Docket: 2014-2006(IT)G

BETWEEN:

M. KATHLEEN GRIMES AND M. ERSIN OZERDINC,
TRUSTEES OF THE OZERDINC FAMILY TRUST NO. 2,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on June 8 and 9, 2016, at Ottawa, Canada

Before: The Honourable Justice Dominique Lafleur

Appearances:

Counsel for the Appellant:	Paul C. LaBarge Estelle Duez
Counsel for the Respondent:	Pascal Tétrault Nicholas MacDonald (student-at-law)

JUDGMENT

The appeal from the reassessment made pursuant to the *Income Tax Act*, the notice of which is dated October 17, 2013, for the 2011 taxation year, is allowed and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment in accordance with the attached Reasons for Judgment and the summary of adjustments found in Appendices B to D which form an integral part of the Reasons for Judgment.

The matter of costs is reserved. The parties will have 60 days from the date of this Judgment with Reasons to reach an agreement on costs, failing which they

are directed to file their written submissions on the issue of costs, not to exceed (10) pages, within 30 days of the expiration of the initial 60-day period.

Signed at Ottawa, Canada, this 29th day of November 2016.

"Dominique Lafleur"

Lafleur J.

Citation: 2016 TCC 280
Date: 20161129
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REASONS FOR JUDGMENT

Lafleur J.

A. OVERVIEW.

[1] This appeal arises out of the reassessment of the Ozerdinc Family Trust No. 2 (the "Trust") with respect to its 2011 taxation year. On October 17, 2013, the Minister of National Revenue (the "Minister") reassessed the Trust, in accordance with the provisions of the *Income Tax Act*, R.S.C., 1985, c. 1 (5th supp.), as amended (the "Act"), and increased the Trust's taxable income by the amount of $4,035,242 and therefore included a corresponding tax liability of $1,870,045.22 and accrued interest of $151,483.35 (Exhibit AR-2, tab 19). The reassessment is the result of the application of the rules found in subsections 104(4) and 104(5.8) of the Act, referred to as the "21-year deemed disposition rules". On January 15, 2014, Ms. Marion Kathleen Grimes and Mr. Ersin Ozerdinc, as trustees of the Trust (the "Appellant"), filed a notice of objection in respect of the notice of reassessment. On May 5, 2014, the Appellant filed a notice of appeal pursuant to paragraph 169(1)(*b*) of the Act, because the Trust had not received a notice of confirmation and 90 days had elapsed since the notice of objection was filed.

[2] The fact that the Trust was subject to the application of the 21-year deemed disposition rules is not in issue in this appeal, the deemed disposition day being February 1, 2011, at the end of the day (the "Valuation Date"). In issue is the determination of the fair market value of some of the capital property held by the Trust at that time.

[3] In accordance with paragraph 7(g) of the Reply to the Notice of Appeal and the Agreed Statement of Facts (Partial) filed as Exhibit AR-1 and as corrected by the parties, the capital property held by the Trust as of the Valuation Date and subject to the 21-year deemed disposition rules comprises the following:

1 Class A Common Share and 2,699,900 First Preferred Shares of the share capital of 1634158 Ontario Inc. ("Holdco") and an interest in Site Preparation Limited Partnership ("SPLP").

[4] The fair market value of the interest in SPLP is not in dispute (Exhibit AR-1, para. 46). Holdco, in turn, held all the issued and outstanding shares of a corporation called Site Preparation Limited ("SPL").

[5] The Minister concluded that the fair market value of the shares of Holdco owned by the Trust as of the Valuation Date was $7,993,655, allocated as follows: $2,699,900 for the 2,699,900 First Preferred Shares and $5,293,655 for the Class A Common Share.

[6] One of the trustees of the Trust, Ms. Marion Kathleen Grimes, testified at the hearing, along with one expert witness called by the Appellant, Mr. Gerald S. Blackman from the firm MNP LLP. The Respondent called two expert witnesses, namely Mr. Timothy Spencer from the Canada Revenue Agency and Mr. Neil de Gray from the firm Campbell Valuation Partners Limited ("CVPL").

B. THE RELEVANT LEGISLATION.

[7] The relevant parts of paragraphs 104(4) and 104(5.8) of the Act read as follows:

104(4) Deemed disposition by trust — Every trust is, at the end of each of the following days, deemed to have disposed of each property of the trust (other than exempt property) that was capital property (other than excluded property or depreciable property) or land included in the inventory of a business of the trust for proceeds equal to its fair market value (determined with reference to subsection 70(5.3)) at the end of that	**104(4) Présomption de disposition** — Toute fiducie est réputée, à la fin de chacun des jours suivants, avoir disposé de chacun de ses biens (sauf les biens exonérés) qui constituait une immobilisation (sauf un bien exclu ou un bien amortissable) ou un fonds de terre compris dans les biens à porter à l'inventaire d'une de ses entreprises, pour un produit égal à la juste valeur marchande du bien (déterminée par rapport au

day and to have reacquired the property immediately after that day for an amount equal to that fair market value, and for the purposes of this Act those days are

. . .

(*b*) the day that is 21 years after the latest of

(i) January 1, 1972,

(ii) the day on which the trust was created, and

(iii) where applicable, the day determined under paragraph (*a*), (*a*.1) or (*a*.4) as those paragraphs applied from time to time after 1971; and

. . .

(5.8) Trust transfers — Where capital property (other than excluded property), land included in inventory, Canadian resource property or foreign resource property is transferred at a particular time by a trust (in this subsection referred to as the "transferor trust") to another trust (in this subsection referred to as the "transferee trust") in circumstances in which subsection 107(2) or 107.4(3) or paragraph (*f*) of the definition disposition in subsection 248(1) applies,

(*a*) for the purposes of applying subsections 104(4) to 104(5.2) after the particular time,

(i) subject to paragraphs (*b*) to (*b*.3), the first day (in this subsection referred to as the "disposition day") that ends at or after the particular time that

paragraphe 70(5.3)) à la fin de ce jour, et avoir acquis le bien de nouveau immédiatement après ce jour pour un montant égal à cette valeur. Pour l'application de la présente loi, ces jours sont :

[…]

b) le jour qui tombe 21 ans après le dernier en date des jours suivants :

(i) le 1er janvier 1972,

(ii) le jour où la fiducie a été établie,

(iii) le cas échéant, le jour déterminé selon les alinéas *a*), *a*.1) ou *a*.4), dans leurs versions applicables après 1971;

[…]

(5.8) Transferts de fiducie — Lorsqu'une fiducie (appelée « fiducie cédante » au présent paragraphe) transfère à un moment donné à une autre fiducie (appelée « fiducie cessionnaire » au présent paragraphe) des immobilisations (sauf des biens exclus), des fonds de terre compris dans les biens à porter à son inventaire, des avoirs miniers canadiens ou des avoirs miniers étrangers dans les circonstances visées aux paragraphes 107(2) ou 107.4(3) ou à l'alinéa *f*) de la définition de disposition au paragraphe 248(1), les règles suivantes s'appliquent :

a) pour l'application des paragraphes (4) à (5.2) après le moment donné :

(i) sous réserve des alinéas *b*) à *b*.3), le premier jour (appelé

would, if this section were read without reference to paragraphs (4)(*a*.2) and (*a*.3), be determined in respect of the transferee trust is deemed to be the earliest of	« jour de disposition » au présent paragraphe) se terminant au moment donné ou postérieurement qui serait déterminé à l'égard de la fiducie cessionnaire si le présent article s'appliquait compte non tenu des alinéas (4)*a*.2) et *a*.3) est réputé être le premier en date des jours suivants :
(A) the first day ending at or after the particular time that would be determined under subsection 104(4) in respect of the transferor trust without regard to the transfer and any transaction or event occurring after the particular time,	(A) le premier jour, se terminant au moment donné ou après, qui serait déterminé selon le paragraphe (4) à l'égard de la fiducie cédante s'il n'était pas tenu compte du transfert ou d'une opération ou d'un événement survenant après le moment donné,
. . .	[…]

[Emphasis added.]

C. THE ISSUES.

[8] In accordance with subsection 104(4) of the Act, I have to determine the fair market value as of the Valuation Date of the Class A Common Share and the 2,699,900 First Preferred Shares of the share capital of Holdco held by the Trust.

[9] In outlining the task faced by this Court, I would first note the classic discussions of the difficulties inherent in the valuation of the fair market value of capital property. The basic approach is aptly defined in *Gold Coast Selection Trust Limited v Humphrey (Inspector of Taxes*), [1948] AC 459, [1948] 2 All ER 379, a leading case decided by the House of Lords. Viscount Simon stated at pages 472-473:

> In my view, the principle to be applied is the following. In cases such as this, when a trader in the course of his trade receives a new and valuable asset, not being money, as the result of sale or exchange, that asset, for the purpose of computing the annual profits or gains arising or accruing to him from his trade, should be valued as at the end of the accounting period in which it was received, even though it is neither realised or realisable till later. The fact that it cannot be

> realised at once may reduce its present value, but that is no reason for treating it, for the purposes of income tax, as though it had no value until it could be realised. If the asset takes the form of fully paid shares, the valuation will take into account not only the terms of the agreement, but a number of other factors, such as prospective yield, marketability, the general outlook for the type of business of the company which has allotted the shares, the result of a contemporary prospectus offering similar shares for subscription, the capital position of the company, and so forth. There may also be an element of value in the fact that the holding of the shares gives control of the company. If the asset is difficult to value, but is none the less of a money value, the best valuation possible must be made. Valuation is an art, not an exact science. Mathematical certainty is not demanded, nor, indeed, is it possible. It is for the commissioners to express in the money value attributed by them to the asset their estimate, and this is a conclusion of fact to be drawn from the evidence before them.

[Emphasis added.]

[10] In *Conn v. MNR*, 86 DTC 1669 [*Conn*], Justice Brulé of this Court noted the summary made by Justice McIntyre of the British Columbia Supreme Court of older Canadian authorities in *Re Mann Estate,* [1972] 5 WWR 23 at 26, 1 NR 518:

> 11 The expression "fair market value" is well known in law and, indeed, there is little dispute before me as to the definition of the term. It has been the subject of much judicial discussion and the appellants referred to such cases as *Untermyer Estate v. A.G. of B.C.*, [1929] S.C.R. 84; *Montreal Island Power Company v. The Town of Laval,* [1935] S.C.R. 304; In *Re Succession Duty Act re Leiser* [1937] 2 W.W.R. 428; *A-G of Alta. v. Royal Trust Co.* [1945] S.C.R. 267; *Smith et al v. M.N.R.* [1950] S.C.R. 602; *Semet-Solvay Co. v. Deputy M.N.R.* [1960], 20 D.L.R. 663.
>
> 12 I do not intend to quote at length from these authorities, but it is clear, from an examination of them, that the expression "fair market value" means the exchange value, the value an asset will bring in the market and where no market exists, that value must be determined by other indicia of value. I refer to a passage in the judgment of Estey J. in *Attorney General of Alberta v. Royal Trust Company, supra*, at p. 288 which is representative of the views expressed in the other authorities referred to:
>
> > "It is not suggested that the Commissioner has overlooked any factor that ought properly to have been taken into account in determining the value of the property. He had to determine the market value and when, as in this case, no market exists, it is the task of the Commissioner, so far as he can, to construct a normal market and to determine the value by taking into account all the factors which would exist in an actual normal market - a market

> which is not disturbed by factors similar to either boom or depression, and where vendors, ready but not too anxious to sell, meet with purchasers ready and able to purchase. Such a task is often very difficult, and this case is no exception."

[11] The specific situation where no ready market exists was examined by Justice Kellock in *Smith v. Minister of National Revenue*, [1950] SCR 602, wherein he said at page 605:

> In determining the fair market value where there is no competitive market at the date as of which the value is to be ascertained, other indicia may be resorted to as pointed out by Sir Lyman Duff C.J. in *Montreal Island Power Co. v. Town of Laval des Rapides*, [1935] S.C.R. 304 at 306. The learned Chief Justice went on to say:
>
> > There may be reasonable prospects of the return of a market, in which case it might not be unreasonable for the assessor to evaluate the present worth of such prospects and the probability of an investor being found who would invest his money on the strength of such prospects; and there may be other relevant circumstances which it might be proper to take into account as evidence of its actual capital value.

[12] In *Henderson Estate and Bank of New York v. MNR*, 73 DTC 5471, [1973] CTC 636, Justice Cattanach of the Federal Court noted that:

> The statute does not define the expression "fair market value", but the expression has been defined in many different ways depending generally on the subject matter which the person seeking to define it had in mind. I do not think it necessary to attempt an exact definition of the expression as used in the statute other than to say that the words must be construed in accordance with the common understanding of them. <u>That common understanding I take to mean the highest price an asset might reasonably be expected to bring if sold by the owner in the normal method applicable to the asset in question in the ordinary course of business in a market not exposed to any undue stresses and composed of willing buyers and sellers dealing at arm's length and under no compulsion to buy or sell</u>. I would add that the foregoing understanding as I have expressed it in a general way includes what I conceive to be the essential element which is an open and unrestricted market in which the price is hammered out between willing and informed buyers and sellers on the anvil of supply and demand. These definitions are equally applicable to "fair market value" and "market value" and it is doubtful if the use of the word "fair" adds anything to the words "market value".
>
> [Emphasis added.]

[13] That definition has since been consistently cited with approval by the Federal Court of Appeal and this Court (see *Attorney General of Canada v. Nash et al.*, 2005 FCA 386, 2005 DTC 5696; *The Queen v. Gilbert et al.*, 2007 FCA 136, 2008 DTC 6295; *Kruger Wayagamack Inc. v. The Queen*, 2015 TCC 90, 2015 DTC 1112). Cattanach J. went on to observe that:

> In my opinion the discussion of the meaning of the expression by Mr Justice Migneault in delivering the unanimous judgment of the Supreme Court of Canada in *Untermyer Estate v. Attorney-General for British Columbia* is a most useful guide to the meaning of the words "fair market value" as used in the *Dominion Succession Duty Act* as applicable to shares listed on a stock exchange. He said at page 91:
>
> > We were favoured by counsel with several suggested definitions of the words "fair market value." The dominant word here is evidently "value," in determining which the price that can be secured on the market—if there be a market for the property (and there is a market for shares listed on the stock exchange)—is the best guide. It may, perhaps, be open to question whether the expression "fair" adds anything to the meaning of the words "market value," except possibly to this extent that the market price must have some consistency and not be the effect of a transient boom or a sudden panic on the market. The value with which we are concerned here is the value at Untermyer's death, that is to say, the then value of every advantage which his property possessed, for these advantages, as they stood, would naturally have an effect on the market price. Many factors undoubtedly influence the market price of shares in financial or commercial companies, not the least potent of which is what may be called the investment value created by the fact—or the prospect as it then exists—of large returns by way of dividends, and the likelihood of their continuance or increase, or again by the feeling of security induced by the financial strength or the prudent management of a company. The sum of all these advantages controls the market price, which, if it be not spasmodic or ephemeral, is the best test of the fair market value of property of this description.
> >
> > I therefore think that the market price, in a case like that under consideration, where it is shown to have been consistent, determines the fair market value of the shares. I do not lose sight of the fact that mining operations are often of a speculative character, that there is always a danger of depletion, and that a time will sooner or later arrive when no more minerals will be available, unless other properties are secured to keep up the supply. But all these elements have an effect on the price of the shares on the

> stock exchange, and no doubt they were fully considered by the purchasers of the stock at the then prevailing prices.

[Emphasis added.]

[14] The *Untermeyer* case makes a distinction between "market value" and "fair market value". Similarly, courts have grappled with the distinction between "fair value" and "fair market value" in the context of other proceedings. For instance, in *1234 Mountain Realty Corp. c. Ioanidis*, [2002] JQ No. 5674 (QL), J.E. 2003-133, a case decided by the Quebec Court of Appeal, a dissenting shareholder, upon the liquidation of a corporation from which he dissented, was entitled to seek the "fair value" of his shares from the corporation under the *Canada Business Corporations Act*, R.S.C., 1985, c. C-44 (the "CBCA"). The relevant provision of the CBCA defines "fair value"; however, Canadian jurisprudence has ruled that "fair value" is a concept that is not identical with "fair market value". Indeed, the trial judge in *1234 Mountain Realty Corp. v. Ioanidis*, [2000] QJ No. 264 (Superior Court), stated at paragraph 6, "fair value" departs from "fair market value" insofar as it excludes the minority discount and may add a premium for the "squeezing-out" of the minority shareholder.

[15] Brulé TCJ, in *Conn* (cited above), noted the following:

> E.N.R. Campbell in Canada Valuation Service, published by Richard De Boo Limited, indicates that there are two distinct markets where valuation determination may be required. One is the open market in which transactions are constantly consumated and the other is the less familiar notional market where valuation requirements are necessary for such things as income tax, expropriation, arbitration or divorce proceedings. In this latter instance, although it is necessary to make a value determination, there may be no contemplation of open market transactions.

[Emphasis added.]

That is the task faced by this Court. In *Attridge v. The Queen*, [1991] 1 CTC 247, 91 DTC 5161 [*Attridge*], Justice Muldoon discussed an important point pertaining to valuation cases: the trial judge is not bound to accept unquestioningly the expert evidence: "[this] Court will have to form its own conclusions necessarily without adopting those of the expert witnesses. . . . Having . . . stated reasons enough for not accepting the expert witnesses' approaches and conclusions, the Court must nevertheless exercise the judgment which Parliament exacts despite its not having stated in the Income Tax Act any definition of "fair market value"" (pages 267 and 270). His conclusion, which departed from the approaches of both sets of experts in that valuation case on the ground that they

reflected extreme views, was confirmed on appeal by the Federal Court of Appeal at [1994] 1 CTC 193, 94 DTC 6132 (leave to appeal to the Supreme Court of Canada was refused, [1993] SCCA No. 555).

[16] I emphasize *Attridge* since it reaffirms the independence of the trier of fact from the opinions of experts as well as the importance of applying the relevant principles drawn from the fair value concept of the CBCA in arriving at a valuation for the purposes of the Act. There is no similarity between the contribution of the experts who testified before Muldoon J. and that of the experts before me. While I have highlighted some erroneous assumptions on the part of the experts, I found their opinions overall quite helpful and well-reasoned in most respects – in no way comparable to the "quite worthless" opinions and conclusions propounded before Muldoon J.

[17] In this appeal, in order to determine that fair market value, I will examine, *inter alia*, five (5) issues:

(1) Which financial statements should be the starting point for the evaluation of the shares of SPL: the internal financial statements of SPL as of January 31, 2011 prepared by the Management (filed as Exhibit AR-2, tab 8; the "Internal Statements") or the audited financial statements of SPL as of February 28, 2011 prepared by Raymond Chabot Grant Thornton, CPA ("RCGT") (Exhibit AR-2, tab 7L; the "RCGT Statements")?

(2) Should the Shareholders' Equity of SPL and, consequently, the fair market value of the shares of SPL, be reduced by the amount of the advances made to a director in SPL ("Directors' Advances") and, in the affirmative, what is the amount that should be deducted ($2,257,132 as indicated on the Internal Statements or $1,904,422 as indicated on the RCGT Statements)?

(3) Should the Shareholders' Equity of Holdco and, consequently, the fair market value of the shares of Holdco, be reduced by the amount of the advances made to a shareholder ($1,144,887) ("Holdco Advances")?

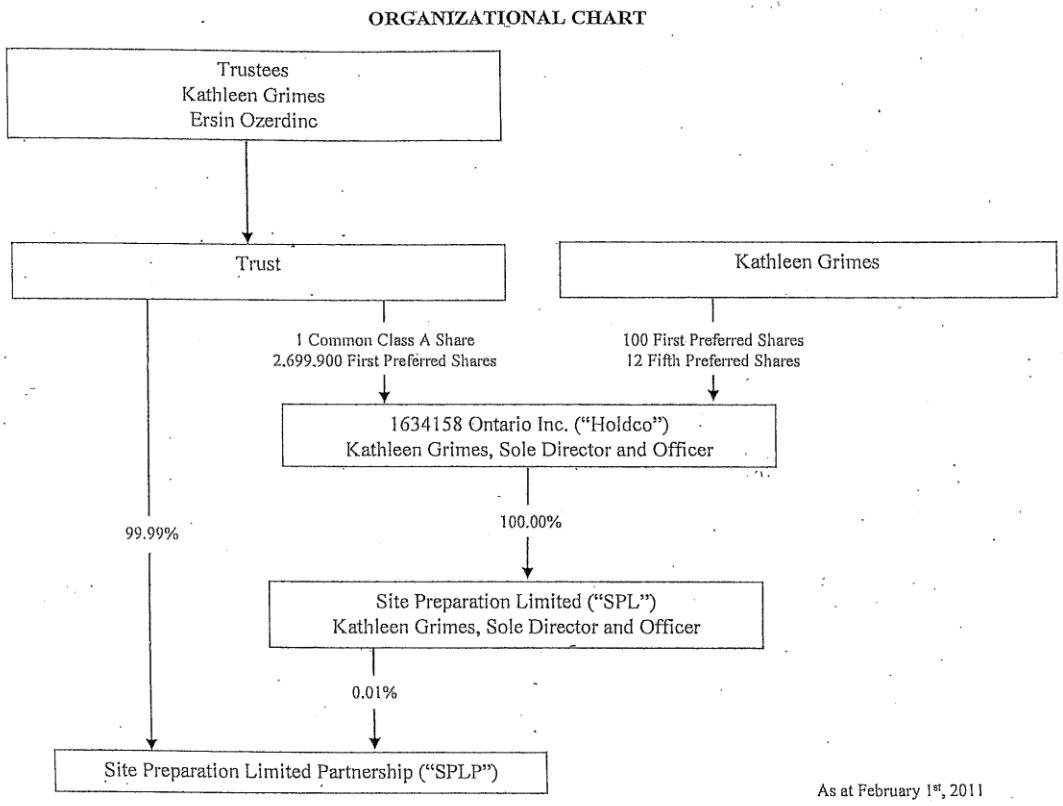
(4) Should embedded income taxes be considered in determining the fair market value of the shares of Holdco?

(5) Should a minority and/or marketability discount(s) be applied in the evaluation of the fair market value of the Class A Common Share of Holdco held by the Trust?

D. THE FACTS.

1. Organizational Chart.

[18] At the hearing, the Appellant filed an organizational chart under Exhibit A-2:



2. Agreed Statement of Facts (Partial).

[19] The parties also filed an Agreed Statement of Facts (Partial) under Exhibit AR-1, which is reproduced in its entirety in Appendix A to these reasons.

At the hearing, the parties indicated that paragraph 31 should be amended to refer to 2,699,900 First Preferred Shares instead of 2,700,000 First Preferred Shares.

3. Testimony of Ms. Grimes.

3.1 Background.

[20] Ms. Grimes testified at trial. She is one of two trustees of the Trust, the other trustee being her husband, Mr. Ersin Ozerdinc. She is also corporate counsel for SPL and was the sole director, president and secretary-treasurer of SPL at all material times (para. 18 of the Agreed Statements of Facts, Exhibit AR-1). Furthermore, she was in 2011 and 2012, the director, president and the secretary-treasurer of Holdco; positions which she currently holds.

[21] She testified that she and her husband have been in business together since 1986. Since 1990, they have been operating SPL, which is active in the industrial, commercial and institutional sectors of the construction industry. SPL also performs excavation and shoring. At all material times, Mr. Ersin Ozerdinc and Ms. Grimes played and continue to play key management roles in SPL, as indicated in paragraph 17 of the Agreed Statements of facts (Exhibit AR-1).

[22] In 2005, Holdco was created. The reason behind the creation of Holdco was to keep a minimal amount of cash in SPL; it was the intent of the controlling minds to transfer all extra cash to Holdco.

[23] Ms. Grimes and her husband were trustees for the Ozerdinc Family Trust (the "Original Trust") which was settled in 1990. According to Ms. Grimes, the Trust was settled in 2007 pursuant to the legal advice of the Ozerdinc family's counsel at that time; the objective was to allow a transfer without tax consequences of all the assets of the Original Trust to the Trust.

[24] In the fall of 2012 (probably around the end of October), an agent of Canada Revenue Agency (the "CRA") informed Ms. Grimes that he was performing an audit of the Trust. As a result of this audit, the Trust was subject to a significant tax burden because of the application of the 21-year deemed disposition rules. According to Ms. Grimes, the result of the audit came as a total surprise to her. She was not aware of any tax consequences that could result from the holding of assets by the Trust. Both parties engaged in lengthy discussions about the proper valuation of the assets held by the Trust (Exhibit AR-2, tab 26 — letter from CRA explaining CRA's position on the deemed disposition following the meeting of

November 7, 2012). Furthermore, a legal proceeding has been commenced (and is still pending) in the Ontario Superior Court of Justice by Ms. Grimes, her husband, Holdco, SPL, the Trust and other parties against the legal counsel who had proposed and implemented the 2007 reorganization, including the creation of the Trust, alleging the legal counsel's negligence and claiming damages resulting, *inter alia*, from the application of the 21-year deemed disposition rules to the Trust (Exhibit AR-2, tab 11) (the "Civil Litigation").

3.2 Holdco Advances.

[25] Ms. Grimes explained that dividends received from SPL are the sole source of revenue of Holdco. Holdco is controlled by Ms. Grimes in her personal capacity through the ownership of shares (approximately 69% of the voting rights).

[26] A total amount of $1,144,887 (namely, the Holdco Advances) was transferred by Holdco to Ms. Grimes qua trustee in order to finance the purchase of an interest in a cooperative housing unit in New York City (the "Co-op"), allowing one of her sons, who was then living in New York and who is a beneficiary of the Trust, to reside in an unit of the Co-op. According to Ms. Grimes, since the Co-op did not allow the Trust to purchase an interest in the Co-op, Ms. Grimes and her husband had to make the purchase in their own names. The closing took place in April 2011. According to the financial statements of Holdco for the year ending February 28, 2011, an advance to a shareholder in the amount of the Holdco Advances (Exhibit AR-2, tab 1D) was made.

[27] Ms. Grimes insisted that the Holdco Advances were made to her as trustee, and not personally. She also insisted that there was no intent to ever pay back the Holdco Advances to Holdco.

[28] According to Ms. Grimes, dividends would be declared by Holdco to the Trust in order to settle the amount of the Holdco Advances. In fact, dividends in an aggregate amount of $2,107,965 had been made payable during the months of January and February 2012 (Exhibit AR-2, tabs 4, 5 and 6) to the holders of the common shares of Holdco (namely, the Trust). The beneficiaries of the Trust were allocated the whole amount as a dividend and were taxed on said income in 2012 (copies of T3 statement, Exhibit AR-2, tab 30). According to the financial statements of Holdco for the year ending February 29, 2012, an amount of nil is found under the heading "advances to a director" (Exhibit AR-2, tab 1E).

3.3 Directors' Advances.

[29] With respect to compensation received from SPL by Ms. Grimes and her husband for their work in SPL, Ms. Grimes explained that she and her husband are compensated by SPL by way of bonuses and they operate by way of a Shareholders' Account. The amount stated in the Shareholders' Account reflects all of their personal expenses (groceries, schooling fees, children's expenses, etc.). At the end of each fiscal year, Ms. Grimes meet with their accountants to determine the amount of the bonus to be paid by SPL to Ms. Grimes and her husband which will be equal to the amount stated in the Shareholders' Account and which was used for personal purposes; then, the Shareholders' Account will be reduced accordingly by way of a set-off against the bonuses. Taxes would be paid on this amount. Ms. Grimes and her husband do not receive a regular salary from SPL; they do not receive any compensation from their work apart from said bonuses.

[30] In cross-examination, counsel for the Respondent referred to the Internal Statements, in particular an item called "Office salaries" in the amount of $99,013.06. According to Ms. Grimes, this amount does not include the bonuses since the bonuses are declared at year-end; this refers to salaries paid to office staff only. In the Internal Statements is found an item called "Shareholders Advances" in the amount of $2,257,132.34. Even if it refers to Shareholders' Advances, it is, in fact, the amount of the Directors' Advances. In the RCGT Statements, this item is referred to as "Advances to directors" in an amount of $1,904,422. On the Financial Statements of SPL for the period ending Feb. 29, 2012 (Exhibit AR-2, tab 7M), this same account is nil. The Agreed Statement of Facts (Partial) (Exhibit AR-1, para. 34) sets out the history of the year-end balances of the advances to a director in SPL and confirms a full repayment of the advances in 2012.

[31] Furthermore, paragraph 35 of the Agreed Statement of Facts (Partial) (Exhibit AR-1) states the remuneration received by each of Ms. Grimes and her husband from SPL for calendar years 2000 to 2013. More specifically, in 2011, each received an amount of $400,000 and, for 2012, each received an amount of $616,025.

3.4 Credibility Findings.

[32] I am of the view that the testimony of Ms. Grimes was credible; she was a very straightforward witness. Furthermore, in view of her interaction with the CRA agent and counsel for the Respondent, I find that Ms. Grimes' testimony reflects the true facts.

(a) In respect of Holdco:

[33] I find that the Holdco Advances were made to Ms. Grimes as trustee of the Trust, and not personally, in order to finance the acquisition of the interest in the Co-op.

[34] The fact that the purchase of the interest in the Co-op was made by Ms. Grimes and her husband personally does not change my conclusion, as Ms. Grimes had indicated that she had been told that the Co-op did not allow a trust to purchase an interest in the Co-op. Her belief as to the veracity of this statement explains her conduct.

[35] Furthermore, Article 10 of the Agreement creating the Trust provides that the assets constituting the trust fund shall be held by, and registered in, the name of the trustees or their nominees or otherwise, as the trustees may deem expedient (Exhibit AR-2, tab 22). Accordingly, I accept that the fact that the interest in the Co-op was in Ms. Grimes' and Mr. Ozerdinc's names, without mention of the Trust, will not preclude a finding that the interest was held by them as trustees of the Trust.

[36] Counsel for the Respondent argued that since the funds were transferred by Holdco to Ms. Grimes' personal US account, this is an indicia that the Holdco Advances had been made to her personally and not as trustee (Exhibit AR-2, tab 2). In accordance with Ms. Grimes' credible testimony, and having regard to Article 10 of the Agreement creating the Trust, this argument does not change my conclusion.

[37] I also note that the financial statements of Holdco for the year ending February 29, 2012 refer to advances to a director but that the financial statements for the year ending February 28, 2011 refer to advances to a shareholder. Counsel for the Respondent did not make submissions on that difference in wording. However, since these financial statements have not been audited, I decline to give any weight to that change of language.

[38] Furthermore, counsel for Respondent insisted on the fact that the financial statements of Holdco have an item called "Due to a shareholder". Consequently, according to the Respondent, if the Holdco Advances have been made to the Trust, there would have been a set-off in the Financial Statements. However, since these financial statements have not been audited, and in view of Ms. Grimes' testimony, I do not accept this argument.

[39] Also, I find that Ms. Grimes, as trustee of the Trust, had no intention to ever repay the Holdco Advances by way of a transfer of cash to Holdco. Her testimony was very clear in that regard (see transcript, June 8, 2016, page 80, lines 13 and following).

[40] The payment of the dividend by Holdco to the Trust in 2012 by way of set-off against the Holdco Advances confirms that such was the parties' intention throughout the relevant period. I recognize that the corporate resolutions contain very broad language without referring specifically to the set-off (Exhibit AR-2, tabs 4, 5 and 6); however, I stand by Ms. Grimes' justification of the facts surrounding the Holdco Advances.

(b) In respect of SPL:

[41] From Ms. Grimes' testimony, I understand that SPL's day-to-day operations are controlled by her and her husband and that the transactions pertaining to the bonuses are decided by Ms. Grimes and the accountants at year-end. The facts also established very clearly that no regular salary is received by Ms. Grimes and Mr. Ozerdinc; more specifically, it was established that Ms. Grimes and Mr. Ozerdinc did not receive compensation from SPL from March 1, 2010 to the Valuation Date, except for the bonuses.

[42] In my view, it is clear that the amounts forming part of the Shareholders' Account (or Advances to Directors) in SPL would never be repaid in cash to SPL. As Ms. Grimes explained, this formed part of a long-standing practice (even if at the beginning of their business operations, they would put money in SPL in order to cover the expenses).

4. Valuation of the Shares.

[43] Various exhibits were filed by the parties in respect of the valuation of the issued and outstanding shares of Holdco.

[44] Exhibit A-4 includes a copy of a letter dated May 16, 2013 sent by James Craigen of the Regional Valuation Unit of the CRA to Ms. Grimes which purported to establish the fair market value of the Trust's property as of the Valuation Date at $11,806,268 (the "CRA May Letter"). This letter is a draft proposal as per paragraph 9 of said letter.

[45] Exhibit A-5 includes a copy of a letter dated July 17, 2013 sent by counsel for the Appellant to James Craigen containing submissions in respect of the CRA May Letter (the "Submissions").

[46] Exhibit A-6 includes a copy of a letter dated September 17, 2013 sent by James Craigen to Ms. Grimes establishing "the fair market value of the outstanding Trust units" as of the Valuation Date at $9,498,511. To this letter was also attached the Estimate Valuation Report dated September 3, 2013 (the "Craigen Report"). This last letter completed the work of Mr. Craigen in the Appellant's file.

[47] I took Exhibit A-7 under reserve at the hearing. I will allow that exhibit to be entered into evidence as I am of the view that it is relevant to my inquiry.

[48] A critique of the Craigen Report made by MNP was filed as Exhibit A-9. The Respondent objected to it on the basis of non-compliance with the *Tax Court of Canada Rules (General Procedure)* in respect of expert reports. However, at the hearing, I determined that this report was not being offered by the Appellant as an expert report but rather as evidence pertaining to the Appellant's attack on the assumptions contained in the Reply. As such, I allowed it to be entered into evidence.

[49] Exhibit R-3 contains a letter from RCGT dated October 5, 2006 (the "RCGT Letter"), purporting to give a valuation of the shares of SPL for the purposes of the reorganisation of the corporate group in 2007. I will discuss the RCGT Letter below.

4.1 Testimony of Mr. Blackman, the MNP Report and the Addendum.

[50] Exhibit A-10 contains an Estimate Valuation Report on the valuation of Holdco and SPL dated June 19, 2014 and prepared by Richard M. Wise and Mr. Blackman of MNP LLP (the "MNP Report").

[51] Exhibit A-11 contains an Addendum to the MNP Report dated October 30, 2014 and prepared by Mr. Wise and Mr. Blackman (the "Addendum"). The Respondent objected to the qualification of the Addendum as an expert report; I will examine that issue below.

[52] Ms. Grimes confirmed in cross-examination that she did not discuss with Mr. Wise or Mr. Blackman the report filed as Exhibit A-10. The Addendum was prepared by MNP following a request Ms. Grimes had received from her lawyer in

respect of the Civil Litigation; she did not commission the production of the Addendum to bolster her case in this appeal.

[53] The Respondent did not object to the expert status of Mr. Blackman. Given the extensive experience, publications and qualifications of Mr. Blackman on the valuation of shares of private corporations and given the similar and extensive experience and qualifications of Mr. Wise, I have determined that Mr. Blackman is an expert on valuation of shares and of businesses and that the MNP Report is an Expert Report.

[54] MNP was hired to provide an estimate of the fair market value as of the Valuation Date of all of the issued and outstanding shares, viewed *en bloc*, of the share capital of Holdco, including its 100% holdings of the issued and outstanding shares, viewed *en bloc*, of SPL.

[55] The MNP Report defines "fair market value" as "the highest price, expressed in terms of cash equivalents, at which property would change hands between a hypothetical willing and able buyer and a hypothetical willing and able seller, acting at arm's length in an open and unrestricted market, when neither is under compulsion to buy or sell and when both have reasonable knowledge of the relevant facts" (para. 1.1 of the MNP Report).

[56] According to the MNP Report, the fair market value of all the issued and outstanding shares of Holdco as of the Valuation Date was approximately $3,556,000, allocated as follows:

i) 2,700,000 First Preferred Shares: $2,031,000

ii) 12 Fifth Preferred Shares: $190,000

iii) 1 Class A Common Share: $1,335,000

[57] In arriving at this estimate, Mr. Blackman reviewed, *inter alia*, the Craigen Report, the unaudited financial statements of Holdco for the two fiscal years ended February 28, 2011, as compiled by RCGT (Exhibit AR-2, tab 1D), the RCGT Statements, the Internal Statements and copies of the CRA May Letter and the Submissions.

[58] According to Mr. Blackman, there are three basic approaches for valuing a business: the Asset-Based (Cost) Approach, the Income Approach and the Market

Approach. In certain cases, a combination of the foregoing approaches may be appropriate.

[59] Mr. Blackman explained to the Court that, in this particular case, the "Asset-Based Approach" was used as the method to evaluate the fair market value of Holdco and SPL considering, *inter alia*, that Holdco is "a holding company whose main asset is its 100% interest in SPL and . . . SPL generates all of its revenues through the bidding and tendering process and as such does not have ongoing contracts with its customers, as a result, it has no goodwill . . ." (para. 8.6 of the MNP Report). It is to be noted that the same method was used in the Spencer Report (as defined below).

[60] In applying this method, all assets and liabilities of Holdco and SPL as indicated in the balance sheets at their respective book values, were written up or down to their respective fair market value as of the Valuation Date on a going concern basis, and further adjustments were made to recognize the tax impact where applicable.

(a) Valuation of the shares of SPL:

[61] Taking the Shareholders' Equity as indicated in the RCGT Statements ($5,985,744), the loss of $95,027 for February 2011 (total loss for that month of February was $730,822 of which $635,795 was applicable to the prior eleven months ended January 31, 2011) was added back to arrive at the Shareholders' Equity as of the Valuation Date of $6,080,771.

[62] Then, the following adjustments were made to arrive at the Adjusted Shareholders' Equity of $3,008,668 before income tax considerations:

i) An amount of $21,430 was deducted, representing the loss on investments (as per the Craigen Report — fair market value of the investments ($3,029,311) minus the book value ($3,050,741));

ii) An amount of $203,549 was added, representing the increase in the fair market value of the land (as per the Craigen Report – fair market value of the land ($260,000) minus the disposition costs (6%) discounted by 50% ($7,800), namely $252,200 minus the book value ($48,661));

iii) An amount of $997,080 was deducted to reflect the unpaid taxes on the deferred income for tax purposes ($3,561,000 X 28%);

iv) An amount of $2,257,132 was deducted representing the advances to directors (namely, the Directors' Advances).

[63] Finally, in order to take into account income taxes resulting from the sale of the land (gain) and the investments (loss), an amount of $21,000 representing the taxes on the disposition of the land and investments was deducted and an amount of $56,000 representing the refundable dividend tax on hand ("RDTOH") to be recovered (already existing as well as resulting from the capital gain from the sale of the land) discounted at 50% was added. Consequently, the Adjusted Shareholders' Equity of SPL was determined to be $3,043,668; an estimate of the fair market value of the shares of SPL was set at $3,044,500.

(b) Valuation of the shares of Holdco:

[64] Taking the Shareholders' Equity as indicated in the unaudited Financial Statements for the year ended February 28, 2011 ($2,789,286) and, assuming there were no material changes, Mr. Blackman determined that this amount is also the Shareholders' Equity as of the Valuation Date.

[65] The following adjustments were then made to arrive at the Adjusted Shareholders' Equity of $4,727,122:

i) An amount of $3,044,300 was added to reflect the fair market value of the shares of SPL ($3,044,500) over the book value ($200);

ii) An amount of $1,144,887 was deducted representing the Holdco Advances; and

iii) An amount of $38,423 was added representing an amount due to a shareholder.

[66] That amount of $4,727,122 was then allocated to the various classes of shares of Holdco as follows:

i) 2,700,000 First Preferred Shares: $2,700,000, representing the redemption amount of the shares;

ii) 12 Fifth Preferred Shares: $253,391, representing an amount of $1 (redemption amount) and an amount of $253,390 as a voting control premium calculated as 12.5% of $2,027,122 (this amount is the

difference between $4,727,122 and $2,700,000) (these shares carry 68.97% of the votes, the balance of the votes being held by the Class A Common Share and the First Preferred Shares; in fact, Ms. Grimes holds approximately 68.97% of the votes of Holdco personally);

iii) 1 Class A Common Share: $1,773,731, representing the difference between $2,027,122 and $253,391 (attributed to the 12 Fifth Preferred Shares). As Mr. Blackman has explained to this Court, the reduction of $253,391 is, in fact, a minority discount, representing the premium attributed to the 12 Fifth Preferred Shares.

[67] Finally, in order to determine the fair market value of the shares of Holdco, Mr. Blackman reduced the value as determined above by an estimate of taxes on redemption or purchase for cancellation of the shares. The personal income tax rate of 49.53% was discounted by 50%. As stated in Schedule A-1 of the MNP Report, the fair market value of the shares of Holdco was then determined as follows:

i) 2,700,000 First Preferred Shares: $2,031,000 ($2,700,000 minus the aggregate of $100 and the taxes of $669,000);

ii) 12 Fifth Preferred Shares: $190,000 (rounded) ($253,391 minus the taxes of $63,000);

iii) 1 Class A Common Share: $1,335,000 (rounded) ($1,773,731 minus the taxes of $439,000).

[68] According to the Addendum, Mr. Blackman provided an estimate of the fair market value of the Class A Common Share of Holdco on a stand-alone basis as of the Valuation Date. Mr. Blackman explained to the Court that this means not in a family context. He applied a marketability discount to the Class A Common Share of Holdco.

[69] As stated in paragraph 2.1.1 of the Addendum, marketability is "the ability to convert the business ownership interest to cash quickly, with minimal transaction and administrative costs in so doing and with a high degree of certainty of realizing the expected amount of proceeds". The market will apply a discount when there is a lack of marketability or lack of liquidity as opposed to a ready marketability that will add value to a share.

[70] Factors listed in paragraph 2.1.2 of the MNP Report (which I will review below in more details) and the rights and privileges attributable to the share were considered in quantifying the marketability discount applicable to the Class A Common Share of Holdco. Considering the lack of control, the limited market for the share, various empirical studies that have quantified the marketability discount in the range of 15% to 45% and studies of the price relationship between private share transactions and subsequent initial public offering that were in the range of 40% to 65%, Mr. Blackman concluded that a marketability discount in the range of 25% to 35%, or mid-point of 30% would be appropriate, giving the illiquid nature of the share.

[71] The discount of 30% applicable to the fair market value of the Class A Common Share represents an amount of $400,500 (30% of $1,335,000). Accordingly, in accordance with the Addendum, the fair market value of the Class A Common Share of Holdco is $935,000, on a stand-alone basis.

4.2 Testimony of Mr. de Gray and the CVPL Report.

[72] CVPL was hired by the Respondent to review and critique the MNP Report and the Addendum. CVPL produced a Limited Critique Report dated April 8, 2016 and co-authored by Neil de Gray and Howard E. Johnson (the "CVPL Report") which was filed as Exhibit R-5. The Appellant did not object to the expert status of Mr. de Gray.

[73] Given the experience and qualifications of Mr. de Gray and Mr. Johnson in the valuation of shares of private corporations, I have concluded that Mr. de Gray is an expert on the valuation of shares and of businesses and that the CVPL Report is an Expert Report.

[74] It is important to note that paragraph 1.10 of the CVPL Report states that:

> This Limited Critique Report does not contain our opinion or conclusion as to the FMV of the Shares and does not contain all the adjustments that may be required to arrive at a conclusion as to the FMV of the Shares. We have not been asked to prepare an independent valuation report setting our estimates of the FMV of the Shares. This Limited Critique Report provides comments on the MNP Report and MNP Addendum and illustrates the quantification of our identified adjustments.

[75] In the CVPL Report, the fair market value is defined as "the highest price available in an open and unrestricted market between informed and prudent parties acting at

arm's length and under no compulsion to act, expressed in terms of cash" (para. 1.8 of the CVPL Report).

[76] The CVPL Report states that the MNP Report had understated the fair market value of the shares of Holdco as follows:

i) In respect of the fair market value of Holdco's interest in SPL, by erroneously deducting an amount due from a director of SPL in the amount of $2,257,132;

ii) By erroneously deducting an amount due from a shareholder of Holdco in the amount of $1,106,464 (net); and

iii) By erroneously deducting personal income taxes in the determination of fair market value of each class of shares which reduces the value ascribed to the shares of Holdco by $1,171,000.

[77] According to the CVPL Report, the fair market value of the shares of Holdco, viewed *en bloc*, should be equal to $8,090,000 (as opposed to $3,556,000 as indicated in the MNP Report) and allocated as follows:

i) 2,700,000 First Preferred Shares: $2,700,000;

ii) 12 Fifth Preferred Shares: $674,000 (a control premium of 12.5% is reasonable according to CVPL: 12.5% X ($8,090,000 - $2,700,000)); and

iii) 1 Class A Common Share: $4,716,000.

[78] With respect to the Addendum, Mr. de Gray is of the view that the application of a minority or marketability discount to common shares in situations of family control is highly unusual, and there appears to be no basis in Holdco's situation for such a minority discount. Mr. de Gray said that, generally, minority and marketability discount would be considered together. However, if we were to apply a minority discount of 30%, the fair market value of the Class A Common Share of Holdco would be equal to $3,301,000 (as opposed to $4,716,000).

[79] The CVPL Report also contains some general comments on the MNP Report. Mr. de Gray had accepted as reasonable in all material respects the valuation method used by MNP namely the Adjusted Net Book Value

Methodology, for the purposes of valuing the shares of SPL and Holdco, as well as the treatment by MNP of the following items: land, investments, RDTOH considerations and the taxes on deferred income.

4.3 Testimony of Mr. Spencer and the Spencer Report.

[80] The Respondent called Mr. Timothy Spencer to testify as an expert witness. Mr. Spencer has been a valuation specialist with the CRA since 2010. Mr. Spencer is a CPA, CA, and also a chartered business valuator (CBV) since 2008. He has been employed by CRA since 2008 and has been a member of the valuation group since 2006. However, this was his first appearance in court as an expert witness. He became involved in the Appellant's file around August 28, 2014, when he was contacted by his team leader and counsel for the Respondent. Mr. Spencer's report, which is a Comprehensive Valuation Report (as opposed to the MNP Report, which is an Estimate Valuation Report), was filed as Exhibit R-4 (the "Spencer Report"). Mr. Spencer's mandate was to determine the fair market value of all the issued and outstanding shares of Holdco as of the Valuation Date.

[81] The Appellant objected to the qualification of Mr. Spencer as an expert witness. After hearing the submissions of the parties, I ruled that Mr. Spencer is an expert in the valuation of equity securities and debt instruments and that the Spencer Report was an Expert Report.

[82] In the Spencer Report, the fair market value is defined as "the highest price available in an open and unrestricted market, between informed and prudent parties acting at arm's length and under no compulsion to transact, expressed in terms of money or money's worth" (paragraph 5 of the Spencer Report).

[83] Mr. Spencer concluded that the fair market value of all the issued and outstanding shares of Holdco as of the Valuation Date was $9,057,001, allocated as follows:

i) 2,700,000 First Preferred Shares: $2,700,000;

ii) 12 Fifth Preferred Shares: $1; and

iii) 1 Class A Common Share: $6,357,000.

[84] In arriving at this estimate, Mr. Spencer reviewed, *inter alia*, the unaudited financial statements of Holdco for the five fiscal years ended February 28, 2011, as

compiled by RCGT (Exhibit AR-2, tabs 1A to D), the audited financial statements of SPL for the five fiscal years ended February 28, 2011, as reported by RCGT (Exhibit AR-2, tabs 7H to L), the Internal Statements, copies of the Submissions, the MNP Report, the Addendum, and the articles of incorporation of Holdco and SPL.

[85] Mr. Spencer used the Adjusted Net Book Value Method to evaluate the shares of Holdco. Mr. Spencer explained that, in applying this method, the value is determined by adjusting the Shareholders' Equity, as stated in the financial statements, by adding (or deducting) an amount by which the fair market value of the assets exceeds their book value (or loss), deducting (or adding) the amount by which the market value of the business' liabilities exceeds their book value (or loss), deducting the book value of intangible assets, adding (deducting) deferred income tax credits (debits), and deducting the present value of the lost tax shield. The same method was used by Mr. Blackman.

(a) Valuation of the shares of SPL:

[86] Taking the Shareholders' Equity as of January 31, 2011 as indicated in the Internal Statements ($7,073,019), Mr. Spencer added the net increase to investments of $64,061, the adjusted value of the land of $132,217 and the Management fees due from SPLP of $121,409. Then, he deducted the book value of the land ($48,661) and the income tax on deferred income ($1,074,166), to arrive at the Adjusted Net Book Value of $6,267,879.

[87] With respect to the land, Mr. Spencer estimated that the fair market value was equal to the municipal valuation of $145,000 (Exhibit AR-2, tab 18 — Municipal Property Assessment Corporation (MPAC) which states that, for 2012, the property value is $145,000 (as opposed to the MNP Report who took the value as estimated in the Craigen Report of $260,000). Mr. Spencer explained that he chose that number in order to be more conservative. In arriving at the proceeds of disposition of $140,650, Mr. Spencer deducted disposition cost of 6% discounted at 50% ($4,350). Then, he calculated the capital gains, deducting from the disposition cost an amount of $48,661 to arrive at a capital gain of $91,989, of which half is taxable, namely $45,995. He calculated the embedded taxes to be paid on a notional disposition of the land as follows: 50% rate, less the RDTOH of 26 2/3% and discounted the taxes by 50%, to arrive at an amount of $8,433. The adjustment of $132,217 was calculated by deducting the amount of embedded taxes from the proceeds of disposition (Schedule 2 notes of the Spencer Report).

[88] With respect to the management fees from SPLP, Mr. Spencer added an amount of $121,409, calculated as the difference between the 2010 Management fees from SPLP ($173,442) (Exhibit AR-2, tab 7L, note 16) and the tax at 30% payable on such income ($52,033).

[89] With respect to the deduction for income tax on deferred income ($1,074,166), Mr. Spencer took the net reserve for contracts not completed at year end (Exhibit AR-2, tab 17) and applied a rate of 30% of taxes.

[90] Mr. Spencer did not make any adjustment with respect to RDTOH.

(b) Valuation of the shares of Holdco:

[91] Taking the Shareholders' Equity as indicated in the unaudited Financial Statements for the year ended February 28, 2011 ($2,789,286), assuming that there were no material changes and noting the absence of any financial statements as of February 1, 2011, Mr. Spencer determined that this amount is also the Shareholders' Equity as of the Valuation Date.

[92] Then, the following adjustments were made to arrive at the Adjusted Net Book Value of $9,056,965:

i) An amount of $6,267,879 was added to reflect the Adjusted Net Book Value of the shares of SPL; and

ii) An amount of $200 was deducted to reflect the book value ($200) of the shares of SPL.

[93] Mr. Spencer did not make any adjustments to take into account the net increase to investments, as it was immaterial. In addition, he did not make any adjustment for the existing RDTOH of Holdco (note 4 to Schedule 1 of the Spencer Report).

[94] That amount of $9,056,965 was then allocated to the various classes of shares of Holdco as follows:

i) 2,700,000 First Preferred Shares: $2,700,000 (equal to their redemption amount);

ii) 12 Fifth Preferred Shares: $1 (redeemable at $0.10 each); and

iii) 1 Class A Common Share: $6,356,963, namely the remainder.

[95] Mr. Spencer explained to the Court that a minority discount is the reduction from the pro-rata portion of the *en bloc* value of the shares as a whole to reflect the disadvantages of owning a non-controlling interest. Accordingly, the Class A Common Share could be subject to a minority discount. However, Mr. Spencer was of the opinion that no minority discount should be applied to said share considering the factors listed in paragraph 70 of the Spencer Report, which I will review below.

[96] Mr. Spencer explained the concept of liquidity discount and marketability discount. A liquidity discount relates to the relative ease of converting non-cash assets into cash. The marketability discount relates to the relative ease of selling a given corporate shareholding or business interest. He further explained that, given the corporate structure and corporate assets held, he has combined these two types of discounts. Mr. Spencer is of the view that no marketability/liquidity discount should be applied in the evaluation of the Class A Common Share of Holdco considering the factors listed in paragraph 72 of the Spencer Report, which I will review below.

[97] Finally, Mr. Spencer made it clear in his testimony that his valuation of the shares of Holdco was based entirely on the fact that Holdco will be sold as a whole and that a purchaser will acquire all the issued and outstanding shares of the capital of Holdco and thus, would acquire control of Holdco on the notional purchase.

E. ANALYSIS.

1. Differences between the MNP Report and the Spencer Report.

[98] The experts were in agreement in respect of some elements that have to be taken into account in the valuation of the shares: the investments and the land owned by SPL as well as the fact that the First Preferred Shares of Holdco derive their value from the redemption and retraction features of the shares.

[99] I will review some of these elements below.

1.1 Valuation of the shares of SPL.

[100] Adjustments made to the Shareholders' Equity calculation in SPL are essentially the same in both reports, apart from the reduction made in the MNP Report for the Directors' Advances ($2,257,132).

[101] In the Spencer Report, the Shareholders' Equity was reduced by $805,140. In the MNP Report, it was reduced by $786,536.

[102] The most important adjustment is the reduction of the Shareholders' Equity in respect of income taxes on deferred income that will be paid in the next fiscal year. According to the MNP Report, an amount of $997,080 should be taken into account and deducted on account of this, but the Spencer Report calculated an amount of $1,074,166 in that respect. In my view, the correct amount is $1,002,555, taking the correct tax rate of 28% and the amount as confirmed by Management of said deferred income, namely $3,580,554.

[103] Another adjustment made is the increase in the value of the Land owned by SPL. Mr. Blackman used the value stated in the Craigen Report, which I do not accept. I am of the view that the proceeds of disposition of $145,000, as used by Mr. Spencer in making his calculation, should be used. I was not able to find any reference to $260,000 as being specified as such proceeds of disposition in the Craigen Report. The tax rate that should be used is 46.2% and not 50%. Accordingly, a net amount of $81,364 should be added to the Shareholders' Equity in respect of the Land (see Appendix C and Appendix D attached hereto).

[104] In respect of the investments owned by SPL, Mr. Blackman deducted an amount of $21,430 as a loss; this amount of loss was taken from the Craigen Report. However, Mr. Spencer added an amount of $64,061 as a net increase. This amount of net increase to investment in the amount of $64,061 was calculated by Mr. Spencer assuming that the change in value in the portfolio of assets was interest and taxed annually at the full rate of 50%; however, having examined the investment statements filed at Exhibit AR-2, tabs 15 and 16, I see that half of the investments are publicly listed shares; accordingly, I would conclude that it is reasonable to assume that half of the increase in value would be capital gains, of which only half is taxable. Furthermore, the tax rate to be used is 46.2% and not 50%. Accordingly, I would calculate the increase in the value of the investments to be $128,122 (as per the Spencer Report) and estimate the taxes at $22,197 (see Appendix D). Since it is not clear as to how the loss was calculated in the Craigen Report and since it took the adjusted cost base of the assets as indicated in the financial statements of SPL for the year ended February 28, 2011, I am of the view that, subject to my comments above, the calculation made by Mr. Spencer is more

accurate since the latter took the figures as of the Valuation Date. Hence, I will add a net amount of $105,925 to the calculation of the Shareholders' Equity of SPL in respect of the investments.

[105] The RDTOH of SPL was fully discounted by Mr. Spencer but Mr. Blackman added an amount of $56,000 in that respect. Mr. Spencer fully discounted the RDTOH in order to be more conservative. However, I am of the view that Mr. Blackman's analysis is more accurate, as confirmed by Mr. de Gray. Since I made some changes to the calculation of the revenues arising out of SPL, an amount of $62,810 should be added to the calculation of the Shareholders' Equity of SPL in respect of the RDTOH (see Appendix D).

[106] Finally, with respect to the management fees of $121,409 due from SPLP (taxed at a rate of 30%), I note that Mr. Blackman did not make any adjustment in that respect, but Mr. Spencer did. Since Mr. Spencer took the Internal Statements, he had to increase the Shareholders' Equity of SPL in that respect. However, since Mr. Blackman took the RCGT Statements and given that the management fees were already accounted for in said statements, there was no need to make such adjustment. My conclusion in respect of the management fees will then depend of my answer to the starting point for the valuation of the shares of SPL. If I conclude that the RCGT Statements are the starting point, then there will be no need for adjustments; however, if I conclude that the Internal Statements are the starting point, then an adjustment will have to be made in that respect.

1.2 Valuation of the shares of Holdco.

[107] In the calculation of the Shareholders' Equity of Holdco, both experts took the same starting point (the financial statements of February 28, 2011) since Ms. Grimes said that there would not be any difference between the end of February and the Valuation Date. The MNP Report however reduced the Shareholders' Equity by the amount of the Holdco Advances ($1,144,887) and added the amounts due to a shareholder ($38,423). No such reduction was made in the Spencer Report.

[108] Furthermore, as mentioned above, the Spencer Report did not apply any minority, marketability or liquidity discount to the fair market value of the Class A Common Share of Holdco and did not apply any premium when calculating the fair market value of the controlling shares of Holdco held by Ms. Grimes (namely, the 12 Fifth Preferred Shares).

[109] These issues will be discussed below.

2. Starting point for the valuation of the shares of SPL.

[110] Mr. Blackman was of the opinion that the starting point for the valuation of the shares of SPL should be the RCGT Statements. According to Mr. Blackman, the RCGT Statements, having been audited, are the most reliable and, therefore, more representative of the Shareholders' Equity than the Internal Statements. Audited financial statements would contain all the proper "adjustments that are required to properly reflect the assets, liabilities, earnings and expenses of the company" (Transcript, June 8, 2016, page 162, lines 3 to 7). Since the RCGT Statements were prepared for the period ending on February 28, 2011, Mr. Blackman made some adjustments in respect of the salaries and apportioned the salaries to the whole fiscal year in accordance with the matching principles to arrive at the Shareholders' Equity of SPL as of the Valuation Date of $6,080,771.

[111] In cross-examination, Mr. de Gray testified that he did not disagree with the starting point used by Mr. Blackman as explained in the MNP Report. Mr. de Gray added that an adjustment made in respect of the salaries amounted to a recognition that $635,000 plus $99,000 was declared as salary for that 11-months period ending on January 31, 2011 (Transcript, June 9, 2016, page 167).

[112] In contrast, Mr. Spencer was of the opinion that the starting point should be the Internal Statements. Under cross-examination, Mr. Spencer testified that he considered using the RCGT Statements, but he did not use them because the Internal Statements were available. He added that any adjustments made in the RCGT Statements, which would have been made at year-end, hence after the Valuation Date, would be based on hindsight. Furthermore, since valuation is a point-in-time issue, the Internal Statements should be used to determine the fair market value as of the Valuation Date since these statements are the closest to the Valuation Date.

[113] I do not agree with Mr. Spencer's reasoning that all adjustments made by the auditors in the RCGT Statements are based on hindsight information. As Mr. Blackman rightly said, adjustments made in audited financial statements are required in order to properly reflect the assets, liabilities, expenses and earnings of a person. These adjustments will be made to give the proper financial situation of a person at a given point in time and will be a reflection of the whole fiscal year; it may contain, for example, a provision for bad debts, amortization of fixed assets, etc. It is not reasonable to claim that the adjustments are based on hindsight

information, as the auditors would review the whole fiscal year to make the appropriate adjustments and would not only examine factors post-Valuation Date, as Mr. Spencer seems to argue. In this particular situation, it is not true that adjustments would reflect only circumstances arising after the Valuation Date.

[114] Furthermore, I am satisfied that, by making an adjustment to the salaries and by starting with the Shareholders' Equity of SPL as indicated in the RCGT Statements, the MNP Report properly determined the Shareholders' Equity of SPL as of the Valuation Date at an amount of $6,080.771. I am of the view that, by using the information found in the Internal Statements, Mr. Spencer's calculations are erroneous in that respect. I do not agree that the Internal Statements should be the starting point for the valuation due to their proximity to the Valuation Date. I am of the view that a proper valuation should start with financial statements that would best reflect the subject's financial situation. In this case, the RCGT Statements, which have the highest level of reliability due to proper adjustments having been made, would best reflect the financial situation of SPL.

3. The Advances.

[115] I have to determine whether (i) the Shareholders' Equity of SPL and, consequently, the fair market value of the shares of SPL, should be reduced by the amount of the Directors' Advances and, in the affirmative, what amount should be deducted ($2,257,132 as indicated in the Internal Statements or $1,904,422 as indicated in the RCGT Statements); and whether (ii) the Shareholders' Equity of Holdco and, consequently, the fair market value of the shares of Holdco, should be reduced by the amount of the Holdco Advances ($1,144,887).

3.1 The reasoning of the experts.

[116] According to Mr. Blackman, the objective of shareholders in a small company is to maximize their after-tax income. Since Ms. Grimes told him that she and her husband did not receive regular salaries and that the Directors' Advances would never be repaid under any circumstances, he felt that these advances should reduce the Shareholders' Equity of SPL. He had examined the financial statements of previous years and confirmed that SPL always operated in that way with respect to advances to directors. He was, therefore, satisfied that SPL would never receive a reimbursement in cash of the Directors' Advances but rather would offset these advances by way of bonuses. Accordingly, he concluded that the Directors' Advances should not be included in the fair market value of the shares of SPL. He testified that, by declaring a bonus, the Shareholders' Equity of SPL is reduced.

[117] Mr. Blackman testified that he deducted the Holdco Advances in the calculation of the Shareholders' Equity of Holdco for the same reasons. More particularly, as Ms. Grimes had advised Mr. Blackman that Holdco would proceed with a declaration of dividends in order to offset the Holdco Advances, and even if no dividends had been declared in previous years by Holdco and Holdco had no history of making advances, he was of the view that the Holdco Advances should reduce the Shareholders' Equity of Holdco and, consequently, the fair market value of the shares of Holdco.

[118] Paragraph 9.1.1(b) of the MNP Report specifically states that adjustments to Holdco's Shareholders' Equity were made, including "adjustments to reflect the write-down of the advances to a shareholder of $1,144,887 (Schedule A-3) which we were advised would not be repaid by way of a cash payment but rather by an offset from dividends that will be declared." At paragraph 9.2.1(b) of the MNP Report, it is stated that adjustments have been made to SPL's Shareholders' Equity, including "the advances to directors of $2,257,132 were written off as we were advised that such amount would not be repaid (see comments in Section 9.1.1(b))".

[119] Mr. Blackman is of the view that he did not use hindsight in order to conduct his evaluation. Under cross-examination, he confirmed that he peeked at the following year's information, which is for the year ending February 28, 2012, in order to confirm what he was told by Ms. Grimes with regards to the Holdco Advances and the Directors' Advances. According to Mr. Blackman, he certainly can use hindsight to corroborate assumptions that were made at the Valuation Date; however, he did not use hindsight to formulate his assumptions (Transcript, June 8, 2016, page 188, lines 11 to 28).

[120] Mr. Spencer testified that he did not look at anything that occurred after the Valuation Date. More particularly, with respect to dividends paid by Holdco and bonuses declared and paid by SPL after the Valuation Date, he is of the view that taking into account these payments to reduce the fair market value of the shares would be an impermissible use of hindsight (Transcript, June 9, 2016, pp. 97-98, lines 26 to 28 and lines 1 to 8). Since the RCGT Statements showed the Directors' Advances as a current asset of SPL and since the financial statements of Holdco for the year ended February 28, 2011 showed the Shareholders' Advances (namely, the Holdco Advances) as a current asset of Holdco, Mr. Spencer was of the view that these amounts were a receivable to SPL and Holdco respectively and represent amounts owed to SPL and Holdco and should be taken into account in the valuation of the shares. The fact that Ms. Grimes had confirmed to him that she and her husband had use of the money and had the financial means to repay the

Directors' Advances to SPL are relevant factors confirming his treatment of the Directors' Advances.

[121] In addition, even considering that Ms. Grimes had told him that there would be a bonus declared by SPL and a dividend paid by Holdco to offset these advances, Mr. Spencer would not have made any adjustment to his calculations since the RCGT Statements and the financial statements of Holdco for the period ending February 28, 2011 showed these advances as an asset and, accordingly, he would expect that these advances would be reimbursed. In his reasoning, Mr. Spencer also considered the fact that Ms. Grimes and her husband had the ability to repay the advances.

[122] According to Mr. de Gray, valuation is point-in-time specific and is based only on facts known at this point in time. Hindsight or retrospective evidence should not be considered. During negotiations between a vendor and a purchaser, neither has the benefit of having the knowledge of future events. However, he agreed that it has been recognized by the courts that hindsight can be used to validate assumptions and conclusions.

[123] As mentioned above, Mr. de Gray was in disagreement with the treatment of the Directors' Advances by the MNP Report. These amounts are recorded as an asset in the RCGT Statements; RCGT had verified whether they were collectible and whether they truly existed. In his view, these advances represent a true asset of SPL at the Valuation Date. In his opinion, it is not relevant that these advances will be repaid or forgiven after the Valuation Date. The amount of the bonuses and the timing of payment are uncertain. He also added in cross-examination that Ms. Grimes has the financial ability to repay these amounts. Therefore, he is of the opinion that the Directors' Advances should not be deducted in the calculation of the fair market value of the shares of SPL.

[124] Mr. de Gray testified that the same reasoning would apply to the Holdco Advances. He also added that there was no history of dividends being paid by Holdco. In cross-examination, Mr. de Gray said that the fact that Ms. Grimes does not own any dividend – paying shares in Holdco was one of the reasons he did not agree with the MNP Report on this point. However, since I have concluded that the Holdco Advances were made to Ms. Grimes as trustee of the Trust, I will not give any weight to that comment.

3.2 Discussion.

[125] I agree with both experts for the Respondent that the Holdco Advances and the Directors' Advances are assets of Holdco and SPL respectively. However, that conclusion does not mean that the fair market value of the Directors' Advances and the Holdco Advances is equal to the respective face value of these advances for purposes of establishing the fair market value of the shares of SPL and Holdco, respectively. An asset may be accounted for in the financial statements of a corporation for accounting purposes and be discounted for in establishing the fair market value of the shares of said corporation. The issue is whether, given the particular facts of this appeal, the Shareholders' Equity of SPL and Holdco, and, consequently, the respective fair market value of the shares of SPL and Holdco, should be reduced by the amount of the Directors' Advances and the Holdco Advances respectively, to account for the fact that bonuses and dividends have been declared and paid after the Valuation Date resulting in the offset of said advances, the whole in accordance with the intent of the controlling mind of SPL and Holdco (namely, Ms. Grimes).

[126] Mr. de Gray stated in his testimony that, in the ordinary course of business, a shareholder in the process of selling his or her shares will take steps to mitigate the impact that accounts such as advances to shareholders or directors appearing in financial statements will have on the marketability of the shares. I accept that this would be the normal conduct of a seller. I am also of the view that such conduct is relevant to the evaluation even in the context of a deemed disposition, but that does not resolve the issue in this particular appeal.

[127] During his oral submissions, counsel for the Respondent stated that the MNP Report wrongly assumed that these advances were not loans. Accordingly, if the advances were not loans, then they would represent an appropriation of corporate assets by the principals and shareholders, and would not be reflected on the financial statements. Consequently, these amounts would have to be included in the income of Ms. Grimes, her husband and the Trust when the amounts are appropriated from Holdco and SPL. In my view, the MNP Report does not deny that the advances were loans. As mentioned above, Paragraph 9.1.1(b) of the MNP Report states that adjustments to Holdco's Shareholders' Equity were made, including "adjustments to reflect the write-down of the advances to a shareholder of $1,144,887 (Schedule A-3) which we were advised would not be repaid by way of a cash payment but rather by an offset from dividends that will be declared". And the same reasoning was applied in respect of the Directors' Advances (para. 9.2.1(b) of the MNP Report). These assumptions were confirmed by the facts of this appeal and were clearly established in the course of this hearing. I have to determine whether

these assumptions have any bearing on the determination of fair market value under the Act.

[128] With respect to the Directors' Advances, I am of the view that the treatment of the Directors' Advances in accordance with the MNP Report is reasonable and should be confirmed. However, the amount of the Directors' Advances should be of an amount equal to $1,904,422, namely the amount indicated in the RCGT Statements and not an amount of $2,257,132 as stated in the Internal Statements. Since I have concluded that the starting point for the valuation is the RCGT Statements, which are for the year ended February 28, 2011, a deduction of an amount higher than $1,904,422 would, *inter alia*, not take into account the fact that amounts have already been taken off these statements through the bonuses and the set-off procedures for the period ending February 28, 2011. On these facts, I am of the view that the use of hindsight information by the MNP Report was generally proper since it is clear that Mr. Blackman used hindsight information to corroborate his assumptions and not to formulate his assumptions, according to principles established by case law.

[129] In this particular case, it would not be proper to conclude that the fair market value of the Directors' Advances is equal to the face value of these advances. I am of the view that the Directors' Advances should be fully discounted in the calculation of the fair market value of the shares of SPL, since it is reasonable to conclude, on the facts of this case, that a willing seller and a willing buyer would have taken into account a corresponding liability of SPL, namely a bonus to be paid to Ms. Grimes and her husband equal to the amount of the Directors' Advances, in determining the price to be paid for the shares of SPL.

[130] In respect of SPL, it is erroneous to argue that no consideration should be given to events that occurred after the Valuation Date, the perceived likelihood of whose occurrence was evident at the Valuation Date. In this appeal, with respect to SPL, this would mean that the Management's stated intentions would be ignored. To ensure a proper valuation, one should not view the Valuation Date in a vacuum, ignoring the consistent actions of the Management and its stated intentions for the future. While evaluation is not an exact science, one cannot ignore the intentions stated by the Management.

[131] As mentioned above, I am of the view that Ms. Grimes' testimony is credible. The evidence showed that Ms. Grimes and her husband are the source of value of SPL's business and that the sole compensation received from SPL by Ms. Grimes and her husband for their work is by way of bonuses, determined at

year-end in consultation with the accountants. The evidence showed that Ms. Grimes is the controlling mind and authority of SPL; she has the sole and exclusive authority to determine the payment of bonuses by SPL. As mentioned above, Ms. Grimes and her husband operate by way of advances from SPL throughout the year. The testimony of Ms. Grimes is clear that the Directors' Advances would never be repaid in cash to SPL. As can be seen in the Financial Statements of SPL for the year ended February 29, 2012, there were no advances to a director (Exhibit AR-2, tab 7M; Exhibit AR-1, para. 34). These statements cover a period ending some 8 months before the beginning of the audit of the Trust by the Minister. It cannot be reasonably argued that Ms. Grimes decided suddenly to change her conduct in that respect. The declaration and payment of the bonuses by SPL that took place after the Valuation Date as well as the history of payment of bonuses by SPL over the past years further support the notion that Ms. Grimes' stated intention would have been taken into account by potential purchasers at the Valuation Date.

[132] Mr. Spencer's reasoning, as detailed in the Spencer Report, fails to take into account any compensation to the principals of SPL, namely Ms. Grimes and her husband, in the determination of fair market value of the shares of SPL. This reasoning is flawed. It does not reflect the concrete operations of the corporate entity in that regard.

[133] Furthermore, I do not agree with Mr. Spencer and Mr. de Gray that there would be sufficient uncertainty at the Valuation Date as to whether the bonus would be paid or not so as to discount its effect on fair market value. On cross-examination, Mr. Spencer said that he does not know if the bonuses are paid in advance, or not; accordingly, he would not take into account these amounts until paid. He is of the view that since the bonus was not paid at the Valuation Date, it is not an expense that should reduce the fair market value of the shares. However, that reasoning does not consider the ordinary meaning of the word "bonus" which, by definition, is not paid in advance but is paid in recognition of the good performance of a person. In the Oxford Dictionary & Thesaurus (2007) that word is defined as follows: "a sum of money added to a person's wages for good performance".

[134] With respect to the use of hindsight, the general rule is that hindsight is not admissible except to test the reasonableness of the assumptions made by the valuators (*Douglas Zeller and Leon Paroian Trustees of the Estate of Margorie Zeller v. The Queen*, 2008 TCC 426, 2008 DTC 4441, at para. 42 [*Zeller Estate*], *Ford Motor Co. of Canada v. Ontario (Municipal Employees Retirement Board)*, 2000 CarswellOnt 1530, [2000] OJ No. 1480, at para. 11) and I am of the view that

that rule was followed by Mr. Blackman in the present case in respect of the evaluation of SPL.

[135] Justice Rip (as he then was) in *McClintock v. The Queen,* 2003 TCC 259 (para. 54), 2003 DTC 576 [*McClintock*], stated:

> 54 . . . First of all, it is the trial judge who must exercise his discretion whether or not, in the particular facts of an appeal, to use hindsight to assist in deciding whether a purported value of property is correct or in setting a value. This is particularly so when there are no sales of any comparable property immediately prior to the valuation date.

[136] Furthermore, in *Allred Estate v. MNR,* 86 DTC 1479 [*Allred Estate*], Justice Sarchuk stated:

> As a general rule it is not proper to use hindsight in the evaluation process. However, in this case the use of the financial statement of Hi-Way (52) as at July 31, 1972 was but one factor considered by Clark in formulating his opinion as to the future maintainable earnings of the company. His conclusions were based on the potential of the company, the plans of the company and the fact that a basis for increased earnings was in place although not yet reflected in the company's books. These facts existed on Valuation Day; were facts which favourably affected the company's projections of future earnings and were properly taken into account in arriving at fair market value.

[137] More recently, Justice D'Arcy of this Court confirmed that principle in *Shulkov v. The Queen,* 2012 TCC 457, 2013 DTC1040: "hindsight information is typically inadmissible unless it is being used to test the reasonableness of an assumption."

[138] I am of the view that the treatment of the Directors' Advances in the MNP Report is an appropriate use of hindsight. Mr. Blackman examined the financial situation of SPL post-Valuation Date to confirm that Management followed through on its stated intentions. Mr. Blackman tested his assumptions in proceeding with the valuation of the fair market value of the shares of SPL.

[139] I am also of the view that the fact that the Directors' Advances were not completely set off against bonuses before 2012 (Exhibits AR-2, tab 1E) does not call for a different conclusion, especially given Management's stated intention in respect of said advances. Such a delay in a small corporation is not unheard of. I understand that the remoteness of the dates is a factor to be taken into account (see *Power v. MNR,* 86 DTC 1065). However, considering the facts of this case,

I am of the view that the delay was reasonable and will not change my conclusion on this issue.

[140] I will now examine the issue of the Holdco Advances. I am of the view that the Holdco Advances should not reduce the Shareholders' Equity of Holdco as of the Valuation Date and hence, the fair market value of the shares of Holdco as of the Valuation Date. I do not agree with Mr. Blackman's treatment of said advances as outlined in the MNP Report, as said treatment was not an appropriate use of hindsight information. I am not convinced that Mr. Blackman, in considering the payment of the dividend by Holdco in February 2012 in the determination of the fair market value of the shares of Holdco as of the Valuation date, tested only the reasonableness of his assumptions. Rather, I am of the view that he formulated his assumptions considering the payment of the dividend made at a date subsequent to the Valuation Date (a year after) and that represents an improper use of hindsight information. The payment of the dividend by Holdco in February 2012 is, in my opinion, a subsequent event that should not be considered in determining the fair market value of the shares of Holdco on the Valuation Date, even accepting Ms. Grimes' testimony that the Holdco Advances would never be repaid in cash to Holdco.

[141] On the facts of this case, it is reasonable to conclude that the fair market value of the Holdco Advances is equal to the face value of said advances, namely $1,144,887, and that no amount should be deducted in determining the fair market value of the shares of Holdco as of the Valuation Date to account for the fact that a dividend was paid by Holdco in February 2012. As of the Valuation Date, the Holdco Advances was an asset of Holdco and I agree with the reasoning of Mr. de Gray and Mr. Spencer in that respect. Indeed, the fact that a dividend was paid by Holdco in 2012 and that the payment of the dividend was made through the set-off of the Holdco Advances further supports the view that the Holdco Advances was an asset of Holdco as of the Valuation Date. That dividend will reduce the fair market value of Holdco as of February 2012, but not as of the Valuation Date. Furthermore, I doubt that Ms. Grimes and Mr. Ozerdinc, as trustees of the Trust, would have agreed to sell their Class A Common Share of Holdco at a price that would not have taken into account an amount of $1,144,887 representing the Holdco Advances that they subsequently would have been called upon to pay to Holdco.

4. Embedded income taxes.

[142] In establishing the fair market value of the shares of Holdco, Mr. Blackman assumed that paragraph 88(1)(*d*) of the Act would apply on a notional winding-up of SPL into Holdco and that effective tax planning would be done. Accordingly, Mr. Blackman did not factor into his evaluation taxes payable by Holdco on the disposition of its shares of SPL (para. 9.1.2 of the MNP report). Mr. Spencer did not make reference to section 88 of the Act in his report, but, concretely, he did not factor in these taxes. I accept that conclusion.

[143] Furthermore, Mr. Blackman was of the view that the valuation of the fair market value of the shares of Holdco should take into account income taxes payable by the shareholder of Holdco on its own account (discounted to 50%) in the event of a redemption of the shares, rather than restricting the deduction to taxes payable at the entity level. He was of the view that this consideration arises out of the requirement to ascertain the "cash equivalents" of those shares. In his view, the likeliest manner in which the shares of Holdco would be liquidated would be by redemption rather than sale to a third party. During his testimony, he agreed that the rate of tax to be used in this calculation should have been the rate of tax applicable to dividend income and not the tax rate he actually used, namely 49.53% (Schedule A-1 of the MNP Report). The reason he discounted the tax rate otherwise applicable by 50% is that the moment of such redemption is not known.

[144] In contrast to Mr. Blackman, Mr. Spencer included only entity-level taxes payable on the disposition of the underlying assets of SPL in the calculation of the fair market value of the shares of Holdco. Also, Mr. de Gray is unequivocal that the determination of fair market value, being the highest price at which a shareholder could sell his shares, is materially different than the determination of the after-tax proceeds. Consequently, embedded income taxes on an eventual disposition of the shares should not be taken into account. According to Mr. de Gray, the determination of fair market value is not a determination of after-tax proceeds in the hands of the seller.

[145] A review of the case law, selected portions of which I have described above and some of which I will refer to below, leads me to conclude, on the facts of this case, that income taxes at the shareholder level should not be taken into consideration in the determination of the fair market value of the shares of Holdco.

[146] There seems to be no definition of the phrase "cash equivalent" at common law that would guide this Court, and it has been interpreted in several senses. In *HDL Investments Inc. v Regina (City)*, 2008 SKCA 47 (CanLII), Justice Jackson of the Saskatchewan Court of Appeal noted various definitions of that phrase, which

revolve around short-term securities so long as they are sufficiently liquid. The known amount of cash to which they relate does not seem to include tax consequences.

[147] In *Zeller Estate*, Justice Campbell took into account the income taxes at the shareholder level (discounted to 50%) in determining the fair market value of shares on a deemed disposition resulting from the death of the sole shareholder of a corporation. It would make sense in that situation to take those taxes into account in determining fair market value since the corporation would likely be liquidated during the settlement of the estate.

[148] In *Re Canadian Rocky Mountain Properties Inc. (Canada Business Corporations Act)*, 2006 ABQB 251 (CanLII), a case cited in *Zeller Estate*, the applicant shareholder dissented from the acquisition of the shares of a publicly traded company. The company's expert evaluation deducted 100% of any taxes payable at the corporate level and 50% of taxes payable by the putative shareholder on the distribution of corporate assets to shareholders. In issue was the "fair value" of the shares under section 190 of the CBCA. Justice Romaine of the Alberta Court of Queen's Bench concluded that it was inappropriate to provide for a deduction for personal taxes payable on a distribution to shareholders. In so doing, he found that the corporation in question was not a classic holding corporation and that there was no immediate intention to liquidate the corporation. As a result, he concluded that it would be inappropriate to find that it would be liquidated and its assets distributed to the shareholders. He emphasized that the determination of the embedded taxes that should be taken into account should be based on factual findings as to when such taxes would be likely to be realized:

> 19 I find that it is not appropriate in the case of CRMP to make a deduction from value for taxes that would be paid on a distribution to shareholders. A prudent purchaser in determining fair market value may take the eventual impact of such taxes into account in setting a price and deciding how it might structure an acquisition, but I am not satisfied that such a prudent purchaser would base its offered price directly on such considerations, since, as long as CRMP is operated as a going-concern, tax on distribution could be deferred. At any rate, the amount of tax that a purchaser would pay on distribution to shareholders is unique to such purchaser, and to ascribe an amount in a fair value calculation is mere speculation. It may be that actual offers received by CRMP were affected by the perceived tax consequences to particular purchasers, but that factor can and should be taken into account in a consideration of the offers received through the marketing efforts.

[149] Bearing in mind that my enquiry is to determine the "fair market value" and not the "fair value", I am still of the view that Justice Romaine's comments are relevant herein.

[150] In this appeal, we are dealing with a deemed disposition resulting from the application of the 21-year deemed disposition rules. No evidence was presented to me as to the possibility that Holdco would be liquidated. I am of the view that there is no reason to believe that Holdco will be liquidated in the near future. If I were to take into account, in the determination of the fair market value of the shares of Holdco, the taxes payable at the shareholder's level on the redemption of the shares of Holdco, that would not lead me to determine the highest price between a willing purchaser and willing seller.

5. Minority and/or marketability discount(s) in the evaluation and the Addendum.

[151] Before addressing the issue of discount(s), I have to determine whether the Addendum is an Expert Report under the *Tax Court of Canada Rules (General Procedure)*, SOR/90-688a (the "Rules"), and whether MNP, in preparing the Addendum, has complied with the Code of Conduct for Expert Witnesses set out in Schedule III of the Rules (the "Code of Conduct").

5.1 The Addendum and the Code of Conduct of Expert Witnesses.

[152] The Respondent is of the view that the Addendum does not qualify as an Expert Report since it does not contain all of the literature or other materials specifically relied on in support of the opinion with respect to the marketability discount (Schedule III, para. 3(*h*)). More specifically, the Addendum states at paragraph 2: "(c) various empirical studies that have quantified Marketability Discounts — often in the range of 15% to 45%, and (d) studies of the price-relationship between private, closely-held share transactions and the subsequent initial public offering of same shares, which were in the range of 40% to 65%". The materials referred to in paragraph 2 of the Addendum were not materials included in the Addendum. As a result, the Respondent submits that the Addendum should be excluded under subsection 145(3) of the Rules.

[153] Furthermore, the Respondent is of the view that the experts from MNP have crossed the line into advocacy simply by having prepared the Addendum in response to a specific request from the Appellant. Counsel for the Respondent pointed out that in the MNP Report, there is already a minority discount (because of the premium allocated to the 12 Fifth Preferred Shares held by Ms. Grimes). He

wonders why there was no marketability discount in the MNP Report, since MNP was aware of the corporate structure and other aspects of the business environment relating to such a discount at the time of preparing and drafting the MNP Report.

[154] The Appellant's position is that a proper issue arising out of the pleadings and the application of subsection 104(4) of the Act is the valuation of the Class A Common Share held by the Trust in Holdco on a standalone basis for the purpose of determining its fair market value. The Appellant submits that the Addendum arose out of its request to MNP to address an argument raised by the Defendants in the Civil Litigation. As such, the Addendum is the product of an independent evaluation of the question asked by the Appellant for the purposes of addressing the argument raised in the Civil Litigation. The Appellant has also highlighted the similarities of the Addendum to the Spencer Report, namely, that both make background reference to general documents and sources. If such general references are sufficient to disqualify the Addendum as being "materials specifically relied on in support of the opinions", then the Appellant asks that the Spencer Report be excluded on the same basis.

[155] For the following reasons, I am of the view that the Addendum does qualify as an Expert Report and that MNP has complied with the Code of Conduct.

[156] Section 145 of the Rules sets out the procedural guidelines with respect to expert witnesses and their reports. It provides that, unless this Court otherwise orders, an expert will not be permitted to testify at a hearing unless "a full statement of the proposed evidence in chief of the expert" has been set out in the expert's report. This limits the expert's evidence in chief to the content of the report (*Bekesinski v. The Queen*, 2014 TCC 35, 2014 DTC 1066, at para. 9 [*Bekesinski*]).

[157] The evidence in chief of the expert witness at the hearing must address an issue that has been defined in the pleadings or agreed to by the parties in writing (para. 145(7)(*a*)). It is possible, however, for the expert witness to give evidence in chief in respect of other matters. To do so requires special leave of the Court, where the Court considers it appropriate to do so (subpara. 145(8)(*b*)(ii)).

[158] The relevant section of the Rules read as follows:

145(2) An expert report shall	**145(2)** Le rapport d'expert :
(*a*) set out in full the evidence of the expert;	*a*) reproduit entièrement la déposition du témoin expert;

. . .	[…]
145(3) If an expert fails to comply with the Code of Conduct for Expert Witnesses, the Court may exclude some or all of their expert report.	**145(3)** La Cour peut exclure tout ou partie du rapport d'expert si le témoin expert ne se conforme pas au Code de conduite régissant les témoins experts.
. . .	[…]
145(7) Unless otherwise directed by the Court, no evidence in chief of an expert witness shall be received at the hearing in respect of an issue unless	**145(7)** Sauf directive contraire de la Cour, la preuve sur interrogatoire principal d'un témoin expert ne peut être reçue à l'audience au sujet d'une question que si les conditions ci-après sont réunies :
(*a*) the issue has been defined by the pleadings or by written agreement of the parties stating the issues;	*a*) cette question a été définie dans les actes de procédure ou par accord écrit des parties définissant les points en litige;
. . .	[…]
SCHEDULE III	**ANNEXE III**
(Paragraph 145(2)(*c*) and Form 145(2) of Schedule I)	(alinéa 145(2)*c*) et formule 145(2) de l'annexe I)
Code of Conduct for Expert Witnesses	**Code de conduite régissant les témoins experts**
Expert Reports	**Rapport d'expert**
3 An expert report referred to in subsection 145(1) of the Rules shall include	**3** Le rapport d'expert visé au paragraphe 145(1) des présentes règles comprend :
. . .	[…]
(*h*) any literature or other materials specifically relied on in support of the opinions;	*h*) les ouvrages ou les documents invoqués expressément à l'appui des opinions;
. . .	[…]

[159] In *Bekesinski*, Campbell J. based her conclusion that an expert report may be excluded if it fails to state the facts and reasoning relied on in reaching its

conclusions, including any quantitative data relied on in formulating these conclusions (para. 27-32), on the former wording of paragraph 145(2)(*b*) of the Rules, which required that "a full statement of the proposed evidence in chief of the expert" be set out in the expert report.

[160] The current version of Rule 145 is somewhat different, in that it enumerates specific requirements in respect to the expert report's content. The new Rule accomplishes this by adding, as a Schedule, a "Code of Conduct for Expert Witnesses", which will enumerate the specific content required to be included in an expert report. That content shall include the reasons for each opinion, the facts and assumptions upon which the opinion is based, the literature or other materials which support the expert opinion and a summary of the methodology, including tests and investigations relied upon. However, the concern in both the former and the current Rule 145 is to maintain procedural fairness and avoid "trial by ambush".

[161] The question then boils down to whether the "(c) various empirical studies that have quantified Marketability Discounts — often in the range of 15% to 45%, and (d) studies of the price-relationship between private, closely-held share transactions and the subsequent initial public offering of same shares, which were in the range of 40% to 65", which the Addendum refers to as having been considered in arriving at the quantum of the marketability discount, are "materials specifically relied on in support of the opinions". The word "specifically" (in the French version "expressément") is key, as is the phrase "relied on in support of" (in the French version "invoqués […] à l'appui des").

[162] I am of the view that the acknowledgement contained in the Addendum, without more, is insufficient to bring the studies in question within the realm of paragraph 3(*h*) of the Code of Conduct. The Respondent was not able to highlight a reference to these studies in the Addendum apart from a summary of what was considered in fixing the quantum. Nor was the Respondent able to highlight a place where the Addendum referenced a specific study or set of studies in support of its conclusion as to the quantum of the marketability discount. Hence, it cannot be said that the mere consideration of various studies in the course of arriving at an opinion means therefore that these studies are "specifically relied on in support of" that opinion.

[163] Furthermore, the Respondent is claiming that the opinion reflected in the Addendum is not impartial, independent or unbiased on the basis that MNP is now advocating for the Appellant in having created the report and counsel for the Respondent cites *White Burgess Langille Inman v. Abbott and Haliburton Co.*, 2015 SCC 23, [2015] 2 SCR 182, where the Supreme Court stated that:

> 32 Underlying the various formulations of the duty are three related concepts: impartiality, independence and absence of bias. The expert's opinion must be impartial in the sense that it reflects an objective assessment of the questions at hand. It must be independent in the sense that it is the product of the expert's independent judgment, uninfluenced by who has retained him or her or the outcome of the litigation. It must be unbiased in the sense that it does not unfairly favour one party's position over another. The acid test is whether the expert's opinion would not change regardless of which party retained him or her: P. Michell and R. Mandhane, "The Uncertain Duty of the Expert Witness" (2005), 42 *Alta. L. Rev.* 635, at pp. 638-39. These concepts, of course, must be applied to the realities of adversary litigation. Experts are generally retained, instructed and paid by one of the adversaries. These facts alone do not undermine the expert's independence, impartiality and freedom from bias.
>
> [Emphasis added.]

[164] The Appellant, however, highlighted the reasons that led to the production of the Addendum — it was a result of the Civil Litigation. The Respondent has not shown that the content of the opinion was altered to favour the Appellant's position or that it unduly favours the Appellant's position over the Respondent's position. The Respondent seems to contend that the very creation of the Addendum is an indicia of bias. I do not agree with the Respondent. The testimony of Ms. Grimes is clear: the Addendum was requested by her lawyer in respect of the Civil Litigation in order to determine the value of the Class A Common Share of Holdco owned by the Trust on a standalone basis absent the effect of being part of a family controlled group. I am satisfied that Ms. Grimes did not ask for, or otherwise direct that, a particular answer or favourable position be taken by MNP so that the Addendum has turned into advocates those expert authors.

[165] Furthermore, I am of the view that the question of the fair market value of the Class A Common Share of Holdco on a standalone basis is critical to the task of this Court. Therefore, the fact that this question was asked to be considered explicitly by the Appellant does not, in my view, constitute a partial assessment of the questions at hand — it constitutes a clarification of the questions that are before the Court. That the Addendum was produced in the context of the Civil Litigation may prove probative in understanding and criticizing the work of MNP, but there seems to be no strong attack by the Respondent on the objective quality of the Addendum's assessment of the questions to which it relates. As the main argument on admissibility and a supposed violation of the Code of Conduct arises out of the proper identification by the Appellant of one of the questions in issue in this appeal, I cannot conclude that it constitutes a breach of the duties owed by Mr. Blackman (or Mr. Wise) to this Court.

5.2 Minority and/or marketability discount(s).

[166] Before discussing the various discounts, I will provide my overall conclusion as to the fair market value of the 2,700,000 First Preferred Shares of Holdco. The articles of incorporation of Holdco provide that the redemption amount of the 2,700,000 First Preferred Shares issued and outstanding in Holdco is equal to $1 per share and that they rank first in the event of liquidation or dissolution (Exhibit AR-2, tab 25). Since the First Preferred Shares are redeemable at the option of Holdco and retractable at the option of the holder for an amount equal to their redemption amount and no evidence was provided to me showing that Holdco was insolvent as of the Valuation Date, I am of the view that the redemption amount of the First Preferred Shares reflects the fair market value of those shares.

(a) Experts' positions.

[167] The MNP Report provides for a minority discount through the attribution of a control premium to the 12 Fifth Preferred Shares equal to 12.5% of an amount equal to the difference between the Adjusted Shareholders' Equity of Holdco and the aggregate redemption amount of the 2,700,000 First Preferred Shares.

[168] The Addendum then incorporates a discount of 30% to the value of the Class A Common Share of Holdco held by the Appellant based on the consequent lack of marketability of such share. The following factors were considered by Mr. Blackman in the quantification of the marketability discount (para. 2.1.2 of the Addendum):

i) Length of the holding period of the ownership interest

ii) There being no put arrangement

iii) The nature of Holdco's activities

iv) Management's plans for the business

v) Lack of control conferred by the share

vi) Potential for capital appreciation during the holding period

vii) Absence of redemption policy

viii) No distributions were made to the shareholders prior to the Valuation Date, and no assurance that the owner of the share or a future owner would receive distributions

ix) The other shareholder would have no reason to offer more than a nominal amount over what arm's length parties would offer should the share have been placed on the market.

[169] Mr. Blackman was of the view that the minority and the marketability discounts are two quite opposite concepts.

[170] Mr. Spencer is of the opinion that no minority discount should be applied to the Class A Common Share of Holdco considering the factors listed in paragraph 70 of his report:

- Ms. Grimes and Ersin Ozerdinc are married and related;

- Ms. Grimes is the Director, President and Secretary Treasurer of Holdco as of the Valuation Date;

- Ms. Grimes and Ersin Ozerdinc are the trustees of the Trust;

- The trustees are related to the controlling shareholder, Director and President of Holdco;

- The Trustees hold legal title to the Trust assets for the benefit of the beneficiaries of the Trust, namely children of the marriage of Ms. Grimes and Ersin Ozerdinc;

- The Trustees are subject to the highest fiduciary obligations, inclusive of, and not limited to, a duty of loyalty, which involves an obligation to avoid conflicts of interest, and a duty of care, which entails acting honestly and in good faith in the best interest of the beneficiaries;

- The issued and outstanding shares of Holdco, other than the Class A Common Share, have redemption amounts that specify their value;

- The Trustees acting in the best interest of the beneficiaries, would be obligated to challenge any redemption of the preferred shares at any amount higher than the set redemption price;

- The Trust's property includes shares in the capital of Holdco, and that 1 Class A Common Share represents all the growth in Holdco;

- The related parties would act in concert to obtain the highest price in an open market transaction.

[171] The Spencer Report also denied any reduction of the fair market value for problems of marketability, in view of the following factors (para. 72 of the Spencer Report):

- The valuation approach used for both SPL and Holdco were asset based;

- The assets of SPL consist mainly of current assets and marketable securities held by Canadian investment banks, which are liquid;

- The assets in Holdco, other than the shares of SPL, consist mainly of current assets and marketable securities held by Canadian investment banks which are liquid;

- Management's business philosophy of "brains and cash", which has resulted in a strong, liquid balance sheet;

- The Management has insured that SPL has accumulated its retained earnings in relatively liquid investments and ensured that Holdco has accumulated its holdings in relatively liquid investments.

[172] Similarly, the CVPL Report criticizes a minority or marketability discount being applied to the value of the Class A Common Share of Holdco as being highly unusual in the case of a closely-held private corporation (particularly spousal control). Mr. de Gray did, however, find it reasonable to apply a 12.5% control premium on the value of the 12 Fifth Preferred Shares held by Ms. Grimes.

(b) Discussion.

[173] For the following reasons, I am of the view that, on the facts of this case, it is reasonable to apply a minority discount in the determination of the fair market value of the Class A Common Share of Holdco held by the Trust at a rate of 12.5% and a marketability discount at a rate of 15% (Appendix B).

[174] A minority discount will be applied to make an adjustment or a discount for lack of control associated with minority shareholdings (*Zeller Estate*, para. 60). A marketability (or liquidity) discount will be applied when there is a lack of marketability for the shares. Marketability has been defined as follows in the MNP Report (see also *Zeller Estate*, para. 60): "the ability to convert the business ownership interest to cash quickly, with minimal transaction and administrative costs in so doing and with a high degree of certainty of realizing the expected amount of proceeds". It is clear from those two definitions that the minority discount and the marketability discount are two different concepts.

[175] Furthermore, in *McClintock*, marketability of the holdings was considered on its own, albeit on the basis that no minority discount was properly applicable given the reference point. In that case, the valuation of shares of a Canadian controlled private corporation had been made three months before the date it went public with an initial public offering (IPO). Justice Rip (as he then was) concluded that the minority shareholding enjoyed by the taxpayer at the valuation date should be calculated with respect to the amount at which the shares were trading publicly as of the IPO, with a 25% marketability discount applied to account for the difficulties of reselling the shares before the IPO. He rejected a proposed minority discount to the shares in question. I agree with this conclusion, as it is well established that the quoted price for publicly available shares already includes a minority discount identified by the experts in the foregoing case (See *Steen v. The Queen*, 86 DTC 6498, [1986] 2 CTC 394 (FCTD), aff'd 88 DTC 6171, [1988] 1 CTC 256 (FCA)).

[176] In *Zeller Estate*, Campbell J. applied both a minority discount and a marketability discount in determining the fair market value of shares of a private corporation.

[177] I am of the view that the Spencer Report rests on improper assumptions in respect of the minority discount. In his testimony and his report, Mr. Spencer made it clear that his valuation is based entirely on the assumption that Holdco would be sold as a whole and that a purchaser would acquire all the issued and outstanding shares of the capital of Holdco, and thus, would acquire control of Holdco on the notional purchase. Mr. Spencer is also assuming that, given her fiduciary duties as trustee of the Trust, Ms. Grimes would be bound to sell the controlling shares of Holdco that she owns personally (12 Fifth Preferred Shares) so as to obtain the highest price for the Class A Common Share of Holdco and that the trustees of the Trust will have to challenge the redemption of the 12 Fifth Preferred Shares of Holdco at an amount higher than the redemption amount of these shares.

[178] I reject the notion that Ms. Grimes, given her fiduciary duties, would have to sell her controlling shares of Holdco in order to obtain the highest price for the Class A Common Share of Holdco. Subsection 104(4) of the Act provides for a deemed disposition of the capital property owned by the Trust on the Valuation Date. Only the Trust is deemed to have disposed of its shares. There are no legal or fiduciary obligations for Ms. Grimes to sell her controlling shares of Holdco. Furthermore, no evidence was adduced at trial by either party showing that she would have sold her shares in that hypothetical scenario which the Court is being asked to consider. The Court cannot assume that Ms. Grimes would be compelled to sell her controlling shares of Holdco. I am of the view that the determination of fair market value has to be done, instead, on the assumption that only the Trust is disposing of its shares, and not all the shareholders of Holdco, namely the group formed by the Trust and Ms. Grimes. Furthermore, the definition of "fair market value" as being the highest price between a willing buying and a willing purchaser, acting at arm's length, implies that we have to look at the Trust (and not the group formed by the Trust and Ms. Grimes) selling its shares to a willing purchaser. Mr. Spencer's reliance on his understanding of trust law is misplaced.

[179] Also, Mr. Spencer refers to the fact that, given their fiduciary duties, the Trustees will have to challenge the redemption of the 12 Fifth Preferred Shares at an amount higher than the redemption amount of those shares. I am of the view that that fact is irrelevant to my task.

[180] Furthermore, Mr. Spencer referred to the fact that Ms. Grimes, as the sole director, president and secretary-treasurer of Holdco and owner of the controlling shares of Holdco, is also acting as a trustee for the Trust. Again, for the reasons mentioned above, I am of the view that this is irrelevant to my task.

[181] The Respondent also relied on the fact that there was no minority discount applied by RCGT when evaluating the shares of SPL for purposes of the reorganisation of 2007 as per the RCGT Letter (Exhibit R-3) and arguing that I should not apply a minority discount. However, at page 2 of the RCGT Letter, there is a clear indication that RCGT had not been hired to provide an opinion on the fair market value of the shares. It reads as follows: "Since we have not been engaged to provide Comprehensive Valuation Reports or an Estimate Valuation Reports, it must be clearly understood that the calculation of value and the comments in this report do not constitute our considered opinion of the fair market values". Thus, I have given no weight to the RCGT Letter.

[182] The case law dealing with the determination of fair market value that I review below has often applied a minority discount in the valuation of minority shares of a family-controlled corporation. One example is *Zeller Estate* (cited above), where Campbell J. applied a 10% discount for a 50% interest and a 15% discount for a 33% interest.

[183] In *Allred Estate*, Sarchuk J. applied a 25% discount in determining the fair market value of shares of a deceased shareholder.

[184] In *Guckert v. Koncrete Construction Ltd.*, 2009 SKQB 484 (CanLII), the Saskatchewan Court of Queen's Bench had to determine the fair market value of a minority shareholding held in private corporations (44.4% and 30% respectively) for purposes of the division of family property. The court stated as follows:

> 93 As to the choice of a minority discount, I am inclined to agree with Mr. Tournquist. A prudent prospective purchaser buying a 30% interest in Kindersley, who is not related to the remaining shareholders, might expect a minority discount of more than 15%. However, KCL and its principals are family and there is no evidence to suggest disharmony between Peter and his brother Frank nor nephew Lyle. Peter can anticipate the familial alliance will continue into the near future. Further, the valuations are cast as of December 31, 2006. We are now three years hence with no evidence at the date of adjudication of a breakdown or potential breakdown in the family accord to respect each other's trading areas. Yet, a prospective purchaser dealing at arms length [*sic*] would, in my opinion, assess the risk associated with a minority interest of 30% of the issued shares to be higher than the 15% which Mr. Wallace opines. The risk in this set of circumstances is more accurately reflected by a minority discount of 25%.

[185] In *McKinney v. McKinney*, 2008 BCSC 709 (CanLII), the Court, in determining the fair market value of a minority shareholding (30%) held in a family-controlled corporation, stated the following:

> 101 The selection of the amount of an appropriate minority discount is a difficult exercise of judgement. In my view, the factors described by Mr. Barbour demonstrate that a substantial minority discount is appropriate, but 75 percent is too extreme. In the circumstances, a minority discount of 50 percent is appropriate.

[186] Counsel for the Appellant referred the Court to a number of foreign authorities. As noted by Associate Chief Justice Bowman (as he then was) in *Klotz v. The Queen*, 2004 TCC 147, 2004 DTC 2236, "one must treat foreign authorities with caution, but they are entitled to respect and they can be instructive where they deal essentially

with the same problem" (para. 47) (see also *Aikman v. The Queen*, 54 DTC 1874, 2000 CanLII 184 (TCC) (para. 101)). In *Estate of Frank v. Commissioner*, 69 T.C.M. 2255 (1995), the United States Tax Court had to determine the fair market value of a 30% shareholding in a family-controlled corporation for purposes of estate tax. The Court stated that while the appropriate amount of discount to apply is a question of facts, it is generally unreasonable to argue that no discount should be considered for a minority interest in a closely held corporation and held that a 20% discount is reasonable. The Court added: "Where indications of value are predicated upon control or complete ownership, a discount must be applied to provide indications of value for a minority or less-than-controlling interest." Also, the Court decided that the lack of marketability principle will apply to both controlling as well as minority shares and concluded that a discount in the value of the closely-held stock is appropriate for lack of marketability. It applied a 30% discount.

[187] I will now examine the marketability discount. I am unable to accept the reasoning of Mr. Spencer that a marketability discount would be improper in this case. In rejecting the application of a marketability discount to the valuation of the Class A Common Share of Holdco, Mr. Spencer relied on a number of factors such as the valuation method used for both SPL and Holdco, the nature of the assets held by both entities and the business philosophy of Management. These factors listed by Mr. Spencer are all factors relating to Holdco as a whole, without any reference to factors relating to the Class A Common Share specifically. I am of the view that it is inappropriate to refer only to factors relating to Holdco as a whole in determining the appropriateness and the quantum of the marketability discount applicable to the Class A Common Share of Holdco. The marketability discount has been described as the ability to convert the property to cash quickly, with minimal transaction costs, with a high degree of certainty of realising the expected amount of net proceeds (*McClintock*, para. 33 and *Zeller Estate*, para. 60). As such, it is obvious that factors relating to the property itself, here the Class A Common Share, have to be considered in determining the appropriateness and quantum of the marketability discount. As a result, given the absence of said factors in Mr. Spencer's evaluation, I must disregard Mr. Spencer's analysis in determining the appropriateness and quantum of the marketability discount applicable to the Class A Common Share of Holdco.

[188] In setting a marketability discount, Mr. Blackman is referring not only to factors relating to Holdco as a whole (the nature of Holdco's activities and management's plans for the business) but to factors applicable specifically to the Class A Common Share, namely the absence of any put arrangements, the limited market for the share, the absence of a redemption policy, the absence of

distributions prior to the Valuation Date or any assurance of future distributions and the potential for capital appreciation during the holding period. In my view, subject to the foregoing, these factors are all relevant in the determination of the appropriateness and quantum of the marketability discount applicable to the Class A Common Share of Holdco. However, I note that another factor taken into consideration by Mr. Blackman is the lack of control conferred by the Class A Common Share. The lack of control was already included in the control premium conferred on the 12 Fifth Preferred Shares of Holdco owned by Ms. Grimes and the resulting minority discount applied to the valuation of the Class A Common Share. Thus, there seems to be a double-counting of the control factor, once in calculating the minority discount and again in calculating the marketability discount. For these reasons, I would reduce the marketability discount to 15% as opposed to 30% as per the Addendum.

F. CONCLUSION.

[189] The appeal is allowed and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment in accordance with my Reasons and the summary of adjustments found in Appendices B to D which form an integral part of these Reasons for Judgment. The matter of costs is reserved. The parties will have 60 days from the date of this Judgment with Reasons to reach an agreement on costs, failing which they are directed to file their written submissions on the issue of costs, not to exceed ten (10) pages, within 30 days of the expiration of the initial 60-day period.

Signed at Ottawa, Canada, this 29th day of November 2016.

"Dominique Lafleur"

Lafleur J.

APPENDIX A

(*Court File No.*: 2014-2000(IT)G)

TAX COURT OF CANADA

BETWEEN:

M. KATHLEEN GRIMES AND M. ERSIN OZERDINC,
TRUSTEES OF THE OZERDINC FAMILY TRUST NO. 2[1]

Appellant

and

HER MAJESTY THE QUEEN

Respondent

AGREED STATEMENT OF FACTS (PARTIAL)

For the purpose of this appeal only, the parties agree to the following facts:

MATERIAL FACTS

A. TAX APPEAL PROCESS

1. This is an appeal under the *Income Tax Act* (Canada) (the "Act") from a Notice of Reassessment dated October 17, 2013 in respect of the Ozerdinc Family Trust No. 2's (the "Ozerdinc Trust #2") 2011 taxation year (the "Reassessment"). [Tab 19 of the Joint Book of Documents]

2. The Ozerdinc Trust #2 filed an objection to the Reassessment on January 15, 2014 (the "Objection"). As of April 15, 2014, the 90th day following the date on which the Objection was filed, the Ozerdinc Trust #2had not received notice that the Reassessment had been either vacated or confirmed. [Tab 20 of the Joint Book of Documents]

3. The Ozerdinc Trust #2 proceeded with this Appeal pursuant to paragraph 169(1)(b) of the Act.

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[1] The parties are not in agreement in respect of the style of cause in the appeal

B. HISTORY OF THE OZERDINC FAMILY TRUST AND THE OZERDINC FAMILY TRUST NO. 2

4. Kathleen Grimes and Ersin Ozerdinc are spouses of one another.

5. On February 1, 1990, the Ozerdinc Family Trust (the "**Ozerdinc Trust #1**") was settled by Kathleen Grimes for the benefit of the children of Kathleen Grimes and Ersin Ozerdinc. [**Tab 21 of the Joint Book of Documents**]

6. On September 28, 2007, the Ozerdinc Trust #2 was settled by Kathleen Grimes for the benefit of the children of Kathleen Grimes and Ersin Ozerdinc.

7. At all material times, the trustees of the Ozerdinc Trust #1 and the Ozerdinc Trust #2 were Kathleen Grimes and Ersin Ozerdinc, who are individuals resident in Canada. [**Tabs 21 and 22 of the Joint Book of Documents**]

8. The Ozerdinc Trust #2 is an *inter vivos* trust governed by the laws of the Province of Ontario.

9. On September 28, 2007, the Ozerdinc Trust #1 transferred all of its assets to the Ozerdinc Trust #2, which was done on a rollover basis in accordance with s. 107.4(3) of the Act and did not result in a change in beneficial ownership. The property transferred included a common share of 1634158 Ontario Inc. ("Holdco"). [**Tab 23 of the Joint Book of Documents**]

10. The Ozerdinc Trust #1 was, after the transfer of the assets to the Ozerdinc Trust #2, dissolved on December 31, 2007.

11. By operation of, *inter alia*, subsections 104(4) and 104(5.8) of the Act, the Ozerdinc Trust #2 was deemed to dispose of certain property on February 1, 2011.

12. On February 1, 2011, the Ozerdinc Trust #2's property included the common share of Holdco and Holdco, in turn, held 100 Common Shares and 100 Class B Preferred Shares, being all of the issued and outstanding shares in the capital of Site Preparation Limited ("SPL"). [**Tab 24 of the Joint Book of Documents**]

C. DESCRIPTION OF HOLDCO, SPL AND SPLP

SPL

13. On May 23, 1990, SPL was incorporated under the *Business Corporations Act* (Ontario). On July 24, 2007, SPL amalgamated with H.E.R. Excavating & Grading Inc.

14. SPL has a fiscal year end of February 28 (or February 29 in leap years).

15. SPL is a construction business that that operates predominantly as a subcontractor to larger construction companies and provides a range of industrial, commercial and institutional contracting services, including water mains and sewers, roads and parking lots up to the granular B, excavating and solar farm construction in the Ottawa region of Ontario.

16. SPL obtains business through a competitive bid and tender process on a contract by contract basis. SPL targets specific types of projects with specific general contractors. The contracts are typically fixed price contracts which require the tenderer to extrapolate information from the plans and specifications and determine the detailed scope of work. There is a high degree of risk associated with these types of projects at the tender stage and the execution stage. The price tendered is a lump sum, all inclusive of the scope of work detailed on the contractor's plans.

17. At all material times, Ersin Ozerdinc and Kathleen Grimes played and continue to play key management roles in SPL.

18. Kathleen Grimes was at all material times the sole director, president, and secretary-treasurer of SPL.

19. SPL operates with between 15 and 50 employees depending on the number of active contracts. On February 1, 2011, SPL had three full-time employees in addition to Ersin Ozerdinc and Kathleen Grimes.

Holdco

20. On May 2, 2005, Holdco was incorporated under the *Business Corporations Act* (Ontario). Holdco owned all of the issued shares of SPL at all material times.

21. Holdco's fiscal year end is February 28 (or February 29 in leap years).

22. Kathleen Grimes was at all material times, and continues to be, the director, president, and secretary-treasurer of Holdco.

23. On February 1, 2011, the issued capital of Holdco consisted of the following classes of shares:

(a) 1 Class A Common Share, with the following attributes:
   (i) one vote per share;
   (ii) entitled to dividends at the discretion of the board of directors; and
   (iii) entitled to the remaining assets of the corporation upon dissolution;

(b) 2,700,000 First Preferred Shares, with the following attributes:
   (i) entitled to 1 vote per share;
   (ii) not entitled to dividends;
   (iii) redeemable and retractable for $1 per share; and
   (iv) rank, as regards to the repayment of the redemption amount, in priority to all other classes of shares of the corporation but shall not confer any further right to participate in profits or assets; and

(c) 12 Fifth Preferred Shares, with the following attributes:
   (i) entitled to 500,000 votes per share;
   (ii) not entitled to dividends;
   (iii) redeemable for $0.10 per share; and
   (iv) rank, as regards to the repayment of the redemption amount, in priority to all other classes of shares of the corporation other than the First Preferred Shares, Second Preferred Shares, Third Preferred Shares and Fourth Preferred Shares but shall not confer any further right to participate in profits or assets.

24. On February 1, 2011, the issued and outstanding shares of Holdco were held as follows:

(a). the Ozerdine Trust #2 held 2,699,900 First Preferred Shares and 1 Class A Common Share; and

(b) Kathleen Grimes held 100 First Preferred Shares and 12 Fifth Preferred Shares.

Site Preparation Limited Partnership

25. On September 2, 1998, Site Preparation Limited Partnership ("SPLP") was formed under the *Limited Partnerships Act* (Ontario). SPLP carries out site servicing and site preparation functions, including, but not limited to, excavation, installation of sewer and water mains, and storm water management. SPLP's business is similar to that of SPL but the projects undertaken consist of smaller jobs that lack the complexity of SPL's projects. In February 2011, SPLP had 14 employees.

26. SPLP's fiscal year end is December 31 of each year.

27. SPLP's allocation of income and loss for both accounting and tax purposes is 99.99% to the Limited Partner and 0.01% to the General Partner. Payment of distributable cash is set to be made at least annually within ninety (90) days after the end of the fiscal year.

28. SPLP's issued and outstanding subscribed units consists of the following:

(a) 4,000 Units (1 is owned by SPL and 3,999 are owned by the Ozerdine Trust #2), with the following rights:

(i) Entitled to receive distributions;

(ii) Rank equal to all other Units;

(iii) One vote per Unit.

29. SPL is the General Partner and holds 1 Partnership Unit. SPL is entitled to reimbursement by SPLP for all costs and expenses that are incurred by SPL as general partner on behalf of SPLP along with an annual management fee equal to ten percent (10%) of the income of SPLP net of all expenses other than such management fee as

outlined in the Partnership Agreement. The management fee is typically recorded at the year end.

30. The Limited Partnership Units are held by the Ozerdinc Trust #2.

31. The table below outlines the tax attributes of the shares of Holdco outstanding as of February 1, 2011:

Class of Shares	Shareholder	Adjusted Cost Base	Paid Up Capital
1 Class A Common Share	Ozerdinc Trust #2	$1.00	$1.00
2,700,000 First Preferred Shares	Ozerdinc Trust #2	$100.00	$199.99
100 First Preferred Shares	Kathleen Grimes	$100.00	$0.01
12 Fifth Preferred Shares	Kathleen Grimes	$1.20	$1.20

32. SPL paid expenses on behalf of and made advances to Kathleen Grimes and Ersin Ozerdinc (the "**Principals**") from time to time and maintained a record of these transactions as advances to the Principals in its general ledger and financial statements. Journal entries were made for lump sum bonuses by SPL to the Principals, often at year end. On February 1, 2011, SPL's general ledger balance for advances to the Principals was $2,257,132 and no bonuses to the Principals were declared by SPL at that date.

33. Prior to the initiation of the audit and subsequent Reassessment, SPL declared bonuses payable to each of Kathleen Grimes and Ersin Ozerdinc such that the balance of the advances to the Principals as at February 29, 2012 was nil. All such remuneration was duly reported by Kathleen Grimes and Ersin Ozerdinc for tax purposes and any taxes exigible thereon, paid.

34. The following are the year end balances of the advances to (or from, if negative) the Principals by (or to) SPL as reported on its financial statements:

(a) February 29, 2000: nil

(b) February 28, 2001: $53,683

(c) February 28, 2002: ($62,481)

(d) February 28, 2003: ($161,839)

(e) February 29, 2004: ($101,381)

(f) February 28, 2005: ($140,726)

(g) February 28, 2006: $79,415

(h) February 28, 2007: $215,379 (modified in subsequent year to $227,879)

(i) February 29, 2008: $454,410 (modified in subsequent year to $450,585)

(j) February 28, 2009: $333,395

(k) February 28, 2010: $370,874

(l) February 28, 2011: $1,904,422

(m) February 29, 2012: nil

(n) February 28, 2013: $502,274

35. The following represents the remuneration from SPI, reported by each of Kathleen Grimes and Ersin Ozerdinc in each of the following calendar years:

Year	Kathleen Grimes	Ersin Ozerdinc	Total
2000	$196,883	$196,883	$393,766
2001	$192,500	$192,500	$385,000
2002	$180,000	$180,000	$360,000
2003	$192,850	$192,850	$385,700
2004	$192,850	$192,850	$385,700
2005	$192,850	$192,850	$385,700
2006	$200,000	$200,000	$400,000
2007	$200,000	$200,000	$400,000
2008	$200,000	$200,000	$400,000
2009	$200,000	$200,000	$400,000
2010	$200,000	$200,000	$400,000
2011	$400,000	$400,000	$800,000
2012	$616,025	$616,025	$1,232,050
2013	$616,000	$616,000	$1,232,000

36. In the year 2011, Kathleen Grimes and Ersin Ozerdinc had personal assets with a value over $2.3 million.

37. In its 2011 taxation year, Holdco advanced funds from time to time to its shareholder and maintained a record of these advances in its financial statements.

38. Prior to the initiation of the audit and subsequent Reassessment, Holdco declared dividends to the Ozerdinc Trust #2 on January 15, 2012 ($530,200), and on February 29, 2012 ($1,113,004 and $464,760) totaling $2,107,964 in its 2012 taxation year [Tabs 4, 5, and 6 of the Joint Book of Documents]

39. The following are the dividends declared by Holdco to the Ozerdinc Trust #2:

(a) July 31, 2009: $38,423

(b) January 15, 2012: $530,200

(c) February 29, 2012: $1,113,004

(d) February 29, 2012: $464,760

(e) February 28, 2013: $16,949

D. VALUATIONS

40. By letter dated November 8, 2012, the Canada Revenue Agency (the "CRA") stated its position that the Ozerdinc Trust #2 had been subject to a deemed disposition of its property by virtue of subsections 104(4) and 104(5.8) of the Act on February 1, 2011. [Tab 26 of the Joint Book of Documents]

41. On or about November 19, 2012, a form RC59 was filed on behalf of the Ozerdinc Trust #2 naming Gowling Lafleur Henderson LLP as authorized representative. [Tab 27 of the Joint Book of Documents]

42. The Ozerdinc Trust #2's file was referred to the Regional Valuation Unit of the Ottawa Tax Services Office in February 2013 for a determination of the fair market value of the property of the Ozerdinc Trust #2 as at February 1, 2011.

43. A final valuation report was produced by the Valuation Unit which formed the basis of the Reassessment and was delivered to the Ozerdinc Trust #2 with a cover letter dated September 17, 2013 (the "Assessment Valuation").

44. The Assessment Valuation concluded that the value of the Ozerdinc Trust #2's shares of Holdco as at February 1, 2011 was $7,993,655.

45. By letter dated September 24, 2013, the CRA auditor confirmed the results of the audit of the Ozerdinc Trust #2's 2011 taxation year. The Ozerdinc Trust #2 would be assessed a capital gain to the extent that the Assessment Valuation established a value of the Ozerdinc Trust #2's assets that exceeded the Ozerdinc Trust #2's adjusted cost base in such assets. [Tab 28 of the Joint Book of Documents]

46. As a result, the Ozerdinc Trust #2 was considered to have realized a capital gain of $8,087,633 on February 1, 2011 by virtue of subsections 104(4) and 104(5.8) of the Act as follows:

(a) $2,699,900 on its First Preferred Shares in Holdco, which is in dispute;

(b) $5,293,654 on its Class A Common Share in Holdco, which is in dispute; and

(c) $94,079 on its interest in SPLP, which is not in dispute.

47. By notice dated October 17, 2013, the Minister of National Revenue (the "Minister") reassessed the Ozerdinc Trust #2's tax liability for its 2011 taxation year by adding to its income a taxable capital gain of $4,035,242 under subsections 3(b) and 38(a) of the Act. [Tab 19 of the Joint Book of Documents]

48. The Reassessment was issued October 17, 2013. It reflected:

(a) An increase to the Ozerdinc Trust #2's taxable income in the amount of $4,035,242;

(b) A corresponding tax liability of $1,870,045.22; and

(c) Accrued interest of $151,483.35 as of the Reassessment date.

49. The Ozerdinc Trust #2 filed the Objection to the Reassessment on January 15, 2014.

DATED at Ottawa, Ontario this 6 day of June 2016.

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(Court File No.: 2014-2006(IT)G)

TAX COURT OF CANADA

BETWEEN:

M. KATHLEEN GRIMES AND M. ERSIN OZERDINC, TRUSTEES OF THE OZERDINC FAMILY TRUST NO. 2
Appellant

and

HER MAJESTY THE QUEEN
Respondent

AGREED STATEMENT OF FACTS

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Solicitor for the Respondent

APPENDIX B

Fair market value ("FMV") of the shares of Holdco as of the Valuation Date		
Shareholders' Equity as of February 28, 2011		$2,789,286
Less: income/loss for the month of February 2011		—
Shareholders' Equity as of February 1, 2011		$2,789,286
Adjustments:		
Add: FMV of SPL shares (Appendix C)	3,424,000	
Less: book value	(200)	$3,423,800
Add: due to a shareholder		38,423
Adjusted Shareholders' Equity		$6,251,509
Allocation to each class of shares:		
Less: redemption amount of 2,700,000 First Preferred Shares (FMV)		(2,700,000)
Balance to Class A Common Share and 12 Fifth Preferred Shares		$3,551,509
12 Fifth Preferred Shares		
Control premium/Minority discount:		
12.5% × 3,551,509 = $443,939		
FMV = redemption amount + control premium/minority discount		
[(0.10) × 12] + 443,939= $443,940		(443,940)
		$3,107,569
1 Class A Common Share		
Marketability discount (15% × 3,107,569)		(466,135)
FMV		$2,641,434

APPENDIX C

Fair market value ("FMV") of the shares of SPL as of the Valuation Date		
Shareholders' Equity as of February 28, 2011		$5,985,744
Add: loss for the month of February 2011	(730,822)	
Add: salaries for the 11 months ended January 31, 2011	635,795	95,027
Shareholders' Equity as of February 1, 2011 (as per MNP Report)		$6,080,771
Adjustments:		
Add: FMV of land (net of disposition costs)	140,650	
Less: book value (as per Spencer Report)	(48,661)	91,989
Add: FMV of investments	2,778,254	
Less: book value (as per Spencer Report)	(2,650,132)	128,122
Less: income tax on deferred income (28% × 3,580,554)		(1,002,555)
Less: Directors' Advances		(1,904,422)
Adjusted Shareholders' Equity before income tax considerations		$3,393,905
Less: estimated tax on notional disposition of land (Appendix D)		(10,625)
Less: estimated tax on notional disposition of investments (Appendix D)		(22,197)
Add: RDTOH to be recovered (Appendix D)		62,810
Adjusted Shareholders' Equity of SPL		$3,423,893
FMV (rounded)		$3,424,000

APPENDIX D

Estimated income tax on notional disposition of land and investments and RDTOH to be recovered on notional disposition of land and investments	
Land:	
Notional capital gain on disposition of land	$91,989.00
Non-taxable portion	(45,994.50)
Taxable capital gain	$45,994.50
Estimated income tax at 23.1% (46.2% discounted by 50%)	$10,625.00
Investments:	
Notional capital gain on disposition of investments	$64,061.00
Notional interest on disposition of investments	64,061.00
Non-taxable portion of capital gain	(32,030.50)
Taxable capital gain and interest	$96,091.50
Estimated income tax at 23.1% (46.2% discounted by 50%)	$22,197.00
RDTOH (as per February 28, 2011 tax return, see MNP Report, Schedule B-1)	$87,726.00
Add: refundable portion of tax on accrued taxable capital gains and interest (26.67% of (45,994.50 + 96,091.50))	37,894.00
Refundable dividend tax to be recovered	$125,620.00
Refundable dividend tax to be recovered, discounted by 50%	$62,810.00

CITATION:	2016 TCC 280
COURT FILE NO.:	2014-2006(IT)G
STYLE OF CAUSE:	M. KATHLEEN GRIMES AND M. ERSIN OZERDINC, TRUSTEES OF THE OZERDINC FAMILY TRUST NO. 2 V. HER MAJESTY THE QUEEN
PLACE OF HEARING:	Ottawa, Ontario
DATES OF HEARING:	June 8 and 9, 2016
REASONS FOR JUDGMENT BY:	The Honourable Justice Dominique Lafleur
DATE OF JUDGMENT:	November 29, 2016

APPEARANCES:

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