

Docket: 2009-3591(IT)I

BETWEEN:

JOCELYN HÉBERT,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on July 8, 2010, at Montréal, Quebec.

Before: The Honourable Justice Réal Favreau

Appearances:

Counsel for the appellant: François Asselin
Counsel for the respondent: Marc-André Rouet

JUDGMENT

The appeal against the reassessment made on August 24, 2009, under the *Employment Insurance Act* for the 2004 taxation year is dismissed in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Canada, this 27th day of January 2011.

"Réal Favreau"

Favreau J.

Translation certified true
on this 25th day of March 2010.
Daniela Possamai, Translator

Citation: 2011 TCC 46
Date: 20110127
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REASONS FOR JUDGMENT

Favreau J.

[1] This is an appeal against the reassessment made on August 24, 2009, under the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.), as amended (the Act), for the 2004 taxation year.

[2] The issues for determination are

- (a) whether the Minister of National Revenue (the Minister) was justified in adding \$30,110 to the appellant's income for the 2004 taxation year; and
- (b) whether the Minister was justified in applying a penalty of \$2,057.93 for the 2004 taxation year pursuant to subsection 163(2) of the Act.

[3] During the year at issue, the appellant operated, as a sole proprietorship, a garage whose main activities consisted in collision repair for automobiles he purchased at auctions and resold. About 50% of the appellant's total sales from goods and services provided to his brother's, Denis Hébert, farming business.

[4] In filing his income tax return for the 2004 taxation year, the appellant reported a gross business income, before the cost of goods sold, of \$25,490, and a net

income of \$3,509, as well as a gross rental income of \$2,400 and a net income of \$1,517, and income derived from another source of \$3,281.

[5] In 2007, the Canada Revenue Agency (the CRA) conducted an audit of the appellant's business by an analysis of his bank deposits and accounting records so as to reconcile the income. Over the course of the audit, the appellant provided his synoptic ledger, bank and credit card statements as well as all other records requested by the auditor. The analysis of the deposits made into the appellant's personal and business bank accounts versus the record of cash receipts disclosed that a number of deposits were made by clients of the appellant that had not been invoiced, hence the addition of the amount of \$30,110 in additional income allocated to the appellant. In particular, the auditor was unable to associate deposits with invoices respecting the two deposits totalling \$20,500 (\$10,000 deposited on August 9, 2004, and \$10,500 deposited on August 10, 2004) and respecting other unexplained deposits totalling \$9,610.

The deposits of \$20,500

[6] During her testimony at the hearing, the appellant explained that the purchase of motorcycles from a dealer was not properly executed resulting in the acquisition of two expensive motorcycles on August 9, 2004, a 1997 Harley-Davidson that cost \$7,915.22 and a 2004 Yamaha that cost \$11,438.08 for a total amount of \$19,353.30. The appellant indicated that he did not have the funds required to pay for the motorcycles and that the available credit on his thirteen credit cards was insufficient. He therefore turned to his mother, who loaned him \$20,000 in cash on August 2, 2004. According to the appellant, he made two deposits on the recommendation of a teller and paid the purchase price of the motorcycles by cheque.

[7] The appellant's mother testified at the hearing and she confirmed that she loaned the appellant \$20,000 on August 2, 2004. She explained that the money borrowed derived from the savings she accumulated in cash at her house, money she hid in her cold storage room and kept in a cardboard box. According to her testimony, her savings came from pension cheques she and her husband received. In cross-examination, she explained that her family farm was sold in 1983 to the youngest of her five children. The original farm was divided into three parts of which a smaller part still belongs to her husband. She also confirmed that on the day of the loan she signed an acknowledgement of debt that was prepared in advance by Gaétan Hébert, one of the appellant's brothers, without terms of repayment, or interest. Finally, she confirmed that she did not make any other loans to the appellant.

[8] Gaétan Hébert, a retired accountant who does bookkeeping and prepares income tax returns and tax reports, testified at the hearing and confirmed that he prepared the blank acknowledgement of debt: the date, the amount of the loan, the interest rate, the name of the lender and borrower were left blank. He also assisted his brother with the audit.

[9] The auditor, Caroline Lacombe, testified at the hearing and she explained that the audit of the appellant's business began on March 15, 2007, when an initial interview was held with the appellant. On that occasion, the auditor completed a form based on the answers provided by the appellant. In response to the question about loans from family and friends, the auditor did not indicate either "yes," or "no." The auditor explained that the appellant was very hesitant in answering said question and finally indicated that no amount greater than \$1,000 was loaned to him at the end of the year. The appellant signed said form for the years 2003, 2004 and 2005 without the auditor providing him with explanations regarding the extent and significance of his answers.

[10] During the audit, the auditor noted that the bookkeeping was inadequate and incomplete, that sales and expenses invoices were missing and that taxes had been included in the expenditures. In the analysis report on the appellant's thirteen credit cards, the amounts of money from the credit cards and deposited into the bank accounts were excluded from the unreported income. The analysis of said credit card accounts revealed that in August 2004 the appellant had an available balance of \$25,798.99 and that between August 4, 2004, and December 31, 2004, four cash advances totalling \$17,000 were taken from credit cards.

[11] The auditor completed her audit in June 2007 and on June 26, 2007, she submitted a draft assessment. On July 18, 2007, she met with the appellant and his accountant but no explanation was provided by the appellant, nor did the appellant make any reference to the \$20,000 loan obtained from his mother. In fact, it was not until August 4, 2007, when the appellant's file was closed, that the appellant submitted the acknowledgement of the \$20,000.

[12] The reason provided by the appellant for not disclosing the loan earlier was to prevent his other family members from finding out the magnitude of the loan from his mother. Although the appellant's brother is the one who submitted the acknowledgement of debt to his mother, he was unaware of either the amount or exact terms of the loan at the time it was made and thereafter, during the audit.

[13] The CRA did not accept the explanations provided by the appellant and an analysis of the mother's income for the years 1995 to 2009 was conducted to verify whether she had the necessary income to accumulate \$20,000 in savings. The analysis was filed as Exhibit I-2. The review revealed that she had declared income of about \$10,000 per year including interest income of \$2,000 on the certificates of deposits for the years 2003 and 2004. The interest income then fell to \$1,600 in 2005 and to about \$1,100 in 2006 and 2007.

The other deposits of \$9,610

[14] During her testimony, the auditor explained that she used the net deposit method. She also confirmed that she prepared a net worth estimate which she did not take into account as the appellant's inventory was not maintained properly and did not yield probative results.

[15] The auditor also explained that she made year-end adjustments that increased the appellant's gross income by \$2,430.84 in 2004. Moreover, she confirmed that she had gained access to the appellant's bank records and invoices which would have allowed her to make the same adjustments at the beginning of 2004 but that she did not. Nor did she take into account an invoice of about \$10,525 (\$12,106.38 with taxes) dated December 18, 2003, which was paid in cash and of which part of the proceeds was partially deposited into one of the appellant's bank accounts. The CRA did not allow an adjustment to be made at the beginning of the year because the appellant was unable to determine exactly the proportion of money he kept at home and that which he claimed to have deposited. The appellant was unable to establish that the deposits made in early 2004 could be quantitatively attached to the invoice of December 18, 2003. Furthermore, the auditor indicated that she made every possible effort to correlate the amounts deposited in early 2004 to the 2003 year-end invoices even though the appellant's accounting did not show any accounts receivable at the end of 2003.

Analysis and conclusion

[16] In his written submissions, counsel for the appellant adopted the following explanations given by Bédard J. of this Court in *9116-0762 Québec Inc. (Belle-Or) v. The Queen*, 2010 TCC 116 (CanLII):

[9] *Hickman Motors Ltd. v. Canada*, [1997] 2 S.C.R. 336 is to the effect that the Minister uses assumptions to make assessments and the taxpayer has the initial burden of demolishing the Minister's assumptions. This is met where the taxpayer

makes out at least a *prima facie* case that demolishes the Minister's assumptions. Then, after the taxpayer has met the initial burden, the onus shifts to the Minister to rebut the *prima facie* case made out by the taxpayer and to prove the assumptions. As a general rule, a *prima facie* case is defined as one with evidence that establishes a fact until the contrary is proved. In *Stewart v. M.N.R.*, [2000] T.C.J. No. 53, Cain J. states that "[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. Moreover, in *Orly Inc. v. Canada*, 2005 FCA 425, at paragraph 20, the Federal Court of Appeal stated that "the burden of proof put on the taxpayer is not to be lightly, capriciously or casually shifted..." considering "[i]t is the taxpayer's business." The Federal Court of Appeal also stated in the same decision that it is the taxpayer who "knows how and why it is run in a particular fashion rather than in some other ways. . . . He has information within his reach and under his control." . . .

[17] In the case at bar, the appellant must therefore demonstrate by *prima facie* evidence that he actually borrowed \$20,000 from his mother. To that end, the appellant submits that he demolishes the Minister's assumptions by putting in evidence an acknowledgement of debt supported by the credible and unrebutted testimonies of his mother and his brother, Gaétan Hébert.

[18] Contrary to the appellant's submissions, I do not believe that the appellant was successful in demolishing the presumption of validity of the Minister's reassessment. First, I fail to see why the appellant would have borrowed \$20,000 from his mother when he surely had the money necessary to pay for one of the two motorcycles. The error, if there is one, was that he purchased a second motorcycle and not he purchased two motorcycles.

[19] The appellant claimed that the loan from his mother was made because he could no longer withdraw money from his credit cards as their respective limit had been reached. However, based on the analysis report on the credit card accounts, there are discrepancies with the appellant's submissions as on the one hand, the credit limits, when taken in conjunction with the balances indicated for the month of August 2004, reveal that at the time the appellant had an available balance of \$25,798.99 and that, on the other hand, the appellant availed himself, between August 4 and December 31, 2004, of four cash advances on his credit cards for an amount totalling \$17,000.

[20] The appellant's brother, Gaétan Hébert, confirmed that he prepared the acknowledgement of debt but did not specify the exact date on which he prepared it and submitted it to his brother or mother. However, the appellant's mother stated that she signed the acknowledgement of debt on the day of the loan, August 2, 2004. I

doubt that was the case and the document in question could have very well have been prepared and signed days or even months after the loan, if there is one, was made. The doubt about the date of the signing of the acknowledgement of debts stems from the fact that the appellant did not disclose the existence of the loan of \$20,000 during the initial interview. It has been demonstrated that the form completed by the auditor did not specifically indicate the loan of \$20,000 in 2004. Moreover, the appellant did not disclose the existence of the loan either during the audit or the meeting of July 18, 2007, with the auditor to discuss the draft assessment.

[21] The explanations provided by the appellant that he did not want to disclose the existence of the loan to prevent his other family members from finding out the amount of the loan made by his mother are not satisfactory as at least one other family member, the appellant's brother, was aware that such a loan may have been made to the appellant by the mother in order to have prepared the draft acknowledgement of debt.

[22] As for the testimony of the appellant's mother, she appeared to be sincere and credible but not reliable owing to her relationship to the appellant and the fact that her testimony was inconsistent with that of her son on one important point: she stated that she did not make any other loans to the appellant, other than the loan of August 2, 2004, when the appellant claimed that he had obtained other loans from his mother. While it is not impossible that the appellant's mother managed to save \$20,000 over a number of years, considering her income, the fact still remains that \$20,000 is a very large amount of money to keep at home in a cardboard box.

[23] As of the date of the hearing in 2010, no reimbursement had been made by the appellant on the loan and the motorcycles still had not been sold.

[24] Under the circumstances, the loan theory has the appearance of an explanation after the fact. The appellant failed to meet his initial burden and demonstrated that the amount of \$20,000 deposited on August 9 and 10, 2004, did not constitute unreported income but derived rather from a loan made to him by his mother to fund the purchase of the motorcycles.

[25] With respect to the other unexplained deposits totalling \$9,610, the appellant failed to meet his initial burden and demolish the Minister's assumptions. The explanations provided by the auditor for not making any adjustments in early 2004, which are described in paragraph 15 above, appear to be justified and reasonable under the circumstances.

[26] The imposition of the penalty provided for in subsection 163(2) of the Act in the amount of \$2,057.93 for 2004 is justified under the circumstances. The facts in evidence are such that the appellant's tax return made a misrepresentation of facts, and the only explanations offered by the appellant were found not to be credible. In my view, given such circumstances, one must come to the inevitable conclusion that the false tax return was filed knowingly, or under circumstances amounting to gross negligence. In the case at bar, the unreported income is important in relation to that which was not. It is hard to imagine how a taxpayer who has the capacity to manage a garage and 13 credit cards could forget to report 54% of his income for the year 2004.

[27] For these reasons, the appeal is dismissed.

Signed at Ottawa, Canada, this 27th day of January 2011.

"Réal Favreau"

Favreau J.

Translation certified true
on this 25th day of March 2010.
Daniela Possamai, Translator

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APPEARANCES:

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