Docket: 2009-1545(IT)I

BETWEEN:

HAGOP HANNA,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on May 17, 2010, at Montréal, Quebec.

Before: The Honourable Justice Robert J. Hogan

Appearances:

For the appellant:	The appellant himself
Counsel for the respondent:	Antonia Paraherakis

JUDGMENT

The appeal from the reassessments made pursuant to the *Income Tax Act* for the 2002, 2004 and 2005 taxation years is dismissed.

The appeal from the reassessment for the 2003 taxation year is allowed in part, without costs, and the case is referred back to the Minister of National Revenue for reconsideration and reassessment so that $14,802 is added to the appellant's income instead of $19,834 to take into consideration the $5,032 reduction of income allowed by the respondent, in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Canada, this 7th day of September 2010.

"Robert J. Hogan"

Hogan J.

Translation certified true
on this 12th day of October 2010.

Elizabeth Tan, Translator

Citation: 2010 TCC 442
Date: 20100907
Docket: 2009-1545(IT)I

BETWEEN:

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REASONS FOR JUDGMENT

Hogan J.

Introduction

[1] This is an appeal regarding the 2002, 2003, 2004 and 2005 taxation years. The Minister of National Revenue (the "Minister") issued reassessments to the appellant using alternative assessment methods. Following an audit conducted by the Ministère du Revenu du Québec ("MRQ"), the Minister adopted the MRQ's findings regarding the 2002, 2003 and 2004 taxation years, making a few changes, and based the reassessments on a method that took into consideration the appellant's monetary flow and expenses during the years in question. Regarding the 2005 taxation year, the reassessment was based on an analysis of deposits the appellant made in his bank accounts during the year in question.

[2] The appellant reported $12,762, $13,240, $10,706 and $13,600 as net business income in his tax reports for the 2002, 2003, 2004 and 2005 taxation years, respectively. The Minister made the following changes for the years in question:

(a) revision of net business income, to $20,258 for 2002; $19,834 for 2003; $52,162 for 2004; and $26,759.09 for 2005;

(b) assessment of gross negligence penalties of $1,645.05 for 2002; $1,614.18 for 2003; $4,410.73 for 2004; and $1,820 for 2005.

[3] The issues in question are:

(a) whether the reassessments dated July 8, 2008, regarding the 2002, 2003 and 2004 taxation years were valid;

(b) whether, in that case, when calculating the appellant's income for the 2002, 2003 and 2004 taxation years, the Minister was justified in adding the respective amounts of $20,258, $19,834 and $52,162 as "Other Income";

(c) whether the Minister was justified in adding $26,750 when calculating the appellant's business income for the 2005 taxation year; and

(d) whether the Minister was justified in imposing a penalty on the appellant for gross negligence for each of the taxation years 2002, 2003, 2004 and 2005.

The facts

[4] The appellant is a taxi driver. He has two taxi permits and owns two vehicles. The evidence shows that the appellant operates one of the taxi permits for five and a half days per week at 9 or 10 hours per day. The evidence also shows that the appellant rents the other permit and another vehicle to two of his brothers, which earns him a gross income not exceeding $12,000 per year according to the appellant. The appellant admitted that the value of these taxi permits is around $185,000 each.

[5] The appellant lives in Brossard with his spouse. He took out a variable interest motrgage when he purchased his residence in 2001. According to the testimony, his mortgage payments for the taxation years in question were around $800 to $1,000 a month. The mortgage loan was repaid in whole at the beginning of 2005.

[6] The evidence shows that the appellant did not keep adequate accounting records for his business. The appellant claims that he noted his gross income and expenses in a calendar but that he destroyed the documents after he filed his income tax reports. He claims that if he knew the Canada Revenue Agency (CRA) would conduct an audit, he would have kept his documents. However, the auditor in charge

of his case testified that, during an interview with the appellant, he gave a completely different version of the facts. According to the auditor, the appellant acknowledged that his net business income was around the same from year to year and, as a result, he reported approximately the same amounts for net income every year. The appellant often contradicted himself during his testimony and the Court finds that the auditor's testimony on these facts is more credible.

[7] As noted above, the evidence shows that the Minister adopted the findings of the MRQ for the 2002, 2003 and 2004 taxation years, despite certain corrections (paragraph 10 of the Reply to the Notice of Appeal):

(c) [TRANSLATION]
…

	2002	2003	2004
(i) total income	$174,475	$46,178	$19,418
(ii) minus: total disbursements	$198,451	$75,976	$71,580
(iii) sub-total	$23 976	$29,798	$52,162
(iv) minus: benefits not calculated in the July 8, 2008, reassessments	$3,718	$9,964	
(v) shortfall of income compared to disbursements	$20 258	$19,834	$52,162

(d) the annual shortfall of income compared to disbursements for the 2002, 2003 and 2004 taxation years was considered additional income under "Other Income" and was subject to the penalty for gross negligence;

(e) the Minister revised the appellants taxi income for the 2005 taxation year according to the analysis of bank deposits:

(i) total corrected deposits from adjustments appellant's bank account	53 159,09 $
(ii) minus: gross reported taxi business income	26 400,00 $
(iii) unreported business income	26 759,09 $.

[8] The appellant testified that the discrepancy between his net reported income, his disbursements and his lifestyle could be explained by various factors the

respondent did not consider. First, the appellant showed that he received insurance and disability benefits from the Société de l'assurance automobile du Québec (the SAAQ) and the Wawanesa Mutual Insurance Company (Wawanesa) for personal injury and damages to the car after various traffic accidents. After hearing the appellant's testimony on this subject, counsel for the respondent considered the appellant had the right to a $5,032 reduction of income for the 2003 taxation year, to take into consideration the insurance benefits received, since the amount had not been considered in the reassessment for 2003. Further to this adjustment, and considering the amounts that the Minister had allowed when making the reassessments, there is no longer a difference between the amounts the appellant presented and those allowed by the Minister in this regard.

[9] Second, the appellant claims to have received US$81,000 in cash between 1998 and 2005, following the settlement of his father's estate; he died at age 40 in Lebanon. According to the appellant, his father was the undivided co-owner, with his brother, of an apple orchard in Lebanon. The appellant explained that from 1998 to 2005, his mother and half-brother, who lived in France, took the initiative to recover some money from his uncle in Lebanon as settlement of the estate. The appellant explained that his mother, his half-brother and wife gave him US$30,000 directly when they came to Canada to visit him. According to the appellant, they had not declared this amount when they arrived in Montreal because at the time the law for those entering Canada required them to declare only amounts exceeding $10,000 cash per person. The appellant also claims that he visited his half-brother and his mother in France and they gave him $26,000 cash at that time. Lastly, the appellant claimed that friends of his half-brother gave him amounts of around $5,000 at various times.

[10] The appellant produced a letter dated November 1, 2009, written by his half-brother, which states more or less the same facts. Since the appellant's half-brother did not testify at the trial, the letter is considered hearsay. For the reasons mentioned below, the Court gives the content of this letter no weight in its analysis and, as a result, the only evidence to consider regarding the inheritance is the appellant's testimony. However, the cross-examination of the appellant showed that he did not know the identity of the half-brother's friends who allegedly gave him money during their visit to Canada. Moreover, according to the testimony of the auditor responsible for the case, during the audit, the appellant claimed that the inheritance came to CAN$220,000 whereas, according to the appellant's testimony and his half-brother's letter, the amount was closer to US$126,000, which is, even with the exchange rate, less than CAN$220,000. The auditor also stated that the appellant told her that the money he claimed to have received over a period of 12

years had already been converted to Canadian dollars, whereas during his testimony, the appellant explained to the Court that he received and kept US dollars at his home, which he converted to Canadian dollars only when he had significant purchases to make.

[11] On cross-examination, the appellant admitted he had no documentation from Lebanon to support his version of the facts. He also claimed that he did not deposit the money in his bank account because it was easier to keep the money at home so it would be available quickly in case he needed it.

[12] Lastly, the appellant claimed that every year he won around $12,000 in prizes by playing various Loto-Québec lottery games. The appellant indicated that most of the prizes were under $600 and that the amounts were paid in cash by the Loto-Québec retailers. As a result, there is no documentary evidence to establish the appellant's winnings.

[13] The CRA auditor testified that during the audit, the appellant mentioned that he had won $3,500 twice in the lottery but around 1986. However, he did not mention that he won anything in the lottery during the taxation years in question.

Analysis

[14] It is well established in the Canadian tax system that the Minister may establish arbitrary assessments using any appropriate method, taking into consideration specific circumstances.[1]

[15] First, the appellant claimed to have received US$81,000 from the settlement of his father's estate; he died at age 40. According to the appellant's version of the facts, this money was given to him more than 25 years after his father's death. In the Court's opinion, is it unlikely for a beneficiary of a will to wait this long for his share of the estate. Moreover, the Court has great difficulty accepting the appellant's version of the facts. Lebanon is a fairly developed country. The Court feels that, with a true inheritance, there would be legal documents noting and confirming the existence of the estate's beneficiaries. The appellant could have at least submitted the property title of the orchard to evidence, which would have shown whether his father was truly the co-owner of the orchard with his brother at the time of his death.

[1] *Hsu v. Canada*, 2001 FCA 240, paragraph 22; *Richard v. Canada*, [1997] T.C.J. No. 643 (QL), paragraphs 13 and 15.

[16] The appellant claimed that the cash he received first went from Lebanon to members of his family in France, and then from those family members to him in Canada. The appellant also claimed that he was given significant amounts by people whose names he does not know. These amounts were not reported and were not deposited to a bank. This story is therefore not credible. The Court also notes that there is a significant contradiction between the appellant's testimony at the hearing and the explanations given during the audit conducted by the CRA. In 2006, he completed a questionnaire for the MRQ for 1998 to 2005, which was submitted to evidence (Exhibit I-1, Tab 8). In this questionnaire, on page 2, the appellant indicated he had received CAN$220,000 over the previous 10 years, whereas at the hearing he claimed to have received US$81,000 cash. The two amounts are not equivalent even when considering the exchange rate.

[17] The appellant claimed to have received significant winnings from Loto-Québec during the years in question. Aside from his testimonial evidence, no evidence to corroborate his testimony, such as the Loto-Québec cheques, was provided. The appellant claimed to have won around $12,000 per year from this source during the years in question and claimed that each winning was less than $600. If the winnings were $600 each, the appellant would have won at least 20 times a year. If the average prize was $400, that would mean the appellant won 30 times a year. The Court has great difficulty believing this, particularly since the Court noted many contradictions in the appellant's testimony about his father's alleged estate, to the point that the Court considers his testimony on the subject less than credible. In the absence of any documentary evidence whatsoever, the Court therefore does not accept his version of the facts regarding the alleged inheritance.

[18] The appellant does not accept the Minister's calculations but does not suggest any other method for consideration; he himself is unable to specify the number of paid trips he made each year for his business. If books existed, the appellant had the obligation to keep them.

[19] Additionally, the Court highly doubts that the appellant only earned the net income he reported. He admitted that the two permits together were worth around $370,000. He is also the owner of two cars and a house with no mortgage, valued at $180,000. In all, the taxpayer has assets exceeding $500,000 and very little debt. The Court feels it is impossible that the appellant managed to accumulate so much savings and all those assets while earning such little income. If a taxi permit is worth $185,000, it is because it allows its holder to earn a normal return on this capital, considering the other expenses that must be paid to earn the income and the time spent by the owner driving his taxi.

[20] The respondent has the burden of proof regarding the 2002, 2003 and 2004 taxation years since the reassessments were sent after the normal reassessment period. The "normal reassessment period" is defined as follows under subsection 152(3.1) of the *Income Tax Act* (the ITA):

> **152(3.1) Normal reassessment period** — For the purposes of subsections (4), (4.01), (4.2), (4.3), (5) and (9), the normal reassessment period for a taxpayer in respect of a taxation year is
>
> (a) where at the end of the year the taxpayer is a mutual fund trust or a corporation other than a Canadian-controlled private corporation, the period that ends 4 years after the earlier of the day of mailing of a notice of an original assessment under this Part in respect of the taxpayer for the year and the day of mailing of an original notification that no tax is payable by the taxpayer for the year; and
>
> (b) in any other case, the period that ends 3 years after the earlier of the day of mailing of a notice of an original assessment under this Part in respect of the taxpayer for the year and the day of mailing of an original notification that no tax is payable by the taxpayer for the year.

[21] Subparagraph 152(4)(*a*)(i) of the ITA addresses the time limit for making assessments:

> **152(4) Assessment and reassessment [time limits]** — The Minister may at any time make an assessment, reassessment or additional assessment of tax for a taxation year, interest or penalties, if any, payable under this Part by a taxpayer or notify in writing any person by whom a return of income for a taxation year has been filed that no tax is payable for the year, except that an assessment, reassessment or additional assessment may be made after the taxpayer's normal reassessment period in respect of the year only if
>
> (a) the taxpayer or person filing the return
>
> (i) has made any misrepresentation that is attributable to neglect, carelessness or wilful default or has committed any fraud in filing the return or in supplying any information under this Act,
>
> …
>
> [Emphasis added]

[22] Associate Chief Justice Bowman (as he then was) stated in *Biros v. The Queen* that "[t]he Minister has the onus of establishing misrepresentation in order to open up the statute-barred year."[2]

[23] Bowie J. confirmed this in *College Park Motors Ltd. v. The Queen*[3]:

> 20 … subparagraph 152(4)(*a*)(i) is not penal but remedial. It balances the need for taxpayers to have some finality in respect of their taxes for the year with the requirement of a self-reporting system that the taxing authority not be foreclosed from reassessing in those instances where a taxpayer's conduct, whether through lack of care or attention at one end of the scale, or wilful fraud at the other end, has resulted in an assessment more favourable to the taxpayer than it should have been. This, quite rightly, is not a penalty case…

[24] Bowie J. also stated that subparagraph 152(4)(*a*)(i) "is not at all concerned with establishing culpability on the part of the taxpayer. Other provisions of the Act are in place to do that."[4]

[25] In *Savard v. The Queen*,[5] Tardif J. reviewed the case law regarding the meanings of "neglect" and "misrepresentation" at subparagraph 152(4)(*a*)(i). The judge cited, approvingly, the following statement by Chairman Cardin of the Tax Review Board in *Froese v. M.N.R.*[6]:

> I do not believe that in this context any inference other than their generally accepted meaning can or should be given to the words "neglect" or "carelessness" which is the contrary of the reasonable care that is ordinarily, usually, or normally given by a wise and prudent person in any given circumstances.

[26] Strayer J., then Federal Court judge, stated the following in *Venne v. Canada*,[7] regarding the Minister's burden:

> [I]t is sufficient for the Minister, in order to invoke the power under sub-paragraph 152(4)(*a*)(i) of the Act to show that, with respect to any one or more aspects of his income tax return for a given year, a taxpayer has been negligent. Such negligence is established if it is shown that the taxpayer has not exercised reasonable care. This is surely what the words "misrepresentation that is attributable to neglects" must mean,

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[2] 2007 TCC 248, paragraph 24.
[3] 2009 TCC 409.
[4] *Ibid.*, paragraph 13.
[5] 2008 TCC 62.
[6] *Ibid.*, paragraph 52, citing *Froese*, [1981] C.T.C. 2282, page 2288.
[7] [1984] F.C.J. No. 314 (QL); see also *Savard*, *supra*, paragraph 53.

> particularly when combined with other grounds such as "carelessness" or "wilful default" which refer to a higher degree of negligence or to intentional misconduct…

[27] In the decision, Strayer J. found that the taxpayer had exercised reasonable care when preparing and filing his income tax reports and added: "[t]his conclusion is based partly on the magnitude of the unreported income".[8]

[28] The Federal Court of Appeal (the FCA) stated in *Lacroix v. Canada*,[9] per Pelletier J.A., that in the vast majority of cases, it is difficult for the Minister to present direct evidence of the taxpayer's state of mind at the time the tax return was filed:

> 32 …Insofar as the Tax Court of Canada is satisfied that the taxpayer earned unreported income and did not provide a credible explanation for the discrepancy between his or her reported income and his or her net worth, the Minister has discharged the burden of proof on him within the meaning of subparagraph 152(4)(*a*)(i) and subsection 162(3).

[29] Létourneau J.A. of the FCA made the following statement in *Molenaar v. Canada*[10] which is similar to those of Pelletier J.A. above:

> 4 Once the Ministère establishes on the basis of reliable information that there is a discrepancy, and a substantial one in the case at bar, between a taxpayer's assets and his expenses, and that discrepancy continues to be unexplained and inexplicable, the Ministère has discharged its burden of proof….

[30] Lastly, subsection 163(2) of the ITA imposes a penalty on the taxpayer who, knowingly or under circumstances amounting to gross negligence, makes a false statement or omission in a return:

> **163(2) False statements or omissions** — Every person who, knowingly, or under circumstances amounting to gross negligence, has made or has participated in, assented to or acquiesced in the making of, a false statement or omission in a return, form, certificate, statement or answer (in this section referred to as a "return") filed or made in respect of a taxation year for the purposes of this Act, is liable to a penalty of the greater of $100 and 50% of the total of…

[31] Under subsection 163(3) of the ITA, the Minister has the burden of proving that the circumstances justify the imposition of a penalty under subsection 163(2):

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[8] *Ibid.*
[9] 2008 FCA 241.
[10] 2004 FCA 349.

> **163(3) Burden of proof in respect of penalties** — Where, in an appeal under this Act, a penalty assessed by the Minister under this section or section 163.2 is in issue, the burden of establishing the facts justifying the assessment of the penalty is on the Minister.

[32] Pursuant to subsection 163(2) of the ITA and according to the case law, it is the Minister's responsibility to justify imposing a penalty under subsection 163(3).[11] In *Corriveau v. Canada,*[12] Archambault J. describes the Minister's burden as follows:

> 26 … he must prove: (1) that the taxpayer made a false statement or omission in a return, and (2) that the false statement or omission was made knowingly or under circumstances amounting to gross negligence.

[33] In *Venne*, Strayer J. stated, in regard to the penalty set out in subsection 163(2) of the ITA:

> …One must keep in mind, as Cattanach, J. said in the Udell case supra that this is a penal provision and it must be construed strictly. The sub-section obviously does not seek to impose absolute liability but instead only authorizes penalties where there is a high degree of blameworthiness involving knowing or reckless misconduct…[13]

[34] In *Morin v. M.N.R.,*[14] Chief Justice Couture stated:

> To escape the penalties provided in subsection 163(2) of the Act, it is necessary, in my opinion, that the taxpayer's attitude and general behaviour be such that no doubt can seriously be entertained as to his good faith and credibility throughout the entire period covered by the assessment…

[35] In *Venne*, Strayer J. stated:

> … "Gross negligence" must be taken to involve greater neglect than simply a failure to use reasonable care. It must involve a high degree of negligence tantamount to intentional acting, an indifference as to whether the law is complied with or not…[15]

[36] In *Farm Business Consultants Inc. v. Canada,*[16] Bowman J. (his then title) stated the following:

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[11] *Lacroix*, paragraph 26; *Venne*.
[12] [1998] T.C.J. No. 1122 (QL).
[13] See footnote 7 above.
[14] [1988] T.C.J. No. 108 (QL).
[15] See footnote 7 above.
[16] [1994] T.C.J. No. 760 (QL); affirmed [1996] F.C.J. No. 82 (QL).

> 22 …If, however, it is misrepresentation attributable to "wilful default" it is much more difficult to conclude that it is not equally a "false statement" which the appellant made "knowingly" within the meaning of subsection 163(2)…

Bowman J. also indicated that "neglect" and “carelessness” in subparagraph 152(4)(*a*)(i) are included in the expression “gross negligence” in subsection 163(2) and the expression “wilful default” in subparagraph 152(4)(*a*)(i) is implicitly included in the expression “knowingly” in subsection 163(2):

> 23 …"Neglect, carelessness, wilful default or... fraud" (negligence, inattention, omission volontaire ou... fraude) cover a wide range of non-feasance or misfeasance, innocent or intentional, to which a misrepresentation in a return may be attributable. There is no hiatus between the words in this series, which starts with ordinary neglect and proceeds by gradual degrees to fraud which would justify a penalty under subsection 163(2). The type of carelessness or neglect encompassed by subparagraph 152(4)(a)(i) may include, but is not as extensive as, that contemplated in the words "gross negligence" in subsection 163(2) ("faute lourde") which implies conduct characterized by so high a degree of negligence that it borders on recklessness. It would be difficult to conclude that the state of mind required for "wilful default" ("omission volontaire") is not the same as that implicit in the word "knowingly" ("sciemment").

[37] In *Lacroix,*[17] the FCA found that the taxpayer had committed gross negligence since he did not provide a credible explanation for the misrepresentation of the facts in his tax return:

> 29 …In the case at bar, the Minister found undeclared income and asked the taxpayer to justify it. The taxpayer provided an explanation that neither the Minister nor the Tax Court of Canada found to be credible. Accordingly, there is no viable and reasonable hypothesis that could lead the decision-maker to give the taxpayer the benefit of the doubt. The only hypothesis offered was deemed not to be credible.
>
> 30 The facts in evidence in this case are such that the taxpayer’s tax return made a misrepresentation of facts, and the only explanation offered by the taxpayer was found not to be credible. Clearly, there must be some other explanation for this income. It must therefore be concluded that the taxpayer had an unreported source of income, was aware of this source and refused to disclose it, since the explanations he gave 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

[17] See footnote 9 above.

> under circumstances amounting to gross negligence. This justifies not only a penalty, but also a reassessment beyond the statutory period.

[38] The FCA comments in *Lacroix* summarize the conclusion in this case. The Minister met his burden of proof. He showed there were gaps between the net income the appellant reported and the net income calculated according to the alternative assessment method. Although the appellant does not accept the Minister's calculations, he does not offer any credible explanation to justify the significant gap between his reported income and his expenses during the years in question. In fact, the appellant himself admitted he did not keep any accounting records and is therefore unable to specify the number of paid trips he made for his business and the corresponding net income; he was happy to claim that his business only brought in a modest income.

Conclusion

[39] For all these reasons, I allow the appeal in part only. The reassessment for the 2003 taxation year is referred back to the Minister to add $14,802 to the appellant's income instead of $19,834, to take into consideration a $5,032 reduction of income accepted by the respondent. For the other elements, the assessments under appeal remain unchanged.

Signed at Ottawa, Canada, this 7th day of September 2010.

"Robert J. Hogan"

Hogan J.

Translation certified true
on this 12th day of October 2010.

Elizabeth Tan, Translator

CITATION:	2010 TCC 442
COURT FILE NO.:	2009-1545(IT)I
STYLE OF CAUSE:	HAGOP HANNA v. HER MAJESTY THE QUEEN
PLACE OF HEARING:	Montréal, Quebec
DATE OF HEARING:	May 17, 2010
REASONS FOR JUDGMENT BY:	The Honourable Justice Robert J. Hogan
DATE OF JUDGMENT:	September 7, 2010

APPEARANCES:

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Counsel for the respondent;	Antonia Paraherakis

COUNSEL OF RECORD:

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