Docket: 2007-3451(IT)G

BETWEEN:

VICTOR CANTORE,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on November 26, 2009 and March 19, 2010,
at Montréal, Québec.

Before: The Honourable Justice Robert J. Hogan

Appearances:

Counsel for the Appellant:	Philippe-Alexandre Otis
Counsel for the Respondent:	Christina Ham

JUDGMENT

The appeal from the reassessments made under the *Income Tax Act* for the 2001, 2002 and 2003 taxation years is allowed, with costs to the Appellant, and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment in accordance with the attached reasons for judgment.

Signed at Ottawa, Canada, this 14th day of July 2010.

"Robert J. Hogan"

Hogan J.

Citation: 2010 TCC 367
Date: 20100714
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BETWEEN:

VICTOR CANTORE,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Hogan J.

Introduction

[1] By notices of reassessment dated May 10, 2007, the Minister of National Revenue (the "Minister") increased the income tax liability of the Appellant for the 2001, 2002 and 2003 taxation years through the addition of undeclared income. The Minister used the deposit method to add $98,261, $83,107 and $55,411 of undeclared income to the Appellant's income for the 2001, 2002 and 2003 taxation years respectively.

[2] The issues to be determined in this appeal are as follows:

(a) Is the Appellant liable for the additional income tax determined by the Minister on unreported income in the amounts of $98,261, $83,107 and $55,411 for the 2001, 2002 and 2003 taxation years respectively?
(b) Is the Appellant liable, pursuant to subsection 163(2) of the *Income Tax Act* (the "*ITA*"), to penalties for the relevant taxation years?

Factual Background

[3] From 1992 to 2000, the Appellant was a registered investment advisor with RBC Dominion Securities ("RBC Securities"). In early 2000, the Appellant left RBC Securities to join a technology company. Following the bursting of the so-called "dot com" bubble, the Appellant set out to launch his own venture capital company called Cantore Capital Inc. ("Cantore Capital").

[4] The business of Cantore Capital was to raise capital for small- and medium-sized corporations from sophisticated or accredited investors. Generally speaking, issuers paid Cantore Capital a commission equal to 10% of the capital that it raised for them.

[5] The Appellant testified that he received disconcerting news concerning his health in November 2001; he was diagnosed with a malignant melanoma, which is one of the few types of skin cancer that can cause death. His physician told him that his prognosis for full recovery was not good and that he had a 75% mortality risk over the next seven years. Around the same time, the Appellant was separated from his wife. This culminated in a divorce in 2003. The Appellant explained that he became severely depressed as a result of these two events. The Appellant wound down his venture capital activities to focus on fighting his cancer and maintaining closer relations with his children. As a result, the Appellant claims, he and Cantore Capital earned little or no income in 2002 and 2003. According to the Appellant, fiscal year 2001 was Cantore Capital's first year of operation; it made a modest profit in that year.

[6] The evidence shows that the Appellant filed a personal income tax return for his 2001 taxation year. In that return, he reported net rental income from two rental properties he owned and a gross salary of $50,000 paid to him by Cantore Capital. He did not file personal tax returns for the 2002 and 2003 taxation years because of his health and marital problems. This led to an audit by the Canada Revenue Agency (the "CRA") of the Appellant's 2001, 2002 and 2003 taxation years.

[7] At the initial reassessment stage, the auditor used the deposit method to determine that the Appellant had failed to declare the following income:

	2001	2002	2003
Declared net income	$52,488	—	—
Undeclared income	**$482,533**	**$250,299**	**$117,616**
Net income	$535,021	$250,299	$117,616

[8] The auditor examined only one of the Appellant's personal bank accounts and assumed that each deposit represented a source of undeclared income.

[9] The evidence shows that the deposit method produced an unreliable picture of the Appellant's income at the initial reassessment stage. The Appellant filed a notice of objection to the reassessments. Following representations made on his behalf, the Appellant's undeclared income was revised downwards as follows:

	2001	2002	2003
Declared net income	$52,488	—	—
Undeclared income	**$98,261**	**$83,107**	**$55,411**
Net income	$150,749	$83,107	$55,411

[10] The Appellant's undeclared income was thus decreased by approximately 80% or $384,272 for his 2001 taxation year, approximately 67% or $167,192 for his 2002 taxation year and, finally, approximately 52% or $62,205 for his 2003 taxation year.

Analysis

[11] It is a well-established principle of Canadian tax law that the Minister may use alternative methods to determine a taxpayer's income when a taxpayer fails to file tax returns or maintain or keep reliable books and records that can be reviewed during the course of an audit undertaken by the CRA. The two most frequently used methods are commonly referred to as the net worth method and the deposit method. Under the net worth method, the auditor begins with a calculation of the taxpayer's net assets (assets less liabilities) at the beginning of the relevant period. The same calculation is made at the end of the relevant period. The increase in net worth plus the estimated cost of living for the taxpayer and the taxpayer's dependants less the declared income of the taxpayer and the taxpayer's partner, if any, is assumed to be the amount of undeclared income of the taxpayer.

[12] The deposit method is based on an analysis of all deposits made in all of the taxpayer's bank accounts. Deposits are assumed by the Minister to constitute taxable revenue. Net income is determined by subtracting transfers of funds among the taxpayer's bank accounts and also borrowings by the taxpayer. The deposit method has been accepted by this Court as an appropriate alternative audit technique.[1]

[1] See for example *Khullar Au Gourmet International Ltd. v. The Queen*, 2003 TCC 383; *2868-2656 Québec Inc. v. The Queen*, 2003 TCC 277, affirmed 2004 FCA 388. In *Khullar*, the audit was based on bank deposits to the corporate accounts. The Court does not refer specifically to the deposit method but speaks of a "modified net worth assessment". In any event, the facts of the case indicate that it was in fact the deposit method that was used: the

[13] In "Anatomy of a Net Worth Assessment", David E. Graham comments that the net worth method often produces a more reliable picture of the taxpayer's income then the deposit method.

> Generally, deposit analyses are not as accurate a method of calculating income as net worth assessments. A deposit analysis may not adequately examine where the money that was deposited into the bank accounts came from (which could result in over taxation) and, similarly, a deposit analysis may omit money that never enters the bank account (which could result in under taxation). Taxpayers who are faced with a deposit analysis, should be careful to ensure that transfers from their other bank accounts have not been treated as deposits.[2]
>
> [Emphasis added.]

[14] In the case at bar, the tax auditor failed to examine all of the Appellant's bank accounts notwithstanding the fact that the bank records for the account that she did examine showed that the Appellant often transferred funds between his various bank accounts. This led to a serious deficiency whereby transfers of funds into the account examined by the auditor from other accounts of the Appellant and from bank borrowings by him were treated as gross revenue by the auditor. I pointed out at trial that a more reliable estimate of the taxpayer's income would have been obtained had the auditor used the net worth method or considered all of the deposits in all of the bank accounts of the Appellant and ignored inter-account transfers and bank borrowings. As regards the latter, this would have ensured that the deposit method captured only transactions between the Appellant and third parties. The auditor did not testify at trial and I am unable to determine whether there were reasons justifying the shortcut that she took.

[15] Nonetheless, the method used by the CRA does not affect the legal burden that must be met by the Appellant in this case. In tax appeals, the onus is on the taxpayer to disprove an assessment[3] and is one of proof on the balance of probabilities.[4] This initial onus of "demolishing" the Minister's exact assumptions is met where the appellant makes out at least a *prima facie* case: *Kamin v. Canada*, [1992] T.C.J. No. 714 (QL); *Goodwin v. M.N.R.*, 82 DTC 1679 (TRB). The law is settled that unchallenged and uncontradicted evidence "demolishes" the Minister's assumptions.

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taxpayer did not have accurate records and the auditor arrived at the amount of total sales by adding the total deposits and then making deductions for the transfers to the three accounts (which were deposits from the appellant's lines of credit), certain corrections and returned goods.

[2] David E. Graham, "Anatomy of a Net Worth Assessment", *2007 British Columbia Tax Conference* (Vancouver: Canadian Tax Foundation, 2007), 11:1-55, at 50.

[3] *Johnston v. M.N.R.*, [1948] S.C.R. 486, at 489.

[4] Robert G. Kreklewetz & Vern Vipul, "Net Worth (and Other Estimated) Assessments", Canadian Tax Foundation, *Tax for the Owner-Manager*, January 2006, Vol. 6, No. 1, at 4-6.

Where the Minister's assumptions have been "demolished" by the appellant, the onus shifts to the Minister to rebut the *prima facie* case made out by the appellant and to prove the assumptions. Where the burden has shifted to the Minister, and the Minister adduces no evidence whatsoever, the taxpayer is entitled to succeed.[5]

[16] The fundamental principle to be taken from *Hickman* is that all that is required in order for a taxpayer to rebut a ministerial assumption is a *prima facie* case. That is achieved where the taxpayer puts forward credible, uncontradicted evidence on the particular point. When the appellant does so, the Minister must lead rebuttal evidence, otherwise he will lose.[6]

[17] In "Onus of Proof and Ministerial Assumptions: The Role and Evolution of Burden of Proof in Income Tax Appeals", the authors provide what constitutes, in my opinion, an accurate summary of the rules regarding the legal burden that must be met by taxpayers in tax appeals:

> 6) If the Crown alleges that the minister relied upon specific assumptions of fact in the course of raising an assessment, the taxpayer must either
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> a) prove, on the balance of probabilities, that the minister did not rely upon such assumptions of fact;
>
> b) demonstrate that the minister's assumptions of fact are irrelevant; or
>
> c) demolish the minister's assumptions of fact.
>
> 7) "Demolition" of the minister's assumptions of fact involves nothing more complicated than adducing a prima facie case that those assumptions are incorrect.
>
> . . .
>
> 9) Where a taxpayer has adduced a prima facie case rebutting the minister's assumptions, the onus and standard of proof revert to the normal rules of civil procedure.[7]

[18] Here, the Appellant must either make a *prima facie* case that demolishes the assumptions relied on by the Minister in making the reassessments, thereby shifting

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[5] *Hickman Motors Ltd. v. Canada*, [1997] 2 S.C.R. 336, paragraphs 92-95. L'Heureux-Dubé J. allowed the tax appeal; McLachlin J. wrote separate reasons allowing the appeal, which were concurred in by La Forest and Major JJ. In dissent, Iacobucci J. would have dismissed the appeal, and his dissent was concurred in by Sopinka and Cory JJ.

[6] William Innes & Hemamalini Moorthy, "Onus of Proof and Ministerial Assumptions: The Role and Evolution of Burden of Proof in Income Tax Appeals", (1998) *Canadian Tax Journal*, Vol. 46, No. 6, 1187 at 1208.

[7] *Ibid.*, at 1210.

the onus of proof to the Minister, or establish on a balance of probabilities that the deposits treated as gross revenue by the Minister were not from a source of income, including capital gains. However, when the auditor takes a blatant shortcut for reasons that remain unexplained in Court, that will affect the type of evidence that must be brought by the Appellant to meet his legal burden. In the present case, the Respondent failed to examine all of the Appellant's bank accounts so as to eliminate inter-account transfers. Therefore, it is sufficient for the taxpayer to demonstrate that deposits made to the particular bank account analyzed by the CRA were made by way of an inter-account transfer of funds. The reason for this is tied to the nature of the Minister's assumptions. In the case at bar, the Minister assumed that all deposits made in the sole bank account of the taxpayer that the Minister chose to analyze originated from an external revenue source. The taxpayer can demonstrate otherwise by showing that a particular deposit was made from funds held in another bank account. A transfer of funds between a taxpayer's bank accounts cannot, generally speaking, give rise to income. In this case, proof of such a transfer would be sufficient to constitute a *prima facie* case that demolishes the Minister's assumption that the particular deposit constitutes gross revenue. The onus would then shift back to the Minister who would be required to present evidence to show that the funds transferred from the other account originated from undeclared gross revenue. Had the Minister analyzed all of the Appellant's accounts and eliminated all deposits traceable to a transfer of funds between the taxpayer's bank accounts, the Appellant would then have had to show that the deposits did not originate from a revenue source.

[19] The Appellant testified that he was the sole employee of Cantore Capital. The company would raise funds for its clients by targeting high net worth individuals deemed to be sophisticated investors by virtue of the fact that they could afford to invest $150,000 or more in private placement offerings. Cantore Capital was a small operation with no reputation in the venture capital world in 2001. It had to prove to its prospective clients that it was able to raise funds. It did so by agreeing to advance funds that would be repaid out of the proceeds of the private placement offering that it would be making on behalf of the issuer. The Appellant explained that he had to advance the funds to Cantore Capital out of personal savings held in the form of marketable securities in order to provide it with sufficient working capital to fund its initial advances. When the private placement closed, Cantore Capital would recover its advance and repay the Appellant's shareholder advance.

[20] The Appellant produced statements from his investment advisor that show that he owned $361,152 worth of marketable securities at the beginning of 2001. Those statements also show that the amount of marketable securities held by the Appellant

in his accounts was reduced to approximately $75,256 at the end of 2003. This evidence corroborates the Appellant's testimony that he was forced to use his personal savings both to cover the working capital needs of Cantore Capital during its start-up phase and to finance his personal expenses in the 2001 and 2002 fiscal years after suffering health and marital problems.

[21] The Appellant produced other evidence to corroborate his testimony on this point. He produced unaudited financial statements for Cantore Capital and documents that analyze the activity in the shareholder's advances account over the relevant period. For example, those documents show that funds were credited to Cantore Capital's shareholder's advances account on three occasions in the 2001 fiscal year, and that those amounts totalled $128,553.40. Funds totalling $72,129.98 were withdrawn from that account, leaving a net balance owing to the Appellant of $56,423.42 at the end of the 2001 taxation year.

[22] The Appellant produced similar corroborating documentary evidence for his 2002 taxation year. That evidence shows that Cantore Capital's shareholder's advances account was reduced from $56,423.42 at the end of 2001 to $6,953.63 at the end of 2002, for a total reduction of $49,469.79 in 2002. In other words, the Appellant was repaid $49,469.79 by Cantore Capital, which was reflected by a reduction in its shareholder's advances account.

[23] Counsel for the Respondent argues that little weight should be given to Cantore Capital's financial statements and tax returns because those documents were produced late and were not audited by the CRA. While it is true that both types of documents were prepared long after the filing due date for Cantore Capital's tax returns, the evidence shows that the CRA had had access to those documents since March 2009. I suspended the hearing of this case on November 26, 2009 in order to allow the CRA time to review the financial statements and tax returns and to see whether the parties could reach an understanding on the impact of the activity in Cantore Capital's shareholder's advances account over the relevant period and on the probative value of the statements that show a decline in the amount of marketable securities held by the Appellant. The hearing resumed on March 19, 2010. Altogether, the CRA had 12 months to audit the statements produced by the Appellant.

[24] The Respondent led no evidence to cast doubt on the probative value of the documents in question or to challenge the testimony of the Appellant. As a result, although the evidence is not perfect on this point, I conclude that the Appellant has established on a balance of probabilities that $69,000 of the deposits in his personal

bank account during his 2001 taxation year was attributable to the repayment of shareholder's loans by Cantore Capital. Similarly, I find that Cantore Capital paid the Appellant $48,000 in 2002 in reimbursement of shareholder's advances. As a result, the amount of undeclared income determined by the CRA was, in this regard, overstated by $69,000 and $48,000 for the Appellant's 2001 and 2002 taxation years respectively.

[25] The Appellant led credible testimonial evidence to show that he received a cheque in the amount of $6,000 from Stéphane Chouinard in repayment of a loan. He deposited that cheque in his personal bank account in 2001. The Respondent did not rebut this evidence. Therefore, the Appellant's undeclared income for the 2001 taxation year has been overstated by $6,000 in this regard.

[26] Nadia Brenhouse testified that she loaned the Appellant, who is a close personal and family friend, a total of $15,000 during 2002. The Appellant corroborated that this amount was deposited in his personal bank account in 2002. I found Ms. Brenhouse to be a very credible witness. Therefore, I conclude that the CRA overstated the Appellant's 2002 income by $15,000 in this regard.

[27] The evidence also shows that the Appellant received a loan of $6,000 from Carlo Borrelli in 2002, which was erroneously treated by the CRA as a source of undeclared income.

[28] Finally, the Appellant led evidence to show that the CRA's reassessments failed to take into account the fact that the following amounts deposited in his bank account over the relevant period were non-taxable transfers from his credit card and from his other bank accounts:

2001 taxation year	
Transfer from U.S. dollar account	$14,775.36
Telephone banking fund transfer	$7,813.00
TOTAL	$22,588.36

2002 taxation year	
Transfer from brokerage account	$5,240.00

2003 taxation year

Cash advance credit card withdrawal	$5,000.00
Citibank credit card advance	$7,000.00
Transfer from U.S. dollar account	$6,914.00
Telephone banking fund transfer	$9,571.10
Transfer from bank account	$1,000.00
Telephone banking fund transfer	$1,326.40
Telephone banking fund transfer	$6,604.00
TOTAL	$37,415.50

[29] In addition, at the outset of the trial, the Respondent admitted that the Appellant's income had been overstated by $1,508.80 for 2002 and by $2,800.94 for 2003 with respect to a number of small deposits.

[30] The Appellant failed to establish on a balance of probabilities that he was entitled to adjustments other than those described above with respect to his 2001, 2002 and 2003 taxation years.

[31] After taking into account all of the adjustments determined above, the Appellant's undeclared income is as follows:

	2001	2002	2003
Alleged additional income per reassessment	$98,261.00	$83,107.00	$55,411.00
Repayment of shareholder's advances	($69,000.00)	($48,000.00)	
Repayment of loan — S. Chouinard	($6,000.00)		
Loan — N. Brenhouse		($15,000.00)	
Loan — C. Borrelli		($6,000.00)	
Interbank transfers and credit card advances	($22,588.36)	($5,240.00)	($37,415.50)
Adjustments admitted by the CRA		($1,508.80)	($2,800.94)
Undeclared income per year	$672.64	$7,358.20	$15,194.56

[32] Finally, in light of the significant amount of adjustments that I have allowed to the undeclared income determined by the CRA, I conclude that the Respondent has failed to establish on a balance of probabilities the existence of circumstances that would justify the imposition of penalties under subsection 163(2) of the *ITA*.

Conclusion

[33] For these reasons, the appeal is allowed, with costs to the Appellant, and the matter is referred back to the Minister for reconsideration and reassessment in accordance with these reasons.

Signed at Ottawa, Canada, this 14th day of July 2010.

"Robert J. Hogan"

Hogan J.

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COURT FILE NO.:	2007-3451(IT)G
STYLE OF CAUSE:	VICTOR CANTORE v. HER MAJESTY THE QUEEN
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DATES OF HEARING:	November 26, 2009 and March 19, 2010
REASONS FOR JUDGMENT BY:	The Honourable Justice Robert J. Hogan
DATE OF JUDGMENT:	July 14, 2010

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