

Docket: 2010-626(IT)I

BETWEEN:

RONALD B. GRIST,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeals heard on June 6 and 7, 2011, at Hamilton, Ontario

By: The Honourable Justice Brent Paris

Appearances:

Agent for the Appellant: Michel D. Cote
Counsel for the Respondent: Jasmeen Mann

JUDGMENT

The appeals from reassessments made under the *Income Tax Act* for the 2001, 2002, 2003 and 2004 taxation years are dismissed.

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

« B. Paris »

Paris J.

Citation: 2011 TCC 304
Date: 20110616
Docket: 2010-626(IT)I

BETWEEN:

RONALD B. GRIST,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Paris J.

[1] These are appeals from reassessments of the Appellant's 2001 to 2004 taxation years. The Minister of National Revenue disallowed the Appellant's claim for a business investment loss of \$199,999 in his 2004 taxation year, and disallowed the related non-capital loss carry backs to his 2001, 2002 and 2003 taxation years. The Appellant claimed the business investment loss on the disposition of 200,000 shares of PSC Financial Services Ltd. ("the Corporation") on May 20, 2004.

[2] The issues in these appeals are:

- (i) whether the Appellant paid \$200,000 to acquire the shares; and
- (ii) whether the Corporation was a "small business Corporation" as defined in subsection 248(1) of the *Income Tax Act* in the 12 months preceding the disposition of the shares. A business

investment loss is only available under subparagraph 39(1)(c)(iii) of the *Act* on the disposition of shares of a “small business corporation.”

Background

[3] All of the companies to which I will refer in these reasons were incorporated by Mr. Michael Cote (whose name also appears in certain places as “Michel Cote”). Except for the Corporation, the evidence did not disclose who the shareholders of the various companies were.

[4] Mr. Cote is an accountant. Since at least 1999, he has also operated an accounting firm through Cote and Associates Professional Corporation (CAPC). He was the Appellant’s accountant, and represented him at the hearing of these appeals.

[5] The Corporation at issue, PSC Financial Services Ltd., was created by the amalgamation of PSC Financial Services Ltd., Cougar Financial Advisors Inc. and Commonwealth Bancorp Ltd. on June 13, 2004.

[6] Previously, on August 7, 2002, Commonwealth Bancorp Ltd. was created by the amalgamation of Commonwealth Bancorp Ltd. and Commonwealth Financial Group Inc. The original Commonwealth Bancorp Ltd. was incorporated in mid-1999.

[7] All of the companies set up by Mr. Cote including CAPC allegedly operated out of an office in Fergus, Ontario, but except in the case of the Corporation and CAPC, the evidence of this is scant. Likewise, there was little evidence of what activities the companies other than the Corporation and CAPC carried on.

[8] The Appellant’s involvement with the Corporation began in 1999, when he was first induced to invest in Commonwealth by Mr. Cote. Over the next year or two, the Appellant said he purchased shares in Commonwealth as well as debentures issued by it. He estimated his total investment at approximately \$285,000, of which \$200,000 was for the purchase of 200,000 shares.

[9] The Respondent submitted that the Appellant had not shown that he had paid the \$200,000 consideration for the shares but there was sufficient documentary evidence combined with credible oral evidence from the Appellant to convince me that he did pay the amounts in question. In addition to a cheque dated August 17, 2000 for \$100,000 payable to Commonwealth, there was evidence that certain Nortel and BCE shares held by the Appellant's spouse and mother-in-law were sold to provide funds to purchase the shares. The Appellant testified Mr. Cote was given authority to sell these shares on his family's behalf and that the proceeds were used to buy shares.

[10] The Appellant also produced copies of share subscription agreements signed by him dated November 10, 1999, February 9, 2000 and August 17, 2000. Those agreements indicate that he acquired a total of 200,000 common shares in Commonwealth on those dates at a cost of \$200,000,

[11] The Appellant said that the business of the Corporation was to earn interest on short-term loans it made to private businesses that required capital. However, it lost a significant amount of money and ceased operations in late 2003 or early 2004. The Ontario Financial Services Commission began an investigation into the activities the Corporation in 2004, and seized most, if not all, of its records. The records were returned a few years later. The results of the investigation were not disclosed to the Court.

[12] After the Corporation ceased operating, the Appellant disposed of his shares to CAPC for \$1 under an agreement dated May 20, 2004. Although the Appellant had little recollection of the agreement, he recognized his signature on it. It is apparent that Mr. Cote orchestrated the sale of the Appellant's shares to CAPC in order to crystallize the loss on the shares, and that the Appellant consented to the sale. The Appellant also presented a receipt signed by him and given to CAPC for the \$1 consideration. In light of this evidence, I accept that there was a disposition of his shares on May 20, 2004 for \$1.

[13] In order to have a business investment loss on the disposition of the shares the Appellant must show that, within the 12 months preceding the disposition, the Corporation was a small business corporation as defined in subsection 248(1) of the *Act*. The relevant parts of that definition read as follows:

248(1) In this *Act*,

"small business Corporation", at any particular time, means, ... a particular Corporation that is a Canadian-controlled private Corporation all or substantially all of the fair market value of the assets of which at that time is attributable to assets that are

- (a) used principally in an active business carried on primarily in Canada by the particular Corporation or by a Corporation related to it,
- (b) ...
- (c) assets described in paragraphs (a) ... including, for the purpose of paragraph 39(1)(c), a Corporation that was at any time in the 12 months preceding that time a small business Corporation, and, for the purpose of this definition, the fair market value of a net income stabilization account shall be deemed to be nil;

[14] According to paragraph (c) of this definition, to qualify as a small business corporation, all or substantially all the Corporation's assets must have been used principally in an active business carried on it at some point within the 12 months leading up to May 20, 2004.

[15] "Active business" is defined in subsection 248(1) to exclude, *inter alia*, a "specified investment business":

"active business", in relation to any business carried on by a taxpayer resident in Canada, means any business carried on by the taxpayer other than a specified investment business or a personal services business;

[16] Subsection 248(1) gives the term "specified investment business" the meaning assigned by subsection 125(7) of the *Act*. That definition reads:

"specified investment business" carried on by a Corporation in a taxation year means a business (other than a business carried on by a credit union or a business of leasing property other than real property) the principal purpose of which is to derive income (including interest, dividends, rents and royalties) from property but, except where the Corporation was a prescribed labour-sponsored venture capital Corporation at any time in the

year, does not include a business carried on by the Corporation in the year where

- (a) the Corporation employs in the business throughout the year more than 5 full-time employees, or
- (b) any other Corporation associated with the Corporation provides, in the course of carrying on an active business, managerial, administrative, financial, maintenance or other similar services to the Corporation in the year and the Corporation could reasonably be expected to require more than 5 full-time employees if those services had not been provided;

[17] The Respondent argued that the Corporation carried on a “specified investment business” at all material times because its principal purpose was to earn income from property and it did not employ more than 5 full-time employees.

[18] According to the notes to the financial statements of the Corporation for its fiscal periods ending June 30, 2002 and June 18, 2003, its business was the provision of merchant banking services for businesses in Ontario. This accords with the Appellant’s evidence that the Corporation’s business was lending money to private businesses. It was not shown that the Corporation carried on any other business at any point in the 12 months leading up to the share disposition.

[19] The Appellant did not dispute that the principal purpose of the Corporation was to earn income from property but maintained that the Corporation fell within the exception listed in paragraph (b) of the definition of “specified investment business”. He said that other corporations associated with the Corporation provided it with managerial, administrative, financial, maintenance or other similar services and that the Corporation could reasonably have been expected to require more than 5 full-time employees if those services had not been provided by those associated corporations.

[20] Unfortunately, the Appellant has presented no evidence to support the position that, in the 12 months before May 20, 2004, or at any other time, the Corporation was associated with any other company within the meaning of subsection 256(1) of the *Act*.

[21] Subsection 256(1) provides that, for the purposes of the *Act*, one corporation is associated with another in a taxation year, if at any time during the year:

- (a) one of the corporations controlled, directly or indirectly in any manner whatever, the other;
- (b) both of the corporations were controlled, directly or indirectly in any manner whatever, by the same person or group of persons;
- (c) each of the corporations was controlled, directly or indirectly in any manner whatever, by a person and the person who so controlled one of the corporations was related to the person who so controlled the other, and either of those persons owned, in respect of each corporation, not less than 25% of the issued shares of any class, other than a specified class, of the capital stock thereof;
- (d) one of the corporations was controlled, directly or indirectly in any manner whatever, by a person and that person was related to each member of a group of persons that so controlled the other corporation, and that person owned, in respect of the other corporation, not less than 25% of the issued shares of any class, other than a specified class, of the capital stock thereof; or
- (e) each of the corporations was controlled, directly or indirectly in any manner whatever, by a related group and each of the members of one of the related groups was related to all of the members of the other related group, and one or more persons who were members of both related groups, either alone or together, owned, in respect of each corporation, not less than 25% of the issued shares of any class, other than a specified class of the capital stock thereof.

[22] On the evidence that was presented, I cannot determine whether the conditions set out in any of paragraphs (a) through (e) of subsection 256(1) were met in this case with respect to the Corporation and any other company.

[23] Likewise, the evidence fails to show what services any other company provided to the Corporation. All I have before me is the Appellant's testimony that he saw 8 or 9 people working in the Fergus office when he visited it, and that some of them helped him by witnessing documents he was required to sign at various times. He also testified that he was under the impression that those employees were "part and parcel of the whole operation". Later in his testimony, the Appellant stated that he believed CAPC did all the work for the Corporation and that the Corporation was "the investment part". Given the vagueness of his testimony, I am not satisfied that the Appellant had any knowledge of how the Corporation or any of the other companies were operated. If the Fergus office was the office for all of

the companies set up by Mr. Cote, including CAPC and the Corporation, the presence of employees on those premises would not be necessarily be conclusive that those employees worked for the Corporation.

[24] Mr. Cote did not testify at the hearing. In light of his apparently extensive involvement in the affairs of the Corporation, as well as his involvement in the affairs of CAPC and all of the other companies, I infer that his testimony would not have been favourable to the Appellant's position either regarding the Corporation's relationship to the other companies or regarding any services provided to the Corporation by the other companies.

[25] In any event, it was not established by the Appellant that the Corporation was associated with any of these other companies, or that the level of managerial, administrative, financial, maintenance or other similar services referred to in paragraph (b) of the definition of "specified investment business" was provided to the Corporation by them.

[26] In conclusion, the Appellant has not shown that the Corporation was a small business corporation at the material time. Therefore, the loss from the disposition of the shares does not qualify as a business investment loss.

[27] For these reasons, the appeals are dismissed.

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

"Brent Paris"

Paris J.

CITATION: 2011 TCC 304

COURT FILE NO.: 2010-626(IT)I

STYLE OF CAUSE: RONALD B. GRIST and
HER MAJESTY THE QUEEN

PLACE OF HEARING: Hamilton, Ontario

DATE OF HEARING: June 6 and 7, 2011

REASONS FOR JUDGMENT BY: The Honourable Justice Brent Paris

DATE OF JUDGMENT: June 16, 2011

APPEARANCES:

Agent for the Appellant: Michel D. Cote
Counsel for the Respondent: Jasmeen Mann

COUNSEL OF RECORD:

For the Appellant:

Name: Michel D. Cote

Firm:

For the Respondent: Myles J. Kirvan
Deputy Attorney General of Canada
Ottawa, Canada