutions financières the same day Special Regulation No. 29 was adopted (see Exhibit A-1, Tab 14, pages 161-175);

b. The appellant submitted a T-4 information slip (Exhibit A-1, Tab 8) regarding the $135,843 paid to Mr. Poulin. This information slip indicates that this $135,843 was paid to Mr. Poulin as employment

income and that the appellant made the appropriate source deductions. Immediately, I note that Mr. Poulin had testified that in his income tax return for the 2003 taxation year, he had treated that amount received by the appellant as employment income (see page 64 of the transcript);

c. The appellant's financial records for its fiscal year ending August 31, 2003, indicate that the subscription for the 75 ordinary Class "C" shares had been cancelled (see Exhibit A-1, Tab 2, page 99);

d. The appellant treated the $135,843 paid to Mr. Poulin in 2003 as an expense for the purpose of earning income from his business for both accounting and tax reasons;

e. The appellant's Regulation No. 21 (Exhibit A-1, Tab 15, pages 194-195) indicates that:

[TRANSLATION]

(1) the company's capital stock may be distributed at the times, in the manner, and to the persons or categories of persons the directors may occasionally determine by resolution;

(2) the company was to keep records at its head office that included the names of all persons who were or had been shareholders in the company in alphabetical order, the number of securities held by each shareholder, and the details of the issuance and transfer of each share in the company's capital;

(3) each share certificate in the company must be issued under the seal of the company and signed by the President or Vice-President and countersigned by the secretary or assistant secretary.

It must immediately be noted that Jacques Lavallée (the Canada Revenue Agency auditor who conducted the audit of the appellant's books that led to the April 18, 2007, assessment made by the Minister) stated during his direct examination (see Exhibit A-2) that during his audit of the appellant's books, he did not see any resolution by the directors authorizing Mr. Poulin to be issued 75 ordinary Class "C" shares, any share certificate indicating these shares had been issued or any entry in the appellant's shareholder record indicating these shares

had been issued to Mr. Poulin. Mr. Lavallée added that after the April 18, 2007, assessment was made and its amendment he became aware of the photocopy of a cheque (Exhibit A-1, Tab 11) indicating that, on August 5, 2000, Mr. Poulin had drawn a cheque on his bank account for $7.50 payable to the appellant. Mr. Lavallée explained during this direct examination that his decision that the 75 ordinary Class "C" shares had been issued by the appellant to Mr. Poulin was solely based on his interpretation of the Agreement and on the provisions of the judgment cited at paragraph 13, below. It is also of note that Mr. Poulin, as Mr. Brosseau, testified that he had not attended nor was he summoned to a meeting of the board of directors during which it was resolved to issue Mr. Poulin 75 ordinary Class "C" shares, and he was not aware that such a resolution had been adopted;

f. The appellant's securities register (Exhibit A-1, Tab 12) indicates that 5% of the ordinary shares held by Mr. Poulin had been redeemed on June 15, 1998, for $375,000 in accordance with paragraph 10.1.4 of his employment contract (Exhibit A-1, Tab 9) and that he no longer held any shares in the appellant's capital;

g. The corporation information report (Exhibit I-1, Tab 5) obtained from the Inspecteur général des institutions financières, dated February 22, 2001, indicates that as of December 19, 2000 (the date the appellant's last annual return was filed) Mr. Poulin was the appellant's director and second shareholder. It must be noted that the evidence submitted by the parties does not provide the name of the person who filed the annual return of December 19, 2000, or the name of the person who audited it or the name of the person who sent it to the Inspecteur général des institutions financières.

Martin Leblanc's testimony

[15] Mr. Leblanc's testimony can be summarized as follows:

i. During his review of the appellant's minute books and share register, he could not find any minutes by the board of directors (or a resolution by its directors) or any entry in the share register indicating that 75 ordinary Class "C" shares in the appellant had been issued;

ii. During the review of the appellant's records, he did not find the original share certificate attesting to the alleged issuance of these 75 ordinary Class "C" shares; this certificate should have been in the appellant's books, duly signed by Mr. Poulin following the appellant's alleged purchase or redemption of the shares in question;

iii. He reviewed the employment contract and the Agreement between the appellant and Mr. Poulin, the legal action brought by Mr. Poulin against his client and the judgment rendered by the Superior Court of Québec in that case;

iv. He knew that Mr. Poulin had drawn a cheque for $7.50 payable to the appellant;

v. He reviewed the appellant's regulations;

vi. Mr. Brosseau pointed out to him that the appellant and Mr. Poulin had entered into the following verbal agreement: the 75 ordinary Class "C" shares would not be issued; however, the appellant would pay Mr. Poulin, in consideration for the services he had rendered, an amount equal to that which he would have been entitled to receive under the Agreement regarding the 75 ordinary Class "C" shares to which he had subscribed;

vii. After his review of all the documents, he found that:

1. Mr. Poulin had subscribed to 75 ordinary Class "C" shares in the appellant, but the shares were not actually issued because the appellant's directors had not adopted a resolution to this effect;

2. In her judgment, Justice Nicole Morneau did not order that these 75 ordinary Class "C" shares be issued;

3. The appellant had not paid Mr. Poulin $135,843 in consideration for the purchase of the shares he held because they had never been issued;

4. The $135,843 paid to Mr. Poulin should instead have been treated from tax and accounting perspectives as an expense incurred by the appellant for the purpose of earning income from his business

as it was paid to Mr. Poulin as compensation for services he rendered to the appellant.

Mr. Brosseau's testimony

[16] Mr. Brosseau's testimony can be summarized as follows:

a. The board of directors of the appellant (for which he was the director for all the relevant periods) never adopted the resolution to issue the 75 ordinary Class "C" shares subscribed by Mr. Poulin;

b. After signing the employment contracts (Exhibit A-1, Tabs 9 and 10), he came to an oral agreement with Mr. Poulin that the appellant would not issue him the 75 ordinary Class "C" shares in the appellant to which he had subscribed, notwithstanding its commitment to issue them in accordance with these contracts. Mr. Brosseau explained that he had come to an oral agreement with Mr. Poulin that the appellant would pay him, in consideration for the services he had rendered to the appellant, an amount equal to that which he would been entitled to receive under the terms of the contracts of employment regarding the shares. Mr. Brosseau added that a ghost stock purchase plan had in a sense been set up for Mr. Poulin under the terms of which 75 ordinary Class "C" shares were used as a reference to calculate the amount of the compensation (for services rendered) to be paid by the appellant to Mr. Poulin. It must be noted that Mr. Brosseau admitted that the use of the term "redemption" regarding the 75 ordinary Class "C" shares in the transaction offer (Exhibit I-1, Tab 3) and in Mr. Gascon's letter (Exhibit I-1, Tab 7) was inappropriate considering the subscribed shares had not been issued under the terms of the verbal agreement between him and Mr. Poulin. Mr. Brosseau explained that he did not pay particular attention to the language used in the two settlement offers considering that under the verbal agreement he had come to with Mr. Poulin the compensation would be calculated based on the shares in question that were subscribed but not issued.

Mr. Poulin's testimony

[17] Mr. Poulin's testimony can be summarized as follows:

a. On June 22, 2000, he attended a meeting of the appellant's board of directors at which it was resolved to give effect to the appellant's commitment (under the Agreement) to reorganize its capital (freeze) such that he could subscribe to 75 of the 1,000 voting and participating shares to be issued after the reorganization. I note that the respondent, in support of Mr. Poulin's testimony on this, wished to submit to evidence a copy of the minutes from the meeting of the appellant's board of directors held June 22, 2000 (Exhibit I-2). I note that the appellant objected to the submission of this document in evidence considering it was not on the respondent's list of documents and it had been brought to his attention a short time before the beginning of the hearing. In my opinion, the respondent should be allowed to produce that document because it is not unknown to the appellant and because its production is not likely to cause prejudice. Indeed, the appellant knew that such a resolution existed. Moreover, I do not see how the submission to evidence of this resolution could cause the appellant prejudice considering that at most it triggered the freeze, without particularly or automatically authorizing the issuance of the 75 ordinary Class "C" shares to Mr. Poulin once the freeze came into effect (namely, once the statute modification certificate was filed with the Inspecteur général des institutions financières).

b. On August 15, 2000, Mr. Hertel, the appellant's secretary, gave him a copy of the front of the original share certificate (Exhibit I-1, Tab 2) noting that since August 15, 2000, he held 75 ordinary Class "C" shares in the appellant after having signed the original certificate as the appellant's president, as required by the appellant's Regulation No. 21;

c. he does not recall either having attended a meeting of the appellant's board of directors at which it was allegedly resolved to issue him 75 ordinary Class "C" shares in the appellant, or having been called to such a meeting, or even having signed a resolution by all the directors to this effect. I must note that in April 2000 (the month in which the appellant had reorganized its capital and 75 ordinary Class "C" shares were allegedly issued according to Mr. Poulin) Mr. Poulin was the appellant's director and president and he was dismissed in 2001;

d. he does not recall whether his $7.50 cheque payable to the appellant for the 75 subscribed ordinary Class "C" shares had been cashed;

e. he did not know who had prepared and sent the appellant's annual return for 2000 to the Inspecteur général des institutions financières;

f. he never orally agreed with Mr. Brosseau to the non-issuance of the 75 ordinary Class "C" shares in the appellant, to which he had subscribed for consideration of an amount equal to that which he would have received under the terms of the Agreement if the shares in question had been issued;

g. he recalls (see page 64 of the transcript) having indicated, in his income tax report for the 2003 taxation year, that the $135,843 was employment income, in accordance with he T-4 information slip he had received from the appellant (Exhibit A-1, Tab 8).

Analysis and conclusion

[18] The respondent essentially submits that the sum of $135,843 the appellant paid to Mr. Poulin in 2003 was used to purchase the 75 ordinary Class "C" shares that Mr. Poulin held in the appellant's capital stock, resulting in a deemed dividend pursuant to subsection 84(3) of the Act. On the other hand, the appellant submits that the amount paid to Mr. Poulin should be treated as compensation for services rendered, which is fully deductible pursuant to paragraph 18(1)(*a*) of the Act, and not a dividend since Mr. Poulin never held the 75 ordinary Class "C" shares in the appellant to which he had subscribed and therefore, never received a dividend. It seems to me then, that the only question to answer is the following: were the 75 ordinary Class "C" shares of the appellant's capital stock to which Mr. Poulin had subscribed issued?

[19] Under the Agreement (Exhibit I-1, Tab 1), the appellant granted Mr. Poulin an option to subscribe to 75 of the 1,000 voting and participating shares to be created following the freeze for consideration of $1 per share. Under the Agreement, the appellant made a prior and irrevocable commitment to issue these shares to Mr. Poulin once the latter had exercised the option. The agreement corresponds somewhat to an order of intent and the appellant is required to follow through. Once the option was exercised, the appellant and Mr. Poulin were required to respect the contract, namely on one hand to issue the 75 voting and participating shares and on the other, take and pay for them. The evidence showed beyond a doubt that Mr. Poulin exercised the option. However, the following question remains: were these subscribed shares actually issued?

[20] The issuance and distribution of shares generally involves three stages: a resolution by the board of directors to order the issuance, entries to the share register ordering them, and lastly the delivery of the share certificates, which, to a certain extent, provide *prima facie* evidence that they were issued and makes the share transfer easier. In this case, the appellant's Regulation No. 21 (Exhibit A-1, Tab 15) clearly stipulates that: (i) the appellant's capital stock shares may be distributed at the times, in the manner and to the persons or categories of persons that the directors may occasionally determine by resolution; (ii) the appellant was to keep records at its head office that included the names of all persons who were or had been shareholders in the company in alphabetical order, the number of securities held by each shareholder, and the details of the issuance and transfer of each share in the company's capital; and (iii) each share certificate in the company must be issued under the seal of the company and signed by the President or Vice-President and countersigned by the secretary or assistant secretary.

[21] At the end of the day, the following question must be answered: did the appellant's board of directors validly adopt a resolution ordering the issuance of the 75 ordinary Class "C" shares to which Mr. Poulin subscribed?

[22] The appellant's evidence that the shares in question were not issued is based solely on Mr. Brosseau's testimony that he came to an oral agreement with Mr. Poulin that the appellant would not issue the shares in question to which he had subscribed and it would instead pay him compensation (in regard to the services he had rendered) calculated based on these non-issued shares. The question, for me, is the following: was Mr. Brosseau's testimony credible and likely? To answer this question, the following evidence that was offered to me that seems to contradict his testimony must be considered::

i. first, Mr. Poulin testified that he never agreed with Mr. Brosseau that the appellant would not issue the shares to which he had subscribed;

ii. on February 15, 2001, the appellant made Mr. Poulin an offer (Exhibit I-1, Tab 3) [TRANSLATION] "to redeem the 75 voting and participating shares in RNCI acquired…pursuant to the Capital Profit Sharing Agreement entered into by the parties on March 19, 1998." The use of the word "redeem" could lead us to conclude that the shares in question had been issued;

iii. the use of the word "redeem" in the settlement offer dated August 22, 2002 (Exhibit I-1, Tab 6) could also lead us to conclude that the shares in question had been issued;

iv. the appellant's information report obtained from the Inspecteur général des institutions financières (Exhibit I-1, Tab 5) indicates that as of December 19, 2000 (date the appellant's last annual return was filed) Mr. Poulin was the director and the appellant's second shareholder.

[23] Considering the following, what is the probative value of Mr. Poulin's testimony?

i. He did not agree with Mr. Brosseau that the appellant not issue the shares to which he had subscribed; in his opinion, the evidence of this fact was that on August 15, 2000, Mr. Hertel, the appellant's secretary, had him sign (as the appellant's president as required under its Regulation No. 21) the original share certificate attesting that the shares in question were issued and also gave him a copy of the front of the original certificate. Mr. Poulin explained that he did not verify whether the formalities for issuing the shares had been followed, considering he was given the original share certificate to sigh, attesting to the issuance of the shares in question. Mr. Poulin's testimony on this should be cited:

> [TRANSLATION]
> I did not conduct any verification, the certificate confirmed that I had 75 shares. I was comfortable with that, I was sure of that acquisition.

ii. He did not participate nor was he summoned to a meeting of the appellant's board of directors at which the issuance of the shares in question was allegedly ordered.

According to Mr. Poulin's testimony, the meeting of the appellant's board of directors, at which the issuance of the shares in question was allegedly ordered, was held without his knowledge. It is very difficult for me to believe that such a meeting could have been held without Mr. Poulin's knowledge because of his duties within the appellant's business and their harmonious relations until he was dismissed. Moreover, it is just as difficult to believe that Mr. Poulin (who was the appellant's director and chief officer at the time such a meeting of the board of directors would have been held) assumed that all the formalities for the shares in question to be issued

had been respected simply because he had been given the original share certificate to sign. At any rate, a director who is also the chief officer of a company incorporated under the *Companies Act* cannot in such circumstances rely on the rule of the internal governance provided under section 123.32 of that act. Lastly, Mr. Poulin's irrational behaviour only confirms my doubts regarding his credibility. Why did Mr. Poulin not object when the appellant made source deductions in the settlement offer of August 22, 2002, and then issued a T-4 information slip indicating that the $135,543 was employment income unless he had agreed with Mr. Brosseau that the appellant would not issue the shares to which he had subscribed and that it would pay him compensation instead for the services rendered, calculated based on the shares that should have been issued? Why did Mr. Poulin declare income of $135,843 in 2003 in accordance with the T-4 information slip if not for that same reason? Why did Mr. Poulin not ask Justice Morneau (in his civil case) to order the issuance of the shares in question when Mr. Brosseau told him on November 1, 2001, that the shares in question had not been issued (see Exhibit A-1, Tab 6, paragraph 6)? In my opinion, the fact Mr. Poulin had agreed with Mr. Brosseau that the appellant would not issue the shares in question could explain such behaviour. The unlikelihood of Mr. Poulin's testimony and his irrational behaviour on these aspects only strengthened my belief that Mr. Brosseau's testimony (regarding the agreement he had with Mr. Poulin) is credible and likely despite some documentation brought to my knowledge that seems to support the theory that the shares in question were issued.

[24] At the end of the day, the version of the facts provided by Mr. Brosseau seems more credible to me than that provided by Mr. Poulin. Mr. Brosseau's explanations regarding the inappropriate choice of the words "share redemption" (when they had not been issued) in the settlement offers of February 15, 2001, and August 22, 2002, also seemed credible to me. I must note that Mr. Brosseau explained that he had not paid much attention to the language used in these two settlement offers considering the verbal agreement he and Mr. Poulin had come to, under which the compensation agreed to would be calculated based on the non-issued shares. In this regard, the settlement offer of August 22, 2002, very clearly shows the confusion that results from the language used: the words "share redemption" are used while the same document indicates that the shares were not issued.

[25] The information report on the appellant obtained from the Inspecteur général des institutions financières (Exhibit I-1, Tab 5) also seems to indicate that the shares in question were issued. Considering it was impossible to obtain the name of the person that had prepared and submitted this document to the Inspecteur général des institutions financières from Mr. Brosseau or Mr. Poulin, I feel it must not be granted too much probative value in the circumstances.

[26] The Minister's theory that the shares had been issued is not based on the appellant's corporate books and records. On this, I note Mr. Lavallée's statements. He stated that during the review of the appellant's books and records, he could not find the directors' written resolution ordering the issuance of these shares (or the minutes of any meeting of the board of directors that reported a decision by its members to issue them and the consideration required from Mr. Poulin), entries in the appellant's share register indicating that the shares had been issued to Mr. Poulin, nor the original share certificate that was allegedly issued to Mr. Poulin and that would necessarily have been cancelled following the alleged redemption of the shares. In fact, the Minister's position was that the issuance of these shares resulted from the Superior Court judgment. On this, the Minister's submissions at paragraphs 7 and 25.1 of the Response to the Notice of Appeal should be cited. Paragraph 7 states:

> [TRANSLATION]
> He denies paragraph 11 of the Notice of Appeal, as written. He states that the appellant neglected to issue the shares to Mr. Poulin following the conclusion of the share acquisition contract. According to the Superior Court judgment, following the action brought by Mr. Poulin against the appellant, the shares were issued because the appellant was ordered to redeem them and pay the amount of $135,843 to Mr. Poulin.

And paragraph 25 states:

> [TRANSLATION]
> It is true the appellant neglected to issue the 75 ordinary Class "C" shares to Mr. Poulin after accepting the subscription on August 15, 2000. However, by ordering the appellant to redeem the 75 shares for the amount of $135,843, the Superior Court required it to correct this error. The appellant cannot claim today that the 75 shares were not issued.

[27] In my opinion, Justice Morneau's judgment does not in any way order the appellant to correct its error (as claimed by the Minister) by issuing the 75 Class "C" shares. The judgment essentially orders the appellant to redeem the 75 Class "C" shares for $135,843. I am of the view that Justice Morneau presumed that the shares to which Mr. Poulin had subscribed had been issued by the appellant, since:

1. on February 15, 2001, the appellant had proposed (Exhibit I-1, Tab 3) to Mr. Poulin that it redeem [TRANSLATION] "the 75 voting and participating capital stock shares in RNCI acquired…pursuant to the capital profit-sharing agreement entered into by the parties on March

19, 1998, and [denies] pay[ment] to Mr. Poulin, in consideration of the said redemption, the amount of $59,193;"

2. in the context of a settlement offer dated August 22, 2002, the appellant had paid Mr. Poulin compensation of $468,986 (Exhibit I-1, Tab 6).

[28] As a result, the appellant has persuaded me that it had paid Mr. Poulin the amount of $135,843 in 2003 as compensation for the serviced he had rendered. Therefore, the appellant was entitled to deduct the amount of $135,843 in the calculation of its income for the year in question.

[29] For these reasons, the appeal is allowed, with costs.

Signed at Ottawa, Canada, this 16th day of February 2011.

"Paul Bédard"

Bédard J.

Translation certified true
on this 15th day of April 2011.

François Brunet, Revisor

CITATION:	2011 TCC 92
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PLACE OF HEARING:	Montréal, Quebec
DATE OF HEARING:	October 18, 2010
REASONS FOR JUDGMENT BY:	The Honourable Justice Paul Bédard
DATE OF JUDGMENT:	February 16, 2011

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