

Docket: 2004-513(IT)I

BETWEEN:

HONG XIAO,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

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Appeals heard on July 18, 2005 at Toronto, Ontario.

Before: The Honourable Justice G. Sheridan

Appearances:

For the Appellant: The Appellant herself

Counsel for the Respondent: Kandia Aird

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JUDGMENT

The appeals from the reassessments made under the *Income Tax Act* for the 2000 and 2001 taxation years are allowed, without costs, and the reassessment is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that the Minister ought to have allowed employment expenses of \$2,073.83 for 2000 and \$803.86 for 2001 as set out in paragraph 16 of the Reply to the Notice of Appeal in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Canada, this 5th day of August 2005.

"G. Sheridan"

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Sheridan, J.

Citation:2005TCC489  
Date: 20050805  
Docket: 2004-513(IT)I

BETWEEN:

HONG XIAO,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

### **REASONS FOR JUDGMENT**

#### **Sheridan, J.**

[1] The Appellant, Xiao, appealed the reassessments made by the Minister of National Revenue of her 2000 and 2001 taxation years in which he disallowed employment expenses claimed by Ms. Xiao for “compensation” to clients, work space in home, office equipment leasing and transportation costs.

[2] As a preliminary matter, counsel for the Respondent advised the Court that in the Notices of Reassessment for each of the taxation years, the employment expense amounts allowed had been understated by \$2,073.83 for 2000 and \$803.86 for 2001. On this basis alone, the Crown submitted that the appeals ought to be allowed and the matter referred back to the Minister for reconsideration and reassessment to allow the deduction of these additional amounts. In respect of the issues raised in Ms. Xiao’s Notice of Appeal, however, the Minister’s position was that her appeals ought not to be allowed. Counsel for the Respondent argued that although Ms. Xiao had satisfied the threshold criteria to claim employee deductions under subparagraph 8(1)(f) of the *Income Tax Act*, she had not met her evidentiary burden of substantiating such expenditures; or alternatively, that even if they were incurred, it was not for the purpose of earning employment income, nor were they reasonable under subsection 67 of the *Act*.

[3] In Schedule “A” to the Reply to the Notice of Appeal are set out the amounts claimed by Ms. Xiao, the amounts allowed by the auditor and/or by the Appeals Officer following the filing of Ms. Xiao’s Notice of Objection. Summarized in chart form below is the history of the claims in respect of the four categories above:

For 2000:

| Category         | Claimed   | Audit Amount | Appeal Amount | Total Allowed |
|------------------|-----------|--------------|---------------|---------------|
| Compensation     | 10,772.50 | 0.00         | No Change     | 0.00          |
| Work space       | 7,993.17  | 715.50       | No Change     | 715.50        |
| Office Equipment | 10,178.43 | 0.00         | 5,778.00      | 5,778.00      |
| Transportation   | 735.00    | 0.00         | No Change     | 0.00          |

For 2001:

| Category         | Claimed  | Audit Amount | Appeal Amount | Total Allowed |
|------------------|----------|--------------|---------------|---------------|
| Compensation     | 1,800.00 | 0.00         | No Change     | 0.00          |
| Work space       | 1,659.12 | 445.54       | No Change     | 445.54        |
| Office Equipment | 437.13   | 0.00         | 437.13        | 437.13        |
| Transportation   | 1,755.22 | 0.00         | No Change     | 0.00          |

[4] As can be seen from the above chart, Ms. Xiao was partially successful at the departmental appeals stage in substantiating the amounts claimed. At the hearing, she argued that she ought to have been allowed the full amounts, although most important to her were the “compensation” amounts in 2000 and 2001. To succeed in these appeals, Ms. Xiao had the burden of proving the Minister’s assumptions wrong. This task was made difficult by Ms. Xiao’s failure to comply with her obligation under the *Income Tax Act* to keep adequate books and records to support the claims made.

[5] Ms. Xiao represented herself and was the only witness to testify. She immigrated to Canada from China in 1991. She had some university-level education in China and took one year of accounting at Seneca College before beginning work as a securities broker in 1998. In 2000 and 2001, she continued to be employed in this position although by that time, her employer was known as Westminster Securities Inc. Ms. Xiao worked out of an office in the home she shared with her husband Weizhen Tang whose business, Weizhen Tang and Associates Inc., was also conducted from the residence. Although her main contact with clients was at meetings or seminars conducted at her home office, Ms. Xiao occasionally had to call on clients; for this purpose, she used a car rented from Weizhen Tang and Associates Inc. Ms. Xiao did not maintain what would be considered normal accounting journals of her business transactions. Her records-keeping consisted of making notes from time to time of some expenditures in separate (but unidentified and not produced)

“books” and of putting some invoices (also not produced) in files for her accountant’s reference at tax time. Many of her dealings were in cash, a method she explained was not considered out of the ordinary in China. It is against this background that each of the four categories is considered below.

#### 1. “Compensation” to Clients

[6] In 2000, Ms. Xiao was required to pay to her employer Westminster \$10,772.50 as reimbursement for the company’s share of an arbitration award made to a dissatisfied client. I accept her evidence that Westminster looked to her for payment and that in due course the company was reimbursed. The only question is whether Ms. Xiao herself made this expenditure. In support of her assertion that she paid this amount, Ms. Xiao put in evidence a copy of a letter describing the arbitration result, a bank draft in this amount payable to Westminster and a copy of a letter from a former Westminster representative<sup>1</sup> to counsel for the Respondent confirming the payment. Ms. Xiao testified that because she didn’t have the money at the time, she borrowed the \$10,772.50 from a close family friend. Because she borrowed from a friend rather than a bank, she had no receipts or other documents that would normally evidence the transaction. In addition to having no documentary evidence to substantiate her version of events, she was unable to call her friend to testify at the hearing because he was out of the country. She testified that she made two payments plus interest. She added that she paid partly in cash by cashing her commission cheques and partly in kind, on one occasion by buying a computer for her friend’s immigrant parents and assisting them in other ways to make their way in their newly adopted country. This, she said, is enough between friends. It is not enough, however, to support her claim that she incurred the cost of the reimbursement.

[7] In 2001, Ms. Xiao was again confronted with unhappy clients. Because of her close relationship with them, this time on her own initiative, she decided to reimburse them for their investment losses of \$1,800. Describing this expense as “client compensation”, Ms. Xiao produced photocopies of two receipts, one for \$500 and another for \$1,300 to show she had paid these amounts. The difficulty with these receipts is that they are made out to either Weizhen Tang or Weizhen Tang and Associates Inc. I do not accept Ms. Xiao’s explanation that this was merely an oversight because her husband happened to be the person who answered the door the day the clients came to pick up the money and make out the receipts, especially since

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<sup>1</sup> Exhibit A-1

each receipt bears a different date. From her testimony, it is clear that both Ms. Xiao and her husband have sufficient business experience to have understood the importance of ensuring a receipt to be used in support of a deduction the Appellant herself described as important, be made in favour of the actual payor.

[8] Ms. Xiao argued that for transactions between friends, formal records-keeping is not necessary. When the objective is to support employee expense deductions under the *Act*, especially for transactions between the taxpayer and friends or family, books and records sufficiently adequate to substantiate such claims are crucial to the taxpayer's success. On the evidence presented, I am not satisfied that Ms. Xiao personally paid the "compensation amounts" claimed in 2000 or in 2001.

## 2. Work Space in Home

[9] Ms. Xiao and her husband and two children live in a detached two-storey four-bedroom house. In 2000, Ms. Xiao claimed 25 percent of the total amounts paid for mortgage interest and other such costs in respect of the Xiao-Tang residence. In 2001, she claimed only 8 per cent although the nature of the business was the same and the same area of the house was used for office purposes<sup>2</sup>. After noting this discrepancy, the Minister reassessed allowing a deduction based on the 8 per cent calculation for both years. Ms. Xiao testified that the lesser amount was claimed in 2001 because she had worked for Westminster for only a few weeks in 2001. She objected to this reduction saying that the Appeals Officer had misinterpreted the information<sup>3</sup> she provided showing the square footage of the house and failed to understand what areas were dedicated to office use. On cross-examination, Ms. Xiao explained that the living room and dining room were used exclusively for her home office as well as the kitchen for preparation of coffee and snacks during seminars. Though pressed to explain what portion of the same space was used for her husband's home-based business, Ms. Xiao could be no more specific than to say it was a very small part because Weizhen Tang and Associates Inc. did not need much space. There was no other evidence before the Court to show the floor plan or dimensions of the rooms. The department's calculations were based on information easily available to and provided by the Appellant herself. I am not satisfied that Ms. Xiao discharged the onus of rebutting the Minister's assumptions for either 2000 or 2001 to permit me to reach a different conclusion than that already assessed by the Minister.

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<sup>2</sup> The rationale for this method of calculation was not made clear at the hearing.

<sup>3</sup> Exhibit R-5

### 3. Office Equipment Leasing

[10] In 2000 and 2001, Ms. Xiao leased computer software from her husband's business, Weizhen Tang and Associates Inc., in respect of which she claimed expenses of \$10,178.43 in 2000 and \$437.13 in 2001. The Minister allowed the full amount for 2001 and approximately half of the deduction claimed in 2000. Ms. Xiao argued that she was entitled to the full deduction. Although invoices<sup>4</sup> for the leasing charges from Weizhen Tang and Associates Inc. to Ms. Xiao were put in evidence, Ms. Xiao had no bookkeeping records, cancelled cheques, banking statements for herself or Weizhen Tang and Associates Inc. to show that the amounts shown in the invoices had been paid. Entered as an exhibit was a copy of a list of payments<sup>5</sup>, hand-written by Ms. Xiao for Agency officials setting out the payments made. There is no direct co-relation between the amounts shown in the invoices and those in the hand-written list. Ms. Xiao explained that she had referred to "payment slips" when preparing the list for the CRA official but these documents were not put in evidence. As was the case above, the evidence before me is insufficient to support claims in excess of what was allowed by the Minister, especially for transactions occurring between non-arm's length parties.

### 4. Transportation Expenses

[11] In 2000, Ms. Xiao claimed transportation expenses of \$735 for miscellaneous costs such as gas and parking tickets; in 2001, \$1,755.22 which included rental costs paid to Weizhen Tang and Associates Inc. for the use of a car owned by her husband's company. Although at odds with Ms. Xiao's earlier evidence that most of her work was with clients at her home office, her testimony was that driving became a necessity in 2001 when Westminster moved its office from Toronto to Oakville. In any event, the primary problem she faced in proving her entitlement to these deductions was again, the lack of documentation to show these amounts were actually paid. Ms. Xiao testified that she had shown cancelled cheques to the CRA official but she did not feel it necessary to bring them to the hearing. Consequently, there was nothing before me to support her assertion that she had paid her husband's company for the use of the company car.

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<sup>4</sup> Exhibit R-2

<sup>5</sup> Exhibit R-3

[12] For the reasons set out above, these appeals are allowed and referred back to the Minister for reconsideration and reassessment on the basis that the Minister ought to have allowed employment expenses of \$2,073.83 for 2000 and \$803.86 for 2001 as set out in paragraph 16 of the Reply to the Notice of Appeal.

Signed at Ottawa, Canada, this 5th day of August 2005.

"G. Sheridan"

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Sheridan, J.

CITATION: 2005TCC489  
COURT FILE NOS.: 2004-513(IT)I  
STYLE OF CAUSE: Xiao v. HMQ  
PLACE OF HEARING: Toronto, Ontario  
DATE OF HEARING: July 18, 2005  
REASONS FOR JUDGMENT BY: The Honourable Justice G. Sheridan  
DATE OF JUDGMENT: August 5, 2005

APPEARANCES:

Counsel for the Appellant: The Appellant herself

Counsel for the Respondent: Kandia Aird

COUNSEL OF RECORD:

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Name:

Firm:

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