
CANADA / JUDGMENT

Pallot v. Pallot

2010 BCSC 1146

COURT

Supreme Court of British Columbia

DECIDED

12 August 2010

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2010 BCSC 1146 Pallot v. Pallot

IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation:

Pallot v. Pallot,

2010 BCSC 1146

Date: 20100812

Docket: 0935698

Registry: Prince George

Between:

Shelley Barbara Pallot

Plaintiff

And

Christopher Bruce Pallot

Defendant

Before: The Honourable Mr. Justice Chamberlist

Reasons for Judgment

In Chambers

Counsel for the plaintiff:

D.W. Lindsay

Counsel for the defendant:

F. Stevens-Guille

Place and Date of Trial/Hearing:

Prince George, B.C.

June 30, 2010

Place and Date of Judgment:

Prince George, B.C.

August 12, 2010

INTRODUCTION

- [1] The plaintiff and the defendant commenced cohabitation in or about 1992 and were married September 23, 1995. They separated September 9, 2009.
- [2] In these proceedings the plaintiff has filed her notice of motion dated June 23, 2010 seeking, inter alia:
 - a) An order that the defendant pay to the plaintiff interim retroactive child support from September 2009 for the children of the marriage, being Brianna Emily Pallot, born July 8, 1998 and Jessica Hayley Pallot, born February 7, 2000;
 - b) An order for interim retroactive spousal maintenance from the defendant to the plaintiff from September 2009; and
 - c) Costs.

BACKGROUND

- [3] At the date of hearing, the plaintiff was 43 years of age and the defendant age 40. The defendant is a pharmacist while the plaintiff is a dietician. For many years the defendant worked as a pharmacist with what is known as the Hart Group of Companies. From 1994 to 2006 the owners of the Hart Group of Companies were the founder and James Ewert. The founder died some 5 ½ years previous and the defendant was given the opportunity to acquire an interest in the businesses. At or about the same time, James Ewert's interest in the businesses was valued and he was issued preferred shares with a value of \$1,300,000.
- [4] At the time the preferred shares were issued to James Ewert, it was agreed that the businesses would buy back the James Ewert preferred shares over the years on a basis that was viable for the operations of the companies so that the Pallots' interest and the Ewerts' interest would eventually be equalized. James Ewert's evidence is that he expects some of his preferred shares to be redeemed next year to facilitate the construction of a new home.

- [5] Over the succeeding years and up to the present time changes were made to the corporate structures with James Ewert, his wife or his holding company owning 49%, 50% and 51% respectively of the common shares of the current four companies, and the plaintiff, the defendant and the defendant's holding company owning the other common shares of the companies.
- [6] The plaintiff and the defendant own their home and investments and shareholder's loans from the Hart Group of Companies. Their assets, excluding the shares of the companies, are worth approximately \$1,400,000.
- [7] By agreement, the defendant and Ewert receive the same amount of money from the companies and have done so for the past several years. The salary for the Ewert family and the Pallot family, when the plaintiff and defendant were residing together, was \$143,000. The defendant says this is a comparable salary to the other pharmacists in their employ, although the evidence is that they do pay some pharmacists more on an hourly basis than what their hourly basis has been calculated at. At the present time the entire \$143,000 salary is paid entirely to the defendant.
- [8] Both parties have provided their respective Form 89 property and financial statements.
- [9] Over the months following their separation monies had been paid by the defendant to the plaintiff but, as I understand it, there was no formalization of the amounts of money to be paid until a consent interim order was made the 19th day of April 2010. The year-ends for the companies are January 31st of each year and at that time it was agreed as follows -
- a) That the defendant would pay to the plaintiff the sum of \$4,000 per month as interim child support commencing February 1, 2010 and continuing on the 1st day of each month until 30 days after he had delivered to the plaintiff's solicitor the financial statements for the year ending January 31, 2010 for Hart Drug Mart Ltd., A & B Hardware Ltd. and Home Drug Mart Ltd.
- b) That the defendant would pay to the plaintiff as interim spousal support the sum of \$6,000 per month commencing February 1, 2010 and continuing on the 1st day of each month until 30 days after he had delivered to the plaintiff's solicitor the financial statements for the year ending January 31, 2010 for Hart Drug Mart Ltd., A & B Hardware Ltd. and Home Drug Mart Ltd.
- [10] The financial statements have now been delivered; however, the plaintiff and defendant have been unable to agree on the defendant's actual income for the purposes of the Federal Child Support Guidelines and the Advisory Spousal Support Guidelines.
- [11] At the time of hearing I understand that the defendant had paid to the plaintiff all sums due under the consent order.

- [12] In April 2010 the financial statements were delivered to plaintiff's counsel. As a result this court is called upon to determine, pursuant to the Federal Child Support Guidelines and with the assistance of the Advisory Spousal Support Guidelines, the appropriate amounts for interim child and spousal support.
- [13] The court has the benefit of the report of Margaret McFarlane, LLB, CA, IFA/CBB, BDO Canada, which was included in the evidence before me for this application. It is dated May 27, 2010 and was prepared to provide some assistance to the court in obtaining information required to establish guideline income under the applicable Federal Child Support Guidelines and Advisory Spousal Support Guidelines.

THE POSITIONS OF THE PARTIES

The Plaintiff

- [14] The plaintiff's position is that Ms. McFarlane has done a thorough review of the Hart Group of Companies and bases her analysis as the basis for finding Mr. Pallot's guideline income. Based on that analysis the plaintiff urges me to find that Mr. Pallot's guideline income is as follows:

2007

\$532,233

2008

\$616,510

2009

\$654,278

for a three-year average of \$601,000 per annum.

- [15] In addition, the plaintiff relies on Ms. McFarlane's findings that the retained earnings of the Hart Group of Companies rose from \$597,000 from the start of fiscal year 2008 and the end of fiscal 2010.
- [16] The plaintiff further submits that the declaration of dividends has been solely made by the Hart Group of Companies for the purpose of minimizing taxes to the companies and shareholders overall. As such the plaintiff argues that the declaration of dividends is completely discretionary and not based upon the companies' ability to pay such bonuses or dividends.

- [17] Thus, based on the average income over the three years of \$601,000 per year, the plaintiff submits that the defendant's child maintenance obligation for two children would be \$7,563 per month. Utilizing the Spousal Support Advisory Guidelines and imputing income to Mr. Pallot of \$601,000 and Ms. Pallot of \$45,369 would lead to a range of spousal maintenance of \$12,381 per month at the low end, \$13,720 per month at the mid-range and \$15,059 at the upper end.
- [18] With respect to the retroactivity claim, the plaintiff points to the fact that prior to legal proceedings being commenced, mediation was attempted by the parties, however when mediation failed, these proceedings were commenced on May 28, 2010. The plaintiff points to the fact that from the months of September 2009 through January 2010 Mr. Pallot's payments to Ms. Pallot were in the range of \$5,000 per month, which the plaintiff submits is less than 50% of what Mr. Pallot's obligation for child and spousal support would be even at an income level of \$350,000 per year.

The Defendant

- [19] There are no issues with respect to entitlement to child maintenance or spousal maintenance. There is also no argument with respect to Ms. Pallot's guideline income. She works a total of 21.6 hours per week and her income for 2009, including some income and dividends from Hart Drug Mart Ltd., was \$45,369. Until January 22, 2010 the plaintiff also received an income from Hart Drug Mart Ltd. in the amount of \$500 per month but at the time of hearing that income had been terminated.
- [20] The real issue is Mr. Pallot's guideline income as determined by s. 18 of the Federal Child Support Guidelines.
- [21] The financial statements and income tax returns, including the interests of the defendant in the respective companies, have now been disclosed, with the most recent disclosure being the financial statements for the Hart Group of Companies for the period ending January 31, 2010.
- [22] The defendant's position is that the plaintiff is being adequately maintained by the defendant based on his line 150 income. The defendant maintains that the defendant's salary is \$143,000 per year and that each year the companies' declared bonuses to each couple in the amount needed to reduce the corporate tax rate payable by the corporations. The defence submits that the declaration is made in February or March and the amount is assigned to the shareholders' loan accounts. The defendant's position is that although he draws down on these accounts throughout the year both he and the remaining principal, being Mr. Ewert, are limited on the amount of cash that can be taken from the business by obligations to their bank. Earnings are reinvested in the business. The defendant states that the cash flow for the business is used to run the day-to-day operations and meet required loan payments. It is also submitted by the defendant that maintaining the franchise rights to "Home Hardware" also requires the company keep the retained earnings in the business and

that is how the businesses have been operated for in excess of 15 years.

- [23] James Ewert, in his affidavit, says precisely that and that he does not intend to make a change to these financial arrangements.
- [24] It is interesting to note that the bonus declared for each couple in February 2009 was some \$200,000, while the bonus declared in February 2010 was only some \$50,000.
- [25] In addition to the \$50,000 bonus the Hart Group of Companies pay to the defendant some \$10,000 annually for his vehicle and telephone expenses.

ANALYSIS

- [26] For the purposes of determining income, not only for the interim child support order but also for the interim spousal support order, I propose to utilize the Federal Child Support Guidelines. Section 18 provides as follows:

18.(1) Where a spouse is a shareholder, director or officer of a corporation and the court is of the opinion that the amount of the spouse's annual income as determined under section 16 does not fairly reflect all the money available to the spouse for the payment of child support, the court may consider the situations described in section 17 and determine the spouse's annual income to include

- (a) all or part of the pre-tax income of the corporation, and of any corporation that is related to that corporation, for the most recent taxation year; or
- (b) an amount commensurate with the services that the spouse provided to the corporation, provided that the amount does not exceed the corporation's pre-tax income.

Adjustment to corporation's pre-tax income

- (2) In determining the pre-tax income of a corporation for the purposes of subsection (1), all amounts paid by the corporation as salaries, wages or management fees, or other payments or benefits, to or on behalf of persons with whom the corporation does not deal at arm's length must be added to the pre-tax income, unless the spouse establishes that the payments were reasonable in the circumstances.
- [27] Under this provision, discretion is given to the court to adjust the income of Mr. Pallot to include all or part of the corporation's pre-tax income only where the court is of the opinion that the amount of Mr. Pallot's income as determined under s. 16 does not fairly reflect all the money available to him for child support.

- [28] The key word under s. 18 is the word "available". There is a substantial difference between the company which is wholly owned and directed by the payor parent and one in which he is not the controlling mind (*Kowalewich v. Kowalewich* 2001 BCCA 450). Likewise there is also a difference between a company that generates its income solely from the work of the payor (for example, a medical doctor or a dentist) and a company that operates retail stores such as the companies we are dealing with.
- [29] In *Kowalewich*, supra, Mr. Kowalewich owned and operated an incorporated small business, the extent of which was disputed. At paras. 44 and 45 Madam Justice Huddart, speaking for the court, said this:
- [44] A court's effort to ensure fairness does not require a court to second-guess business decisions nor, as Justice Pitfield so colourfully noted in *S.(L.) [S.(L.) v. P. (E.)* (1997), 32 R.F.L. (4th) 75 (B.C.S.C.) at para. 44, to "place the largest available shovel in the company store". What it does require is that a spouse's allocation of pre-tax corporate income between business and family purposes be assessed for fairness by an impartial tribunal when parents cannot reach agreement on priorities as they would in an intact family and may upon separation under s. 15(2).
- [45] To determine whether "Total income" fairly reflects money available for child support, a court might ask what an objective well-informed parent would make available for child support in the circumstances of a particular business over which the parent exercised control, having regard to the objectives of the Guidelines, the underlying parental obligation to support children in accordance with one's means, and any applicable situation in s. 17.
- [30] Thereafter, the court stated that it was common ground that line 150 of Mr. Kowalewich's T1 general form did not fairly reflect the amount of money available to him for the payment of child support. It must be remembered however that that was a case where the payor exercised control, unlike the case before me.
- [31] The court went on to conclude that monies which are needed to maintain the value of a business as a viable concern will not be available for support payments. At para. 58 the court said:
- [58] It seems to me regard should also be had to the nature of the company's business and any evidence of legitimate calls on its corporate income for the purposes of that business. Justice Drake cautioned about not killing the goose who lays the golden eggs. Monies needed to maintain the value of the business as a viable going concern will not be available for support purposes. . . .
- [32] In this case, when considering availability of income, I have considered Margaret MacFarlane's report where she assigns the pre-tax income of the companies under review in proportion to the shareholdings of the plaintiff and the defendant as a holding company. One issue I have with respect to her report is the inclusion of monies in Hart Drug Mart Ltd. Neither the defendant nor his holding company appears to own any shares in Hart Drug

Mart Ltd. and he does not appear to be a director of that corporation. As such, it appears not to fit within the definition of s. 18 of the Child Support Guidelines.

[33] In addition, I have considered Mr. Pallot's withdrawals from his shareholder's loan account in 2010. In 2010 Mr. Pallot made use of his shareholder's loan account and I conclude the amount used by him thus far in 2010 have represented monies available to him under s. 18(2) of the guidelines. It does not appear that Mr. Ewert questioned the following outflows of money to Mr. Pallot from his shareholder's loan account as follows, and into the future:

- a) To pay the monthly \$10,000 payment for support pursuant to the consent order, February through May, totalling some \$40,000;
- b) To pay instalments on his personal taxes in the amount of \$5,000 monthly, equalling an anticipated \$60,000 for 2010;
- c) To pay his outstanding 2009 taxes of \$17,769; and
- d) To purchase RSP's in early 2010 in the amount of \$21,000,

for an anticipated total for the year 2010 of \$138,769 on a tax-free basis.

[34] For 2010 I am satisfied that this amount can be included as income of the Hart Group of Companies on the basis that it has been shown that Mr. Pallot is able to draw those monies out without any objection by Mr. Ewert.

[35] I recognize the defence position that the shareholder's loan account does not represent income under s. 18(1) of the guidelines but it surely can represent part of the monies available to Mr. Pallot under s. 18(2) of the guidelines. I accept that the shareholder's loan account is an asset and generally something that will be dealt with at the trial of this action when assets are divided. However, in this case, the shareholder loan account is in fact being utilized and treated, essentially, by the defendant as monies available to him. This of course is a common business practice. Having determined that the monies drawn down by Mr. Pallot from his shareholder's loan account should be utilized for monies available on this application can certainly be an issue before the trial judge and which the trial judge will need to take into account when division of matrimonial property takes place. That, of course, is an accounting matter that counsel and their respective accountants can review and determine.

[36] The next issue is whether or not, because of the substantial reduction in the amount of bonus declared at the present time, I should have occasion to look at s. 17 of the Child Support Guidelines which provide as follows:

17.(1) If the court is of the opinion that the determination of a spouse's annual income under section 16 would not be the fairest determination of that income, the court may have regard to the spouse's income over the last three years and determine an amount that is fair and reasonable in light of any pattern of income, fluctuation in income or receipt of a non-recurring amount during those years.

[37] The evidence before me is that the Hart Group of Companies has just recently constructed a new building and I believe I can take judicial notice of the fact that the economy of Prince George, especially at this time of its history, is in a fluctuating mode.

[38] Brenda Benson, the comptroller of the Hart Group of Companies, states this in her affidavit filed June 21, 2010:

12. The past few years have been good years for the operations and the first complete years that the Pallot's and the Ewert's owned the businesses. Since then we have changed operations drastically with the new location and have fallen into somewhat of an unknown area. We are also further indebted to the bank. The total bonus for the year ending January 31, 2010, was \$100,000, with one half being declared for the Defendant. The bonus was determined by assessing what is best for the business in lowering the corporate tax.

13. The cash flow of the business does not allow for the shareholders to withdraw their bonus in its entirety but to keep it reinvested in the business in their shareholders loan. We are also required, by the agreement with our bank, to maintain defined ratios, thus insisting that a good portion of the shareholders' loans are left in the companies.

14. If the Pallots and the Ewerts were to withdraw the retained earnings personally, that would jeopardize the viability of the businesses. The cash flow is used to run the day to day operations and meet the required loan payments.

15. The business must report the hardware business activities to Home Hardware, where the accounts are scrutinized. In order to maintain the franchise rights, Home Hardware requires that the business have a solid financial situation, again requiring that the retained earnings remain in the business.

[39] In *Bell v. Bell* 1999 BCCA 497, the court in deciding the payor's income said this at para. 12:

[12] Turning to the question of the maintenance for the children, it is my view that the learned trial judge erred in fixing Mr. Bell's income at a figure far in excess of what he was earning. The guidelines that apply in this case require a fair fixing of income for this purpose. I think that the amount that the husband actually earns is a far better indicator of what figure should be used for this purpose than is achieved by averaging, particularly in an economy where employment is sometimes scarce and where there can be wide fluctuations.

[Emphasis added.]

[40] In this case I have found the decision of Staychyn J. of the Ontario Superior Court of Justice in *Koester v. Koester*, [2003] O.J. No. 5406, to be extremely helpful. In that case Justice Staychyn set out the following factors for consideration where corporations are involved as they are here, namely:

- a) To what extent is the availability of access to pre-tax corporate income restricted by the ownership structure?
- b) What restrictions on availability are imposed by nature of a corporation's business including the amount of capital equipment required, the nature of the industry in which the company operates, the outlook in terms of expansion or contraction, the level of debt as well as any banking or financing restrictions?
- c) Historical trends and practices of a corporation.

[41] Applying that type of reasoning in this case, I am of the view that it is just and equitable on an interim application to fix Mr. Pallot's current monies available to him as follows:

- a) Line 150 Income: \$143,000
- b) Shareholders' loan utilization \$138,769

TOTAL \$281,769 per annum

[42] Grossing up the shareholder's loan utilization to make it equivalent to income yields \$198,439.67 ($\$138,769 + (\$138,769 \times 43\%[1])$) for a total of \$341,151.

[43] I have decided it to be wrong in principle to impute additional income to Mr. Pallot on an interim application where the drawing down of retained earnings could threaten the growth and survival of the Hart Group of Companies especially where, according to the evidence, James Ewert has a right to call down up to \$1.3 million in priority to Mr. Pallot's call on retained earnings, and he does intend to do that shortly.

[44] Based on the past history, which is provided by Ms. McFarlane's analysis, I can only conclude that the retention of earnings represents a prudent business measure and one which was the business pattern that had been in place for all the time that Mr. Pallot was a shareholder and before the parties' date of separation.

CONCLUSION

[45] Counsel for the plaintiff provided me with a Divorcemate printout based on a payor's income of \$339,151. That is fairly close to the income equivalent that I have fixed here. Based on the Federal Child Support Guidelines I order interim child support be paid to Ms. Pallot for the two children of the marriage in the amount of \$4,370 per month commencing the 1st day of July 2010 and continuing on the first day of each and every month thereafter until further order.

- [46] With respect to the issue of interim spousal support, the Spousal Support Advisory Guidelines indicates a range of \$5,967 monthly on the low end, \$6,794 monthly on the midrange, and \$7,631 on the high end. Given the history of spending provided to me on this application I fix spousal support at \$6,000 per month commencing July 1, 2010 and continuing on the first day of each and every month thereafter until further order.
- [47] With respect to the retroactive claims of the plaintiff, I decline to make the order retroactive. To fund any further monies at this time would require Mr. Pallot to draw down on family assets or seek further permission from Mr. Ewert. Mr. Pallot has, for the past several months, been paying under the consent order approximately what I have ordered for spousal and child support, and before that monies without a court order. Any retroactive payments can best be dealt with by the trial judge after an accounting, if necessary.
- [48] Unless the parties otherwise wish to address the issue of costs, the plaintiff shall have her costs of this application.

" Chamberlist J."

- [1] 43% Income Tax Rate on gross earnings

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Prepared on 27 October 2026 · Esheria