Federal Court of Appeal | Cour d'appel fédérale

Date: 20220330

Dockets: A-126-21, A-125-21, A-127-21,
A-128-21, A-129-21, A-130-21,
A-131-21, A-132-21

Citation: 2022 FCA 53

CORAM: **GLEASON J.A.**
WOODS J.A.
LEBLANC J.A.

BETWEEN:

NICOLE L. TIESSEN INTERIOR DESIGN LTD., NICOLE L. TIESSEN INTERIOR DESIGN SERVICES LTD., CHRISTOPHER WOOD TECHNICAL SERVICES LTD., CHRISTOPHER WOOD TECHNICAL LTD., JEFF OLFERT TECHNICAL SERVICES LTD., JEFF OLFERT TECHNICAL LTD., DANIEL REEVES ARCHITECT LTD., and DANIEL REEVES ARCHITECT PROF. SERVICES LTD.

Appellants

and

HER MAJESTY THE QUEEN

Respondent

Heard by online video conference hosted by the registry on March 17, 2022.

Judgment delivered at Ottawa, Ontario, on March 30, 2022.

REASONS FOR JUDGMENT BY: WOODS J.A.

CONCURRED IN BY: GLEASON J.A.
LEBLANC J.A.

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REASONS FOR JUDGMENT

WOODS J.A.

[1] These appeals concern an anti-avoidance provision in the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) (the Act) that, if applicable, deems two or more corporations to be associated. In the court below, the Tax Court agreed with the Crown that this provision applied to deem 30

corporations to be associated with each other for purposes of calculating the small business deduction under the Act (*per* Monaghan J., as she then was). The decision, cited as 2021 TCC 29, has been appealed to this Court.

[2] The anti-avoidance provision in s. 256(2.1) is based on a purpose test. In relevant part, the provision deems two or more corporations to be associated with each other for purposes of the Act where "it may reasonably be considered that one of the main reasons for the separate existence of those corporations in a taxation year is to reduce the amount of taxes that would otherwise be payable under this Act …". This test is central to the merits of these appeals.

[3] Thirty corporations were reassessed under this provision for their 2012 and 2013 taxation years. Each corporation filed an appeal in the Tax Court. Of the 30 appeals, 22 were stayed pending a final decision on appeals by 8 corporations which are the Appellants in these appeals.

Background

[4] The reasons of the Tax Court are clear and thorough. It is not necessary that this Court provide the background facts in detail and so a brief overview is provided below.

[5] The reassessments issued to the Appellants stem from a reorganization of an architecture and interior design business from a corporate model to a corporate partnership model.

[6] Prior to the reorganization, the business was carried on primarily through one corporate entity. The corporation's shareholders consisted of 15 professional employees of the business (Principals) and their spouses.

[7] In late 2010 through early 2011, the reorganization was undertaken and the business was transferred to a newly-formed partnership.

[8] The corporate partnership involved 30 corporations, comprising 15 partners of the partnership (Partnercos) and 15 service corporations (Servicecos). Of these, 29 were newly created and one was repurposed. Each Principal controlled a pair of corporations, Partnerco and Serviceco.

[9] Each Partnerco and Serviceco entered into a service agreement under which Serviceco agreed to provide the services of its relevant Principal to Partnerco to enable Partnerco to perform its partnership duties. For this purpose, each Serviceco entered into an employment agreement with its respective Principal.

[10] In the relevant period, the partnership allocated income to each Partnerco. Each Partnerco paid fees to its respective Serviceco for providing the services of its Principal. Each Partnerco deducted the fees in computing income and each Serviceco included the fees in its income. The income of the Serviceco was reduced by a modest salary paid to its respective Principal.

[11] The Appellants filed their income tax returns for the 2012 and 2013 taxation years on the basis that the anti-avoidance provision did not apply to deem any of the corporations to be associated. Each paired Partnerco and Serviceco were considered to be associated with each other by virtue of common control (s. 256(1)(b) of the Act). However, the pair was not considered to be associated with any other pair. The result was that the income limit (the "business limit") applicable in the calculation of the small business deduction was determined separately for each paired Partnerco and Serviceco.

[12] Whereas under the corporate model there was a single business limit available for the entire architectural and interior design business, the tax filings for the corporate partnership model reflected that 15 business limits were available, one for each Partnerco and Serviceco pair. The result was a multiplication of the small business deduction in respect of the income earned from the architectural and interior design business.

The Tax Court decision

[13] The Tax Court concluded that at least one of the main reasons for the reorganization and for the separate existence of the 30 corporations was the reduction of taxes by greater access to the small business deduction. The trial judge wrote that "[m]ultiplication of the SBD was the reason the Reorganization was proposed and the resulting tax savings presented to the Principals led to the decision to undertake the Reorganization." (para. 38).

[14] The trial judge recognized that s. 256(2.1) of the Act required her to consider whether "it may reasonably be considered that one of the main reasons for the separate existence of two or more corporations in a taxation year is to reduce taxes that would otherwise be payable under the Act" (para. 39). However, she commented that in this case, "the reasons for establishing the corporations and their separate existence are inextricably linked because the fifteen pairs were always part of the planned Reorganization and considered necessary to effect it." (para. 40).

[15] The Tax Court's analysis focused on the history of the reorganization and the reasons for pursuing the corporate partnership model. The trial judge considered several reasons for this model as advanced by the Appellants, and noted that the only evidence in support of the Appellants' theory was the Appellants' *viva voce* evidence, which she described as "*ex post facto* assertions of purpose" (para. 92).

[16] Ultimately, the trial judge rejected the Appellants' asserted reasons. She wrote: "for the most part, I am not persuaded they were main reasons for the Reorganization, or the separate existence of the thirty corporations that it required." (para. 92). Instead, she accepted the Crown's theory that the multiplication of the small business deduction was one of the main reasons for the reorganization and the separate existence of the paired Partnercos and Servicecos (para. 155).

Analysis

[17] The Appellants submit that the Tax Court erred in determining that s. 256(2.1) of the Act applies to the reorganization as a whole as opposed to each pair of corporations separately. They take no issue with the Tax Court's determination that one of the main purposes of the reorganization was the reduction of taxes. However, the Appellants assert that the Court misinterpreted s. 256(2.1), and that absent this error the Court would have concluded that s. 256(2.1) does not apply.

[18] Subsection 256(2.1) of the Act provides:

256. (2.1) For the purposes of this Act, where, in the case of two or more corporations, it may reasonably be considered that one of the main reasons for the separate existence of those corporations in a taxation year is to reduce the amount of taxes that would otherwise be payable under this Act or to increase the amount of refundable investment tax credit under section 127.1, the two or more corporations shall be deemed to be associated with each other in the year.	**256. (2.1)** Pour l'application de la présente loi, s'il est raisonnable de considérer qu'un des principaux motifs de l'existence distincte de plusieurs sociétés au cours d'une année d'imposition consiste à réduire les impôts qui seraient payables par ailleurs en vertu de la présente loi ou à augmenter le crédit d'impôt à l'investissement remboursable prévu à l'article 127.1, ces sociétés sont réputées être associées les unes aux autres au cours de l'année.

[19] As I understand the Appellants' position, they submit that the Tax Court misinterpreted 256(2.1) in two ways:

(a) The Court erred in considering the purpose of undertaking the reorganization. Instead, the Court should have considered the purpose of the separate existence of two or more corporations. They submit that these tests should not be conflated.

(b) The Court erred in considering the anticipated reduction of taxes by 30 corporations. Instead the Appellants submit that s. 256(2.1), properly interpreted, requires a focus on a particular taxpayer who has been reassessed. Accordingly, the Tax Court should have considered the purpose test from the perspective of each Appellant separately, that is, one Partnerco or one Serviceco.

[20] The Appellants suggest that s. 256(2.1) has no application to these appeals if the Court applies the proper interpretation of s. 256(2.1). The anticipated tax reduction for any particular Appellant is influenced only by the existence of its pair with which it is associated. The tax reduction is not affected by the existence of the other 28 corporations. Accordingly, s. 256(2.1) does not have the effect of deeming all 30 corporations to be associated with each other.

[21] It is first necessary to consider a preliminary matter. The Crown submits that the Appellants' argument is a new issue that was not raised in the Court below. The Appellants do not dispute this.

[22] The Crown suggests that to raise this issue for the first time in this Court is prejudicial and the Court should not consider it. I agree, but for reasons that differ slightly from the Crown's.

[23] The focus in the Tax Court was on the various tax and non-tax reasons for undertaking the reorganization. The issue raised in this Court is legally and factually different. It is a new issue.

[24] The general legal principles to be applied in determining whether a court should consider a new issue is set out in *Athey v. Leonati*, [1996] 3 S.C.R. 458, 140 D.L.R. (4th) 235 at paras. 51-52:

> 51 In any event, the Court of Appeal erred in refusing to consider the appellant's arguments on the grounds they were not raised at trial. The general rule is that an appellant may not raise a point that was not pleaded, or argued in the trial court, unless all the relevant evidence is in the record: John Sopinka and Mark A. Gelowitz, *The Conduct of an Appeal* (1993), at p. 51. In this case, all relevant evidence was part of the record. In fact, all the requisite findings of fact had been made. The point raised by the appellant was purely a question of law.
>
> 52 Most importantly, the respondents did not suffer prejudice, since they would not have proceeded any differently even if the appellant had expressly relied on *McGhee v. National Coal Board* and *Bonnington Castings, Ltd. v. Wardlaw*, *supra*, from the very beginning. The defence theory was that the disc herniation was not causally related in any way to the injuries suffered in the motor vehicle accidents. The respondents could not have made any more emphatic defence than this. This was a case where "had the question been raised at the proper time, no further light could have been thrown upon it": *Lamb v. Kincaid* (1907), 38 S.C.R. 516, at p. 539, *per* Duff J. (as he then was). Given that the appellant's arguments raised an issue of law which did not require any further evidence (or indeed any further findings of fact) and which would not have caused any prejudice to the respondents, it was an error for the Court of Appeal to refuse to consider the argument.

(See also *Quan v. Cusson*, 2009 SCC 62, [2009] 3 S.C.R. 712 at paras. 36-39.)

[25] In my view, if the new issue had been raised in the Tax Court it is quite possible that further light "could have been thrown upon it". The Appellants submit that the determination of

the reasons for the separate existence of the corporations should be considered from the perspective of each corporation separately. This engages an inquiry that is factually and legally different from the inquiry before the Tax Court. The new issue, if raised earlier, would likely have led to further evidence, factual findings, and legal argument.

[26] This concern is illustrated by considering a statement in the Appellants' memorandum in this Court. The memorandum refers to testimony in the Court below to the effect that "the Principals were advised that any one of them could choose to organize a different way, including by not incorporating a Serviceco." (Appellants' memorandum at para. 7(d)).

[27] I note that the Partnership Agreement that is in the record appears to provide otherwise. My interpretation of arts. 3.01 and 5.08 of that agreement is that all Principals are required to employ the Partnerco/Serviceco structure.

[28] If the new issue had been raised in the Tax Court, it is quite possible that further light would have been shone on this testimony and the Partnership Agreement, and more generally the circumstances relating to the existence of the 30 corporations.

[29] This illustrates that the evidence and factual findings in the Tax Court may well have been different had the parties been focussed before the Tax Court on the issue raised by the Appellants in these appeals. In my view, the Crown would be prejudiced if this Court were to consider this issue now and the Court should not do so.

[30] In light of this conclusion, it is not necessary to discuss the merits of the Appellants' arguments.

[31] Finally, I would mention that the parties agree that the style of cause in these appeals requires a correction. Therefore, the style of cause will be amended to be consistent with the style of cause above.

[32] I would dismiss these appeals with costs.

"Judith Woods"
J.A.

"I agree.
Mary J.L. Gleason J.A."

"I agree.
René LeBlanc J.A."

FEDERAL COURT OF APPEAL

NAMES OF COUNSEL AND SOLICITORS OF RECORD

DOCKETS:	A-126-21, A-125-21, A-127-21, A-128-21, A-129-21, A-129-21, A-130-21, A-131-21, A-132-21
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CONCURRED IN BY:	GLEASON J.A. LEBLANC J.A.
DATED:	MARCH 30, 2022

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