Docket: 2004-1927(IT)G

BETWEEN:

GABRIEL HOULE,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeals heard on May 15, 2006, at Sherbrooke, Quebec.

Before: The Honourable Justice Paul Bédard

Appearances

For the Appellant: The Appellant himself

Counsel for the Respondent: Julie David

JUDGMENT

The appeal from the assessment made under the *Income Tax Act* for the 1998 taxation year is dismissed in accordance with the attached Reasons for Judgment.

The appeals from the assessments made under the *Income Tax Act* for the 1999 and 2000 taxation years are allowed in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Canada, this 9th day of August 2006.

"Paul Bédard"

Bédard J.

Translation certified true
on this 20th day of February 2008.

François Brunet, Revisor

Citation: 2006TCC291
Date: 20060809
Docket: 2004-1927(IT)G

BETWEEN:

GABRIEL HOULE,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

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REASONS FOR JUDGMENT

Bédard J.

[1] The Appellant is challenging reassessments made by the Minister of National Revenue ("the Minister"), using the net worth method, with respect to the years 1998 to 2000 ("the relevant period"). The Minister added $2,761 in unreported income to the Appellant's income for 1998, as well as $50,909 for 1999 and $9,086 for 2000, and imposed a penalty for each of those years under subsection 163(2) of the *Income Tax Act* ("the Act").

[2] The Appellant submits that the Minister erred in computing his income using the net worth method. In this regard, the Appellant submits as follows:

(i) His mother lent him $15,000 in 1999.

(ii) Not all of the loans to 9017-7197 Québec Inc. ("9017") were made by him. Rather, he and his brother Jérôme Houle lent the money on an equal basis.

(iii) He withdrew $9,000 in cash from his safety deposit box in 1999, and $5,000 from the box in 2000.

(iv) The provincial tax amounts included as adjustments in the net worth calculations are erroneous.

Background

[3] During the relevant period, the Appellant was the owner of Bar Salon Chez Hélène Enr. ("Chez Hélène"). The Appellant and his brother Jérôme Houle were also equal co-owners of Pub 17-13 Enr. ("Pub 17-13"). In addition, the Appellant and his brother Jérôme were equal shareholders of 9017-7197 Québec Inc. ("9017").

[4] The Minister used the net worth method to determine the Appellant's unreported income because he had noticed that the Appellant carried out a number of cash transactions and retained few of the supporting documents needed to reconcile the various accounts in the financial statements of his businesses, including the loans allegedly made to 9017.

Preliminary remarks

Burden of proof

[5] Firstly, we must address the burden of proof that the Appellant must meet in his appeals. My colleague Tardif J. had the opportunity to deal with the issue of the burden of proof in a case where, as here, a taxpayer's unreported income had been determined by means of the net worth method.

[6] In *Bastille v. Canada*, Docket 96-4370(IT)G, December 9, 1998, 99 DTC 431, [1999] 4 C.T.C. 2155, Tardif J. wrote as follows at paragraphs 5 *et seq*.

> [5] I think it is important to point out that the burden of proof rests on the appellants, except with respect to the question of the penalties, where the burden of proof is on the respondent.
>
> [6] A NET WORTH assessment can never reflect the kind of mathematical accuracy that is both desired and desirable in tax assessment matters. Generally, there is a certain degree of arbitrariness in the determination of the value of the various elements assessed. The Court must decide whether that arbitrariness is reasonable.
>
> [7] Moreover, use of this method of assessment is not the rule. It is, in a way, an exception for situations where the taxpayer is not in possession of all the

> information, documents and vouchers needed in order to carry out an audit that would be more in accordance with good auditing practice, and most importantly, that would produce a more accurate result.
>
> [8] The bases or foundations of the calculations done in a net worth assessment depend largely on information provided by the taxpayer who is the subject of the audit.
>
> [9] The quality, plausibility and reasonableness of that information therefore take on absolutely fundamental importance.

[7] Another of my colleagues, Bowman T.C.J. (as he then was) made the following remarks in *Ramey v. The Queen*, docket 91-547(IT), April 20, 1993, T.C.J. No. 142 (QL), [1993] 2 C.T.C. 2119, 93 DTC 791:

> I am not unappreciative of the enormous, indeed virtually insuperable, difficulties facing the appellant and his counsel in seeking to challenge net worth assessments of a deceased taxpayer. The net worth method of estimating income is an unsatisfactory and imprecise way of determining a taxpayer's income for the year. It is a blunt instrument of which the Minister must avail himself as a last resort. A net worth assessment involves a comparison of a taxpayer's net worth, i.e. the cost of his assets less his liabilities, at the beginning of a year, with his net worth at the end of the year. To the difference so determined there are added his expenditures in the year. The resulting figure is assumed to be his income unless the taxpayer establishes the contrary. Such assessments may be inaccurate within a range of indeterminate magnitude but unless they are shown to be wrong they stand. It is almost impossible to challenge such assessments piecemeal. The only truly effective way of disputing them is by means of a complete reconstruction of a taxpayer's income for a year. A taxpayer whose business records and method of reporting income are in such a state of disarray that a net worth assessment is required is frequently the author of his or her own misfortunes. . . .

[8] In the instant appeals, Sandrine Nothomb, an auditor with the Canada Customs and Revenue Agency ("the Agency"), and Lucie Bouchard, an appeals officer, testified for the Minister. The Appellant and his brother Jérôme also testified.

[9] In assessing the Appellant's evidence, his failure to call certain witnesses and provide documentary evidence that could have confirmed his assertions must be taken into account. In *Huneault v. The Queen*, 98 DTC 1488, at paragraph 25, my colleague Lamarre J. cited certain remarks made by Sopinka and Lederman in *The Law of Evidence in Civil Cases*, as cited by Sarchuk T.C.J. of our Court in *Enns v. M.N.R.*, Docket APP-1992(IT), February 17, 1987, 87 DTC 208, at page 210:

In *The Law of Evidence in Civil Cases*, by Sopinka and Lederman, the authors comment on the effect of failure to call a witness and I quote:

> In *Blatch v. Archer*, (1774), 1 Cowp. 63, at p. 65, Lord Mansfield stated:
>
> > 'It is certainly a maxim that all evidence is to be weighed according to the proof which it was in the power of one side to have produced, and in the power of the other to have contradicted.'
>
> The application of this maxim has led to a well-recognized rule that the failure of a party or a witness to give evidence, which it was in the power of the party or witness to give and by which the facts might have been elucidated, justifies the court in drawing the inference that the evidence of the party or witness would have been unfavourable to the party to whom the failure was attributed.
>
> *In the case of a plaintiff who has the evidentiary burden of establishing an issue, the effect of such an inference may be that the evidence led will be insufficient to discharge the burden. (Levesque et al. v. Comeau et al. [1970] S.C.R. 1010, (1971), 16 D.L.R. (3d) 425.) (emphasis added)*

Analysis

Loans to 9017

[10] The Minister alleges that the Appellant lent $789, $31,145 and $24,560 to 9017 in 1998, 1999 and 2000, respectively. The Appellant testified that he and his brother Jérôme made these loans on an equal basis because the funds came from the profits of Pub 17-13, which each of them owned on a 50/50 basis. According to the Appellant, all the profits made by Pub 17-13 during the relevant period were invested in 9017 as loans. It should be noted that no documentary evidence was adduced in support of the Appellant's allegations, and that neither 9017 nor Pub 17-13 held books of account that would make it possible to determine the dates on which the loans were made to 9017, the nature of the loans (cash, goods and services paid on behalf of 9017, etc.) or the source thereof. In addition, the Appellant's brother testified that he made the following loans to 9017 and kept a record of those loans (Exhibit A-1):

	Loans from his share of the	Loans made personally

	profits of Pub 17-13	
From 01/04/96 to 30/06/96	$2,081.50	$4,000.00
From 01/07/96 to 30/09/96		$4,453.50
From 01/10/96 to 31/12/96	$9,006.50	
From 01/01/97 to 31/03/97		$3,250.00
From 01/04/94 to 30/06/97		
From 01/07/97 to 30/09/97		$400.00
From 01/10/97 to 31/12/97		
From 01/01/98 to 01/03/98		
From 01/04/98 to 30/06/98	$1,094.00	$2,000.00
From 01/07/98 to 30/09/98	$1,886.50	$1,275.00
From 01/10/98 to 31/12/98	$3,299.00	
From 01/01/99 to 31/03/99	$6,018.50	
From 01/04/99 to 30/06/99	$5,251.00	
From 01/07/99 to 30/09/99	$3,128.00	
From 01/10/99 to 31/12/99	$929.50	$1,200.00
From 01/01/00 to 30/03/00	$1,775.00	
From 01/04/00 to 30/06/00	$8,005.50	
From 01/07/00 to 30/09/00	$4,229.00	
From 01/10/00 to 31/12/00	$4,471.39	$1,100.00

[11] I should emphasize that Appellant's brother's net income was $10,796 in 1997, $19,525 in 1998, $14,523 in 1999 and $11,214 in 2000, and that the Appellant's brother added that the personal funds from which he made the loans to 9017 consisted of personal savings that he had amassed over the course of his 23 years of work, and money that he had borrowed from a friend.

[12] There is no questioning the fact that the Appellant's evidence on this point essentially turns on his testimony. I should reiterate that the Appellant testified that he and his brother Jérôme lent this money in equal amounts and that it came from the profits made by Pub 17-13, a business that they co-owned on a 50/50 basis. It should be noted that, in his testimony, the Appellant did not once state that any part of these loans might have come from a different source. Yet the Appellant's brother testified that he lent 9017 $400, $15,573 and $12,283.50 in its 1998, 1999 and 2000 taxation years, respectively, and that some of the money that he lent came from his savings and from money that he borrowed from a friend. How, then, can the Appellant claim that he and his brother Jérôme lent money to 9017 on an equal basis? The onus was on the appellant to show that the Minister was wrong on this point. The evidence adduced by the Appellant on this point consisted essentially of his testimony, which was contradicted by his brother's testimony. Given this, how can one believe the Appellant's testimony, which was not

supported by adequate documentary evidence or by the testimony of credible witnesses? I hold that the Appellant did not discharge his onus of proof with respect to this point.

Safety deposit box

[13] At the objection stage, the Appellant claimed that he took $9,000 in cash from his safety deposit box on May 19, 1999, and $5,000 in cash from his safety deposit box on July 28, 2000. He told the Minister that he accessed his safety deposit box on May 19, 1999, and on July 28, 2000, and that the cash taken from the box on those occasions consisted of deposits that he had made into the bank accounts of 9017, Pub 17-13 and Chez Hélène. Therefore, he asked the Minister to reduce his net worth difference by that amount. Specifically, the Appellant claimed that the aforementioned cash amounts taken from his safety deposit box consisted in the following amounts that he had deposited:

(i) $2,600, deposited into Chez Hélène's bank account on May 19, 1999. Based on a deposit slip, the Minister had been able to ascertain that this amount had been deposited into that bank account.

(ii) $1,000, deposited into Pub 17-13's bank account on May 19, 1999. Based on a deposit slip, the Minister had been able to ascertain that this amount had been deposited into that bank account.

(iii) $1,000, deposited into the bank account that 9017 held at a branch of the Laurentian Bank on May 19, 1999. The Minister had not received the deposit slip corresponding to this amount from the Appellant or from the bank.

(iv) $750, deposited into Chez Hélène's bank account on May 20, 2000. Based on a deposit slip, the Minister had been able to determine that this amount had been deposited into that bank account.

(v) $1,000, deposited into the bank account that 9017 held at a branch of the Laurentian Bank, on May 20, 1999. The Minister had been unable to obtain the deposit slip corresponding to this amount from the Appellant or the bank concerned.

(vi) $1,600, deposited into the bank account that 9017 held at a branch of the Laurentian Bank, on May 21, 1999. The Minister had been unable

to obtain the deposit slip corresponding to this amount from the Appellant or the bank concerned.

(vii) $400, deposited into a bank account (folio 15221) that the Appellant held at a branch of the National Bank of Canada, on July 28, 2000. Based on a deposit slip, the Minister had been able to ascertain that this amount had been deposited into that bank account.

(viii) $400, deposited into a bank account (folio 49003-4) that the Appellant held at a branch of the Laurentian Bank, on July 28, 2000. Based on a deposit slip, the Minister had been able to ascertain that this amount had been deposited into that bank account.

(ix) $2,600 deposited into Pub 17-13's bank account on July 31, 2000. The Minister had been able to obtain a deposit slip from the Appellant proving that this amount had been deposited into that bank account.

(x) $1,000, deposited into Chez Hélène's bank account on July 31, 2000. The Minister had been unable to obtain the deposit slip corresponding to this amount from the Appellant or the bank concerned.

[14] Ms. Bouchard testified that she agreed to subtract the amounts set out in subparagraphs (i), (ii), (vii) and (viii) above from the net worth totals initially established by the Agency's audit branch. She said that she did so because she thought that it was realistic and plausible that cash amounts thereby deposited could have come from the Appellant's safety deposit box, since the Appellant supplied deposit slips showing that the cash was deposited on the same day that he accessed his safety deposit box. Ms. Bouchard added that she refused to subtract the amounts set out in the other subparagraphs from the net worth totals initially established by the audit branch, either because the Appellant had been unable to support his allegations with deposit slips, or because the cash was not deposited into the bank accounts in question on the same day that the Appellant accessed his safety deposit box, even if, in such cases, the Appellant had produced deposit slips showing that the cash in issue had been deposited into the bank accounts in question a few days after the Appellant had accessed his safety deposit box.

[15] In my opinion, the Minister should have subtracted the amounts set out in subparagraphs (iv) and (ix) above from the net worth totals. As we have seen, Ms. Bouchard did not accept the Appellant's allegations in those instances because the cash was not deposited into the bank accounts in question on the same day that

the Appellant accessed his safety deposit box, even though the Appellant had shown, by means of deposit slips, that cash amounts were deposited a few days after the Appellant accessed his safety deposit box. In my opinion, this short period between the time that the safety deposit box was accessed and the time that the cash was deposited into the bank accounts concerned does not, in and of itself, make the Appellant's claims implausible.

[16] In addition, it is my opinion that the Minister properly did not subtract the amounts set out in subparagraphs (iii), (v), (vi) and (x) above from the net worth totals because the Appellant's allegations in this regard were not supported by deposit slips. The Appellant's evidence before me is no different from the evidence that he submitted to Ms. Bouchard, except that he claimed that he attempted, without success, to obtain from his banker the deposit slips showing that he deposited cash amounts into the bank accounts concerned. Naturally, the Appellant had failed to retain these supporting documents. It seems that certain taxpayers learn nothing from their mistakes. The Appellant knew that he had to retain these supporting documents and keep adequate books of account. Indeed, he had already been assessed for unreported income by means of the net worth method. As I have explained, it is difficult for me to believe the Appellant's testimony when it is not supported by adequate documentary evidence or by the testimony of credible witnesses.

$15,000 loan

[17] The Appellant claims that his mother lent him $15,000 in cash in 1999, and that he repaid his mother on September 24, 2003. It should be noted that no loan contract was offered in evidence, and that the Appellant's mother did not testify. However, the Appellant offered a $15,000 bank draft dated September 24, 2003, payable to Hélène Houle (Exhibit A-4), in evidence. It would have been most interesting to hear the Appellant's mother's testimony on this point. The Appellant was capable of calling her as a witness. The mother's testimony could perhaps have helped clarify certain facts. This omission forces the Court to infer that the evidence of his witness would have been unfavourable to the Appellant. The effect of this inference on the Appellant, who bore the burden of proof as to this point, is that the evidence adduced is insufficient and that he did not discharge his burden of proof.

Income tax refunds

[18] In the net worth calculation attached to the Reply to the Notice of Appeal, the Minister reduced the Appellant's unreported income by $10,276 and $10,827 for the 1999 and 2000 taxation years, respectively, on account of Quebec income tax refunds cashed by the Appellant during the years concerned. The $10,276 refund cashed by the Appellant in the 1999 taxation year was related to the 1998 taxation year, and the $10,827 refund was related to the 1999 taxation year.

[19] The provincial notice of assessment issued on November 22, 1999, in respect of the Appellant's 1998 taxation year, stated as follows:

> [TRANSLATION]
>
> | | |
> |---|---|
> | Income tax | $0.00 |
> | Mandatory QPP contributions | $741.82 |
> | Contribution to the Health Services Fund | $106.74 |
> | Tax credit for child-care expenses | $8,250.00 |
> | Property tax refund | $372.00 |
> | Other credits | $2,502.00 |
> | Interest | $56.79 |

[20] The Appellant argues that if he had not had to contribute to the Québec Pension Plan (QPP) and the Health Services Fund (HSF) in 1999 for the 1998 tax year, he would have cashed an $11,181.05 tax refund with respect to that year, instead of a $10,276 refund, in 1999. Furthermore, he argued that his QPP and HSF contributions were included in his cost of living as initially established by the Minister and that these inclusions were prejudicial to him. Therefore, he asked that his unreported income for 1999 be reduced by $11,181.05, not by $10,276.

[21] The provincial notice of assessment issued on September 18, 2000, in respect of the Appellant's 1999 taxation year, stated as follows:

> [TRANSLATION]
>
> | | |
> |---|---|
> | Income tax | $0.00 |
> | Mandatory QPP contributions | $741.82 |
> | Contributions to the Health Services Fund | $106.74 |
> | Tax credit for child-care expenses | $8,250.00 |
> | Property tax refund | $372.00 |
> | Other credits | $2,502.00 |
> | Interest | $56.79 |

[22] The Appellant argues that if he had not had to contribute to the QPP and HSF in 2000 for the 1999 tax year, he would have cashed a $12,059.40 provincial tax refund with respect to that year, instead of a $10,827 refund, in 2000. Further, he argues that his QPP and HSF contributions were included in his cost of living as initially established by the Minister and that these inclusions were prejudicial to him. Therefore, he asks that his unreported income for 2000 be reduced by $12,059.40, not by $10,827.

[23] In addition, Ms. Bouchard's testimony, and her Report on Objection (Exhibit I-20, page 4), show that the following QPP and HSF contributions by the Appellant were included in his cost of living:

	1998	1999	2000
QPP	$26.62	$741.82	$1,114.05
HSF	$147.82	$106.74	$117.96

[24] In her testimony, Ms. Bouchard admitted that the QPP and HSF contributions initially added to the Appellant's personal expenses for each of the years in the relevant period were the contributions stated in the Appellant's T1 income tax returns for each of those years, even though the contributions had been paid by the Appellant in the subsequent year. Ms. Bouchard acknowledged that the Minister erred in failing initially to use cash accounting in this regard. Based on Ms. Bouchard's testimony, and her Report on Objection (Exhibit I-20), I am satisfied that she corrected the error, firstly by subtracting from the Appellant's cost of living the QPP and HSF contributions that had initially been added for each year of the relevant period, and secondly by adding, to that cost of living, the QPP and HSF contributions that the Appellant actually paid in each of those years.

[25] In my opinion, the evidence shows that the Minister did not err in reducing the Appellant's unreported income from a given year within the relevant period by the income tax refunds actually cashed by the Appellant in that given year, and in adding, to the Appellant's personal expenses in a given year within the relevant period, the contributions that the Appellant actually made in that year. In my opinion, if I added the QPP and HSF amounts that the Appellant actually paid in a given year within the relevant period to the tax refunds cashed by the Appellant in that year, this would have the effect of cancelling the amounts added to the Appellant's personal expenses in that year.

Penalties

[26] I must also consider the penalties that were imposed under subsection 163(2) of the Act. With respect to this issue, the onus is on the Respondent to prove that a penalty must be imposed. In *Venne v. Canada (Minister of National Revenue - M.N.R.)*, [1984] F.C.J. No. 314, Strayer J. discussed the degree of negligence that is required in order for penalties to be imposed. Gross negligence must be interpreted to mean negligence tantamount to intentional acting — recklessness as to whether the Act is complied with. In the case at bar, even after the conceded reductions, the unreported income for the years 1999, 1999 and 2000 is high in comparison with what was reported. The Appellant was aware of his obligation to report all his income. The Appellant is a knowledgeable businessperson. In my opinion, he deliberately failed to keep adequate books of account so that the tax authorities would be confused. In view of these facts, and of the fact that the Appellant repeatedly failed to report all his income, I hold that the Appellant showed the degree of negligence required to warrant the imposition of the penalties for the three years in issue.

Conclusion

[27] Consequently, the Appeal from the assessment in respect of the 1998 taxation year is dismissed, and the appeals from the assessments in respect of the 1999 and 2000 taxation years are allowed to the extent that the Appellant's unreported income should be reduced by $750 for the year 1999 and by $2,600 for the year 2000.[1]

[28] In all other respects, the appeals are dismissed.

Signed at Ottawa, Canada, this 9th day of August 2006.

"Paul Bédard"

Bédard J.

Translation certified true

[1] See paragraph 12 of these Reasons for Judgment.

on this 20th day of February 2008.

François Brunet, Revisor

CITATION:	2006TCC291
COURT FILE NO.:	2004-1927(IT)G
STYLE OF CAUSE :	GABRIEL HOULE v. HER MAJESTY THE QUEEN
PLACE OF HEARING:	Sherbrooke, Quebec
DATE OF HEARING:	May 15, 2006
REASONS FOR JUDGMENT BY:	The Honourable Justice Paul Bédard
DATE OF JUDGMENT:	August 9, 2006

APPEARANCES:

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For the Respondent:	Julie David

COUNSEL OF RECORD:

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Firm:	

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