

Docket: 2010-2867(GST)I

BETWEEN:

9134-2485 QUEBEC INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

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Appeal heard on August 29, 2012, at Montréal, Quebec.

Before: The Honourable Justice Robert J. Hogan

Appearances:

Counsel for the appellant: Christopher R. Mostovac

Counsel for the respondent: Michel Rossignol

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**JUDGMENT**

The appellant's appeal from the assessment, notice of which is dated December 16, 2008, for the period from April 1, 2004, to March 31, 2008, and from the reassessment, notice of which is dated July 14, 2010, for the period from January 1, 2005, to March 31, 2008, is dismissed in accordance with the attached Reasons for Judgment.

Signed at Toronto, Ontario, this 14th day of November 2012.

"Robert J. Hogan"

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Hogan J.

Citation: 2012 TCC 401  
Date: 20121114  
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### **REASONS FOR JUDGMENT**

#### **Hogan J.**

[1] On December 16, 2008, the respondent, through the Minister of Revenue of Quebec (the Minister), made an assessment regarding the appellant under Part IX of the *Excise Tax Act*, R.S.C., 1985, c. E-15 (the ETA), for the period from April 1, 2004, to March 31, 2008.

[2] On May 26, 2010, further to a Notice of Objection filed by the appellant, a Revenu Québec objections officer sent the appellant a letter setting out the adjustments that would be made to the assessment. A reassessment was then made on July 14, 2010. As a result of the adjustments made in this reassessment with respect to the net tax and the interest and penalties, the appellant must pay the following amounts:

a. Adjustment to the net tax reported:	\$84,568.76
b. Net interest:	\$16,510.35
c. Late remittance penalty:	\$7,022.44
d. Gross negligence penalty:	\$21,142.19

[3] In making the assessments at issue, the Minister relied on the following findings and assumptions of fact, among others:

- (a) The appellant is registered under Part IX of the ETA. It operates a sushi restaurant and a bar with a liquor licence.
- (b) All supplies made by the appellant in operating its restaurant and bar are taxable supplies for which a tax, namely, the goods and services tax (GST), is payable on the value of the consideration of the supply.
- (c) The supplies related to the appellant's commercial activities were registered using software created by Khang Nguyen. According to the respondent, during the periods in question, the appellant used a device called a "zapper" to erase certain taxable supplies from its accounting records.
- (d) According to the Minister, in view of the use of a zapper, the appellant's records and accounting documents were incomplete and inaccurate, such that the appellant filed GST returns that did not reflect its true financial situation.

[4] Therefore, to determine the amount of GST that the appellant collected or should have collected during the periods in question, the total amount of the taxable supplies made by the appellant from January 1, 2005, to June 11, 2007, was reconstructed from the records containing all of the transactions made by the appellant.

[5] According to the estimate made by the Minister, the additional sales come to the following amounts:

- a. \$138,705.35 for the fiscal year ending March 31, 2005;
- b. \$449,996.63 for the fiscal year ending March 31, 2006;
- c. \$458,800.57 for the fiscal year ending March 31, 2007;
- d. \$236,098.71 for the fiscal year ending March 31, 2008.

[6] According to the Minister, a review of the available documents shows that, during the periods in question, the appellant did not report all of the taxable supplies for which a tax of 7 percent on the value of the consideration was payable by the purchasers.<sup>1</sup>

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1. The rates were 6% from July 1, 2006, to December 31, 2007, and 5% since January 1, 2008.

[7] The Minister's estimates also indicate that the amount of GST that the appellant was supposed to collect during the period in question is \$145,168.86, whereas the appellant filed net tax returns reporting \$60,600.10.

[8] The Minister therefore submits that the appellant misrepresented the facts by not including, in the computation of the net tax that it filed, an amount of \$84,568.76 in collected or collectable GST.

[9] On April 12, 2008, Dario Grimard, a computer technician at the Agence du revenu du Québec (the ARQ), and an auditor went to the appellant's restaurant to retrieve data from the appellant's electronic sales system.

[10] According to the testimony of Jean-François Gingras, a point of sale systems analyst at the ARQ who analyzed the data retrieved by Mr. Grimard, the appellant or its consultants used "scripts" or a computer program to delete 7,307 invoices issued by the appellant during the period in question.

[11] After some in-depth work, ARQ computer technicians were able to recover the information from 6,863 of the deleted invoices (the recovered invoices), leaving only 444 missing invoices (the missing invoices) for the period in question.

[12] The Minister assumed that all of the recovered invoices relate to taxable supplies that the appellant did not report. The Minister also assumed that the 444 missing invoices relate to unreported taxable supplies with an average value of \$136.83 each. The Minister relied on these assumptions to estimate the appellant's unreported sales, set out above at paragraph 5.

[13] According to the testimony of the appellant's shareholder/manager, My Thanh Phan, a childhood friend of hers, Khang Nguyen, designed the software that the appellant used for registering sales. The software was designed to ensure that no food order would leave the kitchen without being registered by staff using the software. This procedure was supposed to prevent theft or fraud. However, Ms. Thanh claims that the software had significant shortcomings. According to the witness, the software did not include a function for registering complimentary meals for the appellant's employees or customers. All free meal orders were treated as taxable sales. Furthermore, the software did not have a command for deleting entry errors. All errors caused an invoice for a taxable supply to be printed out.

[14] Finally, the system was not conducive to training new staff. Indeed, according to Ms. Thanh's testimony, the system's training code did not work as it was supposed

to. Orders entered during training sessions were therefore treated as taxable sales. According to Ms. Thanh, this explains the large number of deleted invoices that the respondent recovered from the appellant's database.

[15] According to the appellant's witnesses, many free meals were given away during the years at issue: three or four invoices a day for [TRANSLATION] "staff meals", gifts for relatives and for the employee of the week, free meals in exchange for publicity, gift certificates, [TRANSLATION] "staff birthdays", and free meals for shareholders, managers and suppliers. Despite the alleged high number of free meals, Ms. Thanh claims that she has no accounting records for free meals and promotions.

[16] The cross-examinations of the appellant's witnesses reveal that they were evasive and that their evidence regarding the lack of records for free meals and promotions was vague. Moreover, the free meals for staff, shareholders and their relatives are taxable benefits. Exchanging meals for services also gives rise to taxable income. The evidence as a whole suggests that the appellant was doing little accounting to ensure compliance with its tax obligations.

[17] It would appear that no thought whatsoever was given to the reporting of taxable benefits. The testimonies of Xuan Bich Ty Hoang and My Tung Phan also suggest that the business was not keeping inventory. On cross-examination, they could only say that they had been trying but were still not managing to do so.

[18] According to Ms. Thanh, she kept the invoices for free meals, errors or staff training and gave them regularly to Mr. Khang so that he could cancel them in the appellant's accounting system. Once the sales had been cancelled, new numbers were given to the remaining invoices to restore the numerical sequence and avoid gaps.

[19] Ms. Thanh states that she did not keep the paper invoices after Mr. Khang had cancelled them. Mr. Khang testified that he restored the numerical sequence because it was the professional thing to do.

[20] The version of the facts given by the appellant's witnesses was contradicted by the respondent's evidence. The testimony of Mr. Gingras indicates that the appellant's computer system contained an everyday database and a database used solely for training.

[21] The computer system also had a button that allowed free or discounted meals to be registered. Moreover, the respondent's witnesses observed that some of the free meals were accounted for as no-sales. The examination of Ms. Coulombe, the

Minister's auditor, reveals that she found, in a box of documents belonging to the appellant, a report entitled "Cancel/On House" which was filed at trial as Exhibit I-6.

[22] Furthermore, the testimony of Ms. Yip details transactions accounted for as no-sales. She filed Exhibit I-9, a summary of transactions totalling more than \$105,936.08 for the period from January 1, 2005, to June 11, 2007, and \$53,676.06 for the period from June 11, 2007, to March 31, 2008. This contradicts evidence filed by the appellant claiming that that free meals could be offered only by cancelling the invoices. Indeed, sales totalling over \$159,612.14 had already been accounted for as free meals in the system.

[23] Mr. Gingras explained that he found in the appellant's computer system a set of programs that allowed it to erase invoices, restore the numerical sequence and gain access to the database where the sales were registered. Preparing such programs requires very advanced knowledge of computers. According to Mr. Gingras, these programs are unusual. Moreover, properly functioning accounting software does not need them. These programs are instead used to hide sales. It is very difficult to recover the information erased by such means. The appellant provided no reasonable explanation for the existence and use of these programs.

[24] To sum up, the following elements emerge from the evidence introduced at the hearing:

- There was an obvious contradiction regarding the existence of a list or report for free meals;
- The appellant does not deny having sophisticated programs for erasing sales;
- There is clear testimonial evidence that some data were unavailable when the information was extracted from the appellant's databases.

[25] The following elements raise serious doubts and call into question the explanations and credibility of the appellant's witnesses:

- a. The fact that the system has a training code and a discount button, while the appellant claims that it uses an invoice cancellation procedure for training and staff meals;
- b. The lack of documentation supporting the testimony of Mr. Khang regarding the frequent errors in the systems;
- c. The discarding of invoices after cancelling them in the system;
- d. The lack of quarterly stocktaking;

- e. The contradictions and vague answers regarding how Mr. Khang's invoice cancellation procedure works;
- f. The appellant's failure to disclose the invoice cancellations before this was detected by employees of the Minister.

[26] Considering all of the evidence, I find that the invoices that were cancelled by Mr. Khang are real sales that the appellant made but did not report. I therefore find that the respondent has met its burden of proving that there are circumstances justifying the imposition of penalties. For these reasons, the appeal is dismissed.

Signed at Toronto, Ontario, this 14th day of November 2012.

"Robert J. Hogan"

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Hogan J.

Translation certified true  
on this 20th day of December 2012.  
Michael Palles, Translator/Language Adviser

CITATION: 2012 TCC 401

COURT FILE NO.: 2010-2867(GST)I

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REASONS FOR JUDGMENT BY: The Honourable Justice Robert J. Hogan

DATE OF JUDGMENT: November 14, 2012

APPEARANCES:

Counsel for the appellant: Christopher R. Mostovac

Counsel for the respondent: Michel Rossignol

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