Citation: 2007TCC675
Date: 20071214
Docket: 2006-2708(GST)I

BETWEEN:

YVAN DUMONT,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

REASONS FOR JUDGMENT

(Delivered orally from the bench on August 31, 2007,
at Québec, Quebec, and amended for greater clarity and precision.)

Archambault J.

[1] Yvan Dumont is appealing from an assessment made on July 5, 2005, by the Ministère du Revenu du Québec ("the MRQ") for the Minister of National Revenue ("the Minister") under section 323 of the *Excise Tax Act* ("the Act"). The Minister held Mr. Dumont liable, as a director of Les Produits Mark-V Inc. ("Mark-V"), for the net GST that Mark-V failed to remit to the Minister for the period from October 1, 1998, to May 31, 2001 ("the relevant period"). The amount of the assessment is $63,749, but the actual tax amount is $39,770.[1]

[2] The parties agreed that the only questions in issue before this Court are whether the defences set out in subsections 323(3) and 323(5) of the Act were applicable under the circumstances.

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[1] That is, according to the assessment of Mark-V (Exhibit A-2 and Appendix 1 of Exhibit I-4). However, according to the assessment of Mr. Dumont, the total net tax is $40,017 (Exhibit I-1, tab 1, page 2). The $247 discrepancy was not explained.

Time-barred assessments

[3] I will begin by addressing the defence under subsection 323(5) of the Act, which states that an assessment of an amount payable by a director under section 323 shall not be made more than two years after the person has ceased to be a director. The evidence concerning this issue disclosed the following facts. Mark-V was incorporated on November 17, 1982, under Part IA of Quebec's *Companies Act*. It was founded by Yvan Dumont, who was also the sole director.

[4] The parties agreed, and the evidence shows, that during the relevant period, Mr. Dumont was the sole shareholder and director of Mark-V as well as its president. Although the company sent a notice to its suppliers, customers and the MRQ that it would cease doing business on June 1, 2001, the evidence disclosed that certain activities continued after that date. For example, on July 4, 2001, an MRQ auditor contacted Mark-V to notify it that she was commencing an audit. A seizure was made on September 4, 2001 at the request of one of Mark-V's suppliers, and most of the company's assets were apparently sold on September 26, 2001 (Exhibit A-23). The bank account was closed on October 16, 2001. A Ford truck was sold in November 2001.

[5] Later, financial statements dated May 24, 2002 were issued for the fiscal year ended December 31, 2001. They report a deficit of $51,817 and are signed by Mr. Dumont as director (Exhibit A-18, page 4). The balance sheet indicates an amount of $15,334 receivable from the director. A tax return filed on the same day, May 24, 2002, states that the director is Mr. Dumont, and, on it, the question whether the company has ceased to do business is answered in the negative (Exhibit I-1, tab 5, box 29).

[6] The assessment of the tax payable by Mark-V following the audit, most of which was conducted from April to October 2002, was issued on November 22, 2002. On February 17, 2003, Mr. Grondin, a chartered accountant and the company's external auditor, filed a notice of objection to the assessment, acting on the mandate given to him by Mr. Dumont. The Notice of Appeal was filed in the Tax Court of Canada at Mr. Dumont's direction on November 3, 2003, by his counsel in the instant appeal.[2]

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[2] A discontinuance of that appeal, signed by that lawyer on May 12, 2005, was filed on May 20, 2005 (Exhibit A-4).

[7] A notice from Quebec's registrar of businesses ("the Registrar") striking the company off the register was issued on May 6, 2005 under section 5 of the *Act respecting the legal publicity of sole proprietorships, partnerships and legal persons* by reason of a failure to file annual declarations for the years 2003 and 2004 (Exhibit A-24).

[8] The evidence did not show that Mr. Dumont resigned from his position as director of Mark-V. No letter of resignation was adduced in evidence. There is no evidence that a notice was sent to the Registrar concerning Mr. Dumont's resignation or the composition of Mark-V's board of directors, which, in fact, was dissolved on May 6, 2005.

[9] The question that the Court must decide is this: Was the assessment of July 5, 2005, made more than two years after Mr. Dumont ceased to be a director of Mark-V? Essentially, the argument made by counsel for Mr. Dumont is that the assessment was made more than two years after the relevant time, which is June 2001, when the company allegedly ceased to carry on business.

[10] In light of the existing body of jurisprudence, the law on this matter is as follows. According to the Federal Court of Appeal's decision in *Kalef*,[3] this Court must refer to the law under which the corporation was created in order to determine the circumstances under which a duly elected director ceases to be a director of that corporation. In the case at bar, the Quebec *Companies Act* must apply because Mark-V was incorporated under that statute.

[11] The relevant sections were quoted by counsel for the Respondent. Section 123.6 of the *Companies Act* states that certain provisions of Part I apply to companies incorporated under Part IA. Those provisions include section 85, which states that ". . . retiring directors shall continue in office until their successors are elected." There is another section that was not mentioned by the parties but was referred to in *Nagy*,[4] a decision of this Court from 1991, where Judge Dussault cites the provision as justification for the following conclusion:

> . . . The cessation of all business operations by a company does not by itself deprive the directors of any of the powers granted to them by law. In my opinion, it does not as such release them of their obligations and responsibilities either. It is one thing to cease to be a director and quite another to *decide to cease to act* as one following the end of business operations.

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3 [1996] F.C.J. No. 269 (QL).

4 [1991] T.C.J. No. 507 (QL), 91 DTC 993 (French version).

[12] Dussault J. quotes section 123.76 of the *Companies Act,* which states: "Notwithstanding the expiry of his term, a director remains in office until he is re-elected, replaced, or removed."

[13] The following comments of Tremblay J. in *Bergeron* should also be noted:[5]

> [TRANSLATION]
>
> They remain directors until the corporation is dissolved by the government. The latter had the power to create the corporation and it alone, according to the decision of the Quebec Superior Court in 1955 in *Banque provinciale du Canada c. Ross*, at 292, [TRANSLATION] "can terminate it and end its legal existence".
>
> For someone to cease to be a director, he must resign in due form in writing, and this was not done in the instant case.
>
> [Emphasis added.]

[14] In addition, the following comments by Tardif J. in *Plamondon c. La Reine*, 2003 TCC 779, at paragraph 55, are applicable:

> [TRANSLATION]
>
> In *Bonch*[6]. . . the Federal Court of Appeal, reversing the decision below, reiterated that a *de jure* director only ceases to be a director on the day that he has fulfilled the requisite conditions established by the statute governing the incorporation of the company for which he is a director, and that, consequently, the limitation period only begins when the taxpayer has ceased to be a director of the company.
>
> [Emphasis added.]

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5 93 DTC 698, at page 699 (French version).

6 [2002] T.C.J. No. 687 (QL)

[15] Upon applying the relevant rules from the Act as interpreted by the courts, I find that the limitation period commenced only when Mr. Dumont ceased to be a director of Mark-V, and, unfortunately for him, he never resigned. The corporation was in existence until May 6, 2005. The assessment of Mr. Dumont is dated July 5, 2005. Thus, less than two years elapsed between the time that he ceased to be the director of the corporation and the time that the assessment in issue was made. Consequently, the defence in subsection 323(5) of the Act is not applicable under the circumstances.

Due diligence

[16] What remains to be considered is the due diligence defence set out in subsection 323(3). That provision states:

> 323(3) A director of a corporation is not liable for a failure under subsection (1) where the director exercised the degree of care, diligence and skill to prevent the failure that a reasonably prudent person would have exercised in comparable circumstances.
>
> [Emphasis added.]

[17] Thus, the Court must determine whether Mr. Dumont exercised the degree of care, diligence and skill to prevent the failure contemplated in subsection 323(1) of the Act, namely the corporation's failure to pay the net tax required by the Act. The evidence presented to the Court is as follows. Mr. Dumont asserted that he and the corporation always complied with their obligations and behaved very responsibly. They were audited twice: once around 1990, and another time in 1995 or 1996, and in his view, everything was in order. Mr. Dumont said that neither he nor the corporation were assessed for any penalties. He said that he did not steal money from the corporation; he did not pocket anything. While the evidence does not disclose that Mr. Dumont stole from the company, and I do not doubt his good faith on this issue at all, it does show that Mark-V advanced $15,334 to him and that this advance still appears on the company's balance sheet as being payable by him as at December 31, 2001. Consequently, the fact that Mark-V was unable to pay the Minister's assessment is at least partly attributable to the fact that some of the company's money was given to Mr. Dumont and that he did not repay it.

[18] Mr. Dumont also testified that he had no accounting skills. Mark-V hired an accounting technician who used the Simply Accounting software and was responsible for preparing GST and QST returns, making source deductions, filing invoices and performing similar administrative tasks. Mr. Dumont said that the responsibility for filing the returns and paying the net taxes to the Minister rested with this accounting technician, who was supervised by his external accountant, Mr. Grondin, who was assisted in turn by his wife, Ms. Goulet, who also had an accounting degree. However, Mr. Grondin and Ms. Goulet testified that their mandate was limited mainly to producing Mark-V's financial statements and answering any questions that the accounting technician might have. They said that they did not receive the GST returns prior to her filing them.

[19] I share the impression that Mr. Grondin's supervision was much smaller in scope than Mr. Dumont suggests. Mr. Grondin said that that his controls generally consisted of an overall test based on the total sales and the cost of the goods, having regard to the expenses that qualify for input tax credits (ITCs) and the expenses that do not. However, in her testimony, Ms. Goulet revealed that such overall controls were not done until 2002.

[20] There is another contradiction – admittedly a somewhat minor one – in Mr. Dumont's testimony. I asked him where the backup copies of the data processed by the Simply Accounting software could be found, and he said they were with his accountant, an assertion that Mr. Grondin denied. Mr. Grondin had obtained the necessary data when the draft assessment was undertaken.

[21] In addition, contrary to what Mr. Dumont said, he did not always comply with his obligations under the Act. Specifically, the evidence disclosed that no GST returns were filed for the quarters that ended in March and June 2001 and the quarter that included November 2001. Early in 2001, the accounting technician had to be laid off due to the financial problems that Mark-V was experiencing. This meant that the company did not have the benefit of the accounting technician's assistance for the GST returns that had to be filed after the layoff. As a result, the work was not done during that period.

[22] The MRQ's audit also revealed that, throughout the period from October 1, 1997, to May 31, 2001, the reported GST amounts regularly differed from the amounts stated in Mark-V's accounting books (Exhibit I-4). The discrepancies identified by the MRQ's GST/ITC reconciliation totalled $31,132.[7] According to the testimony given by Alain Gauthier of the MRQ, this total represents GST collected but not remitted. After the $1,809 in ITCs is subtracted, the net tax amount is $29,323, which accounts for approximately 75% of the assessment ($29,323 of $39,770). The MRQ's analysis of the financial statements, and, in particular, the company's accounting books, discloses that, as at May 31, 2001, there was a unpaid net tax amount of $29,671.54 (consisting of HST payable (item 2475), plus GST payable (item 2450), minus ITCs ($20,623.38 + $12,224.09 -$3,175.93)).[8]

[23] According to Appendix 1 of Exhibit I-4, the discrepancy identified by the Minister amounted to $29,323 on May 31, 2001, when the period in issue ended. According to Appendix 5 of the same exhibit, that discrepancy was $29,671. This is a difference of $348. By way of verification of the accuracy of the MRQ's calculation of this amount, a similar analysis for the period ended December 31, 2000, discloses that the amount of GST reported was $33,099. The opening balance for account 2450 (GST payable) was $29,029, and the closing balance was $42,444; there was supposedly a payment of $26,608. As for account 2475 (HST payable), the opening balance was $22,354, the closing balance was $16,778, and the payment was $7,012.[9] According to the MRQ's work, the total GST to remit was $43,459,[10] and the discrepancy was $10,360.[11]

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7 See Appendix 1 of Exhibit I-4, which sets out the discrepancies identified during the audit.

8 See Appendix 5 of Exhibit I-4, second sheet.

9 See Exhibit I-4, Appendix 5, fourth sheet, and Exhibit A-29, page 3.

10 $43,459 = ($16,778 + $7,012 − $22,354) + ($42,444 + $28,608 − $29,029).

11 $10,360 = ($43,459 − $33,099). This discrepancy is part of the total of $32,132 in discrepancies referred to above.

[24] Upon examining the accounting book tendered as Exhibit I-6, one does indeed notice that, at the beginning of the period commencing January 1, 2001, there is a balance brought forward of $42,444 for HST (item 2475) and the only payment against this amount payable is $32,050, posted on January 31, 2001. As for the GST payable (item 2450), one can see a $16,778 balance at the beginning of the period commencing January 1, 2001, and that a single payment of $1,048 was made, and posted on January 31, 2001. These two amounts ($42,444 and $16,778) correspond to the opening balance entries made by the MRQ on its work sheets in Appendix 5 for the period ended March 31, 2001 (Exhibit I-4). The two payments, $32,050 and $1,049, were also entered on the work sheets.

[25] It is also intriguing to note that when Mark-V's notice of objection was filed, no reference was made to the problem resulting from the MRQ's GST/ITC reconciliation; rather, the focus was on two other problems that are of relatively minor importance compared with the amount of the assessment, namely $39,770 (Exhibit A-26). Indeed, the discussion was about purchase orders and [TRANSLATION] "delinquent contracts". The calculations related to the GST/ITC reconciliation were not questioned.

[26] Based on the evidence as a whole, I conclude that the Minister has shown, on a balance of probabilities, that Mark-V regularly underestimated the amount of GST collectible in its returns, and thereby contradicted its own accounting entries under accounts 2745 and 2450 in its books.

[27] As I have stated, the question that must be answered is as follows: Did Mr. Dumont act as a reasonably prudent person would have acted to prevent the failure, in this instance, to report the GST that Mark-V was supposed to collect and the ITCs to which it was entitled, or, in other words, the net tax amount? It appears to me that there was a failure within the meaning of the Act because the GST returns do not indicate the amounts that the company collected and recorded in its own accounting books.

[28] In his oral submissions, counsel for Mr. Dumont argued that the Minister had to devote roughly 270 hours of work to his audit, and that there were at least five draft assessments before the amount of $39,770 was arrived at. He also noted that the assessment was initially for $190,000, but was ultimately set at the aforementioned $39,770. It is true that Mr. Grondin, the external accountant, also testified that the audit process was difficult, and that they were in a state of shock when the auditor gave him a draft assessment for such an initially large amount without having gotten back in touch with him or with Mark-V's representatives. He said that he was unable to be of great help at the beginning of the Minister's audit because they were in the very middle of what he called [TRANSLATION] "the April tax rush" and because the auditor was making unreasonable requests for supporting documents that I assume were relevant for ITC purposes.

[29] However, the fact remains that 75% of the tax in the assessment is attributable to GST amounts that were collected but not remitted, and were underestimated in the GST returns. It should be mentioned that Mr. Dumont was not an outside director. He was the sole shareholder, the sole director and the president of Mark-V. He was the person responsible for the operation of this small business.

[30] Under the circumstances, it is reasonable to believe that Mr. Dumont was aware that, from 1997 to 2000, his technician regularly failed to present such cheques, for his signature, as corresponded to the total net GST that he had to remit to the MRQ. It is acknowledged that no GST return was filed for 2001. It is also important to mention that the technician in question did not testify, which meant that it was not possible to determine whether she might, for example, have misled him by telling him that all the GST amounts had been paid to the Minister as required by the Act. I have no such evidence. However, the evidence that I do have shows that Mark-V had access to Simply Accounting software, which could have provided a true picture of the financial situation of the business. In fact, Exhibit I-6 discloses that there were distinct accounts for GST payable and for HST in respect of goods sold in New Brunswick.

[31] The evidence also shows that Mark-V had been experiencing financial troubles for several years. It was explained that this situation resulted from the declining use of carpeting in residential and, presumably, commercial buildings. In any event, reference was made to the great popularity of wood floors at the time, and this is a fact of which judicial notice can certainly be taken. Stiff competition from multinationals was also cited. All of these elements combined to make Mark-V's financial situation difficult. It is therefore entirely plausible that the company decided to use part of the amounts that it collected on account of GST in order to lessen its financial woes, at least temporarily.

[32] It is possible that Mr. Dumont was not aware that the GST payments regularly did not correspond to the amounts in his financial statements. In such an event, I would conclude that there was a flagrant lack of due diligence on the part of the director in question. In my opinion, this is not a case in which the amounts determined by the Minister in his assessment result from a complex legal interpretation, though this might have been the case if the assessment had been limited solely to the problems raised by the purchase orders and the delinquent accounts. Rather, it appears to me that the issue is relatively straightforward. The company correctly entered the GST amounts collected in its accounts. It showed them in its books as GST payable, but the amounts reported were not consistent with those books. It seems to me that if Mr. Dumont had been reasonably prudent, he would have been able to see that, contrary to his initial assertion, the amounts were not properly remitted and he was not complying with his obligations under the Act.

[33] In fact, the existence of an unpaid balance of roughly $30,000 (either $29,323 or $29,671) on May 31, 2001, as it appears from Mark-V's accounting books, shows that the interruption in its operations is what caused the business to cease remitting taxes to the MRQ and to be unable to catch up with the arrears that had accumulated over the years.

[34] In my opinion, the availability of the due diligence defence in subsection 323(3) of the Act to Mr. Dumont has not been shown. Furthermore, it is not appropriate to apply the defence recognized by the case law in relation to the penalty under section 280 of the Act.

[35] For all these reasons, I find that Mr. Dumont's appeal must be dismissed.

Signed at Ottawa, Canada, this 14th day of December 2007.

"Pierre Archambault"

Archambault J.

Translation certified true
on this 13th day of February 2008.

Brian McCordick, Translator

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