Docket: 2006-2525(IT)G

BETWEEN:

GEOFFREY LAST,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on common evidence with the appeal of *Geoffrey Last (2006-2902(GST)I)* on October 24 - November 3, 2011, January 30 and 31, 2012 at Vancouver, British Columbia
(Written submissions subsequently received)
By: The Honourable Justice J.M. Woods

Appearances:

Counsel for the Appellant:	Alistair G. Campbell Michelle Moriartey
Counsel for the Respondent:	Bruce Senkpiel Christa Akey

JUDGMENT

The appeal with respect to assessments made under the *Income Tax Act* for the 2000, 2001 and 2002 taxation years is allowed, and the assessments are referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that:

(a) concessions by the respondent as set out in the appendix to the reasons for judgment should be allowed,

(b) the revenue from the car business for the 2002 taxation year should be reduced by $170,000,

(c) 20 percent of home expenses should be allocated to the car business for periods in which the home was not leased, and

(d) rental income in the amounts of $5,052.80 and $8,460.29 for the 2000 and 2001 taxation years, respectively, should be added to the income of the appellant.

Signed at Toronto, Ontario this 9th day of October 2012.

"J. M. Woods"

Woods J.

Docket: 2006-2902(GST)I

BETWEEN:

GEOFFREY LAST,

Appellant,

and

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Respondent.

Appeal heard on common evidence with the appeal of *Geoffrey Last (2006-2525(IT)G)* on October 24 - November 3, 2011, January 30 and 31, 2012 at Vancouver, British Columbia
(Written submissions subsequently received)
By: The Honourable Justice J.M. Woods

Appearances:

Counsel for the Appellant:	Alistair G. Campbell Michelle Moriartey
Counsel for the Respondent:	Bruce Senkpiel Christa Akey

JUDGMENT

The appeal with respect to an assessment made under the *Excise Tax Act* for reporting periods from 1998 to 2002, inclusive, is allowed, and the assessment is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that:

(a) concessions by the respondent as set out in the appendix to the reasons for judgment should be allowed,

(b) for the purpose of determining goods and services tax collectible for the reporting periods from 2000 to 2002, inclusive, the revenues should be consistent with those determined for purposes of the appeal under the *Income Tax Act*, and

(c) gross negligence penalties for reporting periods from 2000 to 2002, inclusive, should be deleted.

Signed at Toronto, Ontario this 9th day of October 2012.

"J. M. Woods"

Woods J.

Citation: 2012 TCC 352
Date: 20121009
Dockets: 2006-2525(IT)G
2006-2902(GST)I

BETWEEN:

GEOFFREY LAST,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Woods J.

[1] These are income tax and GST appeals by Geoffrey Last concerning three income-earning activities: a car business, trading in shares of InternetStudios.com, Inc. ("ISTO"), and temporary rentals of the appellant's residence. The issues generally involve the determination of revenue and expenses from each of the activities.

[2] The appeal under the *Income Tax Act* (ITA) relates to the 2000, 2001 and 2002 taxation years. The appeal under the *Excise Tax Act* (ETA) relates to the same period as well as 1998 and 1999.

[3] By way of overview, the tables below compare the positions of the parties in the income tax appeal. The first table sets out the income as assessed by the Minister

of National Revenue as reflected in the amended reply. The second table summarizes the appellant's position as set out in his written submissions (para. 207– 209).

Income as assessed by the Minister

	2000	2001	2002
Car Business	$ 39,949.75	$ 73,575.91	$ 314,545.02
Rental Income			69,523.99
ISTO trades – Cap. Gains			601,135.38

Income as per the Appellant

	2000	2001	2002
Car Business	$ 1,003.64	$ nil	$ (20,095.79)
Rental Income	5,052.80	8,460.29	34,707.90
ISTO trades – Bus. Income			117,414.00

[4] There are two unusual aspects to these appeals that are illustrated in the above tables and that are useful to mention by way of background. First, the gains from the share trading transactions were assessed by the Minister as capital gains and yet the appellant submits that they should be assessed as business income which is taxed at a higher rate. Second, the appellant agrees that rental income for 2000 and 2001 should be assessed even though it has not been assessed to date. These matters will be discussed below.

[5] At the commencement of the hearing, it appeared that the parties had made minimal progress in limiting the number of items of revenue and expenses that were in dispute. Significant progress was made throughout the hearing, however, particularly in the area of expenses. A summary of the concessions, which was provided by the Crown subsequent to the hearing, is reproduced in an appendix to these reasons.

[6] The discussion that follows is organized under the headings below.

- Background
- Credibility of witnesses

- Burden of proof
- Share transactions – 2002
- Car business – 2000 and 2001
- Car business – 2002
- Rental income – 2000 and 2001
- Rental income – 2002
- GST
- Conclusion

I. Background

[7] For several years, the appellant has carried on an automobile brokerage and consulting business as a sole proprietor under the name Last Motorcar Co. In general, income is generated from two sources: (1) consulting fees for assisting customers who purchase vehicles, and (2) profit from the purchase and resale of vehicles. The issues relating to this business involve the amount of revenue earned and the expenses incurred.

[8] The appellant also carries on share trading activities. The only period that is at issue is the 2002 taxation year, in which there is a dispute concerning the income attributable to trading in shares of InternetStudios.com, Inc., or ISTO, which is the corporation's former trading symbol.

[9] ISTO was a non-operating U.S. public corporation when it was acquired by three Canadian-based individuals in 1999 during the boom for technology start-ups (the "dot-com" boom). The vision of the founders, Robert MacLean, Michael Edwards and Mark Rutledge, was to create an online marketplace (like eBay) for filmed entertainment, such as movie rights.

[10] ISTO initially raised a significant amount of capital, but it ran out of funds early in 2001 just as the business was becoming operational. As at March 31, 2001, ISTO had a cumulative net loss of over $44 million and reported that it would have to cease operations unless further capital could be raised. By that time, the dot-com bubble had burst, and raising capital became very difficult.

[11] The appellant became acquainted with the founders of ISTO in the summer of 2001. He was instrumental in implementing a plan early in 2002 under which the corporation's shares were actively promoted by individuals who were hired for this purpose, called the investor relations team. According to a report filed with the United States Securities Exchange Commission (SEC), as at July 25, 2002 ISTO had

7 independent contractors providing "product development services, management consulting services and capital raising services" (page 18, annual report).

[12] At the same time that the investor relations team were hyping the shares, the appellant was issued shares of ISTO which he actively traded. He was assessed capital gains for that year in the amount of $601,135 relating to this activity.

[13] The Crown submits that the appellant was involved in a "pump and dump" operation, in which shares of a moribund company are promoted so that insiders can profit. The appellant vigorously denies this, and suggests that the aim was to stabilize the corporation so that it could raise further institutional financing and continue operations.

[14] Whether the operation was a pump and dump or not, the evidence strongly suggests that representations made in ISTO's filings with the SEC relating to the shares issued to the appellant were not accurate, with the strong implication that the appellant's trading activity was contrary to SEC rules.

[15] The share trading history of ISTO is set out in the SEC filings. In the quarter ended March 31, 2000 the share price was at a high of $448 (adjusted for a reverse stock split). In the quarter ended December 31, 2001, which was just before the appellant started trading, the price was at a high of $0.60 (2001 annual report, page 12). Following the work of the investor relations team and the active trading by the appellant, the share price increased. In the quarter ended March 31, 2003, the price was at a high of $1.91. The last information that I could find in the evidence was a trading price of $0.55 on April 8, 2004.

[16] There are two issues involving ISTO. The first is whether gains from the trading of ISTO shares is on income or capital account. The second is whether the appellant is entitled to a deduction for payments that he made to ISTO, either directly or for its benefit. It is the position of the Crown that the payments are loans, which are not deductible in the 2002 taxation year. The appellant takes the view that the payments are not loans.

[17] The third and final activity that is relevant to these appeals involves leasing the appellant's personal residence on a short-term basis to persons in the entertainment industry. This is a relatively minor issue.

II. Credibility of witnesses

[18] I would comment at the outset about the reliability of the testimony of the witnesses, since the testimony is relevant for many of the issues.

[19] The appellant was a central witness for his own case, and, for him to be successful, his testimony must be found to be reliable on the many issues where there is not satisfactory corroboration. In general, I am of the view that the appellant's testimony fell short of the mark on key issues and was not convincing.

[20] First, the objective evidence does not paint a promising picture regarding the appellant's credibility. He has shown a flagrant disregard for the statutory obligation to file proper and timely returns under the ITA and the ETA. During the relevant period from 1998 to 2002, the returns were filed late or not at all, certain sources of income were not reported, some of filings were inconsistent, and the appellant failed to remit some of the GST that he had collected.

[21] Second, in 2002 the appellant engaged in share trading activity that by all appearances was undertaken pursuant to false statements in filings with the SEC. The appellant struck me as a careful and astute person. It is just not believable that he was innocent of any wrongdoing in this activity.

[22] These circumstances do not necessarily make the appellant's testimony unreliable, but it suggests that great caution should be exercised.

[23] As for the testimony itself, generally I have found that it was often insufficiently detailed to be convincing, at times it was evasive, and on some key aspects it was implausible.

[24] The other witnesses that were called for the appellant were:

- Barrie Weiner, an accountant who assisted the appellant at the objections stage, including with the preparation tax returns,
- Timothy Quocksister, a car dealer who dealt with the appellant,
- Robert MacLean, one of the founders of ISTO,
- Michael Edwards, one of the founders of ISTO, and
- John Kirk, an experienced member of the investor relations team.

[25] The Crown called:

- John Dunham, an accountant who prepared tax returns for the appellant prior to the engagement of Mr. Weiner,

- Diana Chen, an auditor with the Canada Revenue Agency (CRA),
- Robert Spankie, a CRA auditor, and
- James Mise, a CRA appeals officer.

[26] As for the testimony of these witnesses, I have found their testimony to be generally reliable except for the testimony of ISTO founders, Mr. Maclean and Mr. Edwards, and one of the accountants, Mr. Dunham.

[27] As for Mr. MacLean and Mr. Edwards, they were two of three original founders of ISTO with active roles similar to a CEO and CFO, respectively. Both had a financial background. Each testified to having a limited understanding of the details of the plan involving ISTO's shares which was implemented in 2002. I found this testimony to be implausible and disingenuous.

[28] In an attempt to justify the witnesses' participation in SEC filings which appear to be improper, the testimony simply described the share arrangements as complex. This is not a satisfactory explanation. The evidence strongly suggests that documents filed with the SEC and signed by Mr. MacLean (and the appellant), contain false statements.

[29] An example is an SEC quarterly report for the period ended June 20, 2001 and signed by Mr. MacLean in July 2002. The report states that a loan in the amount of $199,159 was received from nine individuals in February 2001. It appears from the evidence that these were funds were not provided by nine individuals in 2001 but were provided by the appellant in 2002. The funds were used to subscribe for shares that were registered to nine individuals but all the shares were beneficially owned by the appellant. Mr. MacLean described the arrangement as a "debt-swap." By all appearances, it was simply an improper back-dating exercise.

[30] As for the testimony of Mr. Dunham, who had prepared the initial tax returns for the appellant, some of his explanations were not plausible. For example, he stated that revenue in the returns was over-stated and that he had an incorrect understanding of the threshold for filing GST returns. According to his testimony, he had the mistaken belief that there was no need to file GST returns if income was less than $30,000. At the time that this advice was allegedly given, the GST regime had been in place for many years and the threshold for filing would have been commonly understood by persons with Mr. Dunham's background. Overall, his testimony was not convincing.

[31] As for Mr. Weiner, I found his testimony to be generally reliable except for an

understandable bias in the appellant's favour.

III. Burden of proof

[32] I would also make a brief comment about the burden of proof because both counsel relied on principles which differ somewhat from the most recent pronouncements by the Federal Court of Appeal in cases such as *McMillan v The Queen*, 2012 FCA 126 and *Newmont Canada Corporation v The Queen*, 2012 FCA 214.

[33] The applicable principle is described in *McMillan* by Dawson J.A., at para. 7:

> […] In our respectful view, it is settled law that the initial onus on an appellant taxpayer is to "demolish" the Minister's assumptions in the assessment. This initial onus of "demolishing" the Minister's assumptions is met where the taxpayer makes out at least a *prima facie* case. Once the taxpayer shows a *prima facie* case, the burden is on the Minister to prove, on a balance of probabilities, that the assumptions were correct (*Hickman Motors Ltd. v. Canada*, [1997] 2 S.C.R. 336 at paragraphs 92 to 94; *House v. Canada*, 2011 FCA 234, 422 N.R. 144 at paragraph 30).

[34] As for the meaning of *prima facie*, this was discussed in *House v The Queen*, 2011 FCA 234, at para 57:

> [57] […] In *Amiante Spec Inc. v. Canada*, 2009 FCA 139, [2009] F.C.J. 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).

IV. Share transactions – 2002

A. *Background*

[35] The appellant actively traded shares of ISTO in 2002. During this period, the shares were traded in the United States using quotation services, such as NASD OTC Bulletin Board and Pink Sheets LLC.

[36] The Minister assessed capital gains from this activity for 2002 in the amount of $601,135. The proceeds of disposition were determined based on a review of brokerage statements, mainly statements of one brokerage firm called Golden Capital Securities Ltd. As for the cost of the shares and the characterization of the gains as capital, the Minister accepted the appellant's representations.

[37] The appellant does not dispute that he realized gains of $601,135, but he submits that the gains are ordinary income and not capital gains as assessed by the Minister. This unusual position is being taken in order to enable the appellant to deduct expenses relating to the income. The amount of the expenses that are being claimed are $483,721, leaving a net profit, according to the appellant, in the amount of $117,414 (AWS, para 63).

[38] As an alternative position if the gains are determined to be on capital account, the appellant suggests that the expenses should be added to the adjusted cost base of the ISTO shares.

[39] A number of questions are engaged with respect to ISTO: (1) What is the total amount of the payments? (2) What is their legal nature? (3) Are the gains on income or capital account? and (4) If the gains are on income account, is it appropriate for the Court to order a reassessment on this basis?

B. *Amount and legal nature of payments*

[40] When the appellant became involved with ISTO, he became its primary source of funding and paid most of its expenses. The expenses included legal and accounting expenses relating to the SEC filings, fees of the investor relations team, and what were described as legacy obligations, such as salaries that had not been paid.

[41] The appellant submits that he paid an aggregate of $483,721, of which $120,066 was for investor relations. Significant documentary support for these payments was provided.

[42] The Crown submits that the total is only $429,572, and that the payments were not expenses incurred but were loans to ISTO. This submission is supported by ISTO's financial statements as at December 31, 2002 and a document purporting to be an agreement between the appellant and ISTO made in October 2003 under which the parties agreed to exchange this loan for shares.

[43] There was very little evidence to support the appellant's position that the

payments were not loans, other than the appellant's own self-interested testimony. The testimony simply was not believable.

[44] The appellant testified that he had an informal arrangement with ISTO and that his understanding was that he was to be made whole for these expenditures in the sense of receiving compensation for having to sell shares in order to finance the payments. He also testified that the document made in October 2003 was not intended to be a binding agreement unless financing could be obtained. The explanation as a whole was lacking in detail and was not persuasive.

[45] Counsel for the appellant submits in the alternative that the payments are deductible because ISTO's obligation to repay was contingent. It is not necessary that I consider the correctness of this as a legal principle because I am not satisfied that ISTO's obligation was contingent. The collection of the loan may have been uncertain due to ISTO's financial situation, but this does not make the obligation itself contingent. To the extent that the appellant suggests that the obligation itself is contingent, his testimony is not convincing.

[46] I conclude that the appellant is not entitled to a deduction for any of the payments in the 2002 taxation year.

[47] In light of this finding, it is not necessary that I make a finding on the amount of the payments. Counsel for the appellant asked me to do this in any event so that it would expedite a claim for a deduction in a later year. I do not propose to do so because there is not sufficiently reliable evidence that gives a complete picture.

C. *Are payments on income or capital account*

[48] The appellant submits that the ISTO trading gains are business income. This position appears to be amply supported by the evidence. However, I do not think that the Court should order a reassessment on this basis since it would be statute barred. During argument, I asked the parties to address whether it would be appropriate for the Court to order the Minister to reassess on this basis and written submissions were subsequently received.

[49] The Crown submits that it is proper for the Court to order the Minister to reassess income in the amount of $601,135 on the basis that the ISTO gains are ordinary income as long as the 2002 reassessment does not increase the overall tax for 2002.

[50] The appellant submits that the Crown should not be ordered to reassess income more than $266,276.34, which was the taxable capital gain that was assessed. (My understanding is that this figure includes trading activity from other shares as well as ISTO shares.)

[51] In my view, it is not appropriate for the Court to require a reassessment that changes the character of the gains from capital to income, because the effect of this would be for the Minister to reassess beyond the limitation period set out in s. 152(4) and (4.01) of the ITA.

[52] The applicable principle applies equally to a new basis of assessment and a new argument pursuant to s. 152(9). Whether the Court should order a reassessment that would be a new basis of assessment was considered by Rothstein J.A. (as he then was) in *Pedwell v The Queen*, [2000] 4 FC 616; 2000 DTC 6405 (FCA):

> [16] First, if the Crown is not able to change the basis of reassessment after a limitation period expires, the Tax Court is not in any different position. The same prejudice to the taxpayer results -- the deprivation of the benefit of the limitation period. […]

[53] The same principle applies if the reassessment is pursuant to a new argument under s. 152(9). In *The Queen v Loewen*, 2004 FCA 146; 2004 DTC 6321, Sharlow J.A. comments:

> [22] A new argument asserted by the Crown pursuant to subsection 152(9) could include an argument that would justify an assessment that exceeds the amount assessed. However, subsection 152(9) does not relieve the Minister from subsection 152(4), which imposes time limitations on reassessments. Therefore, the Minister cannot use a subsection 152(9) argument to reassess outside the time limitations in subsection 152(4), or to collect tax exceeding the amount in the assessment under appeal.

[54] The question, then, is whether a reassessment that changes the ISTO gains from capital to income would be statute barred. In my view it would be. The limitation period will have expired unless the appellant has made a careless or negligent misrepresentation in the income tax return. It would be difficult for the Crown to suggest that he has when the Crown's primary argument in this appeal is that the gains are on capital account.

[55] I would conclude that it is not appropriate to require the ISTO gains to be reassessed as ordinary income.

V. Car business – 2000 and 2001

A. *Background*

[56] For purposes of the income tax assessments for 2000 and 2001, the Minister determined that the appellant earned income from the car business in the amounts of $39,948 and $73,576, respectively.

[57] The assessments did not allow any deduction for business use of the home, but at the hearing the Crown conceded that ten percent of home expenditures were deductible as expenses of the car business, except during periods that the residence was rented to third parties. The deductions that are conceded are $5,737.26 and $10,132.49 for 2000 and 2001, respectively.

[58] The appellant submits that the income from the car business was only $1,003.64 for 2000 and nil for 2001. He submits that he actually incurred a loss in the amount of $13,324.21 in 2001, but that the loss is disallowed under the ITA since it is attributable to home office expenses.

[59] There are two outstanding issues to be decided - the amount of revenue earned and whether an amount greater than 10 percent should be allowed for business use of the home.

B. *Determination of revenue*

[60] The first issue is the determination of revenue from the car business in 2000 and 2001. For purposes of the assessments at issue, the Minister assumed revenue in the amounts of $220,995 and $201,106. These amounts are based on figures reported by the appellant in his initial income tax returns that were prepared by Mr. Dunham.

[61] The appellant now disputes these amounts and relies on amounts he determined in collaboration with his new accountant, Mr. Weiner. It is submitted that the proper amounts of revenue are $180,570 and $143,464.

[62] The appellant's submission in a nutshell is that he has demolished the Minister's assumptions on a *prima facie* basis and that the Crown has not introduced any evidence in rebuttal.

[63] Looking at the situation from the 60,000 foot level, the question is really

whether it is believable that the appellant lost over $12,000 from the car business over a two-year period.

[64] The revenue amounts suggested by the appellant were determined by the appellant and Mr. Weiner at the objections stage based on source documentation provided by the appellant and submitted as evidence in this appeal. In light of the cavalier attitude that the appellant has displayed towards his tax obligations, as mentioned above, I have no confidence that the appellant has provided all relevant information. It would not be appropriate to give the appellant the benefit of the doubt on this.

[65] I would also note that no contemporaneous financial records were kept and the initial tax returns were filed late and used different numbers than the subsequent returns prepared by Mr. Weiner. The appellant suggests that his records are reliable because he kept all source documentation. The problem is that I am not satisfied that the documentation provided by the appellant is complete. If the appellant kept as meticulous records as he suggests, why did he not file tax returns on a timely basis? A *prima facie* case has not been made.

[66] Mr. Weiner testified that he had no reason to suspect that the appellant's documents were not complete. He also said that they were well organized. Aside from the problem that Mr. Weiner only had what the appellant had provided to him, I also note that there are significant discrepancies for the 2002 taxation year between what Mr. Weiner had determined as fee revenue (Ex A-8) and what the appellant now acknowledges is fee revenue (AWS, para. 107). The number of items of fee revenue was apparently increased from 10 to 24. This suggests that the documentation is not as complete as was suggested.

[67] For completeness, I would also briefly comment concerning evidence that was led by the Crown. The Crown introduced an SEC filing consisting of a 2004 prospectus for another start up corporation that the appellant had involvement with, Digital Ecosystems Corp. In the prospectus, the appellant's car business is represented to have had annual sales since inception of between $2 to 5 million (Ex. R-9).

[68] If this representation is accurate, it destroys the appellant's testimony as to revenues from the car business. However, I have no greater reason to believe the accuracy of this statement than the appellant's testimony at the hearing. I have given no weight to the accuracy of the statement.

[69] Based on the findings above, no adjustment will be made to revenue of the car business as determined by the Minister for the 2000 and 2001 taxation years.

C. *Deduction for business use of home*

[70] The appellant lives in a 3,000 square foot condominium in downtown Vancouver. During the relevant period, the residence was also used as the appellant's only fixed premises for the car business.

[71] The appellant testified that he used a bedroom exclusively as an office, that the kitchen was used for business meetings, and that his parking spaces were used for the business. He submits that a reasonable allocation of home expenses to the car business is 33 percent (during periods that the residence was not leased).

[72] As mentioned earlier, the Crown submits that the business allocation should be 10 percent.

[73] In reference to the appellant's position, I am troubled that there is no reliable evidence as to how often the appellant met business contacts at his home. I propose to make some adjustment, however, as ten percent assumes very slight business use of the space. I propose to allow 20 percent as a reasonable allocation to the car business for periods that the property was not leased.

VI. Car business – 2002

A. *Background*

[74] The Minister initially made an arbitrary assessment for the 2002 taxation year because no income tax return had been filed. The appellant subsequently filed an income tax return which reported income from the car business in the amount of $29,324.

[75] The CRA then undertook a deposit analysis of the appellant's bank accounts and brokerage statements and determined that the appellant had income in the amount of $314,545 from the car business for the 2002 taxation year. A large portion of this is represented by unexplained bank deposits.

[76] In this appeal, the appellant suggests that the income tax return filed by him after the arbitrary assessment overstates his income from the car business. He submits that a loss was incurred in the amount of $20,095.79 (AWS, para. 58).

[77] At the hearing, the Crown conceded some additional expenses which are set out in the appendix. After taking these into account, the income from the car business as submitted by the Crown appears to be in the neighbourhood of $275,000.

[78] There are two questions to be determined in respect of the car business in 2002: (1) what is the revenue, and (2) what is appropriate deduction for business use of home.

[79] As a preliminary point, I would mention that the Minister assumed that the unexplained deposits were revenue from the car business as opposed to some other source and the pleadings limited the issue to determining income from the car business.

[80] The appellant's response to this argument is that the deposits are not revenue from the car business. His counsel submits that he should succeed on this issue even if the evidence suggests that the revenue is from some other unidentified income source.

[81] During the hearing, the Crown applied to amend its reply to frame the issue more broadly - that the unexplained deposits are income from any source. The application was made on the fourth day of the hearing. I concluded was that it was too late for the Crown to make this change. The appellant had already presented three days of evidence and his trial strategy had been based on the existing pleadings. I also rejected a further argument of the Crown made at the same time that the reference in the reply to the term "car business" includes ISTO share trading activity.

[82] In light of these findings, the issue to be determined is not whether the unexplained deposits are income any source, but whether they are income from the car business.

B. *Are unexplained deposits revenue from car business?*

[83] The CRA auditor who conducted the deposit analysis identified over $500,000 of deposits which she attributed to revenue from the car business. The vast majority of these amounts were deposits into the appellant's business and personal bank accounts with TD Canada Trust.

[84] It is the position of the appellant that his gross revenue from the car business in 2002 was $214,576.56 (AWS, para. 84). This consists of proceeds from car sales in

the amount of $197,647 and fee revenue in the amount of $16,929. He submits that the unexplained deposits are principally transfers from brokerage accounts representing ISTO share trades which have already been subject to tax.

[85] In general, I have the same difficulty with the appellant's position on this issue that I have with several others; it is based to a large extent on the appellant's own testimony. I have no confidence that it is reliable.

[86] There was very little support for most of the testimony relating to the unexplained deposits. Few source documents were introduced and very little reconciliation was provided for the purported transfers from the brokerage accounts to the bank accounts.

[87] The appellant had various explanations as to why many of the withdrawals from the brokerage accounts and the deposits to the bank accounts do not match up. Some of the explanations are simply not plausible. For example, the appellant testified that he took money out of the brokerage accounts in the form of bank drafts and kept some of it at home until it was needed and then deposited it into a bank account. It seems unlikely that the appellant would do this.

[88] The appellant also relies on the testimony of Mr. Weiner. It is suggested that Mr. Weiner reviewed the bank statements and concluded that the revenue reported by the appellant was plausible. Mr. Weiner suggested that, although he was not conducting an audit, he had an ethical responsibility to disengage if he believed that the numbers were misleading (Testimony of Barrie Weiner, p. 103, 104).

[89] This testimony is of little assistance to the appellant. If potential evidence existed that satisfied Mr. Weiner as to the source of the deposits in the bank accounts, the evidence could have been provided at the hearing. The absence of this evidence suggests that Mr. Weiner probably relied on self-serving statements by the appellant as to the source of the deposits.

[90] I would also comment concerning the appellant's submissions at paragraph 127 of his written submissions.

[91] First, the appellant points out that the income for 2002 as suggested by the Crown vastly exceeds the income for prior years. I do not find this convincing because there is no evidence that the CRA conducted thorough audits for the prior years.

[92] The appellant also submits that he only made a modest profit on each car transaction. He suggests that to earn the amount of income suggested by the Crown, he would have had to complete an additional 354 transactions in 2002.

[93] This argument is also not convincing. There is no reliable evidence on which I could determine how much income might reasonably be made by this type of business.

[94] The appellant also submits that the round number deposits of $2,000, $3,000 and $5,000 do not fit with the evidence of the revenue generated by each transaction. The main problem that I have with this argument is that I have no confidence that the appellant's evidence provided a complete and accurate picture of his business.

[95] The final argument that was made in this part of the appellant's written submissions has some merit. The argument is that the revenue from the car business was exclusively Canadian and yet numerous unexplained deposits are represented by bank drafts denominated in United States dollars. Based on the bank deposit analysis in Ex. R-18, the U.S. deposits are approximately Cdn $150,000.

[96] I accept that the appellant has made a *prima facie* case on the U.S. denominated deposits. This conclusion is not based solely on the appellant's own testimony, but it is based on the evidence as a whole which suggests that the appellant's customers were generally Canadian. In order for the Crown to suggest that the business had substantial revenues in U.S. dollars, there should be some evidence to support this. None was provided.

[97] Turning to the submissions of the Crown, the Crown argues that the appellant can only succeed in disputing the deposit analysis by establishing the actual source of the unexplained deposits. Counsel relies on cases such as *Lacroix v The Queen*, 2008 FCA 241, 2009 DTC 5029.

[98] I disagree with this submission. The issue in this case is whether the unexplained deposits are income from the car business. In *Lacroix*, the issue was simply whether the assessed amounts were income from any source. It makes sense in those circumstances that a taxpayer can succeed only by establishing the actual source.

[99] In the present appeal, it is not necessary for the appellant to establish the actual source of the deposits. The appellant is entitled to succeed by establishing that the car business produced less income than that assumed by the Minister.

[100] The appellant's luxury condominium suggests a lifestyle that is at odds with the income that he suggests he earned in the years under appeal. For example, the monthly mortgage payments appear to be in the range of $10,000. The appellant testified that a foreclosure action was started on the property in 2001, but it appears that the foreclosure was averted.

[101] Although the appellant's income is very likely to have been under-reported, the task is simply to determine whether the appellant has made a *prima facie* case that the unexplained deposits are not from the car business. The actual source of the deposits is not revealed but this is not fatal to the appellant's claim.

[102] I have concluded that the appellant has been partially successful on this issue and that the revenue as determined by the deposit analysis should be reduced by $170,000. This amount has not been calculated with mathematical precision but takes into account three items: U.S. dollar deposits of approximately $150,000, a damage deposit in the amount of $10,000 which is acknowledged to be related to the condominium, and other miscellaneous items.

[103] Before leaving this issue, I would comment briefly concerning testimony of John Kirk (investor relations consultant) that the appellant had a full time role at ISTO (Transcript, page 997). The question that should be asked is whether the appellant's work for ISTO restricted his ability to earn income from the car business in 2002. Neither party mentioned this in their submissions.

[104] The conclusion that I have reached is that Mr. Kirk's testimony is not detailed enough for me to conclude that the appellant's work with ISTO significantly impacted the revenues from his car business. It is quite plausible that the appellant attended at ISTO's premises, which were near his condominium, on a regular basis to provide oversight and consultation. It does not follow that his presence reduced his ability to devote time to the car business.

C. *What is appropriate deduction for business use of home?*

[105] The analysis concerning the business use of the home during 2000 and 2001 is also relevant for the 2002 taxation year. An amount equal to 20 percent of the home expenses incurred when the residence was not leased will be allowed as a deduction relating to the car business for 2002.

[106] A further issue relating to 2002 home expenses concerns amounts totalling

$15,000 that the appellant paid to a law firm. The appellant suggests that these are legal fees relating to a foreclosure action on his condominium and that a *pro rata* amount should be allocated to business use.

[107] The Crown submits that there is not sufficient evidence to link the expense with the foreclosure action.

[108] I would first note that the law firm who received the funds was not the appellant's law firm, but was the firm that represented the bank that initiated the foreclosure action. I would also note that the funds were paid to the law firm in trust.

[109] The appellant has not established a *prima facie* case that these amounts represent legal expenses. The amounts could be payments on account of overdue mortgage payments that may have already been deducted by the appellant on an accrual basis. The appellant's vague and brief testimony that they were legal expenses is not credible.

VII. Rental income – 2000 and 2001

[110] In the 2000 and 2001 taxation years, the appellant earned income from short-term rentals of his personal residence in the amounts of $5,052.80 and $8,460.29.

[111] The appellant did not report this income in his income tax returns and the Minister did not include it in the assessments at issue. The income was acknowledged in the appellant's amended notice of appeal.

[112] There is no dispute between the parties in respect of this source of income. They are in agreement that the amounts above should be added to income.

[113] Notwithstanding the agreement of the parties, this item is worthy of some comment because the Court is not bound by the parties' agreement.

[114] The applicable principle is that the consent of the parties should be given effect unless it is contrary to the ITA: *Petro-Canada v The Queen*, 2004 FCA 158, para. 66.

[115] In my view, it is reasonable to conclude that a reassessment now to include this income would not be contrary to the ITA because a reassessment of the rental income would not be statute barred. In particular, it is reasonable to conclude that the

appellant made a misrepresentation in his income tax returns based on carelessness, negligence or wilful default by not reporting the income.

VIII. Rental income – 2002

[116] The appellant also earned rental income in the 2002 taxation year, which was included in the assessment at issue.

[117] Two items are in dispute in relation to this income: (1) the deductibility of amounts paid to a law firm in the amount of $15,000, and (2) whether a damage deposit in the amount of $10,000 should be included in income.

[118] As for the amounts paid to the law firm, earlier in these reasons I concluded that these payments are not deductible in computing income from the car business. The same reasoning applies to the computation of rental income. No adjustment will be made to the rental income for the payments to the law firm.

[119] As for the damage deposit in the amount of $10,000, this amount was included as part of income from the car business pursuant to the deposit analysis undertaken by the Minister. It is now acknowledged that the deposit, which was never returned, relates to the rental business and not the car business.

[120] The Crown submits that this amount should be included in rental income (Respondent's Rebuttal Submissions, para. 17). I would disagree. As this issue was not raised in the pleadings, I would conclude that it is too late to make this adjustment now.

IX. GST

A. *Background*

[121] At the hearing, the GST appeal did not receive nearly the same attention as the income tax appeal. The appellant's submissions in particular were relatively brief.

[122] By way of background, the appellant did not file GST returns for 1998 and 1999, and did not remit any tax for these years even though GST had been collected on some transactions. Returns were filed for 2000, 2001 and 2002 which reported a modest amount of net tax.

[123] The CRA audit actually commenced as a review of GST for 2000, 2001 and

2002. The audit was subsequently expanded to include GST for 1998 and 1999 as well as income tax for 2000, 2001 and 2002. A GST assessment was issued in 2006 which encompassed net tax for all periods between 1998 and 2002.

[124] The table below compares the net tax as filed by the appellant and as assessed by the Minister.

Period Ending	Net Tax as Filed	Net Tax as Assessed
1998-12-31	$ n/a	$ 31,796.45
1999-12-31	n/a	14,411.67
2000-12-31	538.17	3,276.37
2001-12-31	161.46	10,086.75
2002-12-31	639.33	23,564.64
Total	1,338.96	83,135.88

[125] For the 2000, 2001 and 2002 reporting periods, the determination of net tax should be consistent with the conclusions above relating to the income tax appeal. That is not the case for 1998 and 1999, however, as the income tax appeal does not encompass these years.

B. *1998 and 1999 reporting periods*

[126] The general methodology used by the Minister in assessing net tax and penalties for 1998 and 1999 was as follows: (1) GST collectible was determined by the revenue reported in income tax returns, (2) no input tax credits were allowed, and (3) gross negligence penalties were imposed.

[127] It is worthwhile mentioning that the Crown conceded at the hearing that no gross negligence penalties should be imposed for 1998 and 1999 because the relevant provision only applies if returns have been filed: *Lee v The Queen*, 2010 TCC 400.

[128] The amount of input tax credits have been agreed by the parties and are set out in the appendix.

[129] The only issue that remains outstanding regarding 1998 and 1999 is the amount of revenue, or GST collectible (AWS Reply, at para. 34).

[130] The appellant introduced source documentation to support the revenue from the car business for these years. For the same reasons discussed above in respect of

income earned from the car business in 2000 and 2001, I have no confidence that the documentation provided by the appellant for 1998 and 1999 is complete. No adjustment will be made to the assessment for GST collectible for 1998 and 1999.

C. *2000, 2001 and 2002 reporting periods*

[131] As for the 2000, 2001 and 2002 reporting periods, the issues that remain to be decided are the amount of GST collectible and gross negligence penalties (AWS in Reply, para. 34).

[132] As for the GST collectible, this should follow the revenue determined for purposes of the income tax appeal.

[133] As for the gross negligence penalties, the problem that I have with the imposition of the penalties is that the evidence as a whole does not provide a very complete picture and the Crown has the burden. The income tax appeal turned to a great extent on the appellant not providing sufficient reliable evidence. With respect to GST penalties, the Crown has not presented sufficient evidence to warrant the penalties.

[134] As for 2000 and 2001, the Crown relies on revenue as reported in the income tax returns filed by the appellant. The evidence is insufficient to establish the reliability of these amounts.

[135] As for 2002, the Crown relies on the deposit analysis. Again, the evidence is insufficient to establish the reliability of the source of the unexplained deposits. For example, it is quite possible that many of the deposits came from ISTO trades that were not part of the capital gains that were assessed. In this case, the income would not be subject to GST. I would conclude that the Crown has provided insufficient evidence to support the gross negligence penalties.

X. Conclusion

[136] With respect to assessments under the ITA for the 2000, 2001 and 2002 taxation years, the appeal will be allowed, and the assessments will referred back to the Minister for reassessment on the basis that:

(a) the concessions by the Crown as set out in the appendix be allowed,

(b) the revenue from the car business for the 2002 taxation year be

reduced by $170,000,

(c) 20 percent of home expenses be allocated to the car business for periods in which the home was not leased, and

(d) rental income in the amounts of $5,052.80 and $8,460.29 for the 2000 and 2001 taxation years, respectively, should be added to the income of the appellant.

[137] With respect to an assessment under the ETA for the 1998, 1999, 2000, 2001 and 2002 taxation years, the appeal will be allowed, and the assessment will referred back to the Minister for reassessment on the basis that:

(a) the concessions by the Crown as set out in the appendix be allowed,

(b) for the purpose of determining GST collectible for reporting periods from 2000 to 2002, inclusive, the revenues should be the amounts as determined for purposes of the appeal under the ITA, and

(c) gross negligence penalties for the 2000 to 2002 reporting periods, inclusive, should be deleted.

[138] The appellant has requested an opportunity to make written submissions as to costs. The appellant's submissions should be received by the Court within 10 days, the respondent shall have a further 10 days to reply, and the appellant shall have a further 10 days to respond.

Signed at Toronto, Ontario this 9th day of October 2012.

"J. M. Woods"

Woods J.

APPENDIX

Geoffrey O. Last v. Her Majesty the Queen
2006-2525(IT)G and 2006-2902(GST)I

List of Respondent's Concessions

APPEAL NO. 2006-2525(IT)G

A. With respect to the 2000 taxation year, the Respondent states as follows:

Rental Income

(a) the parties agreed that the Appellant earned rental revenue in the amount of $62,000.00;

(b) the Appellant is entitled to deduct rental expenses in the amount of $56,947.20;

(c) accordingly, the Appellant's net rental income is $5,052.80;

Car Business Income

(d) if the Respondent's gross revenue figures are accepted by the Court, the expense amounts allowed by the Minister should remain at $181,045.92 as assessed in 2000;

(e) if, however, the Appellant's gross revenue figures are accepted by the Court, which figures are not conceded by the Respondent, the business expenses (not including business-use-of-home expenses) should be reduced to $160,442.35 in 2000 as conceded by the Appellant;

Business-Use-of-Home Expenses

(f) the Appellant incurred condominium expenses in the amount of $57,372.64 during the period in 2000 in which the Appellant operated the Car Business at the Condominium; and

(g) the Appellant is entitled to deduct 10 percent, or $5,737.26, as business-use-of-home expenses in 2000;

B. With respect to the 2001 taxation year, the Respondent states as follows:

Rental Income

(a) the parties agreed that the Appellant earned rental revenue in the amount of $9,300.00;

(b) the Appellant is entitled to deduct rental expenses in the amount of $839.71; and

(c) accordingly, the Appellant's net rental income is $8,460.29;

Car Business Income

(d) if the Respondent's gross revenue figures are accepted by the Court, the expense amounts allowed by the Minister should remain at $127,530.15 as assessed in 2001; and

(e) if, however, the Appellant's gross revenue figures are accepted by the Court, which figures are not conceded by the Respondent, the business expenses (not including business-use-of-home expenses) should be reduced to $123,013.89 in 2001 as conceded by the Appellant;

Business- Use-of-Home Expenses

(f) the Appellant incurred condominium expenses in the amount of $101,324.85 during the period in 2001 in which the Appellant operated the Car Business at the Condominium; and

(g) the Appellant is entitled to deduct 10 percent, or $10,132.49, as business-use-of-home expenses in 2001;

With respect to the 2002 taxation year, the Respondent states as follows:

Rental Income

(a) the Appellant rented the Condominium for 28 days out of a total of 365 days during 2002;

(b) the parties agreed that the Appellant earned rental revenue in the amount of $42,250.00; and

(c) the Appellant is entitled to deduct rental expenses in the amount of at least $9,391.46;

Car Business Income

(d) the Appellant is entitled to deduct the following additional expenses (not including business-use-of-home expenses) in respect of the Car Business:

(i.) the amount of $1,070.00 in respect of a Mazda 323;

(ii.) the amount of $18,000.00 in respect of a 96 GMC I Ton;

(iii.) the amount of $6,500.00 in respect of amounts paid to Silver Arrow; and

(iv.) the amount of $12,500.00 in respect of accrued expenses to Silver Arrow

resulting in total expenses (not including business-use-of-home expenses) in the amount of $234,287 in respect of the Car Business;

Business-Use-of-Home Expenses

(e) the Appellant incurred condominium expenses totaling $110,125.58 (which includes interest of $4,118.82 paid on appliances) in 2002;

(f) the Appellant operated the Car Business at the condominium for 337 days out of a total of 365 days during 2002; and

(g) the Appellant is entitled to deduct 10 percent, or $10,167.76, as business-use-of-home expenses in 2002;

The Internetstudios.com Inc. Shares

(h) the total cost of the shares of InternetStudios.com, Inc. ("ISTO") that the Appellant bought and sold in 2002 in his own name was $335,158.70;

(i) the total proceeds of the shares of ISTO that the Appellant bought and sold in 2002 in his own name was $936,294.00; and

(j) the Appellant lent money to and paid money on behalf of ISTO in 2002 in the amount of at least US $273,543.00 (being $429,571.93, based on an average annual exchange rate of 1.5704).

APPEAL NO. 2006-2902(GST)I

With respect to the GST appeals, the Respondent has made the following concessions:

(a) the parties agreed that the Appellant was entitled to claim the following additional input tax credits:

(i) in the reporting period ending December 31, 1998, the amount of $6,323.99;

(ii) in the reporting period ending December 31, 1999, the amount of $7,975.51;

(iii) in the reporting period ending December 31, 2000, the amount of $12,473.93;

(iv) in the reporting period ending December 31, 2001, the amount of $4,106.80; and

(v) in the reporting period ending December 31, 2002, the amount of $13,824.09.

(b) gross negligence penalties assessed in respect of the reporting periods ending December 31, 1998 and 1999 should be vacated.

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