Docket: 2008-2997(IT)I

BETWEEN:

ROBERT D. G. LOCKIE,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on February 10, 11 and 12, 2010, at London, Ontario

Before: The Honourable Justice Wyman W. Webb

Appearances:

Counsel for the Appellant:	Rebecca L. Grima
Counsel for the Respondent:	André LeBlanc and Steven D. Leckie

---

JUDGMENT

The appeal from the reassessment made under the *Income Tax Act* (the "*Act*") for the 2003 taxation year is allowed, without costs, and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that:

(a) the fair market value of the 1,728 toothbrushes, 5,184 gel pens and 2 school packs donated by the Appellant to In Kind Canada was the amount that the Appellant paid for these items, $2,850;

(b) the Appellant did not realize a capital gain as a result of donating these products to In Kind Canada;

(c) the Appellant is entitled to a credit under section 118.1 of the *Act* on the basis that he made a gift of $2,850 in donating these products to In Kind Canada, a registered charity;

(d) the fair market value of the products acquired by the Appellant and then transferred by him to his spouse, Danielle Deveau-Lockie was the amount that the Appellant paid for these items, $3,800; and

(e) the Appellant did not realize a capital gain as a result of transferring the products to his spouse, Danielle Deveau-Lockie.

The filing fee of $100 is to be refunded to the Appellant.

Signed at Ottawa, Ontario, this 18th day of March, 2010.

"Wyman W. Webb"

Webb, J.

Citation: 2010TCC142
Date: 20100318
Docket: 2008-2997(IT)I

BETWEEN:

ROBERT D. G. LOCKIE,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Webb, J.

[1] This appeal arises as a result of a disagreement with respect to the fair market value of gel pens, toothbrushes and school packs acquired by the Appellant for $2,850 and then "donated" by the Appellant to In Kind Canada (a registered charity) who issued a receipt to the Appellant for $15,078 for these items. In the Reply to the Amended Notice of Appeal (which is dated January 15, 2010 and which was filed after the Appellant filed an Amended Notice of Appeal) the Respondent raised the new issue of whether the Appellant had a donative intent and hence whether the Appellant had made a gift to In Kind Canada when the items were given to this charity. This issue was not raised in the original Reply that was filed on November 27, 2008 and hence was first raised after the expiration of the normal reassessment period.

[2] In addition to the products purchased by the Appellant and given to In Kind Canada, there was a separate group of products purchased by the Appellant for $3,800, transferred to his spouse, and then given by his spouse to In Kind Canada who issued a receipt to the Appellant's spouse for $20,043 for these items. The Appellant elected that he would be deemed to have received proceeds of disposition equal to the fair market value of the products in relation to this transfer of products to

his spouse [1]. Since it is the position of the Appellant that the fair market value of these products was $20,043 and that his adjusted cost base was $3,800, he reported a capital gain of $16,243. The Appellant chose to structure this transaction in this way (with the Appellant reporting the capital gain) because his spouse was in a higher tax bracket.

[3] There are three main issues in this appeal:

a. did the Appellant have a donative intent when he gave the products to In Kind Canada (and hence did he make a gift to this charity);

b. if the Appellant did make a gift to In Kind Canada, what was the fair market value of the products given to In Kind Canada by the Appellant; and

c. what was the fair market value of the products transferred by the Appellant to his spouse?

[4] Before the issue of whether the Appellant had a donative intent is addressed, there are two preliminary issues. The first is whether the Respondent can raise this new argument in the Reply to the Amended Notice of Appeal. The second preliminary issue is, if the Respondent can raise this new argument, whether the Appellant or the Respondent will have the onus of proof in relation to the facts related to this argument.

[5] The right of the Respondent to raise a new argument in support of an assessment is governed by the provisions of subsection 152(9) of the *Income Tax Act* (the "*Act*"). This subsection provides that:

> (9) The Minister may advance an alternative argument in support of an assessment at any time after the normal reassessment period unless, on an appeal under this Act
>
> (a) there is relevant evidence that the taxpayer is no longer able to adduce without the leave of the court; and
>
> (b) it is not appropriate in the circumstances for the court to order that the evidence be adduced.

[1] Subsection 73(1) of the *Income Tax Act*.

[6] In reassessing the Appellant, the Canada Revenue Agency assumed that the fair market value of the products was $579 and allowed the Appellant to claim a credit for a charitable donation based on a donation of $579. Therefore the position of the Respondent (and the basis of the reassessment) was that the Appellant did have a donative intent and did make a gift, albeit a substantially smaller gift that the Appellant had claimed, but still a gift. If the Appellant did not have a donative intent then he did not make any gift to the charity and hence would not be entitled to any credit for a charitable donation in relation to this transfer of property (and hence would not be entitled to the $579 amount that was allowed as the amount of the gift).

[7] The Federal Court of Appeal in *The Queen* v. *Anchor Pointe Energy Ltd.*, 2003 FCA 294, [2004] 5 C.T.C. 98, 2003 DTC 5512 and in *The Queen* v. *Loewen*, 2004 FCA 146, dealt with the issue of whether the Crown could raise a new argument or a new basis for assessment after the expiration of the normal reassessment period. In each case the new argument or basis, if it would have been the basis for the reassessment, would have resulted in a greater tax liability than was reassessed.

[8] In *Anchor Pointe*, the taxpayer claimed an amount as Canadian exploration expenses in relation to the acquisition of certain seismic data. The taxpayer was reassessed to reduce the amount claimed as Canadian exploration expenses on the basis that the fair market value of the seismic data was less than the amount claimed by the taxpayer. The new argument that the Crown wanted to raise was that seismic data purchased for resale did qualify as Canadian exploration expenses (and therefore presumably that no amount should have been allowed as a deduction for Canadian exploration expenses).

[9] In *Loewen*, the taxpayer had claimed capital cost allowance in relation to the acquisition of certain software. The taxpayer was reassessed to reduce the amount allowed, in part, on the basis that the fair market value of the software was less than the amount determined by the taxpayer. One new argument that the Crown wanted to raise was that there was “no income earning purpose” (and hence no amount would have been allowed as a deduction for capital cost allowance if this would have been the basis for the reassessment).

[10] In each case the new arguments were inconsistent with the basis for the reassessment and if the new arguments would have been the basis for the reassessment, the tax liability of the taxpayer would have been greater. In each case the Crown was not asking to increase the tax liability of the taxpayer by raising the new argument but only using the new argument to support the tax liability as

assessed. In each case the Federal Court of Appeal held that the Crown could, pursuant to the provisions of subsection 152(9) of the *Act*, raise the new argument.

[11] In this case, although the argument that the Appellant did not have a donative intent is inconsistent with the basis on which the Appellant was reassessed, and if this would have been the basis for the reassessment it would have resulted in the Appellant not being able to claim any amount as a gift to a charity, the Crown is allowed to raise this new argument provided that it is not being used to increase the tax liability of the Appellant from the amount as reassessed. Counsel for the Respondent acknowledged that this argument was not being used to increase the Appellant's tax liability from the amount as reassessed. Therefore if I should find that the Appellant did not have a donative intent and did not make a gift to In Kind Canada, then the amount that the Appellant would be allowed to claim as a gift to a charity in relation to the transfer of the assets to In Kind Canada would be the $579 amount that was allowed on the reassessment of the Appellant.

[12] The next issue that arises in relation to this argument is whether the Appellant or the Respondent has the onus of proof with respect to the facts related to this argument. In *Anchor Pointe Energy Ltd., supra,* Justice Rothstein (as he then was) also stated that:

> 23 The pleading of assumptions gives the Crown the powerful tool of shifting the onus to the taxpayer to demolish the Minister's assumptions. The facts pleaded as assumptions must be precise and accurate so that the taxpayer knows exactly the case it has to meet.

[13] In *Loewen, supra,* Justice Sharlow also made the following comments:

> **9** It is the obligation of the Crown to ensure that the assumptions paragraph is clear and accurate. For example, the Crown cannot say that the Minister assumed, when making the assessment, that a certain car was green and also that the same car was red, because it is impossible for the Minister to have made both of those assumptions at the same time: *Brewster, N C v. The Queen*, [1976] CTC 107 (F.C.T.D.).
>
> **10** Nor is it open to the Crown to plead that the Minister made a certain assumption when making the assessment, if in fact that assumption was not made until later, for example, when the Minister confirmed the assessment following a notice of objection. The Crown may, however, plead that the Minister assumed, when confirming an assessment, something that was not assumed when the assessment was first made: *Anchor Pointe Energy Ltd. v. Canada*, 2003 DTC 5512 (F.C.A.).

> **11** The constraints on the Minister that apply to the pleading of assumptions do not preclude the Crown from asserting, elsewhere in the reply, factual allegations and legal arguments that are not consistent with the basis of the assessment. If the Crown alleges a fact that is not among the facts assumed by the Minister, the onus of proof lies with the Crown. This is well explained in *Schultz v. Canada*, [1996] 1 F.C. 423 (C.A.) leave to appeal to S.C.C. refused, [1996] S.C.C.A. No. 4.

[14] Paragraph 11 of the Reply to the Amended Notice of Appeal states, in part, that:

> 11. In determining the appellant's tax liability for the 2003 taxation year, the Minister made the following assumptions of fact:
>
> …
>
> c) on October 28, 2003, the Appellant donated the products to In Kind Canada ("IKC");

[15] Paragraph 15 of this Reply states that:

> 15. The appellant was not driven by a donative intent when he dealt with CEI and IKC.

[16] The fact that the Appellant was not driven by a donative intent (which presumably is only relevant if the result of such a finding of fact would be that the Appellant did not make a gift to In Kind Canada) as alleged in paragraph 15 of the Reply is inconsistent with the assumption made that "the Appellant donated the products to In Kind Canada". It is also clear that the fact alleged in paragraph 15 was not one of the facts that the Minister had assumed in assessing the Appellant. As a result the Minister bears the onus of proving this fact.

[17] The Respondent, in relation to the argument that the Appellant did not have a donative intent, relied mainly on the promotional materials distributed by Charitable Enterprises Inc. ("CEI"). CEI was the promoter of the plan. CEI (or a related company) had approached In Kind Canada, a registered charity, to determine what products charities needed. In Kind Canada is a registered charity that accepts donations of products and distributes these products to other charities. CEI also had access to manufacturers in China who could produce certain products cheaply. CEI was trying to match a need for certain products with its source of low cost products in China. In this case, the match was found for toothbrushes, gel pens, and school packs.

[18] In the pamphlet produced by CEI there is an entire page devoted to the "Financial Aspects of a Gift in Kind Donation". The "Financial Aspects" are described in a table that has the following information:

Summary of Tax Savings (Ontario Resident)

Purchase price of goods for donation	5,000	10,000
Donation receipt based on the Fair Market Value (FMV)	25,000	50,000
Tax credits on donation amount (46%)*	11,500	23,000
Less tax on capital gain (FMV – cost x 50% x 46%)*	4,600	9,200
Net tax credit received by Donor	6,900	13,800
Less purchase price of donated goods	5,000	10,000
Net return to Donor in excess of the donation amount	1,900	3,800
Return on purchase of goods for donation	38%	38%
If you have capital losses, these may be applied against the capital gain		
Net return to donor where capital losses applied ** (tax credit less purchase price)	6,500	13,000
Return on investment (donation) where losses applied	130%	130%

Notes

* Assumes top marginal tax rate

** Where the donor has capital losses equal to the capital gain, the net return to the donor will increase

Tax credits on the donation amount assumes taxable income

[19] The position of the Respondent is that the Appellant was motivated by the attractive return on investment (38% to 130% depending on the capital losses available) and not by a donative intent. It is the position of the Respondent that the Appellant wanted to make money from his acquisition and subsequent giving of the products and not to make a gift.

[20] The Appellant stated that he was not motivated by the indicated return on his "investment" but rather by his own desire to benefit charities since he had recently been informed that his sister has multiple sclerosis. The Appellant indicated that he was concerned about charities that spent a significant amount on overhead. However, he did not conduct any investigation to determine how much In Kind Canada spent on overhead and this did not prevent him from completing these transactions.

[21] Justice Iacobucci of the Supreme Court of Canada in *Symes* v. *The Queen*, [1994] 1 C.T.C. 40, 94 D.T.C. 6001, [1993] 4 S.C.R. 695, stated as follows:

> 74 As in other areas of law where purpose or intention behind actions is to be ascertained, it must not be supposed that in responding to this question, courts will be guided only by a taxpayer's statements, ex post facto or otherwise, as to the subjective purpose of a particular expenditure. Courts will, instead, look for objective manifestations of purpose, and purpose is ultimately a question of fact to be decided with due regard for all of the circumstances.

[22] In the years prior to the year in question the following amounts were the amounts that the Appellant had claimed as charitable donations (and these amounts are set out in the Reply to the Amended Notice of Appeal):

Taxation Year	**Donation Claimed**
1998	$0
1999	$0
2000	$0
2001	$0
2002	$664

[23] The Appellant did not dispute that these were the amounts that had been claimed in his tax returns for these years as charitable donations but stated that since his wife was the higher income earner, she claimed most of the charitable donations in her return. The Appellant did not provide any details of the amounts that would have been claimed by his spouse. His explanation that his spouse was the higher income earner throughout these years (he indicated that she was making substantially more than he was) and therefore that she would have claimed the charitable donations, could explain why he did not make any claim for 1998 to 2001 for charitable donations but does not explain why he claimed $664 for charitable donations in 2002.

[24] The amount of cash that the Appellant paid to participate in the program ($2,850) was over four times the total amount that the Appellant claimed as a charitable donation in 2002. The Appellant is a tax preparer who, in 2003, was the manager at Deveau Accounting. One of his roles at Deveau Accounting was to review this particular charitable donation program. It seems to me that an accounting firm would be attracted to the proposed return on investment.

[25] For the Appellant to suggest that he was not motivated by the apparent very attractive return on investment as proposed by CEI and that his participation in this

program was motivated by the fact that his sister had multiple sclerosis stretches the Appellant's credibility to the point where I do not accept his testimony in this regard. I do not accept that he was not motivated by the very attractive return on investment as outlined by CEI in their brochure. I find that he was motivated by the proposed return on his investment.

[26] The next question is whether this profit motive is sufficient to find that the Appellant did not make a gift to In Kind Canada in 2003. In *The Queen* v. *Friedberg*, [1992] 1 C.T.C. 1, 135 N.R. 61, 92 D.T.C. 6031, Justice Linden of the Federal Court of Appeal stated that:

> 4 The Income Tax Act does not define the word “gift”, so that the general principles of law with regard to gifts are utilized by the courts in these cases. As Mr. Justice Stone explained in *The Queen* v. *McBurney*, [1985] 2 C.T.C. 214, 85 D.T.C. 5433, at page 218 (D.T.C. 5435): “The word gift is not defined in the statute. I can find nothing in the context to suggest that it is used in a technical rather than its ordinary sense.” Thus, a gift is a voluntary transfer of property owned by a donor to a donee, in return for which no benefit or consideration flows to the donor (see Heald, J. in *The Queen* v. *Zandstra*, [1974] C.T.C. 503, 74 D.T.C. 6416, at page 509 (D.T.C. 6420)). The tax advantage which is received from gifts is not normally considered a “benefit” within this definition, for to do so would render the charitable donations deductions unavailable to many donors.

[27] In *Klotz* v. *The Queen*, 2004 TCC 147, 2004 D.T.C. 2236, [2004] 2 C.T.C. 2892[2], Associate Chief Justice Bowman (as he then was) stated that:

> 22 One thing is clear, albeit probably irrelevant to what has to be decided here, and it is that Mr. Klotz's motivation in participating in this program was purely the anticipated tax benefit. The broadening of the cultural or intellectual horizons of the students at FSU was not a factor. He never asked what FSU was going to do with the prints. In 1999, FSU received 1,450 prints from various donors and presumably issued receipts for at least $1,450,000.
>
> 25 It is unnecessary for me to deal at any greater length with the donor. Mr. Klotz made a mass donation of limited edition prints to FSU. He did not see them or have them in his possession. He was indifferent as to what they were or who they went to or what the donor did with them. His sole concern was that he receive a charitable receipt. None of this is relevant to the issue. A charitable frame of mind is not a prerequisite to getting a charitable gift tax credit. People make charitable gifts for

---

[2] Appeal to the Federal Court of Appeal was dismissed (2005 FCA 158, [2005] 3 C.T.C. 78, 2005 D.T.C. 5279) and an application for leave to appeal to the Supreme Court of Canada was dismissed (355 N.R. 392 (note)).

> many reasons: tax, business, vanity, religion, social pressure. No motive vitiates the tax consequences of a charitable gift.

[28] The Respondent referred to the decision of Justice Little of this Court in *McPherson* v. *The Queen*, 2006 TCC 628, [2007] 2 C.T.C. 2277, 2007 D.T.C. 326 as support for the position of the Respondent that the Appellant did not make a valid gift. However, it is clear from the decision of Justice Little that the taxpayer in that case did not make a gift because he expected to receive a "kickback". Justice Little stated as follows:

> 22 It is trite law (and common sense) that the anticipation and receipt of a cash kickback equal to 75% of the donation vitiates the gift. (See *Friedberg* v. *R.*, *supra*.)
>
> 23 Based on the detailed evidence outlined above I have concluded that the amounts transferred by the Appellant to A.B.L.E. in 1996 did not constitute a gift because the Appellant expected to receive a kickback equal to 75% of the amount that he contributed.

[29] In *Webb* v. *The Queen*, 2004 TCC 619, [2005] 3 C.T.C. 2068, Justice Bowie held that the taxpayer did not make a gift to a charity that appears to be the same charity as in the *McPherson* case. Justice Bowie stated that:

> 15 Nevertheless the evidence satisfies me that Mr. Webb made the payment of $30,000, as I have already said, at least in anticipation of the future return of a large portion of his gift back to him, either from ABLE or through an indirect channel, in addition to the receipt itself.
>
> 16 Much has been written on the subject of charitable donations over the years. The law, however, is in my view quite clear. I am bound by the decision of the Federal Court of Appeal in *Friedberg* v. *R.**, among others. These cases make it clear that in order for an amount to be a gift to charity, the amount must be paid without benefit or consideration flowing back to the donor, either directly or indirectly, or anticipation of that. The intent of the donor must, in other words, be entirely donative.
>
> 17 The circumstances that I have referred to lead me to conclude that there was nothing donative at all about Mr. Webb's payment to ABLE. His intention was to receive a tax credit for a charitable donation, as well as a substantial refund of the amount he had given, such that when the two were aggregated they would exceed the $30,000 for which he wrote the cheque.
>
> (The * refers to a footnote that was in the text as written by Justice Bowie.)

[30] In *Norton* v. *The Queen*, 2008 TCC 91, 2008 D.T.C.2701, [2008] 5 C.T.C. 2499, Justice Archambault also found that there was no gift. This case also dealt with

the same charity who provided a refund of a portion of the amount contributed as in *McPherson* and *Webb.*

[31] In this case the Appellant did not receive any consideration from In Kind Canada or from any other person involved with the program. The Appellant only obtained a receipt from In Kind Canada which was based on what CEI and In Kind Canada had determined as the fair market value of the products. He did not receive any consideration or any benefit other than the benefit of a credit under the *Act* in relation to the amount of the donation to In Kind Canada.

[32] Although the Appellant was motivated by his potential return on investment, since the only benefit that flowed to the Appellant is the amount of the credit that he will receive under the *Act* (which credit, as claimed by the Appellant, was based on the fair market value of the property that he transferred to In Kind Canada as determined by CEI and In Kind Canada but which will be determined by the actual fair market value of these products), this benefit alone, in these circumstances, cannot vitiate the gift. Therefore I find that the Appellant did make a gift to In Kind Canada when he donated the products to this charity in 2003.

[33] The next question that must be determined is the amount of this gift (which will be the fair market value of the property that the Appellant donated to In Kind Canada). While the Appellant was reassessed on the basis that the fair market value of this property was $579, during closing arguments counsel for the Respondent changed the position of the Respondent and submitted that the fair market value of this property should be equal to the amount paid by the Appellant to acquire it ($2,850).

[34] It is the position of the Appellant that the fair market value of the gift was $15,079 calculated as follows:

Product	**Retail Price per unit as determined for the purposes of issuing the receipt**	**Discount applied**	**FMV per unit as used in Issuing the Receipt**
Toothbrushes	$4.54	30%	$3.178
Gel Pens	$2.79	35%	$1.8135
School Packs	$92.95	0%	$92.95

Fair Market Value as determined for the products donated by the Appellant:

Product	**Quantity Donated**	**FMV per unit as used in Issuing the Receipt**	**FMV as used in Issuing the Receipt**
Toothbrushes	1,728	$3.178	$5,491.58
Gel Pens	5,184	$1.8135	$9,401.18
School Packs	2	$92.95	$185.90
			$15,078.66

[35] The position of the Appellant is that the fair market value of the items that were donated to In Kind Canada should be based on the retail selling price of these items minus a discount to reflect the fact that the Appellant was donating a significant number of the items. In *The Queen* v. *Nash*, 2005 FCA 386, 2005 D.T.C. 5696, [2006] 1 C.T.C. 158, Justice Rothstein (as he then was) of the Federal Court of Appeal stated that:

> 8 The well-accepted definition of fair market value is found in the decision of Cattanach J. in *Henderson* v. *Minister of National Revenue* (1973), 73 D.T.C. 5471 (Fed. T.D.), at 5476:
>
> > 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. 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. 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.
>
> Although Cattanach J. expressed the caution that his words did not constitute an “exact” definition, the extent to which his words have been adopted in the jurisprudence without change over some thirty years suggests that his approach, although not necessarily exhaustive, is now considered to be the working definition.

[36] The Appellant filed an expert’s report related to the methodology applied in determining the fair market value of the products donated by the Appellant to In Kind

Canada. In the report the heading preceding paragraphs 16 and 17 is CEI'S PROCESS TO DETERMINE THE PACKAGE FAIR MARKET VALUE. Paragraphs 16 and 17 then discuss the procedures undertaken by the CEI representatives in relation to the determination of the fair market value. This suggests that the fair market value was determined by CEI and not by In Kind Canada.

[37] CEI entered into an agreement with In Kind Canada on July 15, 2003 in relation to these proposed transactions. Article 5.3 of this agreement provides in part that:

> IKC will be the sole and exclusive determinant of the price for which charitable receipts will be issued.

[38] It seems to me that since In Kind Canada was the registered charity that issued the receipt that indicated that the fair market value of the products donated by the Appellant was $15,079, it would be the responsibility of the charity to determine the fair market value. Debbie Bianco, who worked for In Kind Canada in 2003, was responsible for determining the fair market value of the products. She testified that she did some research. She reviewed some flyers and advertisements for toothbrushes and gel pens. She also reviewed the work completed by the representatives of CEI. Keith Ly, who worked for CEI also testified and he described the work that he did in purchasing various toothbrushes and gel pens that he thought were comparable products from various retailers. Although In Kind Canada did some research to confirm the amounts as proposed by CEI, In Kind Canada accepted the amounts as proposed by CEI. As noted above, the fair market value of the toothbrushes was determined by CEI to be approximately $3.18 each and the fair market value of the gel pens was determined by CEI to be approximately $1.81 each.[3]

[39] It seems to me that the critical question that must be addressed in determining the fair market value of the products that were donated to In Kind Canada is whether the retail market is the appropriate market to be used for this purpose. This issue is addressed in the expert's report in the section titled COMMENTS ON THE APPROPRIATE MARKET. Paragraphs 26 to 31 of this report are as follows:

---

[3] It also appears that in December 2004, when In Kind Canada was very short of cash and needed space in its warehouse, it sold some of the toothbrushes for three cents each and some of the gel pens for two cents each to a company in the United States. Counsel for the Respondent stated, in argument, that as a result of the circumstances related to this sale of toothbrushes and gel pens in 2004 he was not relying on this sale to establish the fair market value of these items in 2003.

26. The indication of the relevant market is an important issue as well in applying the definition of fair market value. For the purposes of this report and for reasons outlined in the following paragraphs, we have assumed that the appropriate market is either one of the following:

    a) the market in which the Donors would purchase the goods included *[sic]* the Package outside of the Donation Program; or,

    b) the market in which IKC would purchase the goods included in the Package.

27. Further, we have assumed that the market in which CEI purchased the goods on behalf of the Donors, the wholesale market, is not relevant as discussed below.

28. The Donors are individuals who are not in the business of manufacturing, wholesaling, or retailing of the products contained in the Package. Accordingly, they do not have the ability to acquire similar products at prices that would be paid by wholesalers or retailers. Comparable products are readily available and are not unique in nature. In order to donate similar products to IKC (or a similar charity) in the absence of the Donation Program, they would likely purchase them from retail stores such as Business Depot, Grand & Toy, Shoppers Drug Mart, possibly dollar stores (assuming they sold items of similar quality which may not be the case), etc. To our knowledge, the Donors have no contacts overseas that would permit them to acquire the goods directly from the manufacturer as was done by CEI for the purposes of the Donation Program.

29. In our view, it would not be realistic to expect that the Donors would be able to negotiate to pay the price charged by a manufacturer or wholesaler of such goods given the one-time nature of the purchase and the number of products purchased. Further, given the nature of the items in the Package (i.e., consumables that are readily available in numerous locations), selling of the quantity of gel pens and toothbrushes in the Package would not result in a "flooding of the market" for such products. In other words, we do not believe that selling of the items would result in significant downward pressure in the prices beyond a reasonable level of volume discounts. Specifically, given the relatively large quantities of the toothbrushes and gel pens contained in the Package, we expect that the Donors would negotiate a volume discount with the retail stores.

30. We have not reviewed IKC's or any charity's purchasing program or the potential volume discounts that they could achieve. ***Accordingly, we cannot comment on whether IKC or other charities which ultimately utilized the goods in the Package would acquire the toothbrushes, gel pens and school kits in a market other than the retail market. However, we have been advised by CEI that the charities that ultimately benefited from the Package (as well as others) were not large enough or did not have any characteristics that would***

> ***permit them to acquire the goods in the same market or at the same prices as CEI.*** (We have not been provided with details regarding the volumes purchased by CEI or the agreements between CEI and the vendors of the products that were included in the Package and similar packages of donated items.)
>
> 31. We believe that, in general, the highest price for the Package would be obtained by selling each of the goods (or groups of goods) separately to individual consumers. However, this approach would likely entail higher costs than by selling the entire Package. Further, the entire Package was donated to IKC to be used by various charities. ***Accordingly, assuming that IKC*** (and/or the charity which ultimately utilized the goods) ***purchased such products from the retail market in similar quantities, we believe that the most appropriate market to be considered in determining the fair market value of the Package is the retail (consumer) market for similar quantities of each product in the Package; in particular, the total cash amount that would be paid by IKC*** or the relevant charity ***to acquire a similar Package***. Further, we believe it is appropriate to apply volume discounts in calculating the fair market value of each product in the Package and the discounts utilized by CEI are not unreasonable in quantum based on the quantities purchased by the Donors.
>
> (emphasis added)

[40] The statement that the charities could not have acquired the products at the same price as CEI is accurate but not complete. The donors (including the Appellant) did not acquire the products at the same price as CEI. John Groscki (who appears to be the owner of CEI and the related companies involved in the transactions) confirmed that the company selling the products to the donors (including the Appellant) marked these items up 3 or 4 or more times from the amount paid by CEI (or a related company) to the manufacturers of the products.

[41] Since the relevant transaction is the donation of the property to In Kind Canada, it does not seem to me it is relevant whether the donors would have otherwise acquired the products in the retail market. The transaction that is relevant is the acquisition of the products by In Kind Canada and therefore it seems to me that the relevant market would be the market which In Kind Canada would have acquired products if the products would not have been donated by the donors to In Kind Canada. The assumption made in paragraph 31 of the expert's report referred to above is that "IKC … purchased such products from the retail market in similar quantities". It seems to me that the identification of the market in which In Kind Canada would have purchased such products is critical to the determination of the fair market value of the products donated to In Kind Canada. Once the assumption that "IKC … purchased such products from the retail market" is made, the conclusion that the most appropriate market is the retail market seems obvious and

inevitable. However, the critical question is whether the retail market is the correct market in this case.

[42] During her testimony, Melanie Russell, the expert witness, did not directly address the assumption made in paragraph 31 of her report that "IKC … purchased such products from the retail market". The following are excerpts from her testimony at the hearing:

> Q. Okay. Now what were your thoughts with respect to the second market that you mentioned which would be the market in which In Kind Canada could purchase the goods that were included in a package?
>
> A. So the other piece that I considered was what price would be paid by IKC or the charities that benefited from these toothbrushes and gel pens.
>
> I did not speak to any of the charities or In Kind Canada, so I don't have any first-hand knowledge of how much they would have purchased or normally purchased were it not for the donation program. However, my understanding or what I was advised was particularly with respect to the particular charities that benefited, their quantities were not huge for pens or toothbrushes or whatever was used. So similar to Mr. Lockie and Ms. Lockie, I expect that they would be able to get some kind of volume discounts, but again they wouldn't have the ability to go to manufacturer of pens or toothbrushes to get the wholesale price.
>
> Q. Okay. Did you have any additional comments with respect to the market in which the charities would be purchasing the products?
>
> A. Paragraph 30, 31 on page nine, if you go back to the definition of fair market value and it being the highest price, obviously the highest price for that package would be obtained if, from someone like Business Depot, Staples, selling one pen or a package of 12 pens for example. But because the reality is that the package is more than just one pen or 12 pens, I think that while the appropriate market is the retail or consumer level, but volume discounts need to be considered to match the quantities that were sold and bought.

And during cross examination:

> Q. The lower price. And why is it that it never occurred to you in this report that CEI would be the appropriate or the transaction that transpired between Mr. Lockie and EMI and the CEI donation program that was being promoted wouldn't be the proper market to evaluate these items in terms of fair market value?
>
> A. It's an assumption on, if you go to -- there's an assumption that you've already pointed out on paragraph 34.

> Q. Thirty-four, yes.
>
> A. Page ten.
>
> Q. Mm-hmm.
>
> A. (c) so the underlying assumption is that the donation program does not create a market on its own and the definition of fair market value, being the highest price would exclude the investment market.
>
> Q. That's what you need mean by (c)? Donation program should not be considered to be an investment market. An investment market is meant to be just a market.
>
> A. Correct. It doesn't create a market on its own.
>
> …
> A. I made the assumption that the IKC or the charities would not have access or don't have access to the wholesale market.

[43] It seems to me that the transactions in this case were not part of the normal transactions of In Kind Canada and that In Kind Canada would not, in the normal course of their activities, have purchased these items in these quantities. Debbie Bianco testified as follows:

> Q. Okay. And maybe you can just give us a brief description of the operations of In Kind Canada at that time. What was it about?
>
> A. Oh, In Kind Canada was a fabulous idea actually. It started out, John Page and an associate of his starting the business and they -- what In Kind Canada actually did was they took donations from the general public and businesses, mainly businesses in terms of they start out with things like desks and chairs and instead of putting those desks and chairs into landfills, we put them into charities. The charities absolutely loved this because they didn't have access to these materials and it lessened the blow on their bottom line.
>
> Q. All right. And how did the distribution of these products work? How did you identify the charities?
>
> A. In Kind Canada had a fairly sophisticated in the world of charitable industry database system that would be the program allocation people would input the donation, fair market value would have, would be attached by a piece of paper and that would then go into the database. We would then go into our database of over 1200 charities that were member charities at the time and we would know or they would tell

> us via their wish list what they wanted or needed in their operations or for their programs. And then we would then tell them to go and get it or come and collect it.
>
> …
>
> Q. And the items that In Kind Canada distributes to its member charities, are they -- what percentage of those, I guess, are donated items or is there a percentage that In Kind Canada purchases and then redistributes?
>
> A. In Kind Canada was never in the business of purchasing anything and distributing anything. Everything that we distributed to our member organizations were donated.

[44] John Groscki is a chartered accountant and appears to have been the person who owned or controlled CEI and the related companies that were involved in these transactions. It also appears that he was the person who created this structure of transactions. John Groscki wanted to gain experience in importing goods from China and introducing such products into the Canada market. Sometime either in 1995 or later he started attending trade shows or visiting factories in China with some friends that he had met in 1995. He created the brand name "RYT" that was used for the toothbrushes, gel pens and products in the school packs. In 2003, in developing this donation program, he was looking for opportunities to acquire products at a low cost from manufacturers in China and for which the retail price in Canada was several times the cost of acquiring the product from the manufacturer.

[45] One of the initial steps that John Groscki took in establishing the plan was to contact In Kind Canada to determine what types of products would be of interest to the charity. The proposal was that John Groscki, through one of his companies, would arrange for a steady supply or stream of products to the charity who would issue receipts to donors for an amount that would be approximately five times the amount that the donor paid to the particular company that sold the product to the donor. It was important that In Kind Canada was part of the structure from the beginning since the products that were being imported would ultimately end up in the hands of In Kind Canada. The Appellant was only one of many persons who participated in this program.

[46] CEI entered into an agreement with In Kind Canada dated July 15, 2003 (which was approximately three months before the Appellant entered into the transactions related to this appeal). Paragraph 5.3 of this agreement provides as follows:

> 5.3 ***<u>Confirmation of Goods To Be Received As Donations:</u>*** CEI will confirm with IKC the type and quantity of Product that IKC wishes to receive as donations. Prior to shipment, IKC will deliver written confirmation to CEI of the Product its *[sic]* wishes to receive and the price at which it will provide charitable receipts to donors in respect to the delivered Product. IKC will be the sole and exclusive determinant of the price for which charitable receipts will be issued.

[47] John Groscki explained the significance of this paragraph as follows:

> Q. Can you explain the purpose of that paragraph?
>
> A. Again, we're going to undertake to purchase merchandise in China in very large quantities so it's rather critical that we've agreed as to what items are going to be donated so that we know ahead of time that yeah the charity says yeah, we can use these, we want these. That's sort of straightforward. They know the quantities we're going to get so we're confirming they're going to get them so that's fine.
>
> And then prior, it's important that IKC work with us in it terms of due diligence and that it's important they do their due diligence as well in terms of market pricing, receipting, et cetera.

[48] CEI (or a related company) was importing the products by the container. His estimate was that they would be importing dozens of containers of products. There would be 980,000 to just over a million pens in one container. From the evidence presented at the hearing it appears that all of the toothbrushes, gel pens and school packs imported by CEI went to In Kind Canada either through the donation program or as part of the school supplies that were sold to In Kind Canada after the Federal Government announced that changes would be made to the *Act* in relation to the determination of the fair market value of items acquired and then donated to charities. This announcement terminated the donation program. At the time of the announcement (which was made in early December 2003) John Groscki estimated that there were 20 to 30 containers of merchandise that he still had to purchase. He described this as follows:

> A. When the program ended or when the law changed that I could no longer sell the merchandise the way we were selling it, as I said at that point in time, we hadn't had such opportunity to fully commercialize any of the products we were bringing in. So when the program was terminated, sort of retroactively in terms of ability to receipt charitable items, we were forced basically at that time to purchase approximately, I don't know, 20 to 30 containers of merchandise totaling I think 1.2, $1.3 million.

[49] His companies were importing other products in addition to the gel pens, toothbrushes and school packs and it appears that all of the products were channelled

into In Kind Canada. The agreement between CEI and In Kind Canada also included article 5.7 which provides that:

> 5.7 ***Cash Donation Paid to IKC Upon Release of Funds From Escrow:*** When IKC issues donation receipts for delivered Product, IKC will receive (a) in respect to the first $10,000,000 of total donations paid by donors, a cash donation equal to 2% of the total donation amount paid by donors; and (b) in respect to all donation amounts paid by donors in excess of the first $10,000,000, IKC will receive an amount to be negotiated in excess of the said 2%.

[50] John Groscki's explanation of why In Kind Canada would be paid the amount as contemplated by this paragraph is as follows:

> Q. Can you explain why CEI would be paying an amount of money or this particular amount of money to In Kind Canada?
>
> A. Basically, IKC is acting as a conduit for our company as well, in that, the goods that are being donated are not going to go strictly to IKC charities. Because from our standpoint, the donors are free to donate items to any charity in Canada. IKC basically is handling goods on our behalf, bringing them into Canada.
>
> In addition, they're going to be incurring other expenses related to our business because at times we're going to be getting quantities out of those various containers as well. And we understood they would be incurring additional expenses as a result of this. And I think IKC had been struggling to get along at that time, so to me it looked like it was reasonable compensation for additional expenses that IKC would incur in handling the volumes of items that were going to be coming to them.

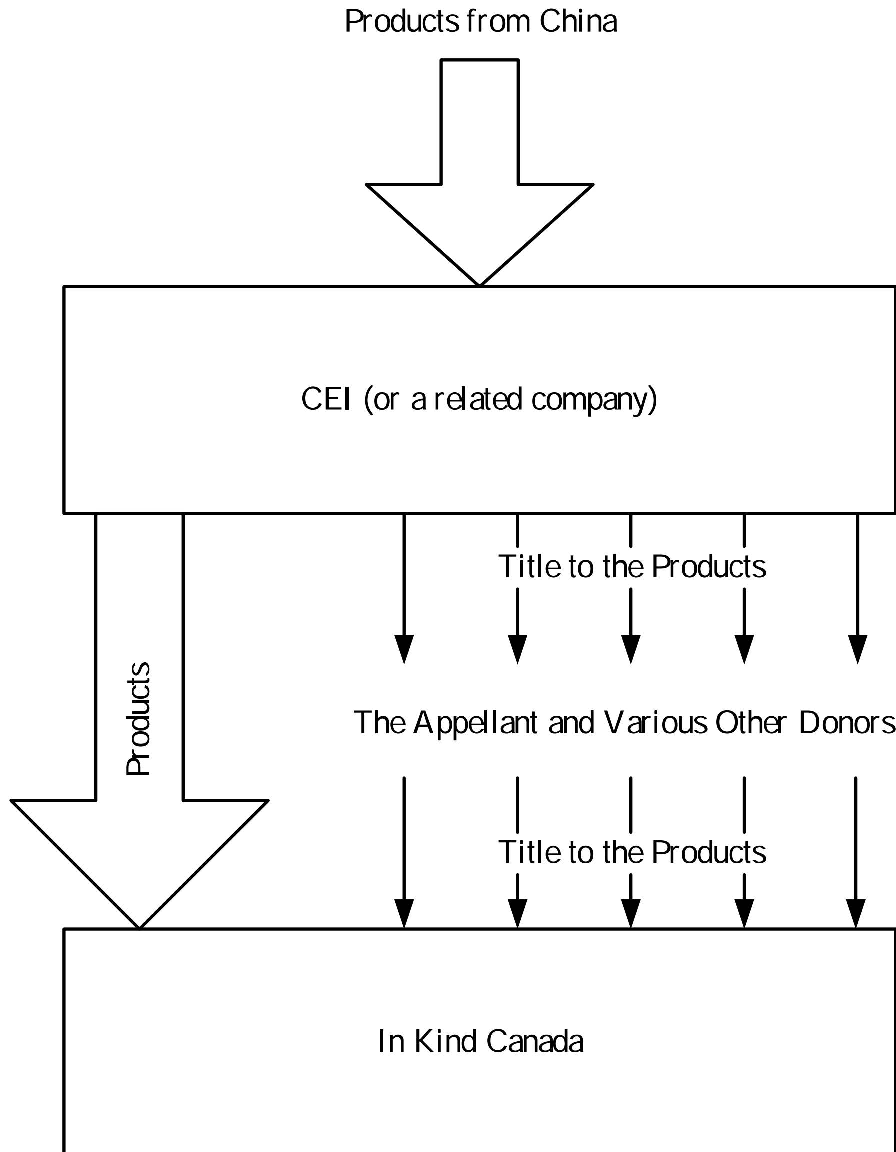
[51] While the agreements provided that the Appellant could donate the goods to any charity or retain them (there were three options provided in the agreement – to donate the products to a charity, to retain ownership, or to transfer ownership) it seems obvious that the logical choice for the Appellant (or for any other participant) would be to donate them to In Kind Canada as the Appellant (or any other participant) knew or expected that In Kind Canada would be issuing a receipt for approximately five times the amount that the Appellant paid for the products. The third option (to transfer ownership) was the one chosen by the Appellant to transfer ownership to his spouse who then donated the products to In Kind Canada.

[52] Whether the products took the direct route from CEI to the Appellant to In Kind Canada or the indirect route from CEI to the Appellant to his spouse to In Kind Canada, it seems obvious that the products would be donated to In Kind Canada and this would be obvious even before the documents were executed. CEI had a checklist of documents that were to be completed by the Appellant. The

checklist included a Deed of Gift to a Charity. Although this document was undated, it appears to have been executed at the same time as the other documents (the Purchase Agreement (pursuant to which the Appellant acquired title to the products) and the Purchaser's Transfer Agent Agreement (pursuant to which the Appellant appointed Canadian Charity Distribution Inc. (a company related to CEI) as his agent to receive, store, package and deliver the products to the charity)).

[53] The products were imported by CEI by the container load. While the donors acquired title to smaller lot sizes (which title was conveyed to In Kind Canada) the products went directly from CEI (or a related company) to In Kind Canada. As noted above, the donors appointed Canadian Charity Distribution Inc. (a company related to CEI) as their agent to receive, store, package and deliver the product to the charity. The products were acquired by the donors on behalf of and for the benefit of In Kind Canada. The role of the donors was to provide the cash to fund the purchase of the products. If In Kind Canada would have had sufficient cash and would have been willing to purchase the products from CEI, then there would not have been any need to flow the product through the donors.

[54] The flow of product can be illustrated as follows:



[55] It seems to me that the retail market is not the appropriate market to use in determining the fair market value of the products donated to In Kind Canada. The donors were a conduit in the pipeline for the products that flowed from the manufacturer to CEI (or a related company) to the donors to In Kind Canada. John Groscki described the role of the donors as:

> So at the end of the day we were basically making donors into wholesale distributors or distributors of products, one way or the other to charities.

[56] It seems to me that if In Kind Canada were to acquire the products from someone other than the Appellant, that it would acquire these products directly from CEI (or a company related to CEI). The arrangement between CEI and In Kind

Canada was in place before the Appellant acquired the products. It seems to me that, contrary to the assumption made by Melanie Russell, that In Kind Canada did have access to the wholesale market as it clearly had an arrangement with CEI, who was the importer, before the Appellant and the other donors acquired the products. Since CEI were "basically making donors into wholesale distributors or distributors of products", CEI could have make In Kind Canada a wholesale distributor.

[57] CEI would presumably be indifferent or would prefer to sell the products directly to In Kind Canada for the same amount that it received from the Appellant (and the other donors). CEI would receive the same revenue whether it sold the products to the Appellant for $2,850 or to In Kind Canada for $2,850 but would have lower costs if the products were sold directly to In Kind Canada as there would be less paperwork and no need to spend time acquiring products that were considered to be comparable. As a result it seems obvious that the alternate source of product, if In Kind Canada were to acquire the products from someone other than the Appellant, would be CEI and not the retail market. CEI, in the normal course of its business, sold the package of products to the Appellant for $2,850 and it seems logical, since CEI would be in the same or a better position if it sold the same products to In Kind Canada for $2,850, that CEI would also sell the same products to In Kind Canada for $2,850.

[58] In *Nash, supra,* Justice Rothstein (as he then was) made the following comments in relation to the selection of the market in determining the fair market value of particular items:

> 19 It is wrong to assume, as did Ms. Tropper and the trial judge, that the fair market value of a group of items is necessarily the aggregate of the price that could be obtained for individual items in the group. That might be so in some cases, but it is necessary to carefully consider the circumstances in which the groups are being acquired and disposed of in order to make that determination.
>
> 20 If the evidence is that the groups are not sold in the same market as individual items, the fair market value of the groups will not be the aggregate of the fair market value of the individual items. For example, if items are sold in large volumes in a wholesale market, the fair market value of the volumes sold in that market will be less than the aggregate of the values of the items considered individually that make up those volumes. If that were not the case, there would be no wholesale market. The wholesalers would sell their large quantities in the retail market to obtain the aggregate of the retail prices for the individual items for the large quantities they sold. But that does not occur because consumers will not purchase the large quantities the wholesalers are selling. There are other differences between a wholesale and retail market such as convenience and other services to the consumer provided by retailers

> but not by wholesalers. That is why there is a difference between prices in the retail and wholesale markets.
>
> 21 On the other hand, if the evidence is that the groups of items are acquired and disposed of in the same market as the individual items, it may be that the fair market value of the groups is the aggregate of the fair market values of the individual items. Generally, shares of common stock might be valued in this way.
>
> …
>
> 29 Where there is a gap between the time an asset is acquired and disposed of, the cost of the asset will normally be an unreliable basis for estimating fair market value. But where the dates of acquisition and disposition are very close in time, barring evidence to the contrary, the cost of acquiring the asset will likely be a good indicator of its fair market value.

[59] The Federal Court of Appeal concluded in *Nash* that the fair market value of art prints acquired in large quantities and then donated to a charity was the amount paid by the purchaser of such prints. In my opinion, in this case, the correct amount to be used as the fair market value of the products is the amount paid by the Appellant. In effect the Appellant was acquiring these products on behalf of and for the benefit of In Kind Canada. Arrangements were put in place before the products were acquired by the Appellant that In Kind Canada would accept the products and would issue the appropriate receipt. The products were delivered directly by CEI (or a related company) to In Kind Canada. Since the Appellant acquired these products in an arm's length transaction from CEI (or a related company) the amount paid by the Appellant to acquire these products is, in my opinion, the fair market value of these products acquired by In Kind Canada and hence the amount of the gift made by the Appellant to In Kind Canada. As noted above it seems obvious that if In Kind Canada were to purchase these products that it could have purchased them directly from CEI (or a related company) for the same purchase price as paid by the Appellant.

[60] The focus of the Appellant's evidence and argument was on the fair market value of the products donated by the Appellant to In Kind Canada. There was also another transaction in which the fair market value of the products is relevant. The Appellant purchased a group of products from CEI (or a related company) for $3,800 and then transferred these products to his spouse. In relation to the transfer of the products to his spouse the Appellant claimed that the fair market value of the products was $20,043. No explanation was provided by the Appellant for the more than fivefold increase in value in relation to this transaction. It appears that he was also relying on the retail market comparisons to determine the fair market value of

the products that he transferred to his spouse. However, it seems to me that the fair market value of the products acquired by the Appellant and transferred to his spouse is the amount that the Appellant paid for these products as it seems obvious that his spouse could have acquired these products from CEI (or a related company) for $3,800. Why would the Appellant's spouse pay him $20,043 for the same products that she could acquire from CEI (or a related company) for $3,800? There is no reason why the retail market should be used as a comparative market for this transaction as it seems clear to me that CEI (or a related company) would have been willing to sell the products to the Appellant or his spouse for $3,800.

[61] As a result there is no need to analyze the products submitted into evidence as comparable toothbrushes and gel pens. However, I would like to make a couple of comments in relation to the toothbrushes. The position of the Appellant is that the retail selling price in 2003 of a comparable toothbrush was $4.54. Since the receipts for toothbrushes that were purchased showed retail prices ranging from $1.49 to $4.99 this would mean that it was the position of the Appellant that the toothbrushes that were included in the products would be comparable to the higher quality toothbrushes on the market in 2003. John Groscki also noted that:

> …So knowing that, we tried to select items that had a long-term market potential in Canada and our focus then was on quality and packaging in every sense. In other words, we wanted to be recognized and known for quality and we wanted to establish as many markets as possible.…
>
> …
>
> … We're trying to buy the very best product we can buy and so at the end of the day, my understanding is we ended up paying probably 30, 40, 50 percent more than the lowest price that had been available to us in China.

[62] On the back of the packaging for the toothbrushes three points are stated. The second and the third point are, as written, as follows:

> Bends to absorb excess pressure reducing the rick *[sic]* of damage to gums
>
> For total contorol *[sic]* of your cleaning

[63] If the quality of the spelling is indicative of the quality of the product, then CEI has not succeeded in its goal of importing a high quality product.

[64] There was also evidence of two retail purchases of the toothbrushes that were part of the donation program. One purchase was made at the Salvation Army store in Hamilton, Ontario. The items purchased were introduced into evidence with the receipt showing that 12 of the toothbrushes were purchased on August 31, 2005 for $3.49 (before taxes). No explanation was provided of the circumstances related to this purchase. This purchase would suggest that the retail price of the toothbrushes was $0.29 (before taxes) each in 2005.

[65] The other purchase that occurred at the retail level was made by the Appellant in Quebec City on September 29, 2006. The Appellant stated that he paid between $3 and $3.50 for this toothbrush. He did not have the receipt for this purchase. This purchase was still significantly less than the $4.54 amount that was used as the retail selling price of the toothbrushes.

[66] It appears that at least some of the toothbrushes did make it to the retail market but the retail selling price varied widely from $0.29 to $3 - $3.50 per toothbrush. Since the retail transactions in the toothbrushes took place in 2005 and 2006, they would not, however, have been of any assistance in 2003 in determining the retail price of the toothbrushes at that time.

[67] The appeal is allowed, without costs, and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that:

a. the fair market value of the 1,728 toothbrushes, 5,184 gel pens and 2 school packs donated by the Appellant to In Kind Canada was the amount that the Appellant paid for these items, $2,850;

b. the Appellant did not realize a capital gain as a result of donating these products to In Kind Canada;

c. the Appellant is entitled to a credit under section 118.1 of the *Act* on the basis that he made a gift of $2,850 in donating these products to In Kind Canada, a registered charity;

d. the fair market value of the products acquired by the Appellant and then transferred by him to his spouse, Danielle Deveau-Lockie was the amount that the Appellant paid for these items, $3,800; and

e. the Appellant did not realize a capital gain as a result of transferring the products to his spouse, Danielle Deveau-Lockie.

Signed at Ottawa, Ontario, this 18th day of March, 2010.

"Wyman W. Webb"

Webb, J.

CITATION:	2010TCC142
COURT FILE NO.:	2008-2997(IT)I
STYLE OF CAUSE:	ROBERT D. G. LOCKIE AND HER MAJESTY THE QUEEN
PLACE OF HEARING:	London, Ontario
DATE OF HEARING:	February 10, 11 and 12, 2010
REASONS FOR JUDGMENT BY:	The Honourable Justice Wyman W. Webb
DATE OF JUDGMENT:	March 18, 2010

APPEARANCES:

Counsel for the Appellant:	Rebecca L. Grima
Counsel for the Respondent:	André LeBlanc and Steven D. Leckie

COUNSEL OF RECORD:

For the Appellant:

Name:	Rebecca L. Grima
Firm:	Giffen & Partners London, Ontario

For the Respondent:	John H. Sims, Q.C. Deputy Attorney General of Canada Ottawa, Canada