CORAM: THE CHIEF JUSTICE
STONE J.A.
McDONALD J.A.

BETWEEN:

A-626-96

HER MAJESTY THE QUEEN

Applicant

- and -

BAYSIDE DRIVE-IN LTD.

Respondent

A-627-96

HER MAJESTY THE QUEEN

Applicant

- and -

ANNE T. MUSIAL

Respondent

A-628-96

HER MAJESTY THE QUEEN

Applicant

- and -

BAYSIDE DRIVE-IN LTD.

Respondent

A-629-96

HER MAJESTY THE QUEEN

Applicant

- and -

DAVID MUSIAL

Respondent

Heard at Halifax, Nova Scotia, on Tuesday, May 6, 1997.

Judgment rendered at Ottawa, Ontario, on Friday, July 25, 1997.

REASONS FOR JUDGMENT BY: THE CHIEF JUSTICE

CONCURRED IN BY: STONE J.A.
McDONALD J.A.

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REASONS FOR JUDGMENT

THE CHIEF JUSTICE

These are applications for judicial review of a judgment of the Tax Court of Canada, pronounced on 10 July 1996, allowing the respondents' appeals from determinations made by the Minister of National Revenue ("the Minister") that the respondents were not engaged during the relevant periods in insurable employment with Bayside Drive-In Ltd. ("the payor"), within the meaning of the *Unemployment Insurance Act*[1]. The applications were heard together, and these reasons are intended to dispose of all of them. A copy of the reasons will be filed in each of the files mentioned in the style of cause.

Facts

The payor is a corporation duly incorporated under the laws of the Province of Nova Scotia. It operates a fast-food restaurant on a seasonal basis, from 1 April to 30 November of each year. At all material times, the payor was a family-owned and family-run business, the outstanding shares of which were owned equally (33 1/3%) by the respondent Anne Musial ("Anne"); her spouse, Gregory Musial ("Gregory"); and their son, the respondent David Musial ("David"). Before 1990, David owned only a 5% interest in the payor, but in that year his parents transferred to him the balance of his present 33 1/3% interest.

David, Gregory and Anne were all employed by the payor during the relevant periods. However, Gregory's employment by the payor is not in issue as he did not appeal to the Tax Court from the determination made by the Minister

[1] R.S.C. 1985, c.U-1, later repealed by S.C. 1996, c.23 ["the *Act*"].

in relation to the insurability of his employment.

David was employed as operations manager by the payor from 1 April to 30 November in each of the years 1992, 1993 and 1994. His duties included ordering stock, paying the sales staff, cleaning, maintenance, cooking when necessary, and closing up at the end of each business day. Although he worked approximately 40 hours per week from 1 April to 30 November, David only received remuneration for his services from early May to October of each year. In 1992, he received a salary of $12,500 and a shareholder bonus in the amount of $6,000. In 1993, he received a salary of $13,000 and a shareholder bonus in the amount of $8,000. In 1994, he received a salary of $13,500 and a shareholder bonus in the amount of $10,000. In addition, he was paid his full salary for vacations which he took in August of each year.

Anne was also employed by the payor from 1 April to 30 November in each of the years 1992, 1993 and 1994. She worked approximately 48 hours per week. Her duties included scheduling and supervising the staff and cleaning the restaurant. In 1992, although she worked the entire season, Anne only received remuneration for her services from 7 July to 17 November. For that period, she was paid a salary of $10,500 and a shareholder bonus in the amount of $5,000. In 1993, she only received remuneration from 28 June to 12 November. For that period, she was paid a salary of $12,500 and a shareholder bonus in the amount of $10,000. She was also paid her full salary for vacations in October of each year. For the reason given below, her employment in 1994 is not in issue.

By way of contrast, non-shareholder employees of the payor were paid at the rate of $5.75 to $6.00 per hour, and 4% of their earnings at the end of each season in lieu of vacation.

On 12 June 1995, the respondents filed an application pursuant to paragraph 61(3)(a) of the *Act* for a determination by the Minister as to whether

Gregory, Anne and David were employed in insurable employment with the payor for the years 1992, 1993 and 1994.[2]

By letters dated 3 November 1995, the respondents were informed that the Minister had determined that Gregory, Anne and David were not employed by the payor in insurable employment. The Minister held, in accordance with paragraph 3(2)(c) of the *Act*, that they were in excepted employment because they and the payor were not dealing with each other at arm's length. The relevant provisions of the *Act* read:

> 3. (1) Insurable employment is employment that is not included in excepted employment ...
>
> ...
>
> 3. (2) Excepted employment is ...
>
> (c) subject to paragraph (d), employment where the employer and employee are not dealing with each other at arm's length and, for the purposes of this paragraph,
>
> (i)the question of whether persons are not dealing with each other at arm's length shall be determined in accordance with the provisions of the Income Tax Act, and
>
> (ii)where the employer is, within the meaning of that Act, related to the employee, they shall be deemed to deal with each other at arm's length if the Minister of National Revenue is satisfied that, having regard to all the circumstances of the employment, including the remuneration paid, the terms and conditions, the duration and the nature and importance of the work performed, it is reasonable to conclude that they would have entered into a substantially similar contract of employment if they had been dealing with each other at arm's length;

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[2]Subsection 61(3) of the *Act* reads in part:

> 61. (3) Where there arises in relation to a claim for benefits under this Act any question concerning
>
> (a) whether a person is or was employed in insurable employment,
>
> ...
>
> an application to the Minister for determination of the question may be made by the Commission at any time and by that person or the employer or the purported employer of that person within ninety days after being notified of the decision of the Commission.

Gregory did not appeal the determination made by the Minister. The respondents Anne and David appealed to the Tax Court of Canada pursuant to subsection 70(1) of the *Act*.[3] David appealed with respect to his employment by the payor in the years 1992, 1993 and 1994. Anne appealed the determination only with respect to her employment in the years 1992 and 1993. She did not appeal the Minister's determination with respect to her employment in 1994 because she did not have the minimum number of insurable weeks required to qualify for benefits under the *Act*, whether or not her employment was insurable within the meaning of subsection 3(1).

Judgment of the Tax Court

The learned Tax Court Judge reversed the determination made by the Minister and allowed the respondents' appeals. In reasons for judgment delivered from the bench on 27 June 1996, the Tax Court Judge held that he was entitled to conduct the appeals as "trials *de novo*" because, in his view, the Minister had failed to give sufficient weight to the facts before him; specifically, the work performed by the respondents and their contributions to the payor's success. His dispositive reasons on this threshold issue read:

> As was determined by the Federal Court of Appeal in the cases of Tignish and Ferme Richard, in order for me to consider these appeals as trials de novo I must first find that the Minister, in making his determination, acted inappropriately or capriciously or did not have all of the relevant facts before him or did not give sufficient importance to those facts. In arriving at that initial finding, the evidence produced and the credibility of the witness is important. In these appeals several exhibits were produced and the only testimony was given by Gregory Musial, who spoke not only for the Payor but also for the two workers [Anne and David]. ***Because of this evidence and the credibility of Gregory Musial, which is accepted, I have concluded that I am entitled to treat these appeals as trials de novo. The Minister seems to have concluded that the***

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[3]Subsection 70(1) reads:

> 70. (1) The Commission or a person affected by a determination by, or a decision on an appeal to, the Minister under section 61 may, within ninety days after the determination or decision is communicated to him, or within such longer time as the Tax Court of Canada on application made to it within those ninety days may allow, appeal from the determination or decision to that Court in the manner prescribed.

> ***element of the change in share control, coupled with the apparently large wages paid for hours worked were crucial. In my view, I do not find that the Minister gave sufficient importance to the work put in by the workers and their contribution to the Payor's success.***
>
> [Emphasis added][4]

The Tax Court Judge then proceeded to review the merits of the determination made by the Minister. Based on the evidence presented at the hearing of the appeal, he held that, having regard to all of the circumstances of employment, it was reasonable to conclude on the balance of probabilities that the respondents and the payor would have entered into substantially similar contracts of employment if they had been dealing with each other at arm's length. He, therefore, concluded that the Minister erred in failing to exercise the discretion conferred upon him by subparagraph 3(2)(c)(ii) to deem the respondents and the payor to be at arm's length for the purposes of the *Act*. Accordingly, he allowed the respondents' appeals.

Analysis

Paragraph 3(2)(c) of the *Act* exempts from insurability employment where the worker and the payor are not dealing with each other at arm's length. Subparagraph 3(2)(c)(i) states expressly that the question of whether or not persons are dealing with each other at arm's length "shall be determined in accordance with the provisions of the *Income Tax Act*." There is no dispute in this case that the respondents are "related persons" within the meaning of section 251 of the *Income Tax Act*[5]. Paragraph 251(2)(b)(ii) provides expressly that a corporation and a person who is a member of a related group that controls the corporation are "related persons". The relevant parts of section 251 read:

> 251. (1) For the purposes of this Act,
>
> (a) related persons shall be deemed not to deal with each other at arm's length;

[4]Reasons for Judgment, at 1-2.

[5]R.S.C. 1985 (5th supp.), c. 1, as amended [¨the *Income Tax Act*¨].

> and
> ...
>
> (2) For the purpose of this Act, "related persons", or persons related to each other, are
>
> (a) individuals connected by blood relationship, marriage or adoption;
>
> (b) a corporation and
> ...
> (ii)a person who is a member of a related group that controls the corporation, or
> ...

In subparagraph 3(2)(c)(ii), however, Parliament has conferred upon the Minister a discretionary power to deem "related persons" to be at arm's length for the purposes of the *Act* where the Minister, having regard to all of the circumstances of employment, forms the opinion that the related persons would have entered into substantially similar contracts of service if they had been at arm's length. The words "if the Minister of National Revenue is satisfied" in subparagraph 3(2)(c)(ii) make it clear that Parliament intended to confer upon the Minister an administrative discretion to make the determination. In this case, the Minister declined to exercise his discretion in favour of the respondents. The threshold issue before the Tax Court Judge was, therefore, whether the Minister made his determination in a lawful manner.

In *Attorney General of Canada v. Jencan Ltd.*[6], this Court recently had occasion to reaffirm the principles governing review by the Tax Court of Canada of ministerial determinations under subparagraph 3(2)(c)(ii). I do not propose to repeat in detail the analysis contained in the reasons for judgment in that case. It is sufficient for the purposes of disposing of these applications for judicial review to restate the governing principles first laid down by this Court in *Tignish Auto Parts Inc. v. M.N.R*[7].

Tignish, supra, requires that the Tax Court undertake a two-

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[6](unreported), File No. A-599-96, 24 June 1997 (F.C.A.).

[7](1994), 185 N.R. 73 (F.C.A.) ["*Tignish*"].

stage inquiry when hearing an appeal from a determination by the Minister under subparagraph 3(2)(c)(ii). At the threshold stage of the inquiry, review by the Tax Court is confined to ensuring that the Minister has exercised his discretion in a lawful manner. If, and only if, the Minister has exercised his discretion in a manner contrary to law can the Tax Court then proceed to a review of the merits of the determination. It is only by limiting the first stage of the inquiry in this manner that the Tax Court exhibits the degree of judicial deference required when faced with an appeal from a discretionary determination.

The specific grounds which justify interfering with the exercise of a statutory discretion, including the discretion given to the Minister by subparagraph 3(2)(c)(ii) of the *Act*, are well known.[8] The Tax Court Judge was justified in interfering with the determination made by the Minister under subparagraph 3(2)(c)(ii) only if he was satisfied that the Minister made one or more of the following reviewable errors: (i) the Minister acted in bad faith or for an improper purpose or motive; (ii) the Minister failed to take into account all of the relevant circumstances, as expressly required by paragraph 3(2)(c)(ii); or (iii) the Minister took into account an irrelevant factor. It is only if the Minister made one or more of these reviewable errors that it can be said that his discretion was exercised in a manner contrary to law, and hence that the Tax Court Judge would be justified in conducting his own assessment of the balance of probabilities as to whether the respondents would have entered into substantially similar contracts of service if they had been at arm's length.

In this case, the Tax Court Judge concluded that his interference on appeal was justified because, in his opinion, the Minister had not given "sufficient importance to the work put in by the workers and their contribution to the Payor's success." The view that a failure by the Minister to give "sufficient importance" (*i.e.*,

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[8] See Lord Macmillan's comments in *D.R. Fraser and Co. Ltd. v. M.N.R.*, [1949] A.C. 24 at 36 (P.C.), quoted with approval by the Supreme Court of Canada in *Boulis v. Minister of Manpower and Immigration*, [1974] S.C.R. 875 at 877. See also, *Friends of the Oldman River Society v. Canada (Minister of Transport)*, [1992] 1 S.C.R. 3 at 76-77; and *Canada v. Purcell*, [1996] 1 F.C. 644 at 653 (C.A.), per Robertson J.A.

weight) to specific facts is a ground for reversible error is not supported by the jurisprudence of this Court and, in my respectful view, is wrong in principle. By questioning not the relevance or truth of the facts relied upon by the Minister but simply the weight to be attached to the various facts otherwise properly considered, the Tax Court Judge, in effect, overruled the Minister's discretionary determination without first having concluded that the determination had been made in a manner contrary to law. In doing so, he improperly substituted his own independent assessment of the evidence for that of the Minister, thereby usurping the discretionary authority which Parliament clearly and unambiguously entrusted to the Minister.

There is no indication in the reasons for judgment that the Minister made any reviewable error in exercising his discretion. There is no indication, for example, that the Minister failed to consider a relevant factor pertaining to the respondents' circumstances of employment. If the Minister considered all of the relevant factors in coming to his determination, and did not consider any irrelevant factors, the Tax Court Judge was not entitled to interfere with that determination merely because he would have placed greater emphasis on some facts and less on others than the Minister did.

The failure to restrict the threshold inquiry to a review of the legality of the determination made by the Minister appears to derive from the view that, as soon as the Tax Court Judge was satisfied that the Minister had made any error in his assessment of the evidence, the appeal was transformed into a "trial *de novo*".

The term "*de novo*" was first used in this context in *Tignish, supra*. Desjardins J.A. stated for the Court that if the Tax Court finds that the Minister exercised his discretion under subparagraph 3(2)(c)(ii) in a manner contrary to law, the appeal to the Tax Court becomes a "*de novo* situation". Desjardins J.A. went on to provide the following definitions of "*de novo*" from *Black's Law Dictionary*[9]:

[9](St. Paul, Minn.: West Publishing, 1990).

> *De novo*: Anew; afresh; a second time. A *venir de novo* is a writ for summoning a jury for the second trial of a case which has been sent back from above for a new trial.
>
> *De novo* trial: Trying a matter anew; the same as if it had not been heard before and as if no decision had been previously rendered.
>
> Hearing *de novo*: Generally, a new hearing or a hearing for the second time, contemplating an entire trial in the same manner in which matter was originally heard and review of previous hearing. On hearing "de novo" court hears matter as court of original jurisdiction and not appellate jurisdiction.
>
> [emphasis added by Desjardins J.A. in *Tignish, supra*][10]

I agree that if the Tax Court Judge is satisfied that the Minister exercised his discretion in a manner contrary to law, the Tax Court is in a *de novo* situation in the sense that it must undertake an ***independent*** review of the evidence in order to assess the merits of the Minister's determination. Unfortunately, however, the use of the term "*de novo*" has, in some cases, led to confusion regarding the nature of the proceedings in an appeal to the Tax Court pursuant to subsection 70(1) from a determination by the Minister under subparagraph 3(2)(c)(ii). In my respectful view, the confusion may be due in part to a misinterpretation of the statement by Décary J.A. in *Ferme Emile Richard et Fils Inc. v. M.N.R. et al.* that, where the Minister exercises his discretion illegally, the proceedings before the Tax Court are "transformed into an appeal *de novo*".[11]

The proceedings in the Tax Court are not, and cannot be transformed into, a trial or appeal *de novo* in the formal sense of this term, as the Tax Court Judge in this case improperly assumed. As reflected in the definitions quoted above, a *de novo* hearing is one in which the reviewing tribunal determines the facts and issues based solely on the evidence before it, without regard to the determination in the inferior tribunal.

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[10] *Tignish, supra*, at 78.

[11] (1994), 178 N.R. 361 at 363 (F.C.A.).

The Tax Court's role when hearing an appeal pursuant to subsection 70(1) is to perform a review function. Because a determination by the Minister under subparagraph 3(2)(c)(ii) is pursuant to a discretionary power, accepted judicial principles require deference to the discretion which the Minister has exercised, unless it has been shown on a balance of probabilities that he exercised that discretion in a manner contrary to law. Only then is the Tax Court entitled to make an independent assessment of the evidence in order to review the correctness of the Minister's determination. At that stage, there is no new hearing and the parties do not start afresh or anew in the sense of calling their evidence and presenting their arguments again. Rather, the Tax Court must proceed with its independent assessment of the evidence on the basis of the record already before it. Thus, while the Tax Court's ***review*** of the evidence at the second stage of the inquiry is *de novo*, the appeal itself is not, and cannot be transformed into, a trial *de novo*.

This distinction would, perhaps, be of little consequence were it not for the fact that the concept of transforming the Tax Court's jurisdiction into an ¨appeal¨ or ¨trial¨ *de novo* has, in some cases, led to a premature review of the merits of ministerial determinations under subparagraph 3(2)(c)(ii) of the *Act*; that is, without a clear finding that the Minister exercised his discretion in a manner contrary to law. This is one such case. The object of review by the Tax Court is to ensure that the Minister exercised his discretion lawfully. If he did, the inquiry ends there. The Tax Court is not entitled to treat the proceedings as a "trial *de novo*" simply because it would have come to a different conclusion on the merits had it decided the issue at first instance. This is, however, precisely what the Tax Court Judge did in this case. In acting as he did, the Tax Court Judge erred in law.

For all of these reasons, I would allow the applications for judicial review, set aside the decision of the Tax Court Judge, and refer the matters back to the Tax Court of Canada for a new hearing before a different judge in a manner

consistent with these reasons.

"Julius A. Isaac"
C.J.

"I agree.
A.J. Stone J.A."

"I agree.
F.J. McDonald J.A."

FEDERAL COURT OF APPEAL

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REASONS FOR JUDGMENT