BETWEEN:

RALPH J. SAZIO ..... APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE ..... RESPONDENT.

Toronto 1968 Nov. 14-15

Ottawa Dec. 2

Income tax—Coach employed by football club—Corporation controlled by coach substituted as employee—Whether remuneration paid corporation assessable as income of coach—Bona fides of transaction.

Appellant, who was employed as coach of a football club until December 1965 at an annual salary of approximately $20,000, resigned in 1964 and the club contracted to employ as coach until December 1965 at the same salary a company controlled by appellant and of whose issued shares all but one were held by appellant and his wife. The company, which also carried on some other businesses, employed appellant as general manager at a salary of $6,000 a year. Appellant was assessed to income tax on the amounts which the football club paid the company in 1964 and 1965 on the footing that those sums were in fact paid for appellant's personal services to the club and that the company received them as his nominee or agent.

Held, allowing the appeal, the contracts between appellant, the company, and the club were *bona fide* and governed the relationships between the parties thereto. The company was not merely a sham, simulation or cloak.

Kindree v. M. N. R. [1965] 1 Ex. C.R. 305, distinguished. *Crossland v. Hawkins* [1961] 2 All E. R. 812; *C.I.R. v. Peter McIntyre Ltd.* 12 T.C. 1006, referred to.

INCOME TAX APPEAL.

Wolfe D. Goodman for appellant.

Gordon V. Anderson for respondent.

CATTANACH J.:—These are appeals from two assessments made by the Minister dated March 23, 1967 in respect of appellant's 1964 and 1965 taxation years wherein the Minister added the amounts $20,143.30 and $22,143.30 to the appellant's income in those respective years and the income tax levied was increased accordingly.

The question involved is whether the amounts so added by the Minister to the appellant's income is income of the appellant, as is contended by the Minister, or income of a company incorporated under the name of Ralph J. Sazio, Limited, as is contended by the appellant.

The appellant became a football coach after an outstanding career as a football player in professional ranks. He was

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first engaged as an assistant coach by the Hamilton Tiger-Cat Football Club Limited (hereinafter referred to as the club) about 1950 in which capacity he contributed substantially to the success of the team operated by the club in the Canadian Football League. His coaching duties did not occupy his full time throughout the entire year and accordingly, as a prudent man, he engaged in other activities most likely as a hedge against the time when his services as a football coach would no longer be in demand.

His first activity, other than as a football coach, was as a life insurance agent from 1950 to about 1963. From that beginning he entered into a variety of other fields. If my recollection of the evidence is correct, the appellant held a share interest in a company engaged in a general insurance agency business known as Frank E. Bliss Limited in which I believe he subsequently terminated his interest. He was also part owner of R and S Insurance Limited together with one Robertson. I also recall that during his testimony the appellant mentioned that about this time he became the manager of a leasing company, that he had an interest in a restaurant called Mathers Restaurant and that he was managing a farm. I think that these multitudinous activities fully justify the allegation in paragraph 1 of the notice of appeal that "The appellant is a football coach and businessman residing in the City of Burlington" in the Province of Ontario.

After the conclusion of the 1962 football season the then head coach for the club terminated his engagement in that capacity in favour of the acceptance of a similar post with a competing team.

The appellant thereupon succeeded to the position of head coach. By an agreement dated February 20, 1963, between the appellant and the club, the appellant was employed as head coach for a three year period ending December 9, 1965, at an annual salary of $18,000 plus a bonus of $1,000 if the team played in the final game to determine the championship of the Eastern conference in any of the three years during the term of the contract plus a further bonus of $1,000 if the team played in the Grey Cup game in any of those three years.

On the advice of his auditor and solicitor the appellant caused to be incorporated, pursuant to the laws of the

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Province of Ontario, a private company under the name of Ralph J. Sazio Limited (hereinafter called the Company) by letters patent dated April 2, 1964, with an authorized capital of 3,600 preference shares of the par value of $10 each and 4,000 common shares without nominal or par value which common shares might be issued for an aggregate consideration of $40,000. Of this authorized capital stock only 1001 common shares without nominal or par value have been issued and are outstanding and of the 1001 common shares so issued the appellant holds 501, his wife 499 and Dr. C. C. Hopmans holds one. Dr. Hopmans has been the president of the Company since its inception, and the appellant has been the secretary for the same period. Mrs. Sazio, while a shareholder and director, has not been an officer of the company.

The objects for which the company was incorporated read as follows:

(a) TO engage in the business of furnishing advice and services with respect to the coaching of sports and athletic endeavours of every nature and kind and for this purpose to enter into, make, perform and carry out contracts of every kind with any person, firm, association, private corporation, public corporation, municipal corporation or body politic;

(b) TO acquire rights to the services of and to employ persons in any and all fields of sports and athletic endeavours of every nature and kind and to contract or deal with others with respect to the services of such persons;

(c) TO organize, reorganize and manage the business or operations of any other company, corporation, firm, business or undertaking whatsoever, and to receive in payment therefor fees, royalties, commissions and other remuneration in cash, securities or other property; and

(d) TO purchase, receive, hold, own, sell, assign, transfer, mortgage, pledge or otherwise acquire or dispose of shares, bonds, mortgages, debentures, notes or other securities, obligations or contracts of any company, corporation or association;

By letter dated April 15, 1964, the appellant tendered to the club his resignation as head coach to be effective May 1, 1964, which resignation was obviously accepted by the Club because by a memorandum of agreement dated April 15, 1964, the club agreed to employ the company, Ralph J. Sazio Limited, as its head coach for the term beginning May 1, 1964, and ending December 9, 1965, that is for the remainder of the term of the contract dated February 20, 1963, between the club and the appellant. The remunera-

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tion payable to the Company was identical to that payable by the Club to the appellant under the agreement dated February 20, 1963.

It is logical to infer that the club was willing to facilitate the appellant in his new arrangement and it is equally logical to infer that the club was anxious to ensure that the duties of head coach, to be performed by the company, would, in fact, be performed by the appellant personally even though he might perform such duties as an officer or employee of the company and further that the appellant would not, through the instrumentality of the company, engage in similar duties for any rival club. The foregoing inferences are substantiated in the correspondence exchanged between the solicitor for the appellant and the solicitors for the club being letters dated April 24, 1964, April 30, 1964 and May 12, 1964, introduced in evidence as Exhibits A-4, A-5 and A-6 respectively.

To ensure these ends the contract between the company and the club dated April 24, 1964, included paragraphs 3 and 8, reading as follows:

> 3. Ralph J. Sazio Limited shall well and faithfully serve the Club and use its best endeavours to promote the interest of the Club and during the term of this Agreement it shall restrict its entire business undertaking and operation and the efforts, endeavours, talents, business operation and undertaking of any of its officers, directors or servants to the business of the Club and shall not, without the consent in writing of the majority of the directors of the Club, engage in any other business or occupation or permit its officers, directors or servants to engage in any other business, operation or undertaking or occupation, other than for and on behalf of the Club.
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> . . .
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> 8. If the Company shall at any time, by reason of the death, illness, mental or physical incapacity of Ralph Joseph Sazio be incapacitated from carrying out the terms of this Agreement, according to its true intent, or if the said Ralph Joseph Sazio shall cease to be an officer, director or servant of Ralph J. Sazio Limited devoting his whole time, attention and talents to the business of the Company, the Club shall be at liberty to terminate this Agreement and the Club shall only be responsible to pay to the Company an amount for remuneration proportionate to the number of months served by the Company during such year.

By an agreement dated December 8, 1964 between the appellant and the company, the appellant was engaged as general manager of the Company at a remuneration to be determined by the board of directors from time to time. The salary so determined was $6,000 per year. By paragraph 5 of this agreement the appellant undertook not to

engage in any other business or occupation in respect of coaching of sports and athletic endeavours without the consent in writing of the board of directors of the Company and the board of directors of the Club.

It will be observed that from April 15, 1964, until the agreement dated December 8, 1964, there was no written agreement between the appellant and the company but in that interval the appellant did act as the general manager of the company and in my view the evidence confirms the allegation in paragraph 6 of the notice of appeal that, "Under an oral agreement made in the month of April, 1964, which was reduced to writing on December 8, 1964, the Appellant became an employee and general manager of the company."

By a further written agreement dated December 8, 1964, between the company and the club, the club again engaged the company as its head coach for a term beginning May 1, 1965 and ending December 9, 1969. This agreement replaced the former agreement between the Company and the club dated April 15, 1964, for the unexpired term of the former agreement and extended the term of engagement until December 9, 1969. The provisions of the latter agreement were identical with those of the former agreement with the exception of the term and, because of the success enjoyed by the football team, the former annual remuneration of $18,000 was increased to $20,000 per year with the same bonuses as formerly.

Pursuant to the agreement dated April 15, 1964, the company was paid the sum of $20,143.30 by the club during the 1964 calendar year and pursuant to the agreements dated April 15, 1964 and December 8, 1964 the company was paid the sum of $22,143.30 by the club during the 1965 calendar year.

The company included these sums in its income for the years in question in the income tax returns it prepared.

At this point I should mention that the company engaged in other activities under paragraph (*c*) of the objects of its incorporation.

The company entered into a contract with Brant Supply Services Limited to manage the affairs of that company which was engaged in the business of leasing and billing. The company also entered into a contract to act as manager

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and rental agent of 68 Charlton Avenue West Limited which owned an office building. The company was also engaged as the manager of a medical clinic and another company, Burlington Holding Limited, which owned an office building and engaged in a real estate business. Contracts were entered into by the company from time to time with other businesses.

In addition the company entered into a contract, presumably verbal, with a newspaper for a series of articles on matters pertaining to football, written by the appellant, the remuneration for which was paid to the company as well as a contract for a regular radio program and a weekly television program with Hamilton broadcasting stations which the appellant would conduct. Here again the remuneration was paid to the company. It frequently occurred that the appellant invited guests to appear on those programs who were reimbursed by the company and in some instances, when the appellant was unable to appear, the assistant coaches would conduct the programs on his behalf for which they were paid by the company.

The appellant described the duties of a head coach as falling into three main categories the first two of which he considered primarily as organizational in nature. These duties were (1) to set up an efficient scouting system to discover football players of outstanding ability and to engage those players, (2) to organize practices and assign the players engaged to those positions where their individual talents and abilities would be most effective and (3) to supervise the conduct of actual football games in which the team participated.

To perform these duties the head coach had, in the present instance, the assistance of two assistant coaches who were under contract with the club. However in conducting a spring training camp for high school players as prospective players for the club and in the conduct of training camp, the company hired additional personnel. It was my understanding of the evidence that these persons were selected and engaged by the company and when the club could be persuaded, either in advance or subsequently, to pay for their services, this was done but if the club declined to do so the responsibility for the payment of persons

engaged was that of the company. It would appear that, except for relatively insignificant amounts, the club bore this expense.

It was elicited in cross-examination that the coaching duties performed by the appellant, as manager of the company, were identical to those performed by him under his previous contract for personal service and that in the radio and television programs and press releases the appellant was therein personally referred to as the head coach. This the appellant conceded to have been the case but he persisted in his contention that this was not necessarily an accurate description of his capacity which was that the company was the head coach and he was the general manager of the company.

The assumptions upon which the Minister acted in assessing the appellant as he did are set out in the reply to the notice of appeal as follows:

> (*a*) the Appellant, Ralph Joseph Sazio was, throughout his 1964 and 1965 taxation years, an employee of the Hamilton Tiger-Cat Football Club Limited (hereinafter referred to as "the Club") and that as remuneration for his services in those years as a football coach, was entitled to receive from the said Club $20,143 30 and $22,143 30 in his 1964 and 1965 taxation years respectively;
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> (*b*) that pursuant to the direction of or with the concurrence of the Appellant, the Club paid the said sums to Ralph J. Sazio Limited for the benefit of the Appellant or as a benefit that the Appellant desired to have conferred on Ralph J. Sazio Limited,
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> (*c*) that the said sums of $20,143 30 and $22,143 30 were income of the Appellant from an office or employment within the meaning of sections 3 and 5 of the *Income Tax Act* and by virtue of section 16 of the *Income Tax Act* and were not income of Ralph J Sazio Limited;
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> (*d*) that the sums of $20,143 30 and $22,143 30 were earned by the Appellant personally and were income of the Appellant for his 1964 and 1965 taxation years respectively, and were paid in respect of the Appellant's services, and not services rendered by Ralph J Sazio Limited to the Club;
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> (*e*) that the series of agreements under which the Appellant purported to cause to be paid to Ralph J. Sazio Limited the remuneration paid by the Club for his services to the Club as a football coach did not constitute valid or *bona fide* business transactions but were in effect an attempt artificially to reduce the Appellant's income from his employment as a football coach for the Club;
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> (*f*) the Appellant and Ralph J Sazio Limited were not persons dealing at arm's length.

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6. In making the reassessments dated March 23, 1967, the Respondent acted upon the further alternative assumption that the Appellant, through a series of contracts or other arrangements by which he has caused to be paid to Ralph J. Sazio Limited the remuneration for his services as a football coach, has in fact transferred or assigned to Ralph J. Sazio Limited, a person with whom the Appellant was not dealing at arm's length the right to amounts (viz. $20,143.30 and $22,143.30) that would, if the right thereto had not been so transferred or assigned, be included in computing the Appellant's income for 1964 and 1965 because the amounts would have been received or receivable by him in respect of those years and that accordingly the said amounts should be included in computing the Appellant's income for 1964 and 1965 by virtue of section 23 of the *Income Tax Act*.

7. The Respondent further says that in any event the said sums of $20,143 30 and $22,143 30 were amounts to which the Appellant was at all times beneficially entitled; that Ralph J. Sazio Limited was a mere puppet of the Appellant and that the said sums were received by it as nominee, agent or trustee for the Appellant; that the said sums were amounts of which the Appellant was at all times entitled to enforce payment. Accordingly, they were income of the Appellant for his 1964 and 1965 taxation years.

Counsel for the Minister in his argument submitted that the appellant was actually an employee of the football club and that the moneys here in dispute which were received by the company represented payment for the appellant's personal service to the club and that those payments were assigned or transferred to the company or that they were received by the company as the appellant's nominee or agent.

He further submitted that the agreements between the appellant and the company and between the company and the club were not valid business transactions. He also submitted that neither the appellant nor the club heeded certain of the provisions of the agreements except with respect to the payments here in dispute and accordingly suggested that the agreements should be disregarded as establishing the relationship of the parties thereto or as characterizing the moneys paid thereunder.

One of the provisions in the agreements to which counsel for the Minister made reference was that the company should not engage in any other business or occupation than that of supplying football coaching services to the club, or permit its officers, directors or servants to do so, without the consent in writing of the majority of the directors of the club.

The appellant readily admitted that the company did not obtain the consent in writing as contemplated by the provision in question but stated that the club, and all its directors were fully aware of the other activities engaged in by the company and were all agreeable thereto as well as that such tacit understanding had been reached prior to the execution of the contracts and that it continued throughout the currency thereof. There is no doubt in my mind that the parties mutually agreed to waive express and strict literal compliance with this particular provision, and that the club and its directors did not consider the other activities of the company as detrimental to the club's interests and accordingly agreed thereto, even though they did not do so in writing.

The other provision to which counsel for the Minister referred was one by which the club undertook to reimburse the company for travelling and similar expenses incurred by the company, its officers or servants on behalf of the club. There were instances where relatively insignificant amounts were expended by the appellant from his own funds for entertaining a prospective player at dinner and like expenditures for which the appellant was reimbursed directly by the club rather than charging those amounts to the company and the company being reimbursed by the club. However the appellant testified that all substantial expenditures were advanced to him by the company and reimbursed to the company by the club.

It is my view and assessment of the evidence in these foregoing respects that while there may have been these minor breaches of a technical nature which were countenanced by the parties, nevertheless the agreements were otherwise scrupulously adhered to by the parties.

There is no doubt whatsoever that the company is a properly constituted legal entity and that the company could legitimately carry on the objects for which it was incorporated. Any person rendering services may incorporate a company to render those services provided there is no prohibition of those services being performed by a corporation rather than a natural person.

An example of such a prohibition occurred in *Kindree v. M.N.R.*[1] where I expressed the view that the practice of

[1] [1965] 1 Ex. C.R. 305.

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medicine could only be carried on by a natural person which conclusion followed from the general tenor of the *Medical Act* and the code of ethics of the medical profession. I also intimated that a clause in the objects of the company insofar as it purported to authorize the company to conduct the practice of medicine must be ineffective.

In this case there is no such prohibition as was present in the *Kindree* case.

A company, from its very nature, must act through natural persons and there are numerous examples, particularly in the entertainment field, where well known persons have incorporated limited companies to exploit their talents.

In *Crossland (H.M. Inspector of Taxes) v. Hawkins*[2] Donovan L.J. said at page 814:

> The heavy incidence of surtax on large incomes has for some time led artists and others in the world of entertainment to adopt the device of forming a limited company which they control, and giving the company, by means of a service agreement, the right to their services In return the company pays the artist some modest salary The company then hires the artist out to whomsoever requires his services and itself obtains the consideration for them ...

In the next following paragraph he adds:

> All this is perfectly legitimate and indeed, in the case of persons whose high earnings may be short-lived, understandable. . . .

In *C.I.R. v. Peter McIntyre, Ltd.*[3] the respondent company carried on the business of auctioneers. The whole conduct of the business was in the hands of the managing director who held more than half the shares, the remainder being held by near relatives. The question arose as to whether the company could claim an exemption for profits of "any profession the profits of which are dependent mainly on the personal qualifications of the person by whom the profession is carried on".

The Lord President (Clyde) pointed out the profits were earned by the company in the business carried on by it. That business consisted in performing for its clients the services of an auctioneer, valuator and estate agent. Such a business was, in part at least, what is known as a profession. Later he added, "For a professional business may be carried on by a company as well as by an individual;".

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[2] [1961] 2 All E R 812. [3] 12 T C 1006

Accordingly I conclude that, with respect to the football coaching activities, the company was fully competent to engage in those activities in the manner it did and that the agreements entered into between the appellant and the company and the club were *bona fide* commercial transactions all in furtherance of the company's legitimate objects and that they govern and determine the relationship between the parties.

Here the appellant and his company are two separate entities. In my view this is not a matter of form but rather a matter of substance and reality. Both the appellant and the company could sue and be sued in its own right and indeed there is nothing to prevent the one from suing the other if need arose.

Ever since the *Salomon* case[4] it has been a well settled principle, which has been jealously maintained, that a company is an entirely different entity from its shareholders. Its assets are not their assets, and its debts are not their debts. It is only upon evidence forbidding any other conclusion can it be held that acts done in the name of the company are not its acts or that profits shown in its accounts do not belong to it. The fact that a company may have been formed to serve the interests of a particular person is not sufficient to establish the relationship of principal and agent between that person and the company. In order to hold otherwise it must be found that the company is a "mere sham, simulacrum or cloak".

It is my view that the evidence in the present appeals is conclusive that such is not the case. It must also be borne in mind that the company engaged in a variety of activities other than supplying the football coaching services of the appellant and I can see no logical reason for segregating the football coaching services from those other activities.

It follows that the appeals are allowed with costs.

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[4] [1897] A C. 22