Docket: 2010-316(EI)

BETWEEN:

JOLAYNE ANVIK,

Appellant,

and

THE MINISTER OF NATIONAL REVENUE,

Respondent.

Appeal heard on July 5, 2010, at Calgary, Alberta.

Before: The Honourable Justice François Angers

Appearances:

For the Appellant:	The Appellant herself
Counsel for the Respondent:	Robert Neilson

JUDGMENT

The appeal is allowed and the decision of the Minister is vacated in accordance with the attached Reasons for Judgment.

Signed at Quebec, Quebec, this 16th day of August 2010.

"François Angers"

Angers J.

Citation: 2010 TCC 404
Date: 20100816
Docket: 2010-316(EI)

BETWEEN:

JOLAYNE ANVIK,

Appellant,

and

THE MINISTER OF NATIONAL REVENUE,

Respondent.

REASONS FOR JUDGMENT

Angers J.

[1] This is an appeal of a decision by the Minister of National Revenue (the "Minister") dated November 13, 2009 that the appellant's employment with Balancing Act Bookkeeping Services Ltd. (the "Payor") for the period from January 1, 2007 to March 31, 2009 was excluded from insurable employment. That period was in fact divided into two parts for each of which there was a different reason for excluding the employment from insurable employment.

[2] For the period from January 1, 2007 to April 5, 2008, the appellant controlled more than 40% of the voting shares of the Payor and her employment was accordingly excluded from insurable employment by virtue of paragraph 5(2)(*b*) of the *Employment Insurance Act* ("the *Act*"). For the period of from April 6, 2008 to March 31, 2009, the Payor and the appellant were not dealing at arm's length and the Minister was not satisfied that they would have entered into a substantially similar contract of employment if they had been dealing with each other at arms' length, hence the employment was excluded from insurable employment by virtue of paragraph 5(2)(*i*) and subsection 5(3) of the *Act*.

[3] The appellant does not dispute that, with respect to the first period, she did control more than 40% of the Payor's voting shares and that, during that period, her employment was therefore excluded from insurable employment pursuant to paragraph 5(2)(*b*) of the *Act*. It is also not disputed that the appellant and the Payor

are related persons as defined in subsection 251(2) of the *Income Tax Act*, since the appellant is the spouse of the person who controls the Payor. What is disputed is the Minister's decision that he was not 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 was reasonable to conclude that the appellant and the Payor would have entered into a substantially similar contract of employment if they had been dealing with each other at arm's length.

[4] Before considering the evidence in this case, it seems appropriate to state what the function of this Court is when it comes to the exclusion provisions found in subsections 5(2) and (3) of the *Act*. The Federal Court of Appeal in *Denis v. Canada (Minister of National Revenue*), 2004 FCA 26, held that:

> The function of the Tax Court of Canada judge in an appeal from a determination by the Minister on the exclusion provisions contained in subsections 5(2) and (3) of the Act is to inquire into all the facts with the parties and the witnesses called for the first time to testify under oath, and to consider whether the Minister's conclusion still seems reasonable. However, the judge should not substitute his or her own opinion for that of the Minister when there are no new facts and there is no basis for thinking that the facts were misunderstood (see *Pérusse v. Canada (Minister of National Revenue - M.N.R.*), [2000] F.C.J. No. 310 (Fed. C.A.), March 10, 2000).

[5] In deciding as he did in the present case, the Minister relied on the following assumptions of fact:

(a) the Payor was in the business of providing bookkeeping services; **(admitted)**
(b) the Payor's business was set up for the Appellant; **(denied)**
(c) the Payor began operating in 2005; **(admitted)**
(d) the Payor's business operated year round; **(admitted)**
(e) prior to April 6, 2008, the share structure of the Payor was as follows: **(admitted)**

the Appellant	50%
Arvid	50%

(f) after April 5, 2008, the share structure of the Payor was as follows: **(admitted)**

the Appellant	35%
Arvid	65%

(g) the Appellant was the wife of Arvid; **(admitted)**

(h) the Appellant's duties included running the business, obtaining the clients and doing bookkeeping; **(admitted)**

(i) on April 10, 2008, the Appellant and the Payor entered into a written agreement which included the following: **(admitted)**

  (i) position of senor bookkeeper,
  (ii) the Appellant will report to Arvid,
  (iii) effective April 16, 2008,
  (iv) compensation of $42,000 annual salary paid semi-monthly,
  (v) the Appellant will work a minimum of 35 hours per week, and
  (vi) the Appellant is entitled to 3 weeks vacation;

(j) the Payor operated out of the Appellant's personal residence; **(admitted)**

(k) the Appellant started working for the Payor when it began operations; **(admitted)**

(l) the Appellant worked full-time for the Payor from January 1, 2007 to March 31, 2009; **(admitted)**

(m) the Appellant ceased working for the Payor when she went on maternity leave; **(denied)**

(n) prior to April 6, 2008, the Appellant earned a set salary of $750.00 per month; **(denied)**

(o) after April 5, 2008, the Appellant earned a set annual salary of $42,000.00; **(admitted)**

(p) after April 5, 2008, the Payor paid the Appellant on a semi-monthly basis; **(admitted)**

(q) prior to April 6, 2008, the Appellant took an artificially low salary to remain below taxable levels; **(denied)**

(r) the Appellant's wage was arbitrarily adjusted to the greatest advantage of the Appellant; **(denied)**

(s) the Appellant had the ability to manipulate her remuneration; **(admitted)**

(t) for the period January 1, 2007 to March 31, 2009, the Appellant's remuneration was not reasonable; **(denied)**

(u) the Payor did not offer any benefit plans; **(admitted)**

(v) the Appellant's earnings were as follows: **(admitted)**

Date	Amount	Date	Amount	Date	Amount
1/1/2007	$750.00	1/3/2008	$750.00	2/1/2009	$1,750.00
2/2/2007	$750.00	4/2/2008	$750.00	16/1/2009	$1,750.00
1/3/2007	$750.00	1/3/2008	$750.00	2/2/2009	$1,750.00
3/4/2007	$750.00	1/4/2008	$820.00	16/2/2009	$1,750.00
1/5/2007	$750.00	1/5/2008	$1,634.85	2/3/2009	$1,750.00
6/6/2007	$750.00	16/5/2008	$1,513.69	16/3/2009	$1,750.00
3/7/2007	$750.00	1/6/2008	$1,191.08	1/4/2009	$1,750.00
1/8/2007	$750.00	16/6/2008	$1,727.85		
14/9/2007	$750.00	1/7/2008	$1,750.00		
2/10/2007	$750.00	16/7/2008	$1,750.00		
1/11/2007	$750.00	1/8/2008	$1,750.00		
4/12/2007	$750.00	15/8/2008	$1,685.62		
31/12/2007	$1,600.00 (bonus)	31/8/2008	$146.15		
		16/9/2008	$1,528.00		
		1/10/2008	$1,512.54		
		16/10/2008	$1,750.00		
		1/11/2008	$1,750.00		
		16/11/2008	$1,750.00		
		1/12/2008	$1,750.00		
		16/12/2008	$1,709.85		

(w) the Appellant normally worked from 8:00AM to 4:30PM, Monday to Friday; **(admitted)**

(x) the Appellant normally worked around 35 hours per week; **(admitted)**

(y) the Appellant's hours of work were somewhat flexible; **(admitted)**

(z) the Appellant's hours and days of work remained consistent before and after April 5, 2008; **(admitted)**

(aa) the Appellant kept a record of her hours work[ed]; **(admitted)**

(bb) if the Appellant worked more than 35 hours in a week, she had the choice of banking the hours or receiving overtime; **(admitted)**

(cc) the Appellant was knowledgeable and fully trained in accounting and bookkeeping; **(admitted)**

(dd) prior to forming the Payor, the Appellant worked for an arm's length accounting firm; **(admitted)**

(ee) the Appellant was the heart of the Payor's business; **(admitted)**

(ff) the Appellant ran the Payor's business; **(admitted)**

(gg) Arvid had no specific bookkeeping training; **(denied)**

(hh) Arvid held an engineering degree which he completed in June 2009; **(denied)**

(ii) the Payor's business finances were managed by both the Appellant and Arvid; **(denied)**

(jj) the Appellant had signing authority for the Payor's bank account; **(admitted)**

(kk) the management of the Payor remained consistent before and after April 5, 2008; **(denied)**

(ll) the Payor issued T4s containing the following income: **(admitted)**

	Appellant	Arvid
2006	$ 9,286	$ 9,286
2007	$10,600	
2008	$27,969	
2009	$14,198	

(mm) the Payor issued dividends as follows: **(admitted)**

	Appellant	Arvid
2006	$ 539	$ 539
2007	$28,277	$11,784
2008		$ 1,762

(nn) the intention of both the Appellant and the Payor was employment; **(admitted)**

(oo) the Appellant was employed under a contract of service with the Payor; **(admitted)**

(pp) prior to April 6, 2008, the Appellant controlled more than 40% of the voting shares of the Payor; **(admitted)**

(qq) the share structure change on April 6, 2008 was designed to enable the Appellant to qualify for employment insurance maternity benefits; **(admitted)**

(rr) the Payor got rid of all of its clients when the Appellant went on maternity leave; **(denied)**

(ss) the Payor's business decisions were made based on what was best for the Appellant; **(denied)**

(tt) the Payor's business decisions were not made in an arm's length manner; **(admitted)**

(uu) the Payor's business decisions were not reasonable; **(denied)**

(vv) the Appellant stated that her employment conditions changed after April 5, 2008 as Arvid became more involved in managing the business, her salary became based on industry standards and she no longer signed paycheques, and **(admitted)**

(ww) the Minister considered all of the relevant facts that were made available to the Minister. **(admitted)**

[6] The appellant does not dispute the facts set out under "duration" and "terms and conditions" headings in the appeals officer's review of the circumstances of her employment contained in the Report on an Appeal. Indeed, the appeals officer concludes in that report that the duration and terms and conditions of the appellant's

employment were such as could reasonably be expected in an arm's length arrangement. It is the appeals officer's conclusions regarding the nature and importance of the work as well as with respect to remuneration that the appellant argues were unreasonable in the circumstances.

[7] The appellant was very candid throughout her testimony. When she and her husband married in July 2005, they incorporated the Payor; they were equal shareholders and both were directors of the Payor. They shared ownership for income-splitting purposes as her husband was a full-time student. The services provided by the Payor were all performed by the appellant. She was the only employee; she did all the work and made all the decisions; her remuneration was paid partly in the form of salary and partly in the form of dividends and was not based on the number of hours she worked. The nature of the Payor's business corresponded with the appellant's expertise.

[8] In late 2007 and early 2008, the appellant and her spouse made the decision to have children. In order to qualify for maternity leave benefits under the unemployment insurance maternity benefits program, the appellant sold some of her voting shares to her spouse, keeping only 35% of all the voting shares in the Payor and thereby avoiding the exclusion set out in paragraph 5(2)(*b*) of the *Act*. She also resigned, effective April 16, 2008, as director of the Payor (see Exhibit A-3). She readily admits that she wanted to qualify for employment insurance benefits.

[9] On April 10, 2008, as stated in subparagraph 6(i) of the Reply to the Notice of Appeal, the appellant and the Payor entered into a written agreement. The appellant was hired, effective April 16, 2008, as a senior bookkeeper, was to report to her spouse, was to work 35 hours per week and was entitled to three weeks' vacation. Her new salary was, according to the appellant, based on the market value for equivalent work and not arbitrarily adjusted to her advantage as alleged by the appeals officer. In order to determine her salary, the appellant and the Payor relied on a market value determination based on the Robert Half *2008 Salary Guide*. The annual salary for a full charge bookkeeper, adjusted to a 35-hour week, ranged from $39,716 to $53,500. The salary itself was found to be reasonable by the appeals officer as the appellant's rate of pay was in line with market rates. She also found that the appellant was paid on a regular basis and for the actual hours she worked.

[10] The day-to-day operation of the Payor's business remained the same after April 10, 2008, except with regard to what the appellant describes as higher management. Her spouse's role increased substantially. He now made the decisions about new clients; he signed all the payor's cheques; he changed the billing process;

he was consulted on billings; he decided if dividends were to be paid; he reviewed the time sheets, he wrote letters to clients concerning new fee schedules; he made any major decisions regarding the Payor's business. The appellant admits she was the one with the expertise to run the business but says that after the sale of the shares, her spouse had sole control of the business.

[11] On January 15, 2009, the appellant sent a letter to the Payor advising of the intended start date for her maternity leave, which was at first to be March 13, 2009 but was later deferred to March 31 by mutual agreement. She was last paid on March 31, 2009.

[12] Prior to the appellant's departure, the Payor had between 30 and 40 clients, which were all let go until July 2009 when the Payor took back four or five who had been waiting for the appellant's return. The appellant went back to work for the Payor in July 2009, but with reduced hours.

[13] The appellant's spouse, Arvid Anvik, testified that the Payor was incorporated to provide family income while he was an engineering student. He admits that, prior to the purchase of his wife's shares in April 2008, he had very little control of the business. All of that changed considerably after his purchase of the shares. Henceforth, he made sure that there was a sufficient cash flow to pay the bills, reviewed and increased the rates charged even though his co-shareholder did not agree, reviewed the invoices, and made all major decisions. He did not replace the appellant when she left on her maternity leave as he had by then completed his studies and was entering the work force. He did, however, hire a bookkeeper on a part-time basis (10 to 15 hours per month) in March 2010, so that the Payor could catch up on some clients' files.

[14] In terms of his bookkeeping background, Mr. Anvik took an accounting course at the high school level and did some bookkeeping for a non-profit organization during his high school years. Asked who had control over the Payor, he answered that he did.

[15] The appeals officer who made the recommendations to the Minister regarding the appellant also testified. She explained why she concluded that, for the period from April 6, 2008 to March 31, 2009, the appellant and the Payor were not dealing at arm's length and that the appellant's employment was therefore excluded from insurable employment.

[16] On the issue of remuneration, the appeals officer does not dispute that the appellant's rate of pay for that period was in line with market rates. What she does take exception to is the fact that the appellant's pay was arbitrarily adjusted to the advantage of the appellant. Prior to April 2008, the appellant was paid a salary of $750.00 a month and took the remainder of her remuneration in the form of dividends, whereas from April 2008, she received no dividends and her salary was increased to market value. This change was not based on market forces, but was made so that the appellant would qualify for EI benefits and was thus intended to benefit the appellant. In her report, the appeals officer stated the following: "In an arm's length arrangement, where the payor and the worker are bargaining with separate economic interests, one would expect the worker to bargain for the best rate of pay possible and the payor to bargain for the most skilled worker it can get at a rate the business can afford". The appeals officer continued as follows:

> To view the situation another way, imagine that the worker had consistently owned 35% of the shares (rather than being distracted by a change in share ownership). Prior to April 6, the worker took an artificially low salary, to remain below the personal income tax exemption threshold, and took the remainder of her remuneration in the form of dividends. After that date, the worker was contemplating and preparing for EI benefits and her salary was increased to "market rates", a five fold increase. Had one reviewed the entire period with a view to arm's length versus non-arm's length, this would not be considered reasonable and would, because of the ability to manipulate the remuneration based on concerns other than normal market forces, indicate a non-arm's length arrangement.

[17] On the issue of the nature and importance of the work, the appeals officer wrote the following:

> When the worker was working full time for the business it had 30 to 40 clients. The business now has just four clients, a drop of ten fold. The clients are those whose needs are simple enough that only data entry is required, or their needs can be met in the four hours a week the worker decided she wants to work and with which she can still qualify for benefits.
>
> The worker stressed that the business remains viable and paid out dividends to the shareholders. However, the business paid the worker an artificially low salary so that she could remain below the income tax exemption threshold, and also thus creating far greater profits for the business. To then say the business is viable is obtuse. It was the worker herself to stated that the business's finances are managed "as a partnership with our personal decisions", as is clear when reviewing the worker's employment. It creates a situation where the business ceases to be run according to the same principles that guide a business in the open marketplace and instead is run according to what would be best for the family; i.e. it creates a non-arm's length

> situation. It is not reasonable to conclude that an arm's length business, run based on separate economic interests, would simply be content to remain "viable" while allowing its client base to dwindle to practically nothing. One would not reasonably expect a business to gear its client base to the four hours of work per week that the worker can put in and still be eligible for EI benefits.
>
> Further, all parties concede that the worker was/is the "heart of the business". She had the knowledge, training and experience to form a company that offered specialized bookkeeping services. While she and her husband were equal shareholders, the worker ran the company. Once the worker sold some of her shares to her husband, there was an effort made to have him become more involved in the decisions regarding business operations and to "keep him in the loop". However, accounting was not Arvid's area of expertise and he would need to rely heavily on the expertise of the worker. Though this is often the case where a worker is engaged for their expertise, in this case, the worker was always at the centre of the business. Though she referred to Arvid as the boss and indicated that he made decisions, regarding loans, when to bill and approving paycheques and reimbursements, and whether to pay dividends, the statement rings hollow when further examined. The worker conceded no loans were contemplated, discussed or taken; customers were generally billed monthly and when there was the occasional exception, Arvid made the decision because the worker "kept him in the loop"; approved the payroll yet payroll documents show the worker was paid a set salary on a semi-monthly basis; and decided when to pay dividends though as previously noted, Jolayne and Arvid made all financial decisions together and ran the business's finances as a partnership with personal decisions. One could reasonably conclude that there was, in fact, little change – merely window dressing to create an artificial distance between the worker and the payor – and any change in the running of the business was less about substance and more about appearance.
>
> The job is of such a nature and importance that one would not reasonably expect the same in an arm's length arrangement.

[18] I will first deal with the remuneration issue. It is not disputed in the present case, that the rate of pay of the appellant, after she reduced her shareholding below 40%, reflected market rates and was reasonable. This new rate of pay was substantially different than that prior to the reduction in her shareholding, and rightly so. Prior to the reduction, her employment with the Payor was excluded from insurable employment by reason of the number of voting shares she owned. At that time, she was an equal shareholder with her spouse and the decision that her remuneration be paid in the form of salary and dividends was theirs to take as long as everything was done within the confines of the law. When the appellant sold some of her shares to reduce her ownership and resigned as a director of the Payor, she wanted her employment to qualify for EI benefits, but at the same time she, along with the Payor, to which she was related, had to satisfy the requirements of the *Act* in

that her contract of employment had to be substantially similar to one that would have been entered into by parties dealing at arm's length.

[19] In order to achieve that, the appellant sold some of her shares, resigned as a director, and abandoned the control she had over the Payor so that her spouse could assume the responsibilities of majority shareholder and sole director of the Payor. It may appear that the salary adjustment made in that process was to the greatest advantage of the appellant in that it may have qualified her for higher EI benefits, but it came at a price, as described above.

[20] There is nothing in the law that prevents contracts of employment between related persons, and if their contract of employment is substantially similar to one that would have been entered into by parties dealing at arm's length, the employee may qualify for EI benefits. The appellant does not deny that what she and the Payor did here was with a view to helping her obtain EI benefits during her maternity leave. So they rearranged their affairs and their relationship to achieve that.

[21] The first big hurdle was to fix a rate of pay that would be a fair market rate and reflect the type and amount of work done. She looked at the Robert Half 2008 *Salary Guide*, among others, and came up with an annual salary of $42,000 to be paid semi-monthly for a 35-hour week, and she was to have three weeks' vacation, as per the April 10, 2008 written agreement they entered into. No one disputes that the appellant provided her services to the Payor as agreed. I do not find, as the Minister did, that the appellant's rate of pay was arbitrarily adjusted to the greatest advantage of the appellant.

[22] I agree with the Minister that if one were to review the entire period in light of the arm's length versus non-arm's length issue, the remuneration would not be considered reasonable as it was based on concerns other than market forces and would indicate a non-arm's length arrangement, but this is not what we are doing. Although we are dealing with a period that includes the period prior to the reduction in the appellant's shareholding, I find it inappropriate not to sever this latter period as the reasons for excluding the employment from insurable employment are totally different for this period. I therefore find that the Minister's decision on the issue of remuneration is not reasonable.

[23] With regard to the issue of the nature and importance of the work, the Minister appears to put a lot of emphasis on the fact that one would not reasonably expect a business like the Payor to gear its client base to the four hours of work per week that the appellant could put in and still be eligible for EI benefits. With respect, I do not

believe that either what transpired outside the period under appeal or the new arrangements agreed to between the Payor and the appellant should be considered in determining the nature and importance of the work during the period under appeal. During the period under appeal, the appellant worked the full week agreed to and did the work necessary to satisfy the Payor's 30 to 40 clients.

[24] The Payor's decision to close down the business for a period of time and not hire a replacement for the appellant was, it seems to me, one that it was entitled to take. The appellant's spouse testified that his reason for so deciding was that he had completed his studies and was entering the work force. This new fact renders more acceptable the Payor's decision to reduce its client base and not replace the appellant.

[25] The appellant may have been, and was no doubt, the heart of the business, but the services rendered by the Payor to its clients could have been provided by hiring someone with similar credentials to those of the appellant. The decision not to do so rested with the Payor, but that does not make the work performed by the appellant during the relevant period any less important.

[26] Although it may appear, on the face of it, that the change in ownership of the shares did not change the way the business of the Payor was conducted, the fact remains, nevertheless, that, legally, it did create a different situation that cannot be ignored and is more than appearance.

[27] For these reasons, the appeal is allowed and the decision of the Minister is vacated.

Signed at Quebec, Quebec, this 16th day of August 2010.

"François Angers"

Angers J.

CITATION:	2010 TCC 404
COURT FILE NO.:	2010-316(EI)
STYLE OF CAUSE:	Jolayne Anvik and M.N.R.
PLACE OF HEARING:	Calgary, Alberta
DATE OF HEARING:	July 5, 2010
REASONS FOR JUDGMENT BY:	The Honourable Justice François Angers
DATE OF JUDGMENT:	August 16, 2010

APPEARANCES:

For the Appellant:	The Appellant herself
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COUNSEL OF RECORD:

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