

Docket: 2009-1136(IT)I

BETWEEN:

SEAN FAHEY,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on common evidence with the appeal of *Arlene Fahey* (2009-2443(IT)I) on May 31, 2010, and decision rendered orally from the Bench on June 4, 2010, at St. John's, Newfoundland.

Before: The Honourable Justice Patrick Boyle

Appearances:

Agent for the appellant:

Michael F. Power

Counsel for the respondent:

Jan Jensen

JUDGMENT

The appeal from the reassessment made under the *Income Tax Act* with respect to the appellant's 2005 taxation year is allowed, without costs, and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment in accordance with the Reasons for Judgment attached hereto.

Signed at Ottawa, Canada, this 30th day of July 2010.

"Patrick Boyle"

Boyle J.

Docket: 2009-2443(IT)I

BETWEEN:

ARLENE FAHEY,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on common evidence with the appeal of *Sean Fahey* (2009-1136(IT)I) on May 31, 2010, and decision rendered orally from the Bench on June 4, 2010, at St. John's, Newfoundland.

Before: The Honourable Justice Patrick Boyle

Appearances:

Agent for the appellant:

Michael F. Power

Counsel for the respondent:

Jan Jensen

JUDGMENT

The appeal from the determination and assessment dated August 20, 2007, made under the *Income Tax Act* is allowed, without costs, and the matter is referred back to the Minister of National Revenue for reconsideration, redetermination and reassessment in accordance with the Reasons for Judgment attached hereto.

Signed at Ottawa, Canada, this 30th day of July 2010.

"Patrick Boyle"

Boyle J.

CITATION: 2010 TCC 407

2009-1136(IT)I

2009-2443(IT)I

BETWEEN:

SEAN FAHEY,
ARLENE FAHEY,

Appellants,

and

HER MAJESTY THE QUEEN,

Respondent.

**EDITED VERSION OF TRANSCRIPT
OF REASONS FOR JUDGMENT**

Let the attached edited transcript of the Reasons for Judgment delivered orally from the Bench at St. John's, Newfoundland, on June 4, 2010, be filed. I have edited the transcript (certified by the Court Reporter) for style, clarity and to make minor corrections only. I did not make any substantive change.

Signed at Ottawa, Canada, this 30th day of July 2010.

"Patrick Boyle"

Boyle J.

Citation: 2010 TCC 407
Date: 20100730
Dockets: 2009-1136(IT)I
2009-2443(IT)I

BETWEEN:

SEAN FAHEY,
ARLENE FAHEY,

Appellants,

and

HER MAJESTY THE QUEEN,

Respondent.

EDITED VERSION OF TRANSCRIPT
OF REASONS FOR JUDGMENT

[delivered orally from the Bench at St. John's, Newfoundland, on June 4, 2010]

Boyle J.

[1] These are my oral reasons delivered in the informal appeals of Sean Fahey and Arlene Fahey heard Monday in St. John's. By agreement of the parties, the appeals were heard together on common evidence. It was also agreed that the outcome of Arlene Fahey's appeal was entirely consequential upon the extent of success, if any, of her husband's appeal.

[2] The taxation year in question is 2005. Mr. Fahey was, at the relevant time, a house builder. He built one house at a time. He was the owner, manager, sole director and sole shareholder of House Builders Inc. His house building activities were, according to the evidence, some form of joint venture between him and his company, although the precise details of the arrangement were not entirely clear. Mr. Fahey was able to make a modest living in house building. Prior to 2002 his homes were pre-sold, built on credit and suppliers, trades and subcontractors were paid on closing, with anything left going to Mr. Fahey. These arrangements were not documented, so I do not know how Mr. Fahey received this, whether as salaries, dividends, share of profits, subcontractor or a combination thereof. Neither side put

his tax returns in evidence which may have clarified this; however in the circumstances, nothing turns on this.

[3] In 2002, Mr. Fahey decided to build a house on spec, that is, one that was not pre-sold. He built the house in the Southlands subdivision in the Mount Pearl area of St. John's. This led to some financial difficulties as the house was not sold until 2005 after Mr. Fahey put a considerable amount of his own money into ensuring that the trades and subcontractors got fully paid. After closing, suppliers, trades and subcontractors were paid, but Mr. Fahey was left owed \$49,000.00 by House Builders Inc. which it was unable to repay upon closing and would have to be repaid out of future income from further house building.

[4] There is no dispute that Mr. Fahey advanced the \$49,000.00 amount in question and was not repaid on the closing of the Southlands house. There was real money advanced by him. The respondent does not maintain that there was any overall tax mischief involved in this matter. Nor is there any suggestion that Mr. Fahey improved his position at the expense of other creditors including the Canada Revenue Agency ("CRA"). The respondent's position is simply that, since the amounts were repaid from the house building income of a wholly-owned company of Mr. Fahey's, House Framing Inc., which then amalgamated with House Builders Inc., he embarked upon an unsuccessful loss utilization plan which instead resulted in taxable shareholder loans or benefits being conferred upon him by House Framing Inc.

[5] As mentioned, the evidence was not always entirely clear. The documentation was somewhat scant. The Minister's assumptions did not fill in all the blanks and some were not correct based upon the evidence that came out at trial. The Crown did not end up calling his CRA colleague as a witness.

[6] Having heard and reviewed all of the evidence in this case, I find as follows: Mr. Fahey was a successful, private business owner / manager engaged in residential house building. Financial problems arose with the construction of the Southlands home. The construction of the Southlands home was a form of joint venture between Mr. Fahey and his company, House Builders Inc., upon terms which are not entirely clear. The end result to Mr. Fahey of the Southlands home venture is that he was left with \$49,000.00 invested in and owing to him by House Builders Inc. which it was not immediately able to repay.

[7] Mr. Fahey recognized this would have to be repaid out of the income from further house construction. By this time, Mr. Fahey was also the sole shareholder and

director and owner / manager of House Framing Inc. which was also involved in home construction. As its name suggests, House Framing Inc. was a subcontractor involved primarily in framing houses. This may have also been in a joint venture of some form with Mr. Fahey, although nothing turns on that. Thereafter, Mr. Fahey set out to continue in house building, get himself repaid for his Southlands investment, earn an income and reorganize his two companies into a single house construction enterprise.

[8] Mr. Fahey began to implement his planned reorganization. It was intended that as part of the reorganization his two companies would merge into one. House Builders Inc. did not fully cease to exist or operate although it was dissolved for a brief period for failure to file annual corporate returns. There was no evidence of any liquidation of its business assets such as its tools of the trade. At times, the evidence was confusing as to which company did what, when. There was certainly no evidence that Mr. Fahey intended to walk away from the \$49,000.00 owing to him. The skeletal financial statements of House Builders Inc. did not have a favourable balance sheet, but it must be noted that it did not record its goodwill either. House Builders Inc. had the goodwill associated with Mr. Fahey's reputation and ability as a successful and profitable house builder.

[9] Some of the accounting entries were recorded well after the fact. The one-pager describing the debt owing to Mr. Fahey by House Builders Inc. and how it was to be repaid from the future house building income of House Framing Inc. is, at best, muddled. I suspect it was the source of this continuing tax dispute. This document headed "Agreement" and signed by Mr. Fahey personally, and on behalf of his two companies, sets out several recitals, but does not, in fact, have any operative provisions. Clearly neither the reorganization nor the tax analysis was performed to Bay Street standards, but this is Mr. Fahey, not Mr. Irving or Mr. Sobey.

[10] Mr. Fahey is running a one man house building business best as he can. Average Canadians would refer to him as self-employed. This was certainly not orthodox tax planning or commercial implementation and I am urged by the respondent to ignore the transactions and related entries and let the chips fall where they may with the wrong company paying the debt.

[11] My best interpretation of this totality of the evidence is that a direct transfer of the debt was not properly and effectively done and may not have been intended. Further, the accounting entries regarding the director's loan at the House Framing Inc. level do not correctly reflect what happened. I find Mr. Fahey agreed to treat payments to him by House Framing Inc. as repayments of the amounts House

Builders Inc. owed to him, just as the CRA itself has been doing. Mr. Fahey would not have walked away from his right and ability to be repaid since he was in a position to generate income with his companies. On this basis, I find that House Framing Inc. did not make a loan to Mr. Fahey. Repayments on the loan owing to Mr. Fahey by House Builders Inc. were recorded in the books as payments or advances by House Framing Inc. to him. However, I am satisfied that the best interpretation of all of the evidence is, and I find, that this was a shorthand way of describing and recording the source of the payments being made to Mr. Fahey by House Framing Inc. on behalf of House Builders Inc.

[12] Mr. Fahey and his efforts were the contributing sources to the reorganization as well as to House Framing Inc. earning the income from which he was repaid. On this basis, I find that House Framing Inc. did not confer a benefit on Mr. Fahey either.

[13] The appeal of Mr. Sean Fahey is allowed in full. The parties agree that the result of this is that the appeal of Mrs. Arlene Fahey will also be allowed. In the circumstances, there is not award of costs. Thank you, Mr. Power. You and Mr. Jensen were most helpful. Thank you, Mr. Fahey and I wish you success in sorting out your remaining tax obligations. Thank you, Madam Registrar.

Signed at Ottawa, Canada, this 30th day of July 2010.

"Patrick Boyle"

Boyle J.

CITATION: 2010 TCC 407

COURT FILE NOS.: 2009-1136(IT)I, 2009-2443(IT)I

STYLE OF CAUSE: SEAN FAHEY v. HER MAJESTY THE QUEEN AND ARLENE FAHEY v. HER MAJESTY THE QUEEN

PLACE OF HEARING: St. John's, Newfoundland

DATES OF HEARING: May 31 & June 4, 2010

REASONS FOR JUDGMENT BY: The Honourable Justice Patrick Boyle

DATE OF JUDGMENT: July 30, 2010

APPEARANCES:

Agent for the appellants: Michael F. Power

Counsel for the respondent: Jan Jensen

ALSO PRESENT:

Court Registrar: Paulette Murphy

Court Reporter: Paulette Murphy

COUNSEL OF RECORD:

For the appellants:

Name:

Firm:

For the respondent: Myles J. Kirvan
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