Docket: 2005-1566(IT)G

BETWEEN:

RICHARD BIBBY,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on July 23, 24 and 25, 2008, at Toronto, Ontario

By: The Honourable Justice E.A. Bowie

Appearances:

Counsel for the Appellant:	Howard J. Alpert
Counsel for the Respondent:	H. Annette Evans

JUDGMENT

The appeal from the reassessment made under the *Income Tax Act* for the 2002 taxation year is allowed, with costs, and the reassessment is referred back to the Minister of National Revenue for reconsideration and reassessment on this basis that the amount of $224,000 included in the appellant's income and the penalty assessed under subsection 163(2) are to be deleted from the assessment.

Signed at Ottawa, Canada, this 13th day of November, 2009.

"E.A. Bowie"

Bowie J.

Citation: 2009 TCC 588
Date: 20091113
Docket: 2005-1566(IT)G

BETWEEN:

RICHARD BIBBY,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Bowie J.

[1] Richard Bibby appeals his income tax assessment for the 2002 taxation year. With the minor exception of some interest that is not in dispute, all of Mr. Bibby's income for the year in question came from a family corporation, Rabco Marketing Ltd. (Rabco). At the material time, Rabco carried on business as a supplier of electronic products to retail merchants. Mr. Bibby was the driving force behind the company. He did the buying and selling, and it appears from the evidence that his was the directing mind of the corporation. His wife Camille ran the office and handled the data entry and accounting functions for the company. Their son Jason handled the information technology and catalogue functions, and acted as traffic manager. Their other son, Christopher, was in charge of the warehouse and shipping operations, assisted as required by temporary employees. Richard Bibby and Camille Bibby each owned 50 common shares. Each family member also owned 50 preferred shares; Richard's were class A, Camille's were class B, and their sons' were class C. Mr. Bibby was the president and his wife was the secretary. The company's year end was January 31.

[2] None of the family members were paid by way of salary. Their practice was to take drawings from time to time throughout the year, and these drawings were

accounted for in the company's books by way of a debit to the shareholder loan account (owing to shareholders). Only one shareholder loan account was maintained in the general ledger and the drawings of all four family members were debited to that account. At each year end a decision was made as to the appropriate remuneration for each family member for the year, and the necessary year end journal entries were posted to reflect the compensation for the shareholders. The evidence was unclear as to the manner in which this decision was arrived at, but it seems most likely that the appellant made the decision, perhaps with advice from his accountant.

[3] One of Rabco's major customers was the HMV chain of music stores, to which it supplied earphones, cases, blank tapes and DVDs and similar accessory products. In 1990, Rabco became the exclusive supplier of such products to HMV, at first under a written contract, but after 1992 simply under an oral agreement. By 2000, HMV accounted for fully 90% of Rabco's sales, and the business had grown to the point where it rented a 13,500 square-foot warehouse and office building. Gross sales in the year ended January 31, 2002 exceeded 3.5 million dollars.

[4] It was on October 22, 2002 that Mr. Bibby's problems began. He was advised by HMV that it would no longer buy from his company. He had already placed orders for the product required to supply HMV with merchandise for the coming Christmas season, and those orders could not be cancelled. He attempted to find other customers for that inventory, but without success. In the end it was sold to jobbers at prices far below cost, with resulting large losses. With no alternative customers, the business was for practical purposes destroyed. The company had been profitable up to and including the year that ended January 31, 2002, but the years ended January 31, 2003 and 2004 were years of substantial losses.

[5] In early 2003, the appellant met twice with Mr. Bruce Davies, the accountant who had acted for the company, and for the family, for many years. He prepared the company's statements annually, and prepared the income tax returns for the company and for the family members. The first of these meetings took place in January 2003. At that meeting, the appellant informed Mr. Davies of the fact that the company had lost HMV as a customer, and that as a result the company was in serious financial difficulty and would cease to be profitable. The second meeting took place in March 2003. Mr. Bibby again told Mr. Davies of the serious consequences resulting from the loss of HMV's business, and Mr. Davies then suggested "that we amend the 2002 tax return"[1] of Rabco. Specifically, his proposal was that the income tax return of

[1] Transcript, p. 31, ll. 23-24.

Rabco for the year ended January 31, 2002 be amended to decrease the management fees that had been accrued to the appellant and the members of his family by the year end journal entries on January 31, 2002, "because the company would not be able to show the profit to handle those types of numbers."[2]

[6] Mr. Bibby accepted this advice, and Mr. Davies prepared an amended T2 income tax return for Rabco for the taxation year ended January 31, 2002. A second amended return for the 2002 taxation year of Rabco was also prepared by Mr. Davies. Unfortunately many of the documents entered into evidence by the parties are incomplete and undated copies, and both Mr. Bibby and Mr. Davies were vague in their evidence about what was done and when. It is clear, however, that Rabco, through the combined efforts of Mr. Bibby and Mr. Davies, filed an income tax return for the 2002 year on May 7, 2002 which showed that it had incurred management fees to the shareholders in the total amount of $322,000, and that its net income for the year was $152,753. It later filed an amended return for 2002 that showed management fees of $98,000 and a net income of $376,753, against which was applied a non-capital loss carried back from the 2003 taxation year of 132,397, leaving a net income of $244,356.[3] It appears that Mr. Davies prepared this return in March 2003, probably about the time that he prepared the individual returns of the appellant and the other family members. Again, the evidence was vague, but it seems that this amended return was filed by Mr. Bibby, by registered mail, probably in November 2003. There is no explanation in the evidence for this delay.

[7] Rabco then filed a second amended return for the 2002 year showing management fees which were now reduced to $71,000, and a net income of $403,742, against which were applied non-capital losses of $132,397 from the 2003 taxation year and $170,000 from the 2004 taxation year, leaving a net income of $101,345[4]. Mr. Davies' evidence was that this second amended return was filed on, or close to, March 1, 2004.

[8] These amended T2 returns were not accepted by the Minister of National Revenue, insofar as the changes to the management fees and the operating income of Rabco for 2002 were concerned. However Rabco was reassessed for the 2002 year to effect the requested carry-backs of its losses from 2003 and 2004.

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2 Transcript, p. 32, ll. 11-14.

3 Exhibit A-1(b), Tab 25.

4 *Ibid.*

[9] Mr. Davies gave his explanation for the preparation and filing of these amended T2 returns for Rabco. He said that it had been the practice of the company for some years to accrue management fees at the year end. The decision as to the amount of the management fees was implemented by a year end journal entry debiting administration fees[5] expense, and crediting the shareholder loan account. As the company maintained only one shareholder loan account for the four shareholders, the remuneration of all four shareholders was established by one journal entry for the amount of their total remuneration. In January 2002, the company was at the end of a profitable year and the decision was made to accrue management fees for the four family members in the total amount of $322,000[6]. There was no suggestion in the evidence that this decision was made contingent on there being future profits sufficient to pay the amounts accrued, nor was the accrual accounted for as a contingent liability.

[10] Mr. Davies went on to explain that he advised Mr. Bibby about the loss carry-back provisions in the *Act*, and that it was possible to file amended income tax returns. On the basis of that advice, and the obvious reality that Rabco would have a substantial loss in its 2003 year, the appellant decided that Rabco should file an amended return for 2002. The first amendment simply purported to reduce the management fees from $322,000 to $98,000, with a concomitant increase in the profit. It is no coincidence that the increased profit was more than offset by the losses carried back from 2003, and later from 2004. The second amended return that Rabco filed for 2002 purported to reduce the administration fee expense for 2002 by an additional $27,000. Mr. Davies' explanation of this change was that $27,000 was an approximation of the amount of deemed income attributable to Mr. Bibby in 2002 under subsection 15(2) and section 80.4 of the *Income Tax Act* as a result of his shareholder loan activity.

[11] The T1 income tax returns of the appellant and the other family members for 2002 were prepared by Mr. Davies. The signatures on them are all dated April 28, 2003, except that of the appellant, which is dated April 28, 2002. This was an error on his part, as the form itself clearly shows that it was his return for 2002. The four

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5 This account is referred to by a number of different names in the evidence.

6 The accrual on January 31, 2002 was actually effected by three journal entries, but they do not show separate amounts for each shareholder. They are found in an extract from the General Ledger at Exhibit R-1 Tab 16.

family members declared the following amounts as professional income, the only source of which is their Rabco management fees:

Richard Bibby	$27,000
Camille Bibby	$27,000
Christopher Bibby	$20,000
Jason Bibby	$24,000

The aggregate of these four amounts is $98,000, the amount to which Rabco's first amended T2 purported to reduce its management fee expense for the year ended January 31, 2002. Mr. Davies' evidence made it clear that he was of the view that the decision made in January 2002 that the remuneration of the family members would be an aggregate of $322,000 was one that could later be changed at will when it became apparent that it would have been to the advantage of both the company and its shareholders to fix the remuneration at a much lesser amount, because there were losses in later years to set off against the higher corporate income, and the revised incomes of the individuals would be subject to much lower taxes in their hands.

[12] The other effect of retroactively decreasing the shareholders' remuneration, of course, would be to increase their liability to Rabco. In fact, when Mr. Bibby accepted Mr. Davies' advice and instructed him to prepare the amended 2002 return for Rabco, and later the second amended return, no entry was made in the Rabco general ledger to reflect the supposed transactions reversing in part the January 31, 2003 journal entry. The only record of it, other than in the amended tax returns, is in certain handwritten notations made by Mr. Davies on a copy of Rabco's Statement of Income and Retained Earnings for the year ended January 31, 2002[7]. This document is reproduced as Appendix 1 to these Reasons.

[13] I have no doubt that Mr. Davies was incorrect when he advised the appellant in 2003 that he could reduce, with retroactive effect, the amount of remuneration that had been allocated to the family members by Rabco, and recorded in its books of account, more than a year before. Counsel for the appellant argues that section 111 of the *Act* entitles a corporate taxpayer that has suffered unexpected losses to go back and recompute its profit for an earlier fiscal year, changing such items as management and administration expenses. For this proposition he relied principally on the decision of the Tax Review Board in *Brazelot Construction Limited v. M.N.R.*[8]

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7 Exhibit A-1(a) Tab 12, 7th page.

8 81 DTC 449.

In that case the appellant, as was its custom, established accrued remuneration for the president at the end of 1976. The amount of the accrual was $195,000. The business took a severe downward turn in 1977, and the president signed a letter foregoing $150,000 of that amount, which had not at that time been paid to him. The company reported its income on the basis that the accrual at the end of 1976 was a deductible expense, and that upon the president in 1977 foregoing the payment of $150,000 outstanding, that amount was income in the 1977 taxation year. The Minister appears to have taken the position in assessing that only the amount actually paid could be treated as an expense in 1976, and that no amount should be taken into income in 1977. The company's appeal was allowed by the Board, on the basis that there were two genuine transactions: one an expense in the 1976 year and the other a revenue in the following year. The distinctions between that case and the present one are that in *Brazelot* the $150,000 that the president relinquished when the business declined in 1977 had not been paid to him; by relinquishing the outstanding balance in 1977 he extinguished a liability of the company, and it was accounted for on that basis in the year that it happened. In the present case Rabco purported to undo a transaction that had taken place in a previous fiscal period. In *Brazelot,* two transactions took place. In 1976, the company agreed to make future payments to its president totaling $195,000; in 1977 the president agreed to forgive $150,000 of the debt. Each transaction was properly accounted for in the year in which it took place. Here, Rabco had only had one transaction. It declared the management fees, and it made a corresponding credit to the shareholder loan account. All this occurred in its 2002 fiscal year. Much later, during its 2004 fiscal year, Rabco purported to change the original transaction by a few penciled notations on a financial statement. Bookkeeping entries cannot change history, they are only a way of recording events that have taken place, when they take place. This truism was perhaps expressed best by M. J. Bonner, when he was a member of the Tax Review Board, in *Brum v M.N.R.,*[9] where he said:

> Generally speaking, bookkeeping entries do not create reality. They are useful only to the extent that they record or reflect reality.

In the present case reality lies in the entries made at the 2002 year end of Rabco. The remuneration decision having been made and executed at that time, it was not susceptible of change simply because to do so would be more advantageous to the company and its shareholders.

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[9] 80 DTC 1607 @ 1609.

[14] The appellant also relied on several other cases dealing with the deductibility by employers of remuneration which was accrued but not paid, generally for reasons relating to the employer's ability to pay. None of them, however, support the appellant's proposition that adjustments to the expenses of a previous fiscal period, and concomitant changes to the income of the employee for a previous year, may be made on a retroactive basis as Rabco and Mr. Bibby sought to do in this case. It is, of course, permissible to enter into a second transaction of the kind dealt with by the Board in *Brazelot*, so long as it is accounted for in the fiscal period when it takes place. What is not permissible is retroactive implementation of tax planning by purporting to undo, or change, transactions that took place in an earlier period.

[15] Following an audit, Mr. Bibby was reassessed for the 2002 taxation year to add to his income for the year the following amounts:

Unreported income	$224,000
Unreported benefit pursuant to subsection 15(2) of the *ITA*	29,767
Unreported benefit pursuant to subsection 80.4(2) of the *ITA*	6,642
Total	$260,409

He also was assessed a gross negligence penalty under subsection 163(2) of the *Act*. The notice of reassessment did not specify the basis upon which the unreported income was being assessed. On October 20, 2003 the assessor, Mr. Ghambir had written to Mr. Bibby to advise him of the reassessment he proposed to make. In that letter he said this:

Dear Sir:

Re: Income tax returns for 2002, 2001 and 2000

As a result of our recent review of the corporate tax returns of Rabco Marketing Limited, we are now proposing the following adjustments to your taxable income:

	2002	**2001**	**2000**

1) Unreported Income	$224,000		
2) Subsection 15(2) Income	29,767		
3) Subsection 80.4(2) Benefit	6,642	25,936	16,589

> 1) The unreported income represents the balance of the amalgamated fees expense of Rabco Marketing Limited that was credited to the shareholders loan account in 2002 and not reflected on your personal return.
>
> 2) This amount represents income by virtue of subsection 15(2) of the *Income Tax Act* and pertains to your indebtedness to Rabco Marketing Limited.
>
> 3) This taxable benefit results from loans you received from Rabco Marketing Limited by virtue of your indebtedness. Pursuant to subsection 80.4(2) of the *Income Tax Act*, you are deemed to have received a benefit equal to the amount by which interest on the loan computed at the prescribed rate for the period in the year it was outstanding exceeds interest paid on the loan in the year or within thirty (30) days thereafter.[10]

[16] The assessment was reviewed following the filing of a notice of objection, and on December 29, 2004 a further reassessment was issued, the only effect of which was to reduce the shareholder benefit assessed under subsection 80.4(2) by $1,859. At that time the Minister also decided to cancel the penalty previously assessed, but through inadvertence the amount of the penalty was not deleted from the assessment.

[17] Mr. Bibby filed a notice of objection to this reassessment on January 12, 2005, and on February 28, 2005 the Minister confirmed the December 29, 2004 reassessment, in the following terms:[11]

> NOTIFICATION OF CONFIRMATION BY THE MINISTER
>
> Your Notice of Objection to the income tax assessment for the 2002 taxation year has been carefully reviewed under subsection 165(3) of the *Income Tax Act*.
>
> The Minister of National Revenue has considered the reasons set out in your objection and all the relevant facts. It is hereby confirmed that the assessment has

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10 Exhibit R-1, Tab 24.

11 Notice of Confirmation, February 28, 2005, Exhibit A-1(a) Tab 6.

> been made in accordance with the provisions of the *Income Tax Act* on the basis that:
>
> The benefits conferred on you by Rabco Marketing Ltd. amounting to $224,000 have been included in computing your income in accordance with the provisions of subsection 15(1) of the *Act*.
>
> The amount of $29,767 has been included in your income in accordance with the provisions of subsection 15(2) of the *Act.*
>
> When you were a shareholder of Rabco Marketing Ltd., you received a loan or otherwise incurred a debt from the corporation because of or as a consequence of such shareholding. The interest you paid on such loans and debts was less than the interest computed at the prescribed rate. A benefit of $4,783 has been calculated according to subsection 80.4(2) and section 4301 of the *Income Tax Regulations.* It has been included in your income as a benefit conferred on a shareholder under subsections 15(1) and 15(9).

[18] At the conclusion of the trial, I invited counsel to make further submissions in writing in relation to the unreported management fee issue, which they both did. The appellant took a number of objections to the assessment under appeal and to the position now advanced by the respondent, which is that the assessment, insofar as it relates to the remuneration, can be sustained under section 15 of the *Act*, or alternatively, under either subsection 5(1) or 6(1). The appellant's first objection is that it is not open to the Minister, even if he assessed under section 6, having confirmed the assessment relying solely on section 15, to argue that the assessment is justified under section 5 or 6. He goes on to argue in the alternative that in any event, the respondent has not pleaded section 5 or 6 in the Reply to the Notice of Appeal, and therefore may not now rely on them. The remuneration portion of the assessment cannot be supported under section 15, he argues, because any benefit to Mr. Bibby resulting from the accrual of management fees was not a benefit conferred on him *qua* shareholder, but *qua* manager of the company and its trading operations.

[19] I do not find any merit in the first of these arguments. Since the decision of the Supreme Court of Canada in *Continental Bank*,[12] and the subsequent enactment of subsection 152(9), there has been considerable debate about the reach of that subsection. The Federal Court of Appeal has now made it clear, however, that subsection 152(9) permits the Minister to raise a new argument, based upon different provisions of the *Act*, at any stage prior to trial, so long as that new argument is based

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12 *Continental Bank of Canada. v. Canada*, [1998] 2 S.C.R. 358.

upon the same transactions that gave rise to the assessment that is before the court, and provided that the new argument would not call for the introduction of relevant evidence that may no longer be adduced without the leave of the court, which leave it is not appropriate for the court to give in the circumstances of the particular case.[13] In this case that requirement is met, as the respondent relies only on the 2002 year end journal entries that created the accrual of management fees, and on the drawings by the appellant and his family members that took place throughout 2002.

[20] However, I am of the view that the appellant's alternative submission must prevail. It is well-settled that subsection 15(1) does not operate to tax all payments made to shareholders by a corporation, only those made outside the ordinary course of business. The applicable principle is expressed this way by professor Krishna:[14]

> Payments to shareholders are taxable as shareholder benefits only if they are made outside the ordinary course of business. Thus, a payment to a shareholder in the ordinary course of, and pursuant to, a *bona fide* business transaction does not trigger a benefit under this rule. Such payments are taken into account in the normal accounting for profit. For example, a person who rents a building to a corporation of which he or she is a shareholder does not necessarily receive shareholder benefit in respect of the rental. If the shareholder rents in his or her capacity as a landlord and charges a fair rental value for the building, the shareholder is taxable on the rental income. The payment to the shareholder is made to him or her not *qua* shareholder, but *qua* landlord.
>
> …
>
> Section 15 is directed towards benefits conferred on a shareholder in his or her capacity as shareholder. It is not concerned with benefits conferred on a taxpayer in his or her capacity as an employee. … (footnotes omitted)

In the present case, the management fees that were the subject of the assessment were amounts earned by the appellant, and also by the other members of his family, in the normal course of carrying on the company's business. For purposes of section 15, it is immaterial whether the amounts were salary, or, as in this case, management fees. What matters is that the payment was made as remuneration, not simply to benefit a shareholder. Indeed, it has never been disputed by the respondent that the company

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[13] See: *Walsh v. Canada*, 2007 FCA 222; [2007] 4 C.T.C. 73, and the cases cited there.

[14] Krishna, Vern, *The Fundamentals of Canadian Income Tax*, 8th ed. Toronto: Thomson/Carswell, 2004, pages 855-6. See also *Youngness v. The Queen*, 90 DTC 6322 at 6325 (FCA).

had the right to a deduction from income for the payments, in 2002 and in earlier years.

[21] The amount of the fees not declared by Mr. Bibby would have been taxable in his hands under paragraph 6(1)(*c*), but only to the extent that they were actually received by him during the year. The specific language of that provision taxes "… fees received by the taxpayer in the year …". It is not clear whether Mr. Bibby was told that paragraph 6(1)(*c*) was invoked by the Minister in assessing him. It is clear, however, that if it had been then it was abandoned at the time the second reassessment was confirmed. That notice of confirmation is in evidence, and it clearly limits the Minister's reliance to section 15. As I have said, it would have been open to the respondent to rely on paragraph 6(1)(c) if that had been done in a timely way, and if the assessment were confined to amounts received in 2002 by Mr. Bibby and not by other members of his family.

[22] The Reply[15] specifically pleads that the $224,000 that represents the difference between the $322,000 management fees credited to the shareholder loan account and the $98,000 reported as income by the four family members "… is a benefit conferred by Rabco Marketing Ltd. on the Appellant in his quality of principal shareholder for the 2002 taxation year."[16] It is not explicitly pleaded that Mr. Bibby received that amount in 2002. Part C of the Reply, which is titled STATUTORY PROVISIONS, GROUNDS RELIED ON AND RELIEF SOUGHT, makes no mention of section 5 or 6 of the *Act,* and suggests no other argument but that the amount is a shareholder benefit. There was no motion to amend the Reply before, or even at, the trial.

[23] Subsection 49(1) of the *General Procedure Rules* requires that every Reply shall state:

> (a) the statutory provisions relied on; [and]
>
> (b) the reasons the respondent intends to rely on

The purpose of these requirements is to ensure that the issues are properly defined for the purposes of discovery and trial, and so that the appellant will know what arguments he must meet, and so that he will be able to marshal and lead his evidence accordingly. This is not a mere formality that may be overlooked when it has not

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15 I note that the Reply was not drawn by counsel who appeared at the trial.

16 Reply, subparagraph 23(j).

been complied with; it is a core component of the trial process, and to ignore non-compliance would undermine the integrity of that process: see *Glisic v. The Queen*.[17]

[24] For these reasons the appellant must succeed in his appeal insofar as it concerns the inclusion in his income of the management fee amount.

[25] The appellant did not really contest the inclusion in his income of a benefit under subsection 15(2) arising out of indebtedness to Rabco that was not repaid by the end of the following taxation year. The relevant provisions of the *Act* are subsections 15(2), (2.3), (2.6) and 80.4(2).

> 15(2) Where a person (other than a corporation resident in Canada) or a partnership (other than a partnership each member of which is a corporation resident in Canada) is
>
> (*a*) a shareholder of a particular corporation,
>
> (*b*) connected with a shareholder of a particular corporation, or
>
> (*c*) a member of a partnership, or a beneficiary of a trust, that is a shareholder of a particular corporation
>
> and the person or partnership has in a taxation year received a loan from or has become indebted to the particular corporation, any other corporation related to the particular corporation or a partnership of which the particular corporation or a corporation related to the particular corporation is a member, the amount of the loan or indebtedness is included in computing the income for the year of the person or partnership.
>
> 15(2.1) …
>
> 15(2.3) Subsection 15(2) does not apply to a debt that arose in the ordinary course of the creditor's business or a loan made in the ordinary course of the lender's ordinary business of lending money where, at the time the indebtedness arose or the loan was made, *bona fide* arrangements were made for repayment of the debt or loan within a reasonable time.

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17 [1988] 1 F.C. 731 (FCA); see also *Fortino et al. v. The Queen*, 97 DTC 55 (TCC); aff'd . 2000 DTC 6060 (FCA).

15(2.6) Subsection 15(2) does not apply to a loan or an indebtedness repaid within one year after the end of the taxation year of the lender or creditor in which the loan was made or the indebtedness arose, where it is established, by subsequent events or otherwise, that the repayment was not part of a series of loans or other transactions and repayments.

80.4(2) Where a person (other than a corporation resident in Canada) or a partnership (other than a partnership each member of which is a corporation resident in Canada) was

(*a*) a shareholder of a corporation,

(*b*) connected with a shareholder of a corporation, or

(*c*) a member of a partnership, or a beneficiary of a trust, that was a shareholder of a corporation,

and by virtue of that shareholding that person or partnership received a loan from, or otherwise incurred a debt to, that corporation, any other corporation related thereto or a partnership of which that corporation or any corporation related thereto was a member, the person or partnership shall be deemed to have received a benefit in a taxation year equal to the amount, if any, by which

(*d*) all interest on all such loans and debts computed at the prescribed rate on each such loan and debt for the period in the year during which it was outstanding

exceeds

(*e*) the amount of interest for the year paid on all such loans and debts not later than 30 days after the later of the end of the year and December 31, 1982.

[26] The Notice of Appeal puts in issue the inclusion by the Minister of benefits under subsections 15(2) and 80.4(2) in the appellant's income. The Minister's assumptions giving rise to these inclusions were pleaded very precisely in subparagraphs 23(k) to (r) and Schedule "A" of the Reply, which are reproduced as Appendix 2 to these reasons. The appellant did not lead any evidence that rebuts these assumptions. In fact, the evidence of Mr. Davies tends to confirm them. He testified that the reason for filing a second amended T2 for Rabco's 2002 taxation year was that reducing the company's management fee expense by $27,000, and

therefore Mr. Bibby's management fee income by the same amount, would in effect offset these benefits, which he said he estimated to be about that amount. Counsel for the appellant submitted in argument that the extracts from the shareholder loan account in Exhibit R-2 were not properly proved and ought not to be relied on. However, the material information from the account was assumed by the Minister in assessing, and was properly pleaded as such. In the absence of any rebutting evidence, the appeal must fail with respect to those two amounts.

[27] In the result, then, the appeal is allowed and the reassessment is referred back to the Minister for reconsideration and reassessment on this basis that the amount of $224,000 included in the appellant's income and the penalty assessed under subsection 163(2) are to be deleted from the assessment. The appellant has been substantially successful and is entitled to his costs.

Signed at Ottawa, Canada, this 13th day of November, 2009.

"E.A. Bowie"

Bowie J.

APPENDIX 1

RABCO MARKETING LTD.
STATEMENT OF INCOME AND RETAINED EARNINGS
FOR THE YEAR ENDED JANUARY 31, 2002
UNAUDITED, See Notice To Reader

		2002		2001
Sales	$	3,663,124	$	4,437,559
Cost of sales		2,919,246		3,747,468
Gross margin		743,878		690,091
Expenses				
Administration		~~322,000~~ 71,000		232,000
Advertising and promotion		1,420		450
Amortization and depreciation		6,806		5,237
Interest and bank charges		174		1,889
Commission expense		28,831		29,050
Insurance		7,734		6,989
Office and general		3,988		11,664
Professional fees		3,350		9,791
Rent and maintenance		119,637		133,576
Telephone		3,759		5,474
Utilities		7,724		6,154
Travel		40,702		49,508
		546,125		491,782
Income before income taxes		~~197,753~~		198,309
Provision for income taxes		45,000		46,000
Net income for the year		~~152,753~~		152,309
Retained earnings, beginning of the year		1,030,579		878,270
Retained earnings, end of the year	$	~~1,182,332~~	$	1,030,579

Amendment to T2: = Reduce Admin Fees By 251,000

Change to F/S

Dr. Due to SH. 251,000

Cr. Admin Fees 251,000

APPENDIX 2

Subparagraphs 23(k) to (r) and Schedule "A" of the Reply:

(k) During the 2002 taxation year, the Appellant, his wife Camille and their sons Christopher and Jason were indebted to Rabco Marketing Ltd. as outlined in the Schedule "A" attached to the present Reply.

(l) 72% of the indebtedness mentioned in subparagraph 23(k) and outlined in Schedule "A" is owed by the Appellant.

(m) No interest was paid by the Appellant, his wife Camille and their sons Christopher and Jason to Rabco Marketing Ltd. during the 2002 taxation year in relation to their indebtedness.

(n) The Appellant, his wife Camille and their sons Christopher and Jason, and Rabco Marketing Ltd. are Canadian residents.

(o) Rabco Marketing Ltd. is not in the business of lending money.

(p) The Appellant, his wife Camille and their sons Christopher and Jason, were indebted to Rabco Marketing Ltd. because of their shareholding.

(q) At the time the debt was incurred, no *bona fide* arrangements were stated for the repayment of the debt within a reasonable time.

(r) The following indebtedness of the Appellant arising during the 2002 taxation year, was not repaid prior to the end of the 2003 taxation year of Rabco Marketing Ltd.:

Rate	Indebtedness
January 1, 2002	$2,700
January 1, 2002	8,066.96
January 1, 2002	3,000
January 1, 2002	2,000
January 1, 2002	3,000
January 1, 2002	1,000
January 1, 2002	2,000
January 31, 2002	8,000
	$29,766.96

SCHEDULE "A"

Date	Indebtedness	days	Prescribed Rate	Deemed Interest
January 1, 2002	$661,549.52	30	3%	$1,631.22
January 31, 2002	$291,253.96	4	3%	$95.75
February 4, 2002	$296,253.96	4	3%	$97.40
February 8, 2002	$311,253.96	10	3%	$255.83
February 18, 2002	$315,253.96	1	3%	$25.91
February 19, 2002	$24,000.00	13	3%	$25.64
March 4, 2002	$27,000.00	1	3%	$2.22
March 5, 2002	$29,000.00	17	3%	$40.52
March 22, 2002	$34,000.00	3	3%	$8.38
March 25, 2002	$38,000.00	7	3%	$21.86
April 1, 2002	$40,000.00	1	2%	$2.19
April 2, 2002	$42,000.00	1	2%	$2.30
April 3, 2002	$43,000.00	12	2%	$28.27
April 15, 2002	$44,000.00	9	2%	$21.70
April 24, 2002	$84,000.00	5	2%	$23.01
April 29, 2002	$104,500.00	3	2%	$17.18
May 2, 2002	$106,500.00	7	2%	$40.85
May 9, 2002	$108,500.00	4	2%	$23.78
May 13, 2002	$111,500.00	3	2%	$18.33
May 16, 2002	$121,500.00	5	2%	$33.29
May 21, 2002	$124,500.00	6	2%	$40.93
May 27, 2002	$125,500.00	7	2%	$48.14
June 3, 2002	$127,500.00	7	2%	$48.90
June 10, 2002	$128,500.00	11	2%	$77.45
June 21, 2002	$129,500.00	10	2%	$70.96
July 2, 2002	$134,500.00	2	3%	$22.11
July 4, 2002	$137,500.00	4	3%	$45.21
July 8, 2002	$138,500.00	7	3%	$79.68
July 15, 2002	$141,500.00	7	3%	$81.41
July 22, 2002	$144,500.00	7	3%	$83.14
July 29, 2002	$148,500.00	3	3%	$36.62

August 1, 2002	$149,500.00	1	3%	$12.29
August 2, 2002	$151,500.00	6	3%	$74.71
August 8, 2002	$171,500.00	8	3%	$112.77
August 16, 2002	$172,500.00	3	3%	$42.53
August 19, 2002	$175,500.00	9	3%	$129.82
August 28, 2002	$176,500.00	1	3%	$14.51
August 29, 2002	$286,500.00	5	3%	$117.74
September 3, 2002	$291,500.00	13	3%	$311.47
September 16, 2002	$293,500.00	14	3%	$337.73
September 30, 2002	$298,500.00	1	3%	$24.53
October 2, 2002	$300,500.00	1	3%	$24.53
October 3, 2002	$303,500.00	1	3%	$24.70
October 4, 2002	$306,500.00	1	3%	$24.95
October 7, 2002	$309,500.00	3	3%	$75.58
October 24, 2002	$315,500.00	17	3%	$432.45
November 25, 2002	$320,500.00	32	3%	$829.81
November 29, 2002	$322,500.00	4	3%	$105.37
December 17, 2002	$325,500.00	18	3%	$477.12
December 18, 2002	$331,500.00	1	3%	$26.75
December 24, 2002	$332,500.00	6	3%	$163.48
December 31, 2002	$332,500.00	8	3%	$218.63
				$6,642.30
Portion attributable to the Appellant:			72%	
Appellant's deemed interest benefit				$4,783.00

CITATION:	2009 TCC 588
COURT FILE NO.:	2005-1566(IT)G
STYLE OF CAUSE:	RICHARD BIBBY and HER MAJESTY THE QUEEN
PLACE OF HEARING:	Toronto, Ontario
DATE OF HEARING:	July 23, 24 and 25, 2008
REASONS FOR JUDGMENT BY:	The Honourable Justice E.A. Bowie
DATE OF JUDGMENT:	November 13, 2009

APPEARANCES:

Counsel for the Appellant:	Howard J. Alpert
Counsel for the Respondent:	H. Annette Evans

COUNSEL OF RECORD:

For the Appellant:

Name:	Howard J. Alpert
Firm:	Alpert Law Firm
For the Respondent:	John H. Sims, Q.C. Deputy Attorney General of Canada Ottawa, Canada