Docket: 2005-1871(IT)G

BETWEEN:

GISÈLE MARCEAU DUMAIS,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on April 10, 2007, at Quebec City, Quebec.

Before: The Honourable Justice Lucie Lamarre

Appearances:

Counsel for the Appellant:	André Lareau
Counsel for the Respondent:	Claude Lamoureux

JUDGMENT

The appeal from the assessment under the *Income Tax Act* for the 2000 taxation year is dismissed with costs.

Signed at Ottawa, Canada, this 22nd day of May 2007.

"Lucie Lamarre"

Lamarre J.

Translation certified true
on this 8th day of February 2008.

Erich Klein, Revisor

Citation: 2007TCC297
Date: 20070522
Docket: 2005-1871(IT)G

BETWEEN:

GISÈLE MARCEAU DUMAIS,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

REASONS FOR JUDGMENT

Lamarre J.

[1] The appellant is appealing from an assessment that pertains to the 2000 taxation year and is based on subsection 15(1) of the *Income Tax Act* (the "Act"). The assessment taxed the appellant on a $42,000 benefit and imposed a penalty under subsection 163(2) of the Act.

[2] The appellant is the sole shareholder and director of Ceaumais Inc. ("Ceaumais"), a corporation whose financial and fiscal year-end is January 31. On July 11, 2000, Ceaumais bought a building from the Caisse populaire Desjardins. The building, located at 1540 Cadillac in Quebec City, had been put up for sale for non-payment of $66,000 in hypothec instalments. On August 9, 2000, Ceaumais resold the building to the appellant by notarial deed; the price stipulated in the contract was $132,000, of which $90,000 was paid on the same day by means of a hypothecary loan obtained by the appellant, and the balance of $42,000 was the [TRANSLATION] "repayment of advances made by the purchaser to the seller prior to this date, and in respect of which full and final release is granted" (see deed of sale, Exhibit I-2, Tab 18, page 3).

[3] However, in Ceaumais's financial statements for the fiscal year ended January 31, 2000, a balance of $22,522.82 is shown for the item [TRANSLATION] "owing to director" under liabilities on the balance sheet. For the fiscal year ended January 31, 2001, this amount not only is not reduced, but has increased to $26,022.30 (Exhibit I-1, Tab 6).

[4] For the fiscal year ended January 31, 2002, there is no longer an "owing to director" item under liabilities. Instead, there is a [TRANSLATION] "owing to a shareholder" item of $27,043, which increases to $37,371 for the fiscal year ended January 31, 2003 (Exhibit I-1, Tab 10). At January 31, 2004, that amount has risen to $41,401 (Exhibit I-1, Tab 12).

[5] Thus, it can be seen from Ceaumais's closing balance sheets for the year ended January 31, 2001, and for subsequent years, that the appellant had granted no release to Ceaumais.

[6] The appellant now acknowledges that she could not release Ceaumais with regard to $42,000 as consideration in respect of the purchase of the property because, on the purchase date, Ceaumais owed the appellant an amount that was, at most, between $22,522.82 (at January 31, 2000) and $26,022.30 (at January 31, 2001). However, the appellant claims to have released Ceaumais with respect to the balance owed to the director at the time that the property was purchased, even though this release is not reflected in the financial statements. If she had actually done so, the "owing to director" item should have been reduced to nil, so that Ceaumais would no longer have owed anything to the appellant.

[7] The appellant says that she does not understand why the financial statements do not reflect such a state of affairs. She says that she always had her accounting done by a certain Gaston Paradis, C.M.A. However, in late 2000, following the death of his wife, Mr. Paradis notified the appellant that he would no longer be looking after either her accounting or the filing of her income tax returns. This caught the appellant off guard, and she asked the Métropolitain group, the equivalent of H&R Block, to do her personal income tax return for the year 2000. Having identified an error (with respect to a withdrawal from her registered retirement savings plan) in the calculation of her investment income and being unable to contact the accountant who had prepared her return, she simply did not file her 2000 tax return. She then tried to recover her documents, which were only given back to her the following year. In the meantime, she entrusted the preparation of Ceaumais's income tax return to one Mr. Turmel. Mr. Turmel prepared the financial statements for the period ended

January 31, 2001, without making any reference therein to the transaction involving the sale of the Cadillac Street building to the appellant. Thus, no capital gain was reported by Ceaumais on the sale of the building, and the financial statements show nothing in that regard. During the audit by the Canada Revenue Agency (CRA), the tax auditor, Sandra Sirois, contacted Mr. Turmel. He told her that he was not made aware of the transaction in question.

[8] In 2002, the appellant finally recovered her documents from Métropolitain, and retained another accountant, Mr. Montpetit, to prepare both the personal and corporate income tax returns. So, on April 29, 2002, Mr. Montpetit finally filed the appellant's 2000 income tax return. In it, he reported a rental loss of $10,478.65 on the Cadillac Street building (Exhibit I-2, Tab 13). No reference to the release with respect to the "owing to director" item was made in Ceaumais's financial statements for the fiscal year ended January 31, 2002, or for subsequent years. Ms. Sirois spoke to Mr. Montpetit in the course of her audit, and, though he was in possession of the notarial deed, he made no change to the financial statements.

[9] Neither Mr. Montpetit nor Mr. Turmel was at the hearing to explain the lack of any reference in the financial statements to the transaction involving the Cadillac Street building.

[10] Jean-François Dumais, the appellant's son, who helps his mother maintain her rental buildings, said that the confusion created when his mother's accountant, Mr. Paradis, withdrew is probably what caused the mistakes. He said that the notarial need was probably included in his mother's personal file, which was only recovered in 2002. This would explain why Mr. Turmel would not have been aware of the transaction. The appellant, for her part, contented herself with saying that she did not understand accounting and that she believed that the advances that she had made to Ceaumais were offset by Ceaumais's transfer of the property to her.

[11] Counsel for the appellant submits that, pursuant to subsection 15(2.6) of the Act, the relevant date for the purpose of analyzing Ceaumais's final debt owing to the appellant is January 31, 2002 (at which time the debt was $27,043). He submits that a part of the appellant's $42,000 liability to Ceaumais was set off, by operation of law, against the $27,043 that Ceaumais owed the appellant. He argues that set-off took place by operation of law under articles 1672 and 1673 of the *Civil Code of Québec* (C.C.Q.). And since set-off is a form of payment, he says the appellant's debt to Ceaumais was extinguished, at least up to the amount of $27,043, pursuant to article 1671 C.C.Q. Thus, he submits, there was a balance owing by the

appellant to Ceaumais of $14,957 ($42,000 - $27,043 = $14,957) (see Exhibit A-1), and that this should be taxed as a benefit in the appellant's hands under subsection 15(1) of the Act.

[12] Counsel for the appellant submits, moreover, that, even though the parties failed to correct the financial statements in order to specify that the appellant had released Ceaumais with respect to her claim against it following this set-off by operation of law, this failure in no way means that the parties renounced the application of the set-off.

[13] Counsel for the respondent does not dispute the fact that a part of the debt may have been set off. He argues, rather, that the failure to have this set-off reflected in the accounting entries constitutes the taxable benefit. Indeed, not only was Ceaumais's liability to the appellant not struck from the financial statements, but, on the contrary, it increased from year to year.

[14] After analyzing the evidence, I find that the appellant did indeed receive a $42,000 benefit from the August 2000 transaction in which Ceaumais assigned to her the Cadillac Street building worth $132,000. Even if, as the appellant's counsel argued, there was set-off by operation of law with respect to an amount of $27,043, the evidence clearly shows that Ceaumais never accounted for it in its financial statements. At January 31, 2001, Ceaumais still owed the appellant $26,022.30, and the debt increased from year to year, reaching $41,401 at January 31, 2004.

[15] Even if the initial intent was to effect a set-off, it appears to me that this set-off was renounced.[1] Indeed, if it was by mistake that the financial statements were not corrected, this mistake continued to be made over the years and was never subsequently corrected. Neither Mr. Montpetit (according to the testimony of Ms. Sirois, the CRA auditor), nor the appellant, nor the appellant's son suggested that this situation be rectified. As for Mr. Turmel, he was not even made aware of the transaction. Mr. Montpetit, on the other hand, must have been aware of it, because, according to Ms. Sirois, he had the notarial deed in his possession, and, moreover, claimed a rental loss on the building in the appellant's income tax return.

[16] In *Smith v. Canada*, [1999] F.C.J. No. 1605 (C.A.) (QL), the following is stated at paragraph 5:

---

[1] Renunciation of set-off can be express or tacit (see Pineau, Burman & Gaudet, *Théorie des obligations*, 3d ed. (Montréal: Thémis), at page 525, paragraph 355, cited by counsel for the appellant.

> 5 The issue of whether or not a benefit was conferred, and whether there was a genuine bookkeeping error are questions of fact. The Tax Court Judge made findings based on the evidence before him that the appellant did receive a benefit.

[17] The situation in the case at bar is different from that in *Canada v. Franklin.*, 2002 FCA 38, cited by the respondent and referred to by counsel for the appellant in his argument. There, the taxpayer used funds of the business that had been paid to him personally by reinvesting them in the business. He received no personal benefit from the funds. Here, Ceaumais's debt to the appellant, which should have been extinguished by the set-off, was never struck from the financial statements. On the contrary, it increased. The appellant undoubtedly received a benefit because the debt, which remains on the books, can still be repaid to her, without any tax consequences, as advances owed to her. In *Chopp v. Canada*, [1997] F.C.J. No. 1551 (QL), at paragraph 4, the Federal Court of Appeal quotes with approval the Tax Court judge's remarks:

> 4 In allowing the taxpayer's appeal, Mogan J.T.C.C. interpreted subsection 15(1) as follows:
>
> > "I think a benefit may be conferred within the meaning of subsection 15(1) without any intent or actual knowledge on the part of the shareholder or the corporation if the circumstances are such that the shareholder or corporation ought to have known that a benefit was conferred and did nothing to reverse the benefit if it was not intended. I am thinking of relative amounts. If there is a genuine bookkeeping error with respect to a particular amount, and that amount is truly significant relative to a corporation's revenue or its expenses or a balance in the shareholder loan account, a court may conclude that the error should have been caught by some person among the corporate employees or shareholders or outside auditors. Shareholders should not be encouraged to see how close they can sail to the wind under subsection 15(1) and then plead relief on the basis of no proven intent or knowledge."

[18] The appellant is the sole shareholder and director of Ceaumais. She managed to detect a mistake in her own tax return for 2000 and that mistake was enough for her to refrain from filing the return within the time fixed by the Act. There were few transactions involving Ceaumais during 2000. The appellant should have verified that the transaction involving the building in question was properly reflected both in the financial statements and in Ceaumais's income tax return. Indeed, no capital gain was reported, and this should have drawn the appellant's

attention. She testified that she had decided to transfer the building so that it would be under her own name in order, among other things, to avoid paying tax on the capital. The appellant is not without business sense, and, in my opinion, she was aware, or at least should have been aware, of the fact that she was receiving a benefit when she took possession of a building worth $132,000 without the amount of the debt to her that was set off being reflected in Ceaumais's financial statements. In my view, the fact that the situation was not remedied thereafter, either in the financial statements or in Ceaumais's income tax return, confirms all the more that this was not simply an error.

[19] I subscribe to the remarks of Linden J.A. in *Friedberg v. Canada*, [1991] F.C.J. No. 1255 (QL):

> In tax law, form matters. A mere subjective intention, here as elsewhere in the tax field, is not by itself sufficient to alter the characterization of a transaction for tax purposes. If a taxpayer arranges his affairs in certain formal ways, enormous tax advantages can be obtained, even though the main reason for these arrangements may be to save tax (see *The Queen* v. *Irving Oil* 91 DTC 5106, *per* Mahoney, J.A.). If a taxpayer fails to take the correct formal steps, however, tax may have to be paid. If this were not so, Revenue Canada and the courts would be engaged in endless exercises to determine the true intentions behind certain transactions. Taxpayers and the Crown would seek to restructure dealings after the fact so as to take advantage of the tax law or to make taxpayers pay tax that they might otherwise not have to pay. While evidence of intention may be used by the Courts on occasion to clarify dealings, it is rarely determinative. In sum, evidence of subjective intention cannot be used to "correct" documents which clearly point in a particular direction.

[20] I am also of the opinion that the appellant displayed gross negligence within the meaning of subsection 163(2) of the Act. She had the ability to detect the error, which, under the circumstances, was quite substantial when one also takes account of the fact that she knew Ceaumais did not owe her $42,000 at the time of the transaction.

[21] The appeal is dismissed with costs.

Signed at Ottawa, Canada, this 22nd day of May 2007.

"Lucie Lamarre"

Lamarre J.

Translation certified true
on this 8th day of February 2008.

Erich Klein, Revisor

CITATION:	2007TCC297
COURT FILE NO.:	2005-1871(IT)G
STYLE OF CAUSE:	GISÈLE MARCEAU DUMAIS v. HER MAJESTY THE QUEEN
PLACE OF HEARING:	Quebec City, Quebec
DATE OF HEARING:	April 10, 2007
REASONS FOR JUDGMENT BY:	The Honourable Justice Lucie Lamarre
DATE OF JUDGMENT:	May 22, 2007

APPEARANCES:

Counsel for the Appellant:	André Lareau
Counsel for the Respondent:	Claude Lamoureux

COUNSEL OF RECORD:

For the Appellant:

Name:	André Lareau
Firm:	Jolicoeur, Lacasse, Geoffrion Jetté & St-Pierre (Quebec City, Quebec)
For the Respondent:	John H. Sims, Q.C. Deputy Attorney General of Canada Ottawa, Canada