

Docket: 2009-2669(GST)I

BETWEEN:

9114-4766 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

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Appeal heard on common evidence with the appeals of  
9113-4882 Québec inc. (2009-2670(GST)I),  
9114-4782 Québec inc. (2009-2671(GST)I),  
9114-9658 Québec inc. (2009-2672(GST)I),  
9114-4790 Québec inc. (2009-2674(GST)I),  
9114-5862 Québec inc. (2009-2675(GST)I), and  
9113-4056 Québec inc. (2009-2676(GST)I), on October 14, 15, 16, 17  
and 20, 2014, at Montréal, Quebec.

Before: The Honourable Justice Lucie Lamarre

Appearances:

Agent for the appellant: Jean Renaud  
Counsel for the respondent: Danny Galarneau

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**JUDGMENT**

The appeal from the assessment made under the *Excise Tax Act*, notice of which is dated April 14, 2005, for the period from September 10, 2002, to January 31, 2004, is allowed, and the assessment is referred back to the Minister of National Revenue for the sole purpose of deleting the penalties.

Signed at Ottawa, Canada, this 2nd day of February 2015.

"Lucie Lamarre"

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Lamarre J.

Translation certified true

On this 24th day of July 2015

Margarita Gorbounova, Translator

Docket: 2009-2670(GST)I

BETWEEN:

9113-4882 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

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Appeal heard on common evidence with the appeals of  
9114-4766 Québec inc. (2009-2669(GST)I),  
9114-4782 Québec inc. (2009-2671(GST)I),  
9114-9658 Québec inc. (2009-2672(GST)I),  
9114-4790 Québec inc. (2009-2674(GST)I),  
9114-5862 Québec inc. (2009-2675(GST)I), and  
9113-4056 Québec inc. (2009-2676(GST)I), on October 14, 15, 16, 17  
and 20, 2014, at Montréal, Quebec.

Before: The Honourable Justice Lucie Lamarre

Appearances:

Agent for the appellant: Jean Renaud  
Counsel for the respondent: Danny Galarneau

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**JUDGMENT**

The appeal from the assessment made under the *Excise Tax Act*, notice of which is dated April 14, 2005, for the period from September 10, 2002, to January 31, 2004, is allowed, and the assessment is referred back to the Minister of National Revenue for the sole purpose of deleting the penalties.

Signed at Ottawa, Canada, this 2nd day of February 2015.

"Lucie Lamarre"

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Lamarre J.

Translation certified true  
On this 24th day of July 2015

Margarita Gorbounova, Translator

Docket: 2009-2671(GST)I

BETWEEN:

9114-4782 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

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Appeal heard on common evidence with the appeals of  
9114-4766 Québec inc. (2009-2669(GST)I),  
9113-4882 Québec inc. (2009-2670(GST)I),  
9114-9658 Québec inc. (2009-2672(GST)I),  
9114-4790 Québec inc. (2009-2674(GST)I),  
9114-5862 Québec inc. (2009-2675(GST)I), and  
9113-4056 Québec inc. (2009-2676(GST)I), on October 14, 15, 16, 17  
and 20, 2014, at Montréal, Quebec.

Before: The Honourable Justice Lucie Lamarre

Appearances:

Agent for the appellant: Jean Renaud  
Counsel for the respondent: Danny Galarneau

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**JUDGMENT**

The appeal from the assessment made under the *Excise Tax Act*, notice of which is dated April 18, 2005, for the period from September 5, 2002, to October 31, 2003, is allowed, and the assessment is referred back to the Minister of National Revenue for the sole purpose of deleting the penalties.

Signed at Ottawa, Canada, this 2nd day of February 2015.

"Lucie Lamarre"

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Lamarre J.

Translation certified true  
On this 24th day of July 2015

Margarita Gorbounova, Translator

Docket: 2009-2672(GST)I

BETWEEN:

9114-9658 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

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Appeal heard on common evidence with the appeals of  
9114-4766 Québec inc. (2009-2669(GST)I),  
9113-4882 Québec inc. (2009-2670(GST)I),  
9114-4782 Québec inc. (2009-2671(GST)I),  
9114-4790 Québec inc. (2009-2674(GST)I),  
9114-5862 Québec inc. (2009-2675(GST)I), and  
9113-4056 Québec inc. (2009-2676(GST)I), on October 14, 15, 16, 17  
and 20, 2014, at Montréal, Quebec.

Before: The Honourable Justice Lucie Lamarre

Appearances:

Agent for the appellant: Jean Renaud  
Counsel for the respondent: Danny Galarneau

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**JUDGMENT**

The appeal from the assessment made under the *Excise Tax Act*, notice of which is dated April 22, 2005, for the period from September 10, 2002, to March 31, 2004, is allowed, and the assessment is referred back to the Minister of National Revenue for the sole purpose of deleting the penalties.

Signed at Ottawa, Canada, this 2nd day of February 2015.

"Lucie Lamarre"

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Lamarre J.

Translation certified true

On this 24th day of July 2015

Margarita Gorbounova, Translator

Docket: 2009-2674(GST)I

BETWEEN:

9114-4790 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

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Appeal heard on common evidence with the appeals of  
9114-4766 Québec inc. (2009-2669(GST)I),  
9113-4882 Québec inc. (2009-2670(GST)I),  
9114-4782 Québec inc. (2009-2671(GST)I),  
9114-9658 Québec inc. (2009-2672(GST)I),  
9114-5862 Québec inc. (2009-2675(GST)I), and  
9113-4056 Québec inc. (2009-2676(GST)I), on October 14, 15, 16, 17  
and 20, 2014, at Montréal, Quebec.

Before: The Honourable Justice Lucie Lamarre

Appearances:

Agent for the appellant: Jean Renaud  
Counsel for the respondent: Danny Galarneau

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**JUDGMENT**

The appeal from the assessment made under the *Excise Tax Act*, notice of which is dated May 16, 2005, for the period from July 20, 2002, to August 31, 2003, is allowed, and the assessment is referred back to the Minister of National Revenue for the sole purpose of deleting the penalties.

Signed at Ottawa, Canada, this 2nd day of February 2015.

"Lucie Lamarre"

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Lamarre J.

Translation certified true  
On this 24th day of July 2015

Margarita Gorbounova, Translator

Docket: 2009-2675(GST)I

BETWEEN:

9114-5862 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

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Appeal heard on common evidence with the appeals of  
9114-4766 Québec inc. (2009-2669(GST)I),  
9113-4882 Québec inc. (2009-2670(GST)I),  
9114-4782 Québec inc. (2009-2671(GST)I),  
9114-9658 Québec inc. (2009-2672(GST)I),  
9114-4790 Québec inc. (2009-2674(GST)I), and  
9113-4056 Québec inc. (2009-2676(GST)I), on October 14, 15, 16, 17  
and 20, 2014, at Montréal, Quebec.

Before: The Honourable Justice Lucie Lamarre

Appearances:

Agent for the appellant: Jean Renaud  
Counsel for the respondent: Danny Galarneau

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**JUDGMENT**

The appeal from the assessment made under the *Excise Tax Act*, notice of which is dated April 18, 2005, for the period from September 10, 2002, to March 31, 2004, is allowed, and the assessment is referred back to the Minister of National Revenue for the sole purpose of deleting the penalties.

Signed at Ottawa, Canada, this 2nd day of February 2015.

"Lucie Lamarre"

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Lamarre J.

Translation certified true  
On this 24th day of July 2015

Margarita Gorbounova, Translator

Docket: 2009-2676(GST)I

BETWEEN:

9113-4056 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

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Appeal heard on common evidence with the appeals of  
9114-4766 Québec inc. (2009-2669(GST)I),  
9113-4882 Québec inc. (2009-2670(GST)I),  
9114-4782 Québec inc. (2009-2671(GST)I),  
9114-9658 Québec inc. (2009-2672(GST)I),  
9114-4790 Québec inc. (2009-2674(GST)I), and  
9113-5862 Québec inc. (2009-2675(GST)I), on October 14, 15, 16, 17  
and 20, 2014, at Montréal, Quebec.

Before: The Honourable Justice Lucie Lamarre

Appearances:

Agent for the appellant: Jean Renaud  
Counsel for the respondent: Danny Galarneau

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**JUDGMENT**

The appeal from the assessment made under the *Excise Tax Act*, notice of which is dated June 30, 2005, for the period from September 10, 2002, to January 31, 2004, is allowed, and the assessment is referred back to the Minister of National Revenue for the sole purpose of deleting the penalties.

Signed at Ottawa, Canada, this 2nd day of February 2015.

"Lucie Lamarre"

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Lamarre J.

Translation certified true  
On this 24th day of July 2015

Margarita Gorbounova, Translator

Citation: 2015 TCC 25  
Date: 20150202  
Docket: 2009-2669(GST)I

BETWEEN:

9114-4766 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

and

Docket: 2009-2670(GST)I

BETWEEN:

9113-4882 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

and

Docket: 2009-2671(GST)I

BETWEEN:

9114-4782 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

and

Docket: 2009-2672(GST)I

BETWEEN:

9114-9658 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

and

Docket: 2009-2674(GST)I

BETWEEN:

9114-4790 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

and

Docket: 2009-2675(GST)I

BETWEEN:

9114-5862 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

and

Docket: 2009-2676(GST)I

BETWEEN:

9113-4056 QUÉBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

## REASONS FOR JUDGMENT

Lamarre J.

[1] These are appeals from assessments made by the Deputy Minister of Revenue of Quebec (Minister) under Part IX of the *Excise Tax Act* (ETA), in which he disallowed input tax credits (ITCs) that each of the seven appellants claimed for reporting periods between July 20, 2002, and March 31, 2004 (periods at issue), as the case may be. Penalties and interest as well as additional penalties under section 285 of the ETA were also assessed. According to the documents appended to the Notices of Appeal, the assessment amounts are as follows:

<b>Appellants</b>	<b>ITCs claimed and disallowed</b>	<b>Interest and penalties</b>	<b>Penalties under s. 285 ETA</b>	<b>Periods at issue</b>	<b>Shareholders</b>
9114-4766 Québec inc	\$1,349.82	\$135.17	\$547.50	From 2002-09-10 to 2004-01-31	Jean Renaud
9113-4882 Québec inc	\$1,349.82	\$135.44	\$547.50	From 2002-09-10 to 2004-01-31	Pauline Leroux
9114-4782 Québec inc	\$1,342.81	\$192.86	\$547.50	From 2002-09-05 to 2003-10-31	Yvon Gagné
9114-9658 Québec inc <sup>1</sup>				From 2002-09-10 to 2004-03-31	Johanne Huot
9113-4056 Québec inc	\$1,349.82	\$164.81	\$547.50	From 2002-09-10 to 2004-01-31	Éliane Vaillancourt
9114-4790 Québec inc	\$1,200.47	\$40.26	\$297.50	From 2002-07-20 to 2003-08-31	Guyleine Champoux
9114-5862 Québec inc	\$1,343.36	\$98.38	\$547.50	From 2002-09-10 to 2004-03-31	Christine Hamel

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<sup>1</sup> It is impossible to specify the assessment amount for this appellant because there were no documents regarding this appended to its Notice of Appeal.

[2] The respondent disallowed the ITCs on the ground that, during the periods at issue, the appellants were not engaged in any commercial activity within the meaning of subsection 123(1) of the ETA.

[3] The appeals were heard on common evidence under the informal procedure. Several witnesses were heard and numerous exhibits were filed.

## Facts

### *Preliminary remarks*

[4] In brief, the appellants each acquired an [TRANSLATION] "e-commerce solution" with the goal of operating a Web site enabling them to sell subscriptions to a financial simulation service. The main issue is whether the appellants are entitled to deduct ITCs relative to the Goods and Services Tax (GST), which they paid when they bought the e-commerce solution.

[5] Guyleine Champoux, Christine Hamel, Éliane Vaillancourt, Johanne Huot, Pauline Leroux and Yvon Gagné testified for the appellants. Each of these people is a shareholder and director of his or her own corporation, each of which is an appellant in this case.<sup>2</sup> Jean Renaud and Steve Renaud, shareholders and directors of the companies that supplied the e-commerce solutions, as well as Michel Blouin, external accountant for some of the appellants, also testified for the appellants.

[6] The respondent called as witnesses, among others, Pierre Martel, Objections Officer for the Agence du Revenu du Québec (ARQ) working on this file; Larry Morneau, ARQ investigator assigned to the appellants' file; and Francine Denis and Marc Corriveau, who had also taken part in the investigation of the appellants.

[7] Before I set out the facts disclosed by the evidence, some preliminary remarks should be made. The main witness called by the appellants is also the appellants' representative, namely, Jean Renaud. During the relevant periods, he was the directing mind of the appellants. In 2010, he also became a shareholder and director of one of the corporate appellants, 9114-4766 Québec inc., which had

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<sup>2</sup> It should be noted that each of these people, except Pauline Leroux, is the person who incorporated his or her company in March or February 2002. Ms. Leroux acquired the shares of 9113-4882 Québec inc. on September 20, 2003, from Marie-Christine Levasseur, who had initially incorporated that company. She was not called as witness.

been originally incorporated in 2002 by someone named Clément Corriveau, who was not called as witness. Jean Renaud was also the shareholder and director of one of the two corporations that had developed the e-commerce solution.

[8] To understand the dispute, it would be helpful to provide a brief historical background on how the appellants acquired their e-commerce solution. It is worth describing the events that took place from 2001 to 2005.

[9] Jean Renaud is the instigator of the entire project that led to the incorporation of the appellants. In his testimony, he explained that he wanted to provide an online service that enabled individuals to improve their knowledge about personal finances. According to his testimony, the contemplated service consisted in providing a tool that would make it possible to make a detailed financial simulation, which would be located in the paid part of the Web site. A free part of the Web site had to provide the user with financial information and the possibility of creating a budget. For Jean Renaud this was an innovative project that he had designed because of the significant growth of the Internet at that time. He began to talk about the project with his brother Steve, who worked in information technology. He said that the need to hire programmers made his project very costly. His strategy was to design the service and then to find a way to distribute it.

[10] Jean Renaud's business plan was that several independent corporations would provide the same financial simulation service on their own Web sites. Jean Renaud testified that, for the success of the project, the distribution of the service was just as important to him as its design. He said that he had tried to establish a network of people geographically spread out all over Quebec, who would be able to attract a diverse clientele. At the outset, there were 17 companies like those of the appellants who were asked to sell the financial simulation service once the e-commerce solution was designed. The other companies did not appeal the assessments.

#### *Tax credit for the integration of e-commerce solutions*

[11] The appellants were incorporated at the beginning of the 2000s, when the Quebec government introduced a tax credit for the integration of eligible e-commerce solutions (provincial tax credit) with the goal of refunding part of the expenses incurred by a company as part of implementing an electronic solution such as a transactional Web site. To be eligible for the provincial tax credit, a

company had to show that it operated a business in Quebec, among other things. It was a refundable credit, which was available only for a two-year period.

[12] The evidence in its entirety shows that the funding for Jean Renaud's project had to mainly be obtained through this provincial government assistance. All of the companies involved in the project had to receive the provincial tax credit to make it possible to develop the e-commerce solution and then ensure its proper maintenance. Ultimately, all the provincial tax credits claimed were disallowed, which prevented the project from becoming reality.

*Designing the e-commerce solution: Expert-conseil inc. and Netweb inc.*

[13] The e-commerce solution acquired by each of the appellants was designed by the corporations owned by Jean Renaud and his brother Steve Renaud. Each appellant purchased the same e-commerce solution.

[14] The e-commerce solution consisted of a transactional Web site using the Internet. Each appellant's Web site had to enable subscribers to plan their personal finances. Before being able to access the service, the client had to obtain a user name and password.

[15] The design of the e-commerce solution was comprised of two components. The first was to develop the solution's content, that is, the financial planning function. That part was the design of what was called the financial simulation [TRANSLATION] "software". The second component was to integrate the software into the Web site. That part involved computer programming work to make the service available on the Internet.

[16] Expert-conseil inc.<sup>3</sup> (Expert-conseil) was incorporated on July 20, 2001, under the *Companies Act*, Part 1A (R.S.Q., c. C-38) (*Companies Act*). Its president and principal shareholder was Jean Renaud. Expert-conseil had the task of developing the content of the financial simulation software and the Web sites.

[17] Netweb inc. (Netweb) was also incorporated on July 20, 2001, under the *Companies Act*. Its president and sole shareholder was Steve Renaud. Netweb was mandated to program the software and the Web sites. It also had to take care of managing and hosting the Web sites.

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<sup>3</sup> Incorporated under the name Gesweb inc. On December 1, 2003, the corporation changed its name to Expert-conseil inc. The company had also used the name Sead inc.

[18] On August 20, 2001, Expert-conseil and Netweb billed each other for designing a Web site. Expert-conseil claimed \$100,000 (before tax) for 1,000 hours of work done, among other things, with regard to the content of the software and the Web sites (Exhibit I-22). Netweb also claimed \$100,000 (before tax) for 1,000 hours of work mainly for programming (Exhibit I-24).

[19] Expert-conseil and Netweb each claimed the maximum amount of \$40,000 that could be claimed for the provincial tax credit for their respective fiscal years ending on August 31, 2001. The Minister disallowed the claims on the ground that the proof of payments needed to obtain the credit was not provided.

[20] Expert-conseil and Netweb concluded a similar agreement in 2002, but this time made cheque payments in order to be able to provide the proof needed to get the provincial tax credit. On March 24, 2002, Expert-conseil billed \$85,000 (before tax) for work done on the content of the Web site (Exhibit I-26), and Netweb billed \$105,000 (before tax) for programming the software and a database (Exhibit I-27).

[21] Between April and August 2002, a series of cheques exchanged between Expert-conseil and Netweb were used to pay the amounts owed on the invoices dated March 24, 2002.

[22] Netweb claimed the provincial tax credit for its fiscal year ending on August 31, 2002. Expert-conseil did not claim the provincial tax credit for its fiscal year ending on August 31, 2002.

*The appellants' acquisition of the e-commerce solution*

[23] The appellants were incorporated in February and March 2002 under Part 1A of the *Companies Act*. During the periods at issue, they were registered for the purposes of Part IX of the ETA.

[24] The appellants' role was intended to be limited to promoting a financial planning service, which would be provided on each one's own Web site. The appellant's shareholders testified that it was Jean Renaud who urged them each to create a corporation. They said that he offered them a [TRANSLATION] "turnkey" service, where he would be responsible for all aspects of starting the businesses.

[25] In fact, all that Expert-conseil did was sell a limited-time licence to the appellants through Jean Renaud for the operation of the financial planning software integrated into their Web sites. Under this licence, the appellants could sell

subscriptions to their respective Web sites so that potential clients could use them to do their financial planning online. They would pay royalties to Expert-conseil for the subscriptions they sold. The licence was renewable at Expert-conseil's discretion only.

[26] It was mentioned several times in the testimony that the "turnkey" service provided by Jean Renaud also included management and accounting for the appellants. The appellants' shareholders stated that they had no knowledge of accounting or information technology. Their strength was being socially active and having a vast contact network to which they could promote the financial planning service available on their Web sites.

[27] The appellants' witnesses stated that they knew that several companies were providing the same service and added that they had agreed that the service should be provided to each one's own clients.

[28] Jean Renaud presented his business plan to the appellants as a project that required little investment. A large part of the funding was supposed to come from government assistance granted by means of the provincial tax credit. Each appellant was expected to claim the provincial tax credit on the ground of purchasing the e-commerce solution. The amount of the provincial tax credit that each appellant wanted to receive was \$26,000. However, to be entitled to the credit, the expenses related to implementing the e-commerce solution had to have been incurred by a company before October 1, 2002, as long as a written contract had been concluded before April 1, 2002. By March 31, 2003 at the latest, the e-commerce solution also had to comply with all of the conditions allowing it to be recognized as such (Exhibit A-11).

[29] In March 2002, the appellants all concluded contracts through which they acquired the e-commerce solution from Expert-conseil (tab 5 of Exhibits I-1, I-3, I-4, I-6, I-9, I-11 and I-12). According to the agreement, the appellants each acquired a Web site as well as an operating licence for the financial simulation software for \$65,000. The contract provided that, as consideration, Expert-conseil acquired exclusive rights to advertise on the appellants' Web pages for \$45,000.

[30] The amounts initially set out in the written contracts were \$80,000 for the e-commerce solution and \$60,000 for the exclusive advertising rights. It was filed in evidence that these amounts were changed by verbal agreements. Apparently,

the amounts were reduced because it was decided that the secure transactional module of the Web sites would not be designed by Expert-conseil.

[31] According to the testimony of the appellants' representatives, the transactions with Expert-conseil were originally supposed to be made without monetary payments. They described the situation as an exchange of services or [TRANSLATION] "barter". However, this practice was not accepted when Expert-conseil and Netweb claimed the provincial tax credit in 2001. Invoices were thus produced and payments made.

[32] The invoices related to the March 2002 contracts were filed in evidence (tab 6 of Exhibits I-1, I-3, I-4, I-6, I-9, I-11 and I-12). Invoices dated September 10 or 15, 2002, show that the appellants sold advertising rights to Expert-conseil for \$45,000 and functionality tests and comments for \$3,000. Invoices dated September 15, 2002, show that Expert-conseil sold to the appellants the [TRANSLATION] "Internet version of the application software" (the e-commerce solution) for \$65,000.

[33] The invoices put in evidence were all designed based on the same template. Invoices were paid in the following chronological order:

- Expert-conseil paid the appellants \$51,761.25 after tax, representing the \$45,000 cost of exclusive advertising rights.
- The appellants then each paid Expert-conseil the same amount of \$51,761.25 for part of the application software. The balance to be paid for the software was then \$23,005 for each appellant;
- In April and July 2004, Expert-conseil paid the appellants \$3,450.75, representing the cost of \$3,000 plus tax for the functionality tests and comments.
- In April and July 2004, Expert-conseil made loans of \$18,000 or \$20,000 as the case may be, to the appellants to enable them to finish paying off the e-commerce solution.
- In April and July 2004, the appellants each paid \$23,005 to Expert-conseil, representing the unpaid balance for their e-commerce solutions.
- The witnesses' evidence disclosed that the loans made by Expert-conseil were never repaid by the appellants.

[34] Because it was initially planned that the appellants and Expert-conseil would proceed through an exchange of services, not through monetary payments, the appellants did not have tax numbers when invoices were established in September 2002. The majority of the appellants were registered for GST/HST purposes retroactive to September 2002 (tab 2, Exhibits I-3, I-4, I-6, I-9, I-11 and I-12). Only appellant 9114-4790 Québec Inc. was registered before September 2002 (tab 2, Exhibit I-1). In addition, the appellants' bank accounts were not immediately opened.

[35] On September 15, 2003, Expert-conseil presented to some of the appellants an invoice for \$1,000 in fees (before tax) for accounting work. On September 15, 2003, Netweb also presented to the appellants an invoice of \$1,000 (before tax) for hosting fees. These invoices were never paid by the appellants concerned. Some of the appellants claimed ITCs relative to these services.

[36] The testimony revealed that Jean Renaud asked an accounting firm to prepare some of the appellants' first income tax and GST returns, first financial statements and initial provincial tax credit application. The accounting firm also prepared the objections when the provincial tax credit was disallowed to those appellants. Because of the "turnkey" service provided by Expert-conseil, Jean Renaud then filled out these documents for the other appellants based on the work done by the accounting firm. Jean Renaud said that a great deal of effort was put forward in objecting to the Minister's refusal to allow the appellants' claim of the provincial tax credit.

[37] It is also apparent from the testimony that Jean Renaud prepared the invoices presented by the appellants, because of the start-up service that he provided to them. He also explained that the appellants' mailing address was that of Expert-conseil because of the "turnkey" service. He said that it was a question of functionality. The testimony of the investigator, Larry Morneau, indeed shows that tax refund cheques payable to the appellants were sent to the address of Expert-conseil and Netweb. Cheques were sometimes deposited in the appellants' bank account by Jean Renaud or given directly to the appellants.

[38] In the financial statements, the appellants' products are advertising and functionality tests and comments sold to Expert-conseil and amounts claimed as the provincial tax credit, while their expenses are mainly management fees paid to Expert-conseil, hosting fees paid to Netweb and [TRANSLATION] "incorporation" fees. During the periods at issue, the appellants had no income from the operation

of their Web sites. The loan amounts from Expert-conseil appear in the appellants' financial statements under [TRANSLATION] "accounts payable".

[39] A paper copy of the software and of one company's Web site was filed (Exhibit A-2). In light of the testimony, it is unclear whether the design of the e-commerce solution was entirely completed at any time during the periods at issue. The appellants' witnesses claim that the e-commerce solution became operational in 2003. Furthermore, it is clear from the testimony that the appellants' Web sites were practically identical.

[40] In reality, the appellants never began to promote their financial planning service because their Web sites were never live. In explaining why the project never got off the ground, the witnesses stated that they were waiting for funding. Guyleine Champoux and Christine Hamel also said that they were waiting for Jean Renaud's consent to launch their activities. The appellants' witnesses said that the provincial tax credit was essential to ensuring the technical maintenance of the service and to resolving potential IT problems. The appellants' witnesses also cited the risk to their reputation should there be defects in the service provided. According to them, it was wise to delay the project launch in order to have adequate financial resources to face potential problems. The provincial tax credit had to be used to pay the appellants' suppliers, namely, Expert-conseil and Netweb, who could maintain the service.

[41] In addition, it is evident from the testimony that the appellants' shareholders and directors personally invested little to no money in their corporations. In cross-examination, Ms. Champoux stated in this regard that she had paid \$50 or \$100 for her business. It is worth noting that none of the appellants' representatives seemed interested in investing more in the project. For example, Mr. Gagné stated, in cross-examination, that he did not want to invest any money because he wanted to invest in projects that would generate money more quickly and would involve less risk (Transcript of 15-10-2014, at pages 142-143).

[42] The witnesses for the appellants maintained that they had had several meetings during which Jean Renaud explained the financial simulation service to them, informed them about the development of the software and presented various documents to them relative to the corporations that had to be signed. They have also said that business cards with their Web addresses were created to promote their financial simulation service in the future (Exhibit A-5). Even though no income was earned from operating the Web sites and even though none of them really invested any money in the project, the appellants' shareholders and directors

told the Court that their intention was to earn income and to give added value to their businesses.

[43] Pierre Martel, an ARQ objections officer, began receiving files related to the appellants in the fall of 2003. He stated that, at the outset, it was Notices of Objection concerning eligibility for the provincial tax credit. He said that the Minister claimed that there was no operation of a business, which was necessary to be entitled to that tax measure. He said that he was unable to make an informed decision because of a lack of information and decided to request a supplementary audit.

[44] In 2004, the special investigations division told Pierre Martel that it was taking the files for investigation purposes. He said that he had suspended the objection files, but added that, during the investigation, other assessments and other Notices of Objection were made.

[45] Larry Morneau, the ARQ auditor assigned to the appellants' file, explained that the investigation mostly focused on the existence of a scheme devised to illegally obtain the provincial tax credit. He maintained that the ITC claims were incidental to the main investigation.

[46] On January 26 and 27, 2005, search warrants were executed as part of the investigation. The search warrants were executed at the homes of the appellants' representatives as well as at Expert-conseil's and Netweb's establishments. They made it possible to obtain the accounting records of Expert-Conseil, purchase and sale invoices and the server containing each appellant's Web site. After the seizures, it was impossible for the appellants to access the Web sites. The shareholders and directors of the appellants all made statements during the searches.

[47] In her testimony, Guyleine Champoux alleged, *inter alia*, being threatened and intimidated by the respondent's representatives when her home was searched. She stated that the statement made at the time of the search was made out of fear. Her spouse, Yvon Gagné, corroborated that version of events. Between June and August 2005, the shareholders and directors of the appellants wrote a letter to the Minister explaining the purpose of each of their companies.

[48] Counsel for the respondent also discussed the issue of the searches and seizures that took place on January 26 and 27, 2005. Francine Denis and

Marc Corriveau, officers responsible for the searches, stated in their testimony that no intimidation had taken place.

[49] Larry Morneau testified that his investigation resulted in criminal charges being laid against Jean Renaud for participating in the offence of making false statements in the appellants' income tax returns. On May 8, 2013, Jean Renaud pleaded guilty to the following amended charge:

[TRANSLATION]

Prescribed, acquiesced in or participated in the performance by the corporation Expert-Conseil inc. and performed or failed to perform something with a view to aiding the corporations: Netweb inc., [all of the corporate appellants as well as other corporations are listed] . . . , to commit the following offence: . . . , between November 13, 2001, and September 6, 2004, made false or misleading statements or participated in, assented to or acquiesced in making them on corporate income tax return forms CO-17 filed for all these corporations with the Ministère du Revenu du Québec under the *Taxation Act*, (R.S.Q. c. I-3), thus committing an offence set out in paragraph 62(a) of the *Act respecting the Ministère du Revenu*, (R.S.Q. c. M-31); . . . [Respondent's motion record, October 25, 2013, Exhibit B, page 17, Exhibit I-18, pages 26 and 27.]

[50] Jean Renaud gave his version of the facts. He explained that he had entered a guilty plea thinking that there was no element of intent in the offence to which he was pleading guilty. He also wanted to avoid a long and exhausting trial. In cross-examination, Jean Renaud acknowledged that he had pleaded guilty to the offence.

[51] In his testimony, Larry Morneau commented on a worksheet (Exhibit I-34) that he had prepared for the purposes of the investigation. The worksheet provided a [TRANSLATION] "summary table" of the scheme. Mr. Morneau concluded that all of the bank transactions constituted a financial arrangement making it possible to obtain the proof of payments needed to support the tax credit claims. Mr. Morneau indicated that all the money did was go in and out of the appellants' bank accounts, and that they made no external cash contributions. He stated that the purpose of the scheme was that the money end up in the bank account of Expert-conseil.

[52] Mr. Morneau concluded that Jean Renaud wanted to mislead the Minister in providing false documents, which led him to believe that the appellants had commercial activities allowing them to claim, among other things, the ITCs that are at issue here.

Appellants' arguments

[53] The appellants maintain that they were engaged in a commercial activity entitling them to ITCs during the periods at issue. They stated that they had begun operating a business when preliminary steps were taken. According to them, the acquisition of the e-commerce solution and the sale of advertising rights were preliminaries essential to their normal operations.

[54] The Notices of Appeal refer to Interpretation Bulletin IT-364 of the Canada Revenue Agency in order to allege that "a business commences whenever some significant activity is undertaken that is a regular part of the income-earning process in that type of business or is an essential preliminary to normal operations".

[55] Jean Renaud maintained that obtaining the provincial tax credit was never the appellants' purpose indicating that it was simply a form of funding.

#### Respondent's arguments

[56] The respondent submits that the appellants were not engaged in any commercial activity and that they are not entitled to the ITCs claimed.

[57] According to the respondent, the situation is analogous to that in *Orly Automobiles Inc. v. The Queen*, 2004 TCC 86, [2004] G.S.T.C. 57 (affirmed by the Federal Court of Appeal (F.C.A.), 2005 FCA 425, [2005] G.S.T.C. 200), where a sham was put in place in order to receive ITCs. The respondent alleges that the appellants were involved in a scheme by which they gave the illusion that they had commercial activity, with the sole purpose of unduly receiving tax credits, including the ITCs that are the subject of these appeals.

[58] The respondent alleges that no evidence was filed with respect to the intention of appellant 9114-4766 Québec inc. to operate a business during the periods at issue. That is the corporation acquired by Jean Renaud in 2010, whose shareholder at the time was not called as witness. Counsel for the respondent also asked the Court to draw a negative inference from the absence of the original shareholder and director of appellant 9113-4882 Québec inc., who had sold her company to Pauline Leroux during the periods at issue, and who, according to the respondent, was the only relevant witness to present the business's original intentions.

[59] Finally, the respondent considers that the penalties imposed are justified because the appellants clearly and directly participated in the scheme. According to

the respondent, the appellants allowed the money to circulate between the corporations and ultimately to return to Jean Renaud.

### Analysis

[60] It must be determined whether, during the periods at issue, the appellants were engaged in a commercial activity entitling them to ITCs.

[61] The existence of commercial activity is necessary to be entitled to an ITC based on the formula set out in subsection 169(1) of the ETA, which reads as follows:

**169. (1) General rule for credits** — Subject to this Part, where a person acquires or imports property or a service or brings it into a participating province and, during a reporting period of the person during which the person is a registrant, tax in respect of the supply, importation or bringing in becomes payable by the person or is paid by the person without having become payable, the amount determined by the following formula is an input tax credit of the person in respect of the property or service for the period:

$$A \times B$$

where

A is the tax in respect of the supply, importation or bringing in, as the case may be, that becomes payable by the person during the reporting period or that is paid by the person during the period without having become payable; and

B

is

(a) where the tax is deemed under subsection 202(4) to have been paid in respect of the property on the last day of a taxation year of the person, the extent (expressed as a percentage of the total use of the property in the course of commercial activities and businesses of the person during that taxation year) to which the person used the property in the course of commercial activities of the person during that taxation year,

(b) where the property or service is acquired, imported or brought into the province, as the case may be, by the person for use in improving capital property of the person, the extent (expressed as a percentage) to which the person was using the capital property in the course of commercial activities of the person immediately after the capital property or a portion thereof was last acquired or imported by the person, and

(c) in any other case, the extent (expressed as a percentage) to which the person acquired or imported the property or service or brought it into the

participating province, as the case may be, for consumption, use or supply in the course of commercial activities of the person.

[62] The expression "commercial activity" is defined as follows in subsection 123(1) of the ETA:

**123. (1) Definitions** — In section 121, this Part and Schedules V to X,

...

“**commercial activity**” of a person means

(a) a business carried on by the person (other than a business carried on without a reasonable expectation of profit by an individual, a personal trust or a partnership, all of the members of which are individuals), except to the extent to which the business involves the making of exempt supplies by the person,

(b) an adventure or concern of the person in the nature of trade (other than an adventure or concern engaged in without a reasonable expectation of profit by an individual, a personal trust or a partnership, all of the members of which are individuals), except to the extent to which the adventure or concern involves the making of exempt supplies by the person, and

(c) the making of a supply (other than an exempt supply) by the person of real property of the person, including anything done by the person in the course of or in connection with the making of the supply.

[63] In this case, during the periods at issue, the appellants were in the process of starting up their business. It must therefore be determined whether they had commercial activity during that period even though they had not yet begun their normal operation.

[64] *Gartry v. Canada*, [1994] T.C.J. No. 240 (QL), 94 DTC 1947, deals with the issue of whether a taxpayer has begun operating a business. In that decision, Judge Bowman made the following comments at paragraph 16 (QL):

. . . In determining when a business has commenced, it is not realistic to fix the time either at the moment when money starts being earned from the trading or manufacturing operation or the provision of services or, at the other extreme, when the intention to start the business is first formed. Each case turns on its own facts, but where a taxpayer has taken significant and essential steps that are necessary to the carrying on of the business it is fair to conclude that the business has started. . . .

[65] In *Kaye v. Canada*, [1998] T.C.J. No. 265 (QL), 98 DTC 1659, Judge Bowman summarized the analysis for determining when a business had been started as follows at paragraphs 4, 5 and 7:

4 . . . It is the inherent commerciality of the enterprise, revealed in its organization, that makes it a business. Subjective intention to make money, while a factor, is not determinative, although its absence may militate against the assertion that an activity is a business.

5 One cannot view the reasonableness of the expectation of profit in isolation. One must ask "Would a reasonable person, looking at a particular activity and applying ordinary standards of commercial common sense, say 'yes, this is a business'?" In answering this question the hypothetical reasonable person would look at such things as capitalization, knowledge of the participant and time spent. He or she would also consider whether the person claiming to be in business has gone about it in an orderly, businesslike way and in the way that a business person would normally be expected to do.

...

7 Ultimately, it boils down to a common sense appreciation of all of the factors, in which each is assigned its appropriate weight in the overall context. One must of course not discount entrepreneurial vision and imagination, but they are hard to evaluate at the outset. Simply put, if you want to be treated as carrying on a business, you should act like a businessman.

[66] After referring to the above observations made by Judge Bowman in *Gartry and Kaye, supra*, Justice Campbell of this Court stated the following in *Land and Sea Enterprises Ltd. v. The Queen*, 2011 TCC 101:

[14] It is clear that an activity may be considered a commercial activity well in advance of the stage of profitability. It will always be a question of fact. Expenditures giving rise to ITCs in the start-up phase of a commercial activity may be eligible provided that there is clear intention to commence a business and that measurably significant and fundamental steps and actions have been put into place.

[67] In this case, the appellants did not satisfy me that they were engaged in a commercial activity under the ETA.

[68] The appellants base their ITC claims for the periods at issue on their preliminary activities, which consisted only in the acquisition of the e-commerce solution and the sale of advertising rights.

[69] The e-commerce solution is no doubt the asset that should have enabled the appellants to have commercial activity. Michel Blouin, the accountant for some of the appellants, also indicated in his testimony that the acquisition of the e-commerce solution was for him the essential preliminary that made it possible to operate the businesses and to justify the provincial tax credit claims and, for the purposes of this case, the ITC claims.

[70] Thus, even though the appellants' witnesses claim that the software and the Web sites were completed, the e-commerce solution was never implemented by the appellants' supplier, Expert-conseil. The reason that was given to justify the fact that none of the Web sites was launched was the lack of funding, which prevented the appellants from being able to maintain the service that they wanted to provide.

[71] The appellants remained at the preliminary stage and never began operating their businesses and generating revenue from the sale of subscriptions to their Web sites because, among other things, they never wanted to personally invest in the project. The financial feasibility of a project is a fundamental step in creating a business. In this case, the appellants incurred practically no financial risk and did not want to incur any. The appellants were at the stage where they needed to find the funding necessary to breathe life into their project. To do so, they were counting only on government assistance in the end. They were still at the stage of organizing the businesses they were planning to operate and were not at that point financed so that they could one day earn income from them.

[72] In addition, it is clear from the testimony that the appellants were mandated to promote the financial planning service that was supposed to be provided on their Web sites through their own knowledge networks. The appellants' directors had no knowledge in information technology or in financial simulation. The appellants' witnesses stated that they had concluded a "turnkey" agreement based on which Expert-conseil took charge of all aspects of starting up the businesses. While waiting for their e-commerce solution to be implemented, the appellants played a very passive role. Developing the software was their suppliers' activity. During the periods at issue, the appellants' shareholders and directors committed very little time to the project, and their involvement in it was very minimal.

[73] In sum, they contributed little to no money to their companies and put forth no serious or relatively sustained effort in their companies. Other than the mention of some meetings with Jean Renaud, there was no evidence establishing that they really put an effort into the companies' activities. The few bank transactions, the accounting, the purchase of the e-commerce solution and the sale of advertising rights were done by Jean Renaud. Moreover, the only sale made by the appellants, namely, the sale of the advertising rights to Expert-conseil, was done early and seems to have been orchestrated mainly with the aim of financing the acquisition of the e-commerce solution. In addition, the loans granted by Expert-conseil to pay for part of the e-commerce solution were never repaid by the appellants.

[74] Even though the appellants' witnesses intended to promote the service when it was ready to be sold, I am of the view that their activities were still at the preparatory stage and that the measures essential to the claim that the appellants had started operating a business and therefore engaging in a commercial activity were not seriously implemented.

[75] Accordingly, I conclude that the Minister was correct in disallowing the ITCs for the periods at issue.

#### Penalty under section 285 of the ETA

[76] The second issue to dispose of in these appeals is whether the Minister was correct in imposing penalties under section 285 of the ETA.

[77] It is for the respondent to prove the facts needed in order to establish that the appellants, knowingly or under circumstances amounting to gross negligence, made or participated in, assented to or acquiesced in the making of a false statement in a return or other document made in respect of a reporting period or transaction.

[78] In *897366 Ontario Ltd. v. Canada*, [2000] T.C.J. No. 117 (QL), [2000] G.S.T.C. 13, Judge Bowman indicated at paragraph 19 that penalties under section 285 of the ETA may only be imposed “in the clearest of cases, and after an assiduous scrutiny of the evidence”.

[79] The penalty for false statements or omissions set out in section 285 of the ETA is analogous to that set out in subsection 163(2) of the *Income Tax Act*. In *Farm Business Consultants Inc. v. Canada*, [1994] T.C.J. No. 760 (QL), 95 DTC 200 (affirmed by the F.C.A., [1996] F.C.J. No. 82 (QL), 96 DTC 6085), Judge Bowman stated the following at paragraph 27:

. . . Moreover, where a penalty is imposed under subsection 163(2) although a civil standard of proof is required, if a taxpayer's conduct is consistent with two viable and reasonable hypotheses, one justifying the penalty and one not, the benefit of the doubt must be given to the taxpayer and the penalty must be deleted. . . .

[80] Counsel for the respondent alleged that the appellants participated in a scheme designed by Jean Renaud by signing the various documents prepared by him. In addition, counsel for the respondent relied, *inter alia*, on *Raposo v. The Queen*, 2013 TCC 265, to highlight the consequence in civil matters of pleading

guilty in a criminal case. That decision states that a criminal conviction is *prima facie* proof of the facts underlying the conviction. In that decision, Justice Paris examined the impact of a guilty plea on a penalty for gross negligence and treated the taxpayer's conviction as *prima facie* proof of gross negligence.

[81] In light of the evidence heard, I am, nonetheless, not satisfied that the Minister has shown that penalties should have been imposed.

[82] Unlike in *Raposo, supra*, there was no evidence that has sufficiently shown, in my view, that the appellants intended to participate in making false statements and that they had exercised a high degree of negligence amounting to gross negligence.

[83] It is true that Jean Renaud pleaded guilty respecting a charge related to this case. He played an important role in the entire project. The appellants' participation at the time when the false statements were allegedly made, namely, before Jean Renaud's guilty plea, should be assessed. The appellants did not have much knowledge in accounting and tax matters. They had a great deal of trust in Jean Renaud, who has a university education in these fields and let him take care of preparing invoices, financial statements, provincial tax credits and tax refund claims. In his testimony, Jean Renaud stated that the supplier Expert-conseil paid the taxes collected from the appellants to the government.

[84] It seems to me from the testimony that the appellants did have some desire to start a business. The project appeared possible to the appellants because of the actions taken by Jean Renaud. The appellants believed in the project even though it was still at the formative stage.

[85] In this case, although the appellants had no commercial activity, software and Web sites were being developed. The appellants believed that they were acquiring real supplies, which would become essential to their business.

[86] I also acknowledge that the individuals who had founded the corporations later acquired by Jean Renaud and his mother, Pauline Leroux, did not testify. However, with regard to penalties, the onus is on the respondent to make out a case for gross negligence. Considering the testimony of the appellants' other witnesses, the respondent did not satisfy me that the situation was different for those two other people when they had incorporated their companies.

[87] For all of these reasons, the appeals are allowed and the assessments at issue are referred back to the Minister with the sole purpose of deleting the penalties.

Signed at Ottawa, Canada, this 2nd day of February 2015.

“Lucie Lamarre”

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Lamarre J.

Translation certified true  
On this 24th day of July 2015

Margarita Gorbounova, Translator

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STYLE OF CAUSE: 9114-4766 QUÉBEC INC., 9113-4882 QUÉBEC INC., 9114-4782 QUÉBEC INC., 9114-9658 QUÉBEC INC., 9114-4790 QUÉBEC INC., 9114-5862 QUÉBEC INC., 9113-4056 QUÉBEC INC. v. HER MAJESTY THE QUEEN

PLACE OF HEARING: Montréal, Quebec

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REASONS FOR JUDGMENT BY: The Honourable Justice Lucie Lamarre

DATE OF JUDGMENT: February 2, 2015

APPEARANCES:

Agent for the appellants:	Jean Renaud
Counsel for the respondent:	Danny Galarneau

COUNSEL OF RECORD:

For the appellants:

Name:	
Firm:	

For the respondent: William F. Pentney  
Deputy Attorney General of Canada  
Ottawa, Canada