Federal Court of Appeal | Cour d'appel fédérale

Date: 20110811

Dockets: A-261-09
A-262-09

Citation: 2011 FCA 234

CORAM: **NADON J.A.**
EVANS J.A.
LAYDEN-STEVENSON J.A.

BETWEEN:

CLYDE HOUSE

Appellant

and

HER MAJESTY THE QUEEN

Respondent

Heard at St. John's, Newfoundland, on June 1, 2011.

Judgment delivered at Ottawa, Ontario, on August 11, 2011.

REASONS FOR JUDGMENT BY: NADON J.A.

CONCURRED IN BY: EVANS J.A.
LAYDEN-STEVENSON J.A.

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REASONS FOR JUDGMENT

NADON J.A.

[1] Before us are appeals from two decisions of Associate Chief Justice Rossiter (the Associate Chief Justice) of the Tax Court of Canada.

[2] The first of these decisions, wherein the Associate Chief Justice dismissed the appellant's appeals from the Minister of Revenue's (the Minister) reassessments of his 2003 and 2004 taxation years, was rendered on June 19, 2009. I will refer to this decision as the Tax Decision. The only issue under appeal from that decision concerns the appellant's 2003 taxation year. More

particularly, the appeal pertains to the Associate Chief Justice's determination that the Minister was correct in including a sum of $305,000 in the appellant's income for 2003.

[3] The second decision under appeal (2009 TCC 245), also dated June 19, 2009, is one wherein the Associate Chief Justice dismissed a motion brought by the appellant pursuant to Rules 168 and 172 of the *Tax Court of Canada Rules (General Procedures)*, for an order setting aside or varying the Tax Decision.

[4] Because I conclude that the appeal from the Tax Decision should be allowed, we need not decide the issues raised by the second appeal which I would dismiss, but without costs.

[5] I now turn to a brief review of the salient facts.

The Facts

[6] The appellant, Mr. House, is 77 years of age. Around 1954, he left the island portion of Newfoundland and Labrador for Goose Bay, in search of employment. Commencing in 1954, the appellant worked at many things, including piloting small airplanes. In January 1980, he was involved in an airplane crash in which he was severely injured and lost his right foot.

[7] During the course of his years in Goose Bay, the appellant operated a hunting, fishing and air charter business under the name of Hunt River Camps/Air Northland Ltd. (Hunt River), which

he incorporated in the province of Newfoundland and Labrador in 1978. Both the appellant and his wife were shareholders in Hunt River.

[8] Hunt River operated from approximately 1978 to either 1998 or 1999, when its assets were sold. Following the sale of the assets, the appellant and his wife returned to the island portion of the province to retire.

[9] In 2004, Canada Customs and Revenue Agency (CCRA) requested that Hunt River file income tax returns for its 2001, 2002 and 2003 taxation years. The income tax returns were duly filed by Mr. Fred Cole (Mr. Cole), a chartered accountant, retained by the appellant and Hunt River.

[10] The income tax return filed by Mr. Cole for the 2003 taxation year indicated that Hunt River had cashed in a $305,000 investment during that year. This led CCRA to commence an audit of Hunt River and, in due course, CCRA also commenced an audit of the appellant's 2003 taxation year.

[11] On November 19, 2004, Ms. Elaine Ryan Brophy (Ms. Brophy), of the Verification and Enforcement Division of the Newfoundland and Labrador Tax Services Office, wrote to Hunt River advising it that its income tax returns were under review and, for that purpose, certain books and records of the company were necessary for a proper review. More particularly, Ms. Brophy requested the following documents:

1. Summaries, journals or ledgers used to document the investments in the amount of $305,000, and any transfer of these assets, including source documents;
2. Invoices/receipts in connection with any asset purchased/disposed;
3. Business bank account statements, deposit books and cancelled cheques;
4. Copies of accountant's working papers with respect to the completion of the tax returns, including ledgers, journals, adjusting entries, etc; and
5. Personal bank records of the shareholder(s), documenting the source of the funds for the personal investments.

[12] On November 30, 2004, Mr. Cole responded to Ms. Brophy's letter and indicated, *inter alia*,

> There were no transactions during 2002. The amounts shown on the balance sheets are balance forwards from 2001. This company has not been operating since 1999. Because there were no transactions to record, none of the records you request above exist. At the time this company was winding down, in 1999, the company and its shareholders were audited by your agency.
>
> [Emphasis in the original]

[13] With his letter, Mr. Cole provided to Ms. Brophy a schedule and copies of Term Deposit Certificates in the name of the appellant's wife with Labrador Savings and Credit Union (Labrador Credit Union) for the period of November 18, 2000 to November 18, 2002. These documents showed a balance of $652,000 in the appellant's wife's account.

[14] On November 18, 2005, Ms. Brophy wrote to the appellant informing him that unless he submitted additional information or an acceptable explanation, CCRA intended to include an additional amount of $305,000 in his income for the 2003 taxation year.

[15] On December 1, 2005, Mr. Cole responded to Mr. Brophy's letter of November 18, 2005, by providing her with information concerning the shareholders' loan account and with copies of balance sheets from Hunt River's financial statements.

[16] On July 7, 2006, Ms. Brophy wrote to the appellant informing him that CCRA was increasing his income for the 2003 taxation year by $305,000.

[17] The appellant filed a Notice of Objection to the reassessment and, on December 21, 2006, CCRA's Appeals Division informed the appellant that the Minister had confirmed the reassessment. The Notification of Confirmation by the Minister reads, in part, as follows:

> The benefit Hunt River Camps/Air Northland Ltd. conferred on you in 2003 amounted to $305,000. This amount has been included in your income according to subsection 15(1).

[18] In February 2007, the appellant appealed the Minister's Notification of Confirmation by filing a Notice of Appeal with the Tax Court, arguing that the $305,000 had not been withdrawn from Hunt River in 2003. More particularly, the appellant said that a review of Hunt River's 2002 tax return led to the discovery of an accounting error, i.e. that a $305,000 investment account carried on the books against an amount due to shareholders/directors in the sum of $311,251 did not exist. As a result, a general journal entry was recorded to correct the error and an accounting entry was made to debit the investment account in the sum of $305,000 so as to reduce the balance to $0. Further, an offsetting entry was made to charge the shareholders/directors' account with a sum of

$305,000 thereby reducing the current balance of $311,251 to a balance of $6,251. That sum represented the balance due to shareholders/directors.

[19] The Minister filed a Reply to the appellant's Notice of Appeal and, at paragraph 11 thereof, set out, *inter alia*, the following assumptions:

> b) At all relevant times. [Mr. House] was the majority shareholder and an officer of [the Company]…;
>
> …
>
> i) In the 2000, 2001 and 2002 taxation years, [the Company] held a long term investment totalling $305,000;
>
> j) In the 2003 taxation year, [the Company] transferred an investment of $305,000 to [Mr. House];

[20] The trial was held at St. John's, Newfoundland on April 21 and 22, 2009, before the Associate Chief Justice who, on April 22, 2009, delivered oral Reasons dismissing the appellant's appeal without costs.

[21] On June 19, 2009, the Associate Chief Justice signed a Judgment dismissing the appellant's appeals from the reassessments of his 2003 and 2004 taxation years. As I have already indicated, the only issue before us in the appeal from the Tax Decision is whether the Associate Chief Justice made a reviewable error in concluding that appellant had received $305,000 from Hunt River in 2003 as a shareholder's benefit.

The Tax Court Decision

[22] The Associate Chief Justice, at the end of the hearing on April 22, 2009, delivered oral Reasons dismissing the appellant's appeals. After a brief review of the facts, the Associate Chief Justice highlighted the assumptions put forward by the Minister in his Reply to the appellant's appeals of his reassessments. He concluded that part of his Reasons by stating that the issue before him was whether the appellant had received $305,000 in 2003 from Hunt River and, if so, whether that sum constituted a repayment of a shareholder's loan or whether it was a shareholder benefit.

[23] The Associate Chief Justice then stated that the burden of proof "clearly" fell upon the appellant to demonstrate, on a balance of probabilities, that the Minister had erred in regard to his assumptions, adding that the appellant had to "destroy" the Minister's assumptions. This led the Associate Chief Justice to observe that the income tax system in Canada is a voluntary, self-reporting and self-monitoring system premised on the fact that taxpayers have in their possession the information required to make a proper report, adding that the self-monitoring system is a privilege not to be abused by taxpayers. He then referred to a number of cases which discussed what he characterized as the "principle of self-monitoring", including this Court's decision in *Njenga v. R.*, 96 D.T.C. 6593, [1997] 2 C.T.C. 8 (FCA) (*Njenga*), and the Tax Court of Canada decisions in *Redrupp c. R.*, 2004 D.T.C. 3320 (*Redrupp*), and *Scragg v. R.*, 2008 D.T.C. 4511 (*Scragg*), for the proposition that taxpayers should provide all relevant documents in support of their claims.

[24] The Associate Chief Justice then made the following remarks found at page 114 of the transcript of the evidence of April 22, 2009 (Transcript 2) (Appeal Book, Vol. 2, p. 391)

> … This case before me comes down to whether or not the Appellant has discharged the onus of proof in relation to whether or not he received funds, when he received the funds, what he did with them, the consideration for the $305,000, whether or not Hunt River owed him any money and did the Appellant loan Hunt River any money, and whether any money was received by whom and in what capacity shareholders' loan – payment of shareholders' loan or otherwise, and was it all done in some year other than 2003?
>
> [Emphasis added]

[25] The Associate Chief Justice answered the above questions by holding that the appellant had not succeeded in "destroying" the Minister's assumptions. He continued by stating that the quality of the evidence before him was insufficient to support the granting of the appellant's appeal in regard to the Minister's decision to include $305,000 of income in his 2003 taxation year. At pages 116-117 of Transcript 2 (Appeal Book, Vol. 2, pp. 391-392), the Associate Chief Justice opined as follows:

> … The obligation of record-keeping and production is on all taxpayers, not just a few, but all taxpayers regardless of their station in life, rich, poor, educated, uneducated, sophisticated, unsophisticated. Mr. Frederick Cole, should have known better than anyone. He is a chartered accountant. He works in his venue daily. He should have been aware as to what sort of documentation would have been required. All we do know and know for sure is, No. 1, Hunt River in 2003 had a 305-thousand-dollar long-term investment. No. 2, Hunt River post 2000 [clearly a typographical error, and should have read post 2003] did not have a 305-thousand-dollar long-term investment. No. 3, Ms. House had investments in various amounts, none $305,000, between November of 2000 and November of 2002 totalling $652,000. There was no nexus or connection or documentation or otherwise for the $305,000. The explanations provided were simply not sufficient to discharge the burden upon the Appellant. The explanations provided were an assertion at best. I find as a fact based upon the evidence before me that the Appellant did receive a shareholders' benefit of $305,000 in 2003, the amount received by the Appellant in 2003 was not repayment of a shareholders' loan, and that an accounting error may well have been made, but that is not sufficient to find without additional proof to discharge the assumptions that the money was received in 2003 by the Appellant.
>
> [Emphasis added]

[26] The Associate Chief Justice further opined that by producing additional documentation, the appellant might have succeeded in discharging his onus of proof. As a result, he dismissed the appellant's appeal.

The Issue

[27] The only issue in this appeal is whether the Associate Chief Justice erred in finding that the appellant had received a shareholder's benefit of $305,000 in 2003.

Analysis

[28] The matter before us is an appeal from a decision of the Tax Court. Consequently, questions of law are to be reviewed on a standard of correctness, whereas findings of fact on the part of the Judge are to be reviewed on the standard of palpable and overriding error (see: *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235, paragraphs 8 and 10 (*Housen*)). Finally, questions of mixed fact and law, i.e. questions involving the application of a legal standard to a set of facts, are to be reviewed on a standard of palpable and overriding error, unless the question of mixed fact and law contains an extricable question of law (see: *Housen*, paragraphs 33 and 36).

[29] For the reasons that follow, I conclude that the Associate Chief Justice erred in dismissing the appellant's appeal with regard to the Minister's reassessment of his 2003 taxation year and, more particularly, in finding that the appellant had failed to meet his burden of "demolishing" the Minister's assumptions that he had received a sum of $305,000 during that taxation year.

[30] In determining the issue before us, it is important to keep in mind the Supreme Court of Canada's decision in *Hickman Motors Ltd. v. Canada*, [1997] 2 S.C.R. 336 (*Hickman*), where Madam Justice L'Heureux-Dubé enunciated, at paragraphs 92 to 95 of her Reasons, the principles which govern the burden of proof in taxation cases:

1. The burden of proof in taxation cases is that of the balance of probabilities.
2. With regard to the assumptions on which the Minister relies for his assessment, the taxpayer has the initial onus to "demolish" the assumptions.
3. The taxpayer will have met his initial onus when he or she makes a *prima facie* case.
4. Once the taxpayer has established a *prima facie* case, the burden then shifts to the Minister, who must rebut the taxpayer's *prima facie* case by proving, on a balance of probabilities, his assumptions (in this case, that Hunt River held at the end of taxation year 2002 a long-term investment of $305,000, which it transferred to the appellant in 2003).
5. If the Minister fails to adduce satisfactory evidence, the taxpayer will succeed.

[31] More particularly, at paragraphs 92 and 93 of her Reasons in *Hickman*, Madam Justice L'Heureux-Dubé explained in clear terms what onus had to be met by the taxpayer at the initial stage:

> 92. It is trite law that in taxation the standard of proof is the civil balance of probabilities: *Dobieco Ltd. v. Minister of National Revenue*, [1966] S.C.R. 95, and that within balance of probabilities, there can be varying degrees of proof required in order to discharge the onus, depending on the subject matter: *Continental Insurance Co. v. Dalton Cartage Co.*, [1982] 1 S.C.R. 164; *Pallan v. M.N.R.*, 90 D.T.C. 1102 (T.C.C.), at p. 1106. The Minister, in making assessments, proceeds on assumptions (*Bayridge Estates Ltd. v. M.N.R.*, 59 D.T.C. 1098 (Ex. Ct.), at p. 1101) and the initial onus is on the taxpayer to "demolish" the Minister's assumptions in the assessment (*Johnston v. Minister of National Revenue*, [1948] S.C.R. 486; *Kennedy v. M.N.R.*,

> 73 D.T.C. 5359 (F.C.A.), at p. 5361). The initial burden is only to "demolish" the exact assumptions made by the Minister but no more: *First Fund Genesis Corp. v. The Queen*, 90 D.T.C. 6337 (F.C.T.D.), at p. 6340.
>
> 93 This initial onus of "demolishing" the Minister's exact assumptions is met where the appellant makes out at least a *prima facie* case: *Kamin v. M.N.R.*, 93 D.T.C. 62 (T.C.C.); *Goodwin v. M.N.R.*, 82 D.T.C. 1679 (T.R.B.). In the case at bar, the appellant adduced evidence which met not only a prima facie standard, but also, in my view, even a higher one. In my view, the appellant "demolished" the following assumptions as follows: (a) the assumption of "two businesses", by adducing clear evidence of only one business; (b) the assumption of "no income", by adducing clear evidence of income. The law is settled that unchallenged and uncontradicted evidence "demolishes" the Minister's assumptions: see for example *MacIsaac v. M.N.R.*, 74 D.T.C. 6380 (F.C.A.), at p. 6381; *Zink v. M.N.R.*, 87 D.T.C. 652 (T.C.C.)…
>
> [Emphasis added]

[32] In my view, on the evidence before him, the Associate Chief Justice erred in law in concluding that the appellant had not met his burden of "demolishing" the assumptions made by the Minister at paragraphs 11(i) and (j) of his Reply to the Appellant's Notice of Appeal that Hunt River had, at the end of 2002, an investment of $305,000 which it transferred to the appellant in 2003. The Associate Chief Justice confused the appellant's initial onus to "demolish" the Minister's assumptions by adducing evidence that, *prima facie*, supported his position with the overall burden resting on the parties to prove that the investment had or had not been paid to the appellant in 2003.

[33] Underlying the Associate Chief Justice's conclusion is his view that the appellant had failed to adduce evidence of sufficient quality to "support granting the appeal in relation to the $305,000" (Transcript 2, p. 114 / Appeal Book, Vol. 2, p. 389). Specifically, the Associate Chief Justice criticized the appellant and his accountant, Mr. Cole, for not producing relevant documents such as

minute books, general ledgers, cheques, invoices, bank statements, etc. As a result of his view that source documents were required as a matter of law (I will address this issue in detail later in these Reasons), the Associate Chief Justice failed to give any consideration to Mr. Cole's evidence. In other words, I am of the view that the Associate Chief Justice erred in law in failing to consider crucial evidence that was before him.

[34] I now turn to the evidence before us on this record and begin by making a preliminary remark. At the time of the trial, both the appellant and his wife were advanced in age and had difficulty recollecting, with precision, the events that took place between 1999 and 2003. Consequently, the crucial evidence in this case was, in my view, that of their accountant, Mr. Cole.

[35] I begin with the appellant's evidence. The appellant agreed that at one point in time, Hunt River did hold a $305,000 investment. Although he could not remember precisely in what year it had been held, he testified that it had been transferred by Hunt River to his wife, not to him.

[36] The appellant went on to explain that his wife "kept the records" (Transcript of April 21, 2009 (Transcript 1), p. 48 / Appeal Book, Vol. 2, p. 301), i.e. that she kept the records and then sent them on to Mr. Cole. The appellant indicated that he had nothing to do with "… these, this paperwork as such" (*ibid.*) and he made it clear that Mr. Cole handled everything.

[37] The appellant explained that Hunt River sold three camps prior to 2000, for the sum of $500,000 and that it further sold one airplane, also prior to 2000, for the sum of $90,000. The

proceeds from the sale of both the camps and the airplane were placed in Hunt River's account at the Royal Bank. He also explained that he sold two houses prior to leaving Goose Bay for the sum of $200,000, which was also placed "into the company" (Transcript 1, p. 76 / Appeal Book, Vol. 2, p. 308).

[38] When questioned specifically about the investment of $305,000, he indicated that that sum came out of Hunt River's account and went into his wife's account at the Labrador Credit Union. The appellant explained why the $305,000 was transferred to his wife's account at the Labrador Credit Union. His explanation is found at page 26 of Transcript 1, p. 26 (Appeal Book, Vol. 2, , p. 296):

> A. Well, what happened was we were – my wife was with the Labrador Credit Union in Goose Bay. That was a new Credit Union. It – I think it's Eagle River Credit Union now, but at that time it was the Labrador Credit Union. And a company couldn't become a member of that bank. So my wife was a member of that bank, and we were in the process of moving. And so anyway, they offered her seven and a half percent on her money, and so we took the money out of the Royal Bank which was under Hunt River, because we were finished with that, and we put it in her name in the Credit Union, and we got seven and a half percent on our investment in the bank.

[39] I now turn to the evidence of Mrs. Theresa House, the appellant's wife.

[40] Mrs. House testified that she was a shareholder in Hunt River, with one share. She indicated that the $305,000 was taken out of Hunt River and given to her (Transcript 1, p. 207 / Appeal Book, Vol. 2, p. 341). She explained that the money was put in her account at the Labrador Credit Union because "… we were told that we would get fairly good interest" (Transcript 1, p. 210 / Appeal

Book, p. 342). She could not, however, specifically remember cashing out the $305,000. In her opinion, it had been cashed out around 2000, when it was placed in her account at the Labrador Credit Union. She indicated that "I was given the money by my husband, but I don't remember taking it out of the bank" (Transcript 1, p. 224 / Appeal Book, p. 345). She made it clear that neither she nor her husband had good memories, saying that hers was worse than his. At the time of the trial, Mrs. House was almost 76 years of age.

[41] I now turn to Mr. Cole who has been a chartered accountant since 1980 and Hunt River's accountant since 1982.

[42] He was asked questions regarding the filing of Hunt River's tax return for the year 2003 and indicated that he had filed that tax return. He added that there was a request by CCRA for the filing of Hunt River's tax returns for the years 2001, 2002 and 2003. He began by saying that he initially filed returns for 2001 and 2002 only. Then, with respect to the 2003 tax return, he made the following remarks (Transcript 1, p. 92 / Appeal Book, Vol. 2,l p. 312):

> Q. - would you tell us what you did?
> A. Well, I – well, the company had basically been in operative [*sic*] since it sold property called Boarder Beacon, and that sale occurred in 1999. And essentially there were – there wasn't a lot left of the company. It was more or less a shell. So the first thing to do is pull out, you know, the last tax return that was filed and have a look at it. And on that tax return it showed that there was an amount invested at the Royal Bank, and that investment no longer was there.

[43] He was then referred to balance sheet information prepared by Ms. Brophy which showed that Hunt River held a long-term investment of $305,000 at the end of December 2002. He stated that he went looking for that investment so as to determine whether it existed or not. His search led him to the conclusion that the investment did not exist. Hence, he charged the $305,000 to the shareholders' account, i.e. he reduced the amount owing from $311,000 to $6,000 (Transcript 1, pp. 93-95 / Appeal Book, Vol. 2, p. 313).

[44] This finding led him to inform CCRA that there had been no transactions during 2002 for Hunt River, that "… the amounts that were filed for 2002 were amounts carried forward from 2001" (Transcript 1, p. 97 / Appeal Book, Vol. 2, p. 314) and that "… the company had not been operating since 1999" (*ibid.*).

[45] In answer to questions posed by the Associate Chief Justice, Mr. Cole indicated that the $305,000 had initially been placed in an account at the Royal Bank in Hunt River's name, adding that for the 2003 taxation year, he had "… discovered that investment no longer existed in the company's name" (Transcript 1, p. 110 / Appeal Book, Vol. 2, p. 317) and that he had "… reduced the shareholders' account corresponding it" (*ibid.*). He then went on to explain that in the course of his search, he had examined Hunt River's records from 1998-1999 to December 31, 2003, finding that the $305,000 investment no longer existed, which is why he reduced the shareholders' account by $305,000. When asked why he had reduced the shareholders' account by $305,000, he answered as follows (Transcript 1, p. 111 / Appeal Book, Vol. 2, p. 317):

> A. Well the – when I tried to find the investment certificate, I couldn't find it at the Royal Bank, and apparently Mrs. House had it in her name at the Credit Union, so I did – I charged it to her.

[46] In cross-examination, he was asked specific questions concerning the $305,000 investment, in regard to which CCRA took the position that it had been transferred to the appellant in 2003. First, he disagreed with the statement made by counsel for the respondent that "[i]n the 2000, 2001 and 2002 taxation years, Hunt held a long-term investment totalling $305,000" (Transcript 1, p. 117 / Appeal Book, Vol. 2, p. 319). He indicated that the investment had been cashed out in the year 2000 and reiterated his view that the $305,000 investment had been taken out by Mrs. House, adding that he had discovered this information when filing, in 2006, Hunt River's 2003 tax return.

[47] When again questioned by the Associate Chief Justice, Mr. Cole explained that he was satisfied that the $305,000 had been paid to the appellant's wife and that she had bought "additional GICs at the Labrador Credit Union" (Transcript 1, p. 154 / Appeal Book, Vol. 2, p. 328).

[48] The only witness called by the respondent was Ms. Brophy, who explained the basis of the Minister's reassessment of the appellant's 2003 taxation year. At page 164 of Transcript 1 (Appeal Book, Vol. 2, p. 330), she was asked why she assessed a benefit of $305,000 to the appellant. Her answer was as follows:

> A. As I conducted the review and spoke to Mr. House and his presentative [*sic*], Mr. Cole, in conversations I was advised by Mr. Cole that the asset was held by either one of the corporations or one of the individuals. He was unsure at that time. So I requested information to substantiate where exactly the investment was, who the shareholders were, and any general ledgers, bank deposits. There's actually an exhibit in the Book of Exhibits which is an

> initial contact letter where I asked for information pertaining to that transaction.

[49] Ms. Brophy added the following at pages 165-166 of Transcript 1 (Appeal Book, Vol. 2, p. 331:

> A. I spoke with him [Mr. Cole] on a couple of occasions. I initially spoke with him, I think it was October '04, and the file had been postponed for a little bit of time actually because Mr. House was undergoing some medical procedures. So I spoke to Mr. House then and I spoke to him again – or I'm sorry, I spoke to Mr. Cole then, and I spoke to him as well around, I think it was April 13th or 14th of '05, and we spoke about the $305,000 investment again. And basically Mr. Cole made the same statement that the investment does exist, but at that time he didn't know who held the investment, whether it was ECJ Eagle Incorporated, Hunt River Camps, or if it was one of the individuals.
> Q. Okay.
> A. And actually after that, shortly after that, probably in May I discovered that an additional financial statement, the balance sheet, had been filed, the initial assessment for the 2003 taxation year which indicated that $305,000 was no longer on the balance sheet of Hunt River Camps.

[50] Ms. Brophy further explained that she had not received "source documents" from Mr. Cole or the appellant. Later on in her testimony, in response to a question posed by the Associate Chief Justice, she said that she had not been made aware by the appellant or by Mr. Cole, in the course of her audit, that the $305,000 had been paid out in 2000. The following questions and answers appear at Transcript 1, pp. 187-188 (Appeal Book, Vol. 2, p. 336):

> Q. Oh, yes. Okay. Okay, well Mr. Cole in your absence explained that.
> A. Oh, OK.
> Q. Explained that the $305,000 shouldn't be there December 31st, 2003. It should have gone out on December 31st, 2000, because December 31st – by December 31st, 2000, the $305,000 had already left Hunt, Hunt River.
> A. Well, we weren't provided with any information on that end –
> Q. No, no. I realize that, but that's – that was the explanation he gave.
> A. Okay.

[51] On that point, she was questioned by counsel for the respondent and again answered that she had not been made aware, during the course of her audit, that the $305,000 had come out of Hunt River's account in 2000 (Transcript 1, pp. 188 to 190 / Appeal Book, Vol. 2, pp. 336-337), adding that she was also not aware, at the time of the audit, that the entry for December 31, 2003, showing an investment of $305,000, was an error (Transcript 1, pp. 193-194 / Appeal Book, Vol. 2, p. 338).

[52] That, in essence, is the evidence that was before the Associate Chief Justice when he rendered the Tax Decision.

[53] The Associate Chief Justice dealt with that evidence as follows. As I indicated earlier, he concluded that the appellant had not discharged his onus of "demolishing" the Minister's assumptions. He came to this conclusion because, in his view, the evidence was of insufficient quality. The Associate Chief Justice so held because, in effect, the appellant and Mr. Cole had failed to adduce documents such as cancelled cheques, deposit statements, registered retirement savings plan documents, etc. More particularly, with regard to Mr. Cole's evidence, he stated that Mr. Cole, a chartered accountant, "… should have been aware as to what sort of documentation would have been required" (Transcript 2, p. 116 / Appeal Book, Vol. 2, p. 391), adding that "… an accounting error may well have been made, but that is not sufficient to find without additional proof [i.e. source documents] to discharge the assumptions that the money was received in 2003 by the Appellant" (Transcript 2, p. 117 / Appeal Book, Vol. 2, p. 392). In other words, the Associate Chief Justice was

of the view that Mr. Cole's testimony was not sufficient on its own, without corroboration by the production of source documents to "demolish" the Minister's assumptions.

[54] For this view, the Associate Chief Justice relied, *inter alia*, on the statement made by Bowie J. in *Scragg*, that "assertion without proof is simply not sufficient" and on this Court's decision in *Njenga*, where the Court held that all taxpayers had an obligation to keep proper records and to produce them.

[55] Before stating why I conclude that the Associate Chief Justice erred, I should note that he made no credibility findings against Mr. Cole nor, for that matter, did he make credibility findings against the appellant or his wife. To this, I would add, as I indicated earlier, that the evidence of both the appellant and his wife was somewhat confusing because of the difficulty they both obviously had in recollecting events which had taken place almost 10 years before. As to Mr. Cole's evidence, he testified under oath that he had made an error in preparing Hunt River's tax return for 2003 and that he had taken steps to correct that error, explaining why a correction was necessary in the circumstances. Mr. Cole also made it clear that he had no doubt whatsoever that the $305,000 investment was no longer in Hunt River's account at the end of 2002 and that it had been paid out around 2000 when the decision was made to transfer the funds from Hunt River's account at the Royal Bank to Mrs. House's account with the Labrador Credit Union. One further point – Mr. Cole's testimony was neither contradicted nor impeached in any way whatsoever by the respondent.

[56] In considering the question of whether or not a taxpayer must adduce the type of documents which the Associate Chief Justice felt were required, it is important to keep in mind the remarks of Madam Justice L'Heureux-Dubé in *Hickman*, where she states, at paragraph 87, that "[f]urthermore, where the *ITA* [The *Income Tax Act*] does not require supporting documentation, credible oral evidence from a taxpayer is sufficient notwithstanding the absence of records", which led her to state at paragraph 88 that "… the *ITA* does not require that the revenue be shown in the financial statements and, accordingly, since no issue of credibility was raised, the evidence adduced by the appellant is clearly sufficient".

[57] In my view, the Associate Chief Justice made two errors of law. First, he confused the appellant's initial onus to "demolish" the Minister's assumptions with the overall burden resting on the parties to prove their respective cases. Second, he erred in failing to consider Mr. Cole's evidence. Had he considered Mr. Cole's evidence, as he was bound to, he would necessarily have concluded, in my view, that the appellant had made a *prima facie* case "demolishing" the Minister's assumptions. In *Amiante Spec Inc. v. Canada*, 2009 FCA 239, 2009 FCJ No. 603 (QL), our Court, at paragraph 23, explained a *prima facie* case in the following terms:

> **[23]** A *prima facie* case is one "supported by evidence which raises such a degree of probability in its favour that it must be accepted if believed by the Court unless it is rebutted or the contrary is proved. It may be contrasted with conclusive evidence which excludes the possibility of the truth of any other conclusion than the one established by that evidence" (*Stewart v. Canada*, [2000] T.C.J. No. 53, paragraph 23).

[58] I now turn to the Associate Chief Justice's first error. Although he appears to have been aware that the initial burden on the appellant was that of "demolishing" the Minister's assumptions,

he did not, in my view, apply that burden but rather applied that of the overall burden resting on the parties.

[59] After referring, at the outset of his Reasons, to the appellant's burden of demonstrating that the Minister had erred in regard to one or more of his assumptions, adding that the appellant "must destroy the assumption or assumptions by his evidence in presentation of his case", he went on to state that the case before him "… comes down to whether or not the appellant has discharged the onus of proof in relation to whether or not he received funds, when he received the funds, what he did with them, the consideration for the $305,000, etc." (Transcript 2, p. 114 / Appeal Book, Vol. 2, p. 391). He then concluded, after reviewing the evidence and the case law, that the appellant had not "discharged his onus to destroy the assumptions relied upon by the respondent". His conclusion was based on his view that the evidence adduced by the appellant was of poor quality. Finally, he stated that he found as a fact that the appellant had received $305,000 in 2003. In considering the view taken by the Associate Chief Justice with regard to the applicable burden, it is important to remember that, other than the reliance on his assumptions, the Minister adduced no evidence whatsoever to demonstrate that the appellant had received $305,000 in 2003.

[60] With respect, I am unable to conclude that the Associate Chief Justice applied the correct burden of proof in regard to the Minister's assumptions. Rather, I believe that the Associate Chief Justice was looking, not for evidence on the part of the appellant "demolishing" the Minister's assumptions, but for positive evidence that the appellant had not received $305,000 in 2003. As

Madam Justice L'Heureux-Dubé stated in *Hickman*, at paragraph 92, the taxpayer's burden is that of "… "demolishing" the Minister's assumptions but no more".

[61] As stated earlier, the appellant's burden was that of mounting a *prima facie* case "demolishing" the Minister's assumptions. In other words, the appellant's burden was to demonstrate that the Minister's assumptions were incorrect, not to establish that he had not received $305,000 in 2003. On my understanding of the Associate Chief Justice's Reasons, he believed that the appellant had to demonstrate, on a balance of probabilities, that he had not received $305,000 in 2003. In my view, this explains why he was not satisfied with Mr. Cole's oral testimony and required that source documents be produced to establish that the appellant had not received $305,000 in 2003. In particular, it explains why he totally disregarded Mr. Cole's testimony to the effect that his errors had led the Minister to assume that $305,000 had been transferred to the appellant in 2003.

[62] Had the Associate Chief Justice properly understood and applied the correct burden, he would not have been looking for positive evidence establishing that the appellant had not received $305,000 in 2003 but, rather, for evidence establishing that the Minister's assumptions were incorrect. By adducing evidence which explained why the Minister's assumptions could not be right – because the returns on which the Minister had relied in making his assumptions were in error and that these errors had been corrected – the appellant had offered evidence which, unless disbelieved or rebutted, was capable of establishing a *prima facie* case "demolishing" the Minister's assumptions.

[63] It is therefore my opinion that the Associate Chief Justice erred in law in misapprehending the nature of and in not applying the correct burden of proof.

[64] I now turn to the Associate Chief Justice's second error. In my view, he erred in law in failing to consider Mr. Cole's testimony. This error was caused by the mistaken view that Mr. Cole's testimony, without the support of source documents, could not help the appellant in making out his case.

[65] The Associate Chief Justice deals with Mr. Cole's testimony at page 116 of Transcript 2 (Appeal Book, Vol. 2, p. 391) in very brief terms. That part of his Reasons, which I have already reproduced at paragraph 25 of these Reasons, simply states that Mr. Cole, as a chartered accountant, "… should have known better than anyone" that source documents should have been produced, adding that "… an accounting error may very well have been made, but that is not sufficient to find without additional proof to discharge the assumption that the money was received in 2003 by the Appellant".

[66] This is the extent of the Associate Chief Justice's analysis of Mr. Cole's testimony. It is clear, in my view, that he gave no consideration to this evidence because of his view that source documents ought to have been produced. This view, in my respectful opinion, is an error. As I indicated at paragraph 57 of these Reasons, Madam Justice L'Heureux-Dubé, at paragraph 87 of her

Reasons in *Hickman*, made it clear that credible oral evidence does not need the support of source documents to establish a point.

[67] The *Income Tax Act* (the *ITA*) did not require the appellant to produce source documents and the Associate Chief Justice made no credibility findings against Mr. Cole. By reason of his mistaken view that source documents were necessarily required, the Associate Chief Justice did not consider Mr. Cole's evidence. After stating that the evidence of both the appellant and his wife was unclear, the Associate Chief Justice dealt with Mr. Cole. Rather than attempting to determine whether or not Mr. Cole's evidence was credible and, more particularly, whether his evidence was sufficient to explain why the entries made in the 2001, 2002 and 2003 tax returns were in error and whether, as a result of his testimony, the Minister's assumptions had been "demolished", the Associate Chief Justice simply stated that Mr. Cole should have known that source documents had to be produced. There is no assessment of Mr. Cole's oral evidence. The Associate Chief Justice disregarded it because source documents had not been produced. In my respectful view, he erred in law in not considering Mr. Cole's evidence.

[68] Although Mr. Cole's evidence, coupled with that of the appellant and his wife, is far from perfect, it is, in my view, sufficient to demonstrate, on a *prima facie* basis, that there was no long-term investment held by Hunt River at the end of 2002 and that, consequently, no transfer of that investment to the appellant had taken place in 2003. As I have already indicated, the Associate Chief Justice made no findings of credibility against Mr. Cole and his evidence was neither challenged nor impeached by the respondent. Absent evidence challenging Mr. Cole's explanation

for the erroneous entries in the 2001, 2002 and 2003 tax returns and his explanation that no funds were left at the end of 2002, there was no basis upon which the Associate Chief Justice could refuse to accept Mr. Cole's evidence.

[69] Confronted with Mr. Cole's evidence, the respondent was bound, in my view, to adduce evidence rebutting the appellant's *prima facie* case by proving, on a balance of probabilities, that his assumptions were correct, i.e. by demonstrating that $305,000 had been transferred to the appellant's account in 2003. As the Minister failed to adduce any evidence challenging Mr. Cole's testimony, the appellant's *prima facie* case was not rebutted. Consequently, in these circumstances, the Associate Chief Justice ought to have concluded in favour of the appellant.

[70] In summary, I am satisfied Mr. Cole's evidence was capable of "demolishing" the Minister's assumptions and that had the Associate Chief Justice considered Mr. Cole's evidence, he would have concluded that a *prima facie* case had been made by the appellant "demolishing" the Minister's assumptions.

[71] I indicated earlier that I would address the Associate Chief Justice's view that source documents were required for the appellant to succeed on his appeal. As I have already stated, the Associate Chief Justice relied on this Court's decision in *Njenga* and on the Tax Court decisions in *Scragg* and *Redrupp*, which he summarized as follows (Transcript 2, p. 113 / Appeal Book, Vol. 2, p. 391):

> … These authorities clearly show the obligation of the taxpayer to produce documentation to support their claims. They basically stand for the following

> propositions: No. 1, “Self-written receipts or assertions without proof.” That’s the Federal the Federal Court of Appeal in *Njenga*. No. 2, “Year-end balances on balance sheets are not sufficient to prove who advanced funds to the corporation nor the source of those funds.” That’s the *Scragg* case. “Taxpayers are responsible themselves with the dilemma that they may face if they don’t have proper records.” That’s the *Njenga* case, the Trial Division. And finally, “The best evidence is what is required, not schedules or summaries, but original source documents,” and that is the *Redrupp* case.

[72] The Associate Chief Justice appears to have elevated the judicial requirement that supporting documents may be required for a taxpayer to establish his or her claims and deductions to an authoritative principle that documents will always be required for a taxpayer to establish his or her case. There is, in my respectful view, no principle to the effect that oral evidence must necessarily be supported by source documents. Whether documents are required to establish a point will depend on the particular circumstances of the case. However, whether documents are required or not, a judge must nonetheless assess the oral evidence and determine whether it is credible. The requirement for documents, or not, will often turn on such an assessment.

[73] I have carefully considered this Court’s decision in *Njenga* and the Tax Court’s decisions in *Scragg* and *Redrupp* and find nothing in those decisions to support the Associate Chief Justice’s view that oral evidence, on its own, cannot suffice to establish what it is intended to establish.

[74] I first turn to *Njenga*. In that case, the taxpayer was claiming that she could deduct, *inter alia*, child care expenses from her income, pursuant to section 63 of the *ITA*. In concluding that the taxpayer ought to have produced documents in support of her expenses, the Tax Court Judge, in

Njenga v. Canada, [1995] T.C.J. No. 927 (QL), made it clear that he could not rely on her oral evidence that these expenses had been incurred and, at paragraph 19, opined as follows:

> **19** However, the major focus arising from the trial, is the total conduct of the Appellant during the years relevant. To accept that the Appellant during those years in question left her children - some as young as three years old - in the care of a person about whom she knew so very little and monitored so nonchalantly requires more confidence in her statements than I am able to muster - no address, no social insurance number, no other domestic details, no set schedule, no hours of work record, no report filed by Kabogo before payment, no cheque, no regular receipts, etc. And her statements to that effect is all that I have.
>
> [Emphasis added]

[75] In other words, the Tax Court Judge did not find the taxpayer credible and, thus, could not entertain her claim for expenses unless she provided documents to support her statement that she had incurred them. It is in that context that the remarks of McDonald J.A., for this Court in *Njenga*, at paragraphs 3 and 4 of his Reasons, must be understood:

> 3. The Income tax system is based on self monitoring. As a public policy matter the burden of proof of deductions and claims properly rests with the taxpayer. The Tax Court Judge held that persons such as the Appellant must maintain and have available detailed information and documentation in support of the claim they make. We agree with that finding. Ms. Njenga as the Taxpayer is responsible for documenting her own personal affairs in a reasonable manner. Self written receipts and assertion without proof are not sufficient.
>
> 4. The problem of insufficient documentation is further compounded by the fact that the Trial Judge, who is the assessor of credibility, found the applicant to be lacking in this regard.
>
> [Emphasis added]

[76] In *Scragg*, the Minister had disallowed the taxpayer's claim for the deduction from his income of interest paid on borrowed money by him during taxation years 1999 to 2001. The

taxpayer argued that he had used the borrowed funds to provide working capital for a number of his corporations, which produced income for him in the form of both profit and management consulting fees, and thus was deductible under paragraph 20(1)*(c)*(i) of the *ITA*. The Tax Court Judge concluded that the taxpayer had not discharged his burden of demonstrating that the borrowed funds had been put to an eligible use. In so concluding, the Tax Court Judge noted that the taxpayer had been unable to produce the books and records of the companies to which he had allegedly lent the borrowed money. At paragraph 7 of his Reasons, the Tax Court Judge made the following remarks:

> **7**. Mr. Scragg's testimony was both confused and confusing. He referred repeatedly to SDC and 286603, as well as three other companies that were at one time involved in the entertainment industry, as being his companies, without ever making clear how the shares were actually held, or whether he held shares carrying a right to receive dividend income. He identified the August 7, 1996 deposit as part of the loan proceeds, but was unable to say exactly what he had done with the remaining $76,596.59, other than to aver that some $32,970 of it was applied to pay his obligation as guarantor of a bank loan for one of his screen production companies. Here, as elsewhere, he was vague as to the exact amount of the obligation that he paid.

[77] It is in that context that the Tax Court Judge found support in our decision in *Njenga*, referring in particular to paragraph 3 of McDonald J.A.'s Reasons. The Tax Court Judge concluded his Reasons with the following remarks:

> **10.** I do not wish to leave the impression that Mr. Scragg was not an honest witness. I have no doubt that he believed quite sincerely that he had put these loan proceeds to an eligible use in one or more of his corporations. It was clear throughout his evidence, however, that he did not have any clear recollection of the specific application of the funds in question, either initially or throughout the period of almost four years between the initial borrowing and the repayment. The quality of the evidence before me as to the use of the borrowed funds is simply not sufficient to support a claim to deduct the interest that was paid.

[78] In *Redrupp*, the taxpayer had deducted significant amounts as business expenses, carrying charges and farm losses. The taxpayer also claimed a provision against income and a deduction regarding a wrongful debt. The Tax Court Judge began his analysis by stating at paragraph 14:

> **14**. … The Appellant faces questions of credibility, reasonableness and common sense. The amounts in dispute are high and not proven. The best evidence would be an invoice from the creditor, a cancelled cheque, a receipt or other proof of payment. The best evidence was not presented in Court.

[79] After referring to McDonald J.A.'s remarks found at paragraph 3 of his Reasons in *Njenga*, the Tax Court Judge stated at paragraph 16:

> **16**. I will not permit the deduction of the amounts in dispute based on the Appellant's schedules and oral testimony alone. Certain amounts, in particular, cry out for verification.

[80] What these cases stand for is the proposition that, depending on the circumstances of the case, a taxpayer may be required, in addition to his oral testimony, to adduce supporting documents to prove a given point. In both *Njenga* and *Scragg*, the Court was not satisfied with the taxpayers' credibility. In *Redrupp*, the Tax Court Judge was of the view that the nature of the claims being made by the taxpayer required supporting documents.

[81] In the present matter, there are no findings of credibility made in regard to Mr. Cole's evidence. It is also of importance to note that contrary to *Njenga*, *Scragg* and *Redrupp*, the appellant herein is not seeking to deduct disbursements or expenses but, rather, is attempting to show that the Minister's assumptions that he received $305,000 in 2003 were incorrect. More particularly, Mr. Cole's evidence sought to explain why, at the end of 2002, there was no investment of $305,000 left in Hunt River's account and, hence, that that amount had not been disbursed in 2003 to either the

appellant or his wife. Further, in *Njenga*, *Scragg* and *Redrupp*, the Tax Court judges scrutinized the oral evidence presented by the taxpayers and made clear determinations with regard to the quality of that evidence. In the present matter, the Associate Chief Justice did not perform that task.

[82] I therefore conclude that the authorities relied upon by the Associate Chief Justice do not support his view that Mr. Cole's oral evidence could be disregarded simply because he had not produced supporting documents.

[83] For all of these reasons, the Associate Chief Justice's factual determination that the appellant did receive a shareholder's benefit of $305,000 in 2003 constitutes a palpable and overriding error.

[84] In view of my conclusion that the appellant made out a *prima facie* case "demolishing" the Minister's assumptions that Hunt River held an investment of $305,000 at the end of 2002, which it transferred to the appellant in 2003, and that the Minister has not rebutted the appellant's case, I need not address the question of whether the $305,000 was, in law, paid out to the appellant or to his wife.

Disposition

[85] For these reasons, I would allow the appeal of the Tax Decision with costs, I would set aside the Judgment of the Associate Chief Justice and, rendering the Judgment which ought to have been

rendered, I would allow the appellant's appeal from the Minister's reassessment of his 2003 taxation year and return the matter to the Minister for reassessment in accordance with these Reasons.

"M. Nadon"

J.A.

"I agree.
John M. Evans"

"I agree.
Carolyn Layden-Stevenson J.A."

FEDERAL COURT OF APPEAL

NAMES OF COUNSEL AND SOLICITORS OF RECORD

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STYLE OF CAUSE:	CLYDE HOUSE v. H.M.Q.
PLACE OF HEARING:	St. John's, Newfoundland
DATE OF HEARING:	June 1, 2011
REASONS FOR JUDGMENT BY:	NADON J.A.
CONCURRED IN BY:	EVANS J.A. LAYDEN-STEVENSON J.A.
DATED:	August 11, 2011

APPEARANCES:

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Martin Hickey	FOR THE RESPONDENT

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