

Docket: 2007-3472(IT)G

BETWEEN:

MICHEL CORRIVEAU,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeals heard on November 3, 2008, at Québec, Quebec.

Before: The Honourable Justice François Angers

Appearances:

Counsel for the Appellant: Denys Saindon

Counsel for the Respondent: Michel Lamarre

JUDGMENT

The appeals from the assessments made under the *Income Tax Act* for the 2002, 2003 and 2004 taxation years are allowed in part, and the assessments are referred back to the Minister for reconsideration and reassessment, in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Canada, this 3rd day of February 2009.

“François Angers”

Angers J.

Translation certified true

on this 12 day of May 2009.

François Brunet, Revisor

Citation: 2009 TCC 33
Date: 20090203
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BETWEEN:

MICHEL CORRIVEAU,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

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REASONS FOR JUDGMENT

Angers J.

[1] The Appellant is appealing from assessments made by the Minister of National Revenue (the Minister) with respect to the 2002, 2003 and 2004 taxation years. In reassessing the Appellant, the Minister added, for the taxation years in question, \$24,225, \$67,855 and \$29,539, respectively, to the Appellant's income as unreported business income. The Minister also imposed penalties under subsection 163(2) of the *Income Tax Act* (the Act) for each of the taxation years in question.

[2] During the three taxation years in question, the Appellant operating a taxi business and the income derived from that business represents the Appellant's sole source of income. The Appellant purchased a first taxi licence (no. 88) in 1980 for \$15,000. On August 25, 1999, he purchased another operating licence (no. 36) with a partner from his brother Marcel Corriveau for \$73,000. His brother financed the purchase up to \$50,000 repayable in six years. On April 19, 2001, the Appellant also purchased another taxi permit (no. 58). He paid \$24,140 cash to the seller and the seller financed the balance of \$50,000 by accepting amortized payments over 48 months.

[3] On February 26, 2003, the Appellant sold licence no. 88 for \$86,500. The Appellant had to collect from the purchaser payments of \$1,000 per month over 120 months. On that same date, the Appellant purchased his partner's share, that is, 50% of licence no. 36, by giving him \$7,000 cash and committing to make ten monthly payments of \$500. The Appellant also committed to pay the company's debts. In 2006, the Appellant sold licence no. 58. Hence, in 2002, the Appellant operated his business with two and a half licences. At the beginning of 2003, he sold a licence and purchased his partner's share, and therefore he had two taxi licences in his name in 2003 and 2004.

[4] For the taxation years in question, the Appellant reported the following business income:

	Gross Revenues	Net Income
2002	\$84,677.84	\$13,142.41
2003	\$88,957.79	\$9,585.40
2004	\$94,153.44	\$14,726.19

[5] The Respondent added the income of \$24,225, \$67,855 and \$29,539, respectively, to the Appellant's income for the years in question using the net worth method of computation. According to the auditor, the person to whom the Appellant's file was entrusted in June 2005 was forced to use the net worth method of computation following a review of the accounting records of the business owing to the Appellant's weak accounting controls and the fact that numerous transactions were conducted in cash.

[6] The Appellant had to hire drivers to ensure the operation of the taxi licences he held during the years in question. Once the drivers completed their workweek, the Appellant recorded their gross receipts for the week in notebooks, gave them 36% of that gross revenue and the drivers kept their tips. He kept a notebook for each of his drivers for each of the three taxation years in question. It was possible for him to roughly verify his drivers' income by examining the taximeters and the kilometres travelled. It was also possible for him to verify his drivers' income as approximately 70% of the income from the taxi runs derived from taxi chits submitted by customers. The taxi chits were used by various government departments, by businesses such as garages and certain major companies. Each month, taxi chits so received were submitted to the cooperative that had issued them and, on every 10th day of the following month, the Appellant received his payment by cheque.

[7] The Appellant did not treat his own income as a driver in the same way. In fact, he did not keep any records for himself as a driver. He stated that he worked 30 to 40 hours per week during the years in question. He entered his hours on pieces of paper which he did not keep. He stated however that it would be possible for him to determine his income as a driver considering that the amounts are entered in his quarterly reports on the sales tax and the goods and services tax which he prepared himself and which were necessary to subtract from the amount reported as income what he paid his drivers and that would be his income. The auditor did not accept that approach.

[8] Therefore, the auditor, with the help of the Appellant, prepared a personal expenses sheet to determine the Appellant's cost of living. For certain expenses, the amount provided by the Appellant was used, and for the rest, the amount used corresponds to that determined by Statistics Canada. The Appellant identified four headings where he objected to the amounts used by the auditor for the purposes of the case. Under the heading [TRANSLATION] "Lodging, Electricity and Heat," he stated that he uses wood to heat his home and that he lives alone and, therefore, the amount of \$1,800 should be reduced. The Appellant did not provide any evidence to justify a reduction in costs. Furthermore, the amount used by the auditor is that provided by the Appellant and not that of Statistics Canada.

[9] Under the heading [TRANSLATION] "Transportation," the figures used are those of Statistics Canada. The Appellant stated that his taxi was parked at his door but did not provide any evidence that justified a reduction. Under the headings [TRANSLATION] "Education" and [TRANSLATION] "Gifts," the Appellant argued that there was simply nothing to report and, therefore, the Appellant's annual cost of living, according to him, should be reduced by \$1,292.17 for those two headings for the three years.

[10] The Appellant's cost of living was set at \$14,707.70 for the year 2002, at \$16,956.62 for 2003 and at \$16,275.30 for 2004. The increase is related to the health care and entertainment expenses reported by the Appellant for 2003 and 2004.

[11] The auditor therefore proceeded to determine the cost of the Appellant's assets and his liabilities. He met with the Appellant on November 1, 2005, and subsequently prepared a first draft. The auditor found that the discrepancy between his calculations and those of the Appellant quite significant; therefore, he contacted the Appellant again who told him that he had cash in hand, that is, \$5,000. The draft was accordingly amended and the auditor met the Appellant again with the final draft on

December 19, 2005. The Appellant informed the auditor at the time that he would talk to his accountant.

[12] On January 19, 2006, the auditor received a letter from the Appellant's accountant explaining that the Appellant had understood that the auditor asked him how much money he needed to run the business, to which he answered that he had \$5,000 in hand. Now, It appears that the Appellant, according to his accountant, had \$93,650 in hand in 2001 and that it was money the Appellant had earned since he has been working. Although the figures were amended accordingly, there is still a discrepancy of \$4,223, \$4,286 and \$20,640, respectively, for the years in question between the Appellant's calculations and those of the auditor.

[13] About a month later, the Appellant's accountant informed the auditor that the amount of money the Appellant had in hand in 2003 should be reduced by \$30,000, since that amount represented a loan from the Appellant's brother. That change did not affect the discrepancy calculated by the Appellant's accountant. The Appellant indicated in writing to the auditor where the cash, a total of about \$88,000, came from and which he had obtained over the years. Furthermore, during his cross-examination, the Appellant explained that the actual amount he had in hand was not \$63,650 but rather about fifty thousand dollars, which he kept in his home in cash. These particulars were not taken into account by the auditor, who stuck to his calculations.

[14] The Appellant testified that he was an innkeeper and operated a country bar until the business was sold in 1978 for \$25,000 cash. He submits that he kept that money in addition to the tips he received because, at the time, no one reported their tips, and that, over the years, he has accumulated a nest egg. He stated that he inherited money from his parents in 1991, namely \$9,000 (according to Exhibit I-5), and from two other family members also. According to Exhibit I-5, his inheritance was \$6,500 between 1970 and 1980 and \$3,500 in 1991. Exhibit A-6 was filed as pertaining to the winding up of the estate of the Appellant's mother dated September 16, 1991, and was described as being a deposit slip. In my view, it was a cheque stub and it did not show the name of the beneficiary.

[15] The Appellant testified that, when he purchased his partner's share of licence no. 36 in February 2003, his brother Marcel Corriveau loaned him \$30,000 in three instalments of \$10,000 in consideration of the promissory notes of which he did not adduce copies in evidence. A portion of that money was used to purchase two Honda cars (Exhibit A-7) for the operation of taxi licence nos. 36 and 58. One of those cars was paid for in cash and the other car was paid for in part with the \$6,000 cheque

(Exhibit A-8) and in part in cash. The Appellant did not have to reimburse that money to his brother who passed away in 2004. The only amount he deposited in his bank account was \$6,000, which he used to cover the \$6,000 cheque.

[16] In the Appellant's personal assets for the 2004 taxation year, the auditor entered a \$10,000 investment with Desjardins Securities. The Appellant explained that he had initially loaned that money to his son and that his son reimbursed it in increments. Once the \$10,000 was reimbursed, the Appellant invested that money with Desjardins as his son worked for that institution. On cross-examination, he stated that he had deposited a portion of the money reimbursed by his son and used another portion of the money to pay for operating expenses for his taxi business.

[17] The Appellant's accountant submitted three work sheets during the audit in order to narrow the gaps between his assessment of the Appellant's net worth and that of the Respondent's auditor and for the purpose of taking into consideration the amounts of money the Appellant had in hand, the \$30,000 advanced by his brother, the \$10,000 reimbursed by his son and finally a \$3,000 reduction per year in the Appellant's personal expenses. The final gap, according to the Appellant's accountant, was \$1,223, \$1,286 and \$7,460 for the respective taxation years. According to the accountant, who had already been the owner of a taxi business, it was almost impossible that the calculations of the Respondent's auditor were due to the income earned from the operation of his taxis given that the income from a taxi business is similar from year to year.

[18] There had been an increase in taxi fares in 2003 and in 2005. That increase was approved by the Commission des transports du Québec following public hearings held before three of its members. The reports of the hearings were adduced so as to enable the Court to compare the income reported by the Appellant with the average income that was submitted and analyzed by the Commission in setting the new fares. The analysis of the operating costs took into account fixed costs, variable costs, the salary and benefits drivers earn based on current and proposed fares. The purpose of this exercise, for the Appellant, was to demonstrate that the income and expenses reported by him were average for taxi businesses in Quebec for the three years in question. Working on average 30 to 40 hours per week, the Appellant also worked fewer hours than his drivers.

[19] As for the Respondent's auditor, he testified about a conversation he had with the Appellant regarding the explanations given by his accountant concerning the \$93,650 the Appellant had in hand. The Appellant is said to have told him that he did

not have that money in hand. According to the auditor, when he asked him whether he had put the money elsewhere, the Appellant said no.

[20] The auditor explained that he imposed penalties for each of the years because the Appellant did his own bookkeeping without taking into account his income as a driver and, more particularly, because the gap between the reported income and that established by the net worth method of computation was significant. The auditor acknowledged however that the Appellant's bookkeeping was beyond reproach, except for the source documents with the Appellant's income.

[21] Was the Minister justified in adding \$24,225, \$67,855 and \$29,539 to the Appellant's income as unreported income for the 2002, 2003 and 2004 taxation years, respectively, and in imposing penalties for each of the taxation years in question?

[22] Counsel for the Appellant argues that the income and expenses, as reported by the Appellant, are in the averages established in the report of the Commission des transports on the setting of taxi service fares. He explained the increase in the Appellant's net worth for each year by stating that the Appellant had more than \$60,000 in cash, and that he used that money to offset the his lost income, as was the case for the \$30,000 his brother loaned him and the \$10,000 loan reimbursement, by his son, in 2004. Counsel for the Appellant also argued that a reassessment of the Appellant's cost of living would reduce that item by about \$3,000 per year. The Appellant claims that, in the case at bar, it was inappropriate for the Minister to proceed by the net worth method of computation.

[23] As for counsel for the Respondent, he argues that the evidence offered by the Appellant rests primarily on the Appellant's credibility as he was unable to provide supporting documentation or to support his allegations through testimony. The explanations given by the Appellant for the increase in his net worth are unreliable as he gave several versions of the facts from the audit until the hearing of the case.

[24] The Minister is entitled to conduct an investigation in such manner as deemed necessary if the Minister doubts, for whatever reason, the accuracy of a taxpayer's return. That is what the Federal Court of Appeal stated in *Régent Lacroix v. Her Majesty The Queen*, 2008 FCA 241, at paragraph 18 of the decision. In the case at bar, the auditor in charge of the Appellant's case saw that the Appellant did not keep any personal income records, despite the fact that those kept by his drivers were in order. The auditor also established that the Appellant conducted many cash transactions, considering that taxi services were paid in part in cash and that the Appellant did not report his tips. There were therefore, in the case at bar, very few ways of verifying income. Furthermore, several expenses were paid for in cash. I concede that it is not illegal to be paid in cash or to pay for expenses in cash, except that this approach is risky when having to justify one's income and expenses. In my view, the use, by the auditor, of the net worth method of computation in this case, was warranted.

[25] When this method reveals an increase in the net worth of a taxpayer which cannot be explained by the amount of his or her reported income, the onus is on the taxpayer to demonstrate that the increase is not attributable to a failure on his or her part to report taxable income. In this case, the Appellant, through his accountant, provided us with three different tables representing the computation of his net worth which, although established from the one prepared by the auditor, reflect changes made by the Appellant, that is, the amount of cash he had, namely \$30,000 borrowed from his father, \$10,000 reimbursed by his son and a reduction in his cost of living by about \$3,000 for each of the years in question.

[26] First, I wish to point out that the last table (Exhibit A-12) which represents the sum of the Appellant's explanations still reveals a discrepancy of about \$1,200 for 2002 and 2003 and of \$7,460 for 2004. Furthermore, the decrease in the discrepancy, according to the calculations provided by the Appellant's accountant, rests primarily, as already mentioned, on the hypothesis that the Appellant had \$63,650 in cash at his home in 2001 and that he used that money to offset his lost income or reduce the gap, that is to say, of \$20,000 in 2002 and \$33,659 in 2003. It should also be noted that the Appellant did not challenge the auditor's information as to the total assets of the business or the Appellant's and the business's liabilities for the purposes of his accountant's calculations.

[27] At the time of the audit, the Appellant stated that he had \$5,000 in hand in 2001 and during the three years in question. That amount is indicated in the Appellant's balance sheet table prepared by the auditor. The auditor was then told

that the Appellant thought he had been asked how much money he kept to run the business. The Appellant's accountant offered a first table (Exhibit I-5) according to which the Appellant had \$93,560 in hand in 2001. The accountant explained that it was difficult for the Appellant to disclose to a stranger that he had close to \$100,000 in his "nest egg." About a month later, the Appellant's accountant amended that amount, setting at \$63,500 the amount belonging to the Appellant and adding the \$30,000 borrowed in 2003 from the Appellant's brother (Exhibit I-4). In the third table (Exhibit A-12), the accountant added the \$10,000 from the reimbursement of a loan he made to his son and reduced his cost of living expenses.

[28] At the hearing, the Appellant provided a few explanations justifying the fact that he had cash that he accumulated over the years. However, the explanations given only provided insight as to a portion of the total amount he stated he had in hand and, if I take into consideration the fact that he spent that money in 2002, in 2003 and in 2004, leaving him with only \$1,000 in 2004, he would have had to have spent a portion of it in the years prior to 2001. Not only did the amount of cash he had in hand increase from \$5,000 to \$93,650 before being subsequently reduced to \$63,650, but the Appellant also told the auditor, when the latter asked him a few questions about the \$93,650, that he did not have that money at the time. At the trial, he testified that he only had about fifty thousand dollars in cash at home. At the end of the day, the evidence is hardly reliable and it casts doubt on the accuracy of the amount suggested by the Appellant under that item.

[29] In my view, the same is true of the explanations put forward by the Appellant regarding the money he had received from his brother. He explained that he signed promissory notes to his brother, but none of them were adduced in evidence. He stated that he had purchased cars with that money, but once again those purchases were apparently cash transactions, except for a \$6,000 cheque that was drawn on his bank account in which he deposited the money borrowed from his brother. Proof that the amount had been deposited could possibly have substantiated the Appellant's claims, as would an inventory of the assets of his brother's estate and the estate's waiver on the Appellant's loan repayment.

[30] The Appellant stated that he had invested \$10,000 with Desjardins Securities and that that money was from the reimbursement of a loan made to his son. The terms and conditions of the loan repayment were not provided. All the Appellant said is that that money was used to fund investments and expenses, thus leaving the Court uncertain as to the exact amount of that money. The Appellant's son did not testify.

[31] The only evidence that seems to somewhat support the Appellant's submission and that in part supports his explanations is that his income and expenses were average for the industry according to what was recognized by the Commission des transports du Québec in its decision regarding the setting of taxi service fares. It is therefore possible that the Appellant did not generate the income determined by the Minister from his taxi business.

[32] There is no doubt that the use of the net worth method of computation produces imprecise results. A taxpayer who chooses to operate his or her business without properly maintaining his or her records and without keeping his or her supporting documents to back up cash transactions will have a more difficult time meeting his or her burden of proof. His or her credibility will definitely be put to the test.

[33] In the case at bar, based on the evidence as a whole, I am willing to reduce the Appellant's total cost of living by \$3,000 per year for each of the years in question. I accept the fact that the Appellant leads a relatively sedentary life and that he perhaps did not incur all the expenses determined by the auditor, even though the information concerning those expenses came from the Appellant himself. Still, in that case, they are approximate amounts but I believe a reduction is warranted here.

[34] In my view, a reduction in the business income attributed to the Appellant by the net worth method of computation is also warranted on the simple ground that his income as calculated by the auditor would be far greater than the industry's average calculated by the Commission des transports du Québec. That being said, it is however impossible to determine the amounts that would be appropriate in the circumstances on the basis that the average and amounts are approximate. As for the money the Appellant had in hand, he was unable, at least convincingly, to not only offer an approximate amount but to also show on a balance of probabilities where part of that money came from.

[35] The Appellant and his accountant told the auditor at one point that the Appellant had \$93,650 in hand before backtracking and explaining that part of that amount, that is, \$30,000, was in fact a loan given by the Appellant's brother which he did not have to repay. The Appellant later reduced the amount of \$63,650 to about fifty thousand dollars after having initially told the auditor that he did not have any cash in hand. Those contradictions cast doubt on, and also undermine the Appellant's credibility. Three different reports from the Appellant's accountant were needed to arrive at the result proposed by the Appellant owing to his contradictory statements.

[36] The same is true of the reimbursement of the loan made to his son and which the Appellant subsequently invested. No specific details were provided as to the exact amount of the loan made to his son or the exact amounts of the reimbursement or the date of the payments. The Appellant's son, in my view, could have testified to substantiate those claims. I therefore infer from this that his testimony would not have been helpful to the Appellant.

[37] Taking all these factors into account, I reduce on a strictly arbitrary basis the Appellant's unreported business income by \$10,000 for each of the taxation years in question.

[38] I am also of the view that the Minister has met the burden of proof with respect to the imposition of penalties. Pelletier J.A., in *Lacroix (supra)*, made the following comments with regard to the Minister's burden of proof relating to the imposition of penalties following a net worth assessment:

32 What, then, of the burden of proof on the Minister? How does he discharge this burden? There may be circumstances where the Minister would be able to show direct evidence of the taxpayer's state of mind at the time the tax return was filed. However, in the vast majority of cases, the Minister will be limited to undermining the taxpayer's credibility by either adducing evidence or cross-examining the taxpayer. Insofar as the Tax Court of Canada is satisfied that the taxpayer earned unreported income and did not provide a credible explanation for the discrepancy between his or her reported income and his or her net worth, the Minister has discharged the burden of proof on him within the meaning of subparagraph 152(4)(a)(i) and subsection 162(3).

33 As Justice Létourneau so aptly put it in *Molenaar v. Canada*, 2004 FCA 349, 2004 D.T.C. 6688, at paragraph 4:

4. Once the Ministère establishes on the basis of reliable information that there is a discrepancy, and a substantial one in the case at bar, between a taxpayer's assets and his expenses, and that discrepancy continues to be unexplained and inexplicable, the Ministère has discharged its burden of proof. It is then for the taxpayer to identify the source of his income and show that it is not taxable.

[39] The appeals are allowed in part and the assessments are referred back to the Minister for reconsideration and reassessment on the basis that the Appellant's total cost of living is reduced by \$3,000 for each of the years in question and that the business income is reduced by \$10,000 for each of the taxation years as well. The

penalties are imposed on the amount of the unreported income once the reductions are made. The Respondent will be entitled to 70% of her costs.

Signed at Ottawa, Canada, this 3rd day of February 2009.

“François Angers”

Angers J.

Translation certified true

on this 12st day of May 2009.

François Brunet, Reviser

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