

Docket: 2019-45(IT)I

BETWEEN:

ESTRA FLOORING SERVICES CORP.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard October 1, 2020 at Ottawa, Ontario

Before: The Honourable Justice B. Russell

Appearances:

Agent for the Appellant: Tony Wark

Counsel for the Respondent: Laurence Charron-Raymond

JUDGMENT

The appeal of the two assessments raised January 29, 2016 under the federal *Income Tax Act* for the Appellant's taxation years ending December 31, 2013 and 2014 is dismissed, with costs to the Respondent fixed at \$500 to be tendered within 40 days of the issuance date of this Judgment.

Signed at Halifax, Nova Scotia, this 17th day of March 2021.

“B. Russell”

Russell J.

Citation: 2021 TCC 20

Date: 20210317

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BETWEEN:

ESTRA FLOORING SERVICES CORP.,

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REASONS FOR JUDGMENT

Russell J.

I. INTRODUCTION:

[1] The corporate Appellant, Estra Flooring Services Corp. (Estra Corp.), appeals two assessments raised under the federal *Income Tax Act* (Act) by the Minister of National Revenue (Minister).

[2] Estra Corp. was incorporated August 9, 2012. At all material times it carried on a family business selling residential and commercial flooring and related installation services. Prior to Estra Corp.'s incorporation, another corporation with a similar name - Estra Flooring Inc. (Estra Inc.) - had carried on this family business.

[3] Three years after its incorporation, Estra Corp. still had not filed any income tax returns. On October 7, 2015, the Minister wrote to Estra Corp. requesting that it file returns for the three taxation years ending December 31, 2012, 2013 and 2014. The letter informed also that absent the requested returns being filed by November 6, 2015, arbitrary assessments per subsection 152(7) of the Act would be raised.

[4] On January 29, 2016, with Estra Corp. not having filed any income tax returns, the Minister assessed it pursuant to subsection 152(7) for taxation years ending December 31, 2012, 2013 and 2014. This appeal concerns only the latter two assessments, being those for the December 31, 2013 and 2014 taxation years. They respectively reflect assessment of unreported taxable income of \$127,210 and \$89,819.

These figures each represent 10% of gross sales for the particular year. The Minister assumed that for each year business expenses equated with the other portion (90%) of gross sales.

[5] On February 10, 2016, Estra Corp. served notices of objection respecting these two assessments. Well more than a year later, on March 31, 2017 Estra Corp. filed “T2 short returns” for taxation years ending July 31, 2013 and 2014. They showed respectively a net loss of \$80,022 and net income of nil. The Minister took these returns into consideration in her deliberations respecting the two objected-to assessments.

[6] On September 17, 2018, the Minister confirmed the two objected-to assessments for the December 31, 2013 and 2014 taxation years. The allowed expense totals were kept at 90% of the HST reported total gross income for each of the two years, in the absence of any “source documentation” corroborating the Estra Corp. expenses said to have been claimed in the belatedly filed returns (which returns were not submitted in evidence.) On December 14, 2018, Estra Corp. instituted this appeal of those two confirmed assessments.

II. ISSUES:

[7] At the hearing’s commencement, Estra Corp.’s agent clarified for the Court what was specifically at issue for his client, stating respecting both appealed assessments:

It really comes down to the expense amount...The sales that were reported by the CRA arbitrary assessments matched the HST returns, which were filed quarterly for the calendar year, so no dispute with the revenue. And, the expense was based on a percentage of sales... [being] 90 percent...We believe the expenses are greater than that amount.¹

[8] This made clear that the appeal did not concern the assessed corporate gross revenue amounts (which the Minister had derived from Estra Corp.’s filed HST returns over the pertinent period). Rather, as indicated, the issue was simply the

¹ Transcript, pages 4, 5.

quantum of business expenses (being 90% of gross revenues) assumed by the Minister in raising the two appealed assessments.²

III. EVIDENCE:

[9] Estra Corp.'s first witness was Walter Lubiana (WL). At all relevant times, he was acting president of Estra Corp. and operations manager of its business. His elderly father, Benito Lubiana (BL) was Estra Corp.'s principal shareholder. In cross-examination, WL acknowledged receipt of the Minister's above-referenced October 7, 2015 letter requesting the filing of overdue income tax returns.

[10] WL testified that during the years in issue he ran the operations and administration of the business, including doing bookkeeping. He testified that he could not be sure when - perhaps in or about 2012 - this flooring business had suffered a substantial financial downturn after being outbid on a significant contract it had held for several years with a prominent builder for the supply of flooring and installation services.

[11] He testified that the filing of income tax returns for years commencing in 2012 did not occur because Estra Corp. did not have funds to retain its usual accounting firm to prepare corporate financial statements. Initially, each morning WL had completed bank reconciliations using bookkeeping software, based on daily online banking data. (When he was doing this, was not specified. To the extent it may have been prior to the August 2012 incorporation of Estra Corp., this daily bookkeeping would instead have concerned the prior corporation, Estra Inc.)

[12] WL testified that eventually he ceased doing this daily bookkeeping work, as he felt obliged to focus fully on drumming up business. Apart from WL the business was not staffed, although his elderly father BL would come into the Ottawa store/showroom daily to handle phone calls.

[13] WL testified that in due course he fell eight months behind in his daily bookkeeping and he was unable to catch it up. He said that subsequently Estra Corp.

² This was more specifically articulated in post-hearing written submissions. Estra Corp.'s paragraph 16 of its rebuttal submissions expresses concurrence with the Respondent Crown's written submissions at paragraphs 35 and 36. The said paragraph 36 identifies the "sole issues to be decided", agreed to by Estra Corp., as being whether the expenses for each of the two years were correctly assessed, in leading to the assessed amounts of unreported taxable income.

could not afford to pay its accounting firm to do the required accounting catch-up work.

[14] He explained that Estra Corp.'s bank statements with cancelled cheques would be put in bankers boxes stored in the attic of Estra Corp.'s store/showroom. But when Canada Revenue Agency (CRA) asked for "source documentation" (as further referenced below) to back up expenses claimed in the returns belatedly filed March 2017, WL could not find the box or boxes containing that requested documentation, including bank statements and copies of cancelled cheques.

[15] He said he thoroughly searched the attic, where apparently many boxes of bookkeeping documentation from over the years were being kept. While subsequently he was able to obtain from the corporation's bank copies of bank statements that he could not find, he could not obtain replacement copies of cancelled cheques.

[16] WL did not provide documentary or *viva voce* evidence that addressed specific expenses incurred by Estra Corp., although quantum of expenses was the acknowledged issue in this appeal. Nor was there evidence of third-party witnesses with their own documentation that potentially could have corroborated specific expenses claimed by Estra Corp.

[17] Rather, WL testified generally as to a re-financing of his father's house, said (although not shown) to have been to inject funds into Estra Corp. to aid cash flow. General references were made also to borrowing from other family and arm's length sources, although largely absent documentation confirming where borrowed funds ended up.

[18] There also was general evidence indicative of modest personal living circumstances of WL and BL.

[19] Respondent's counsel objected to much of this general evidence on the basis of relevance. However, I admitted into the record most of such evidence, of course subject to weight and keeping in mind this is an "informal procedure" appeal.

[20] According to Estra Corp.'s agent, this general evidence as to challenging financial conditions would show that Estra Corp. could not have earned the net taxable income as had been assessed (being 10% of gross revenues); thus there had

to have been greater expenses than the assessed amounts equating to 90% of gross revenues per the HST returns.

[21] Of note, in cross-examination, WL acknowledged drawing funds from Estra Corp. to make payments on an Ontario Superior Court Judgment of approximately \$138,000 that had been entered against the prior corporation, Estra Inc., and several individuals including WL.

[22] The only other witness called by Estra Corp. was CRA auditor S. Kirkham (SK). SK had audited the income tax returns Estra Corp. belatedly had filed in March 2017, well after Estra Corp. had filed notices of objection regarding the assessments under appeal. SK did so at the request of the CRA Appeals officer addressing those notices of objection.

[23] In his direct examination of SK, Estra Corp.'s agent referenced an email SK had sent to the Appeals officer, which included the statement that, "[t]he books and records for this file are a mess to the point where the accountant even is having a lot of difficulty understanding the bookkeeping..."³ The agent asked SK if that was "a correct statement", to which he answered in the affirmative.⁴

[24] As part of his audit work at the notice of objection stage, SK requested of Estra Corp. specified information and documentation. The requested documentation included "source documentation" in respect of a number of bank deposits and expense transactions, as selected by SK, recorded in Estra Corp.'s general ledger.

[25] SK in a questionnaire sent to and filled out by Estra Corp. at commencement of SK's audit work provided examples of source documentation for expenses. For proof of payments for inventory, source documentation could include purchase invoices (and Estra Corp. added cancelled cheques). For proof of payments to "trades and subcontracts", source documentation could be written agreements and cancelled cheques (and Estra Corp. added invoices). Examples of source documentation, given for payments for "delivery, freight and express" were purchase invoices and shipping documents, with Estra Corp. also suggesting cancelled cheques. Examples of source deduction given by CRA for the expense category "short-term debt" were bank statements and mortgage statements, etc. Again to this, Estra Corp. suggested cancelled cheques. Cancelled cheques, bank

³ Transcript, page 83.

⁴ Transcript, page 84.

statements, signed agreements constituted much of what would constitute source deduction for the various expense classifications.

[26] In its ultimate response however, Estra Corp. provided to SK no source documentation at all relating to expenses for the two years in issue. This was acknowledged by Estra Corp.'s agent in the course of his questioning of SK. He stated (with SK concurring):

...you had bank statements, but we didn't give you any source documentation for '13 and '14...to support purchases, trades [and] subcontracts, delivery, freight, interest, all these expenses. We didn't provide any documentation.⁵

[27] SK was asked by Estra Corp.'s agent what rationale had CRA used to arbitrarily assess expenses as equaling 90% of sales revenue. SK replied that in respect of taxpayers not having filed any returns, CRA "...would use between 80 percent and 90 percent of the sales in order to determine the expenses for the assessment raised under [subsection] 152(7)."⁶ He said he could not explain specifically the basis for this standard as he had never worked in CRA's "non-filers" section.⁷

[28] In good part due to the Appellant's non-provision of the requested source documentation, SK ended up making two alternative recommendations to the Appeals officer regarding how to conclude the objections to the two subject assessments. The first proposed alternative was that for each objected-to assessment, net taxable income be increased to specified new amounts. The other alternative recommendation was that the Minister simply confirm the objected-to assessments, thereby not increasing assessed net taxable income. The Minister selected the latter, more lenient alternative, and proceeded simply to confirm the subject two assessments.

[29] In friendly cross-examination, SK stated that net worth assessments (a type of arbitrary assessments) could not meaningfully be conducted in respect of corporate entities (as of course is Estra Corp.). SK testified also that when he first was assigned to do this work for the Appeals officer, he noted from the file that CRA's Business

⁵ Transcript, page 93.

⁶ Transcript, page 80.

⁷ Transcript, page 81.

Intelligence and Quality Assurance office had identified, upon preliminary screening of the belatedly filed returns:

...[an] issue...with costs of goods sold because it was a lot higher than the industry average, so I think that was the main issue in regards to potential over-claimed costs of goods sold.⁸

IV. ANALYSIS:

[30] As stated, the only issue is whether the Minister erred in assessing allowed expenses of \$1,144,866 (2013) and \$808,371 (2014). At paragraph 30(1) of the Respondent's Reply is pleaded, as an assumption the Minister made in raising the appealed assessments, that:

The Appellant had expenses of not more than \$1,144,866 and \$808,371 with respect to this taxation years ending December 31, 2013 and December 31, 2014, respectively, representing 90% of the above-stated gross revenue.

[31] It is trite law that in tax appeals assumptions of fact pleaded as having been made by the Minister are presumed correct⁹, although that presumption is rebuttable on the civil standard of a balance of probabilities.

[32] Thus, the pertinent question here is whether evidence adduced at the hearing has rebutted the Minister's above-noted assumption respecting quantum of expenses, as assessed for each of the two subject taxation years.

[33] My ready view is that Estra Corp. did not at all rebut the said ministerial assumption to the effect that neither of the two appealed assessments reflects understated business expenses of Estra Corp.

[34] To elaborate, the general evidence put forward by Estra Corp. tending to show that during the relevant period WL and BL personally had financial challenges and modest lifestyles, and that funds may have been advanced to Estra Corp., has virtually no probative value in establishment of the specific point at issue, that Estra Corp.'s expenses exceeded the amounts reflected by the two appealed assessments.

⁸ Transcript, page 125.

⁹ A fact pleaded as a ministerial assumption and thus presumed correct also may be defeated through evidence (typically from an audit report or notice of objection report) that the Minister actually had not made the particular pleaded assumption.

[35] Sufficiently probative evidence would be expected to have been provided through Estra Corp.'s business books and records. But, surprisingly, at the hearing Estra Corp. put forward no source documentation whatsoever to substantiate its expense claims.

[36] This is quite counter to and in breach of subsection 230(1) of the Act, which stipulates the fundamental requirement that a taxpayer's books and records be available, to allow determination of that taxpayer's taxation liabilities.

[37] Consequently, the Minister's above-noted pleaded assumption - that Estra Corp. incurred expenses of not more than \$1,144,866 and \$808,371 in its taxation years ending December 31, 2013 and 2014 – emerges from this appeal affirmed as an established fact.

[38] This appeal will be dismissed.

Signed at Halifax, Nova Scotia this 17th day of March 2021.

“B. Russell”

Russell J.

CITATION: 2021 TCC 20

COURT FILE NO.: 2019-45(IT)I

STYLE OF CAUSE: ESTRA FLOORING SERVICES CORP.
AND HER MAJESTY THE QUEEN

PLACE OF HEARING: Ottawa, Ontario

DATE OF HEARING: October 1, 2020

REASONS FOR JUDGMENT BY: The Honourable Justice B. Russell

DATE OF JUDGMENT: March 17, 2021

APPEARANCES:

Agent for the Appellant: Tony Wark
Counsel for the Respondent: Laurence Charron-Raymond

COUNSEL OF RECORD:

For the Appellant:

Name: N/A

Firm: N/A

For the Respondent: Nathalie G. Drouin
Deputy Attorney General of Canada
Ottawa, Canada