Lucien Venne, Plaintiff,

and

Her Majesty The Queen, Defendant.

Federal Court — Trial Division (Strayer, J), April 9, 1984 (Court No T-815-82), on appeal from assessments of the Minister of National Revenue.

Lorenzo Girones for the plaintiff.
Robert McMechan for the defendant.

Strayer, J:—This is an action by way of an appeal under subsection 172(2) of the *Income Tax Act*. It is an appeal from notices of reassessment by Revenue Canada of the plaintiff's income for the taxation years 1972, 1973, 1974, 1975, 1976, 1977, and 1978. The notices were dated September 3, 1980. Each of them reassessed income at a higher figure, and levied taxes on such unreported income together with interest on that tax, plus a penalty under subsection 163(2) of the *Income Tax Act* for "false statements" (as defined in that subsection) in the taxpayer's income tax returns for the years in question. In the notice of reassessment for the taxation year 1972 there was also a late filing penalty of $193.50. That penalty is not contested herein.

Issues

(1) *Power to reassess for more than four years* — I shall refer to this issue first since its resolution will determine whether some of the particular items of income in dispute will require consideration. Subsection 152(4) of the *Income Tax Act* provides:

> (4) The Minister may at any time assess tax, interest or penalties under this Part 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 taxation year, and may
>
> (a) at any time, if 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, or
>
> (ii) has filed with the Minister a waiver in prescribed form within 4 years from the day of mailing of a notice of an original assessment or of a notification that no tax is payable for a taxation year, and

(b) within 4 years from the day referred to in subparagraph (a)(ii), in any other case.

reassess or make additional assessments, or assess tax, interest or penalties under this Part, as the circumstances require.

Subparagraph (4)(a)(i) is relevant to the present case: it means that in order to reassess for more than four years counted backwards from the date of reassessment (in this case September 3, 1980) it was necessary for the Minister to show that there has been "misrepresentation that is attributable to neglect, carelessness or wilful default" or "fraud" by the taxpayer in filing the return or in supplying information under the Act. It appeared to be common ground in this case that for the notices of reassessment to be effective for taxation years 1972, 1973, 1974, and 1975, it is necessary for the Minister to prove misrepresentation or fraud.

(2) *Exclusion of certain income from such extended reassessment* — Subsection 152(5) of the *Income Tax Act* provides in part:

(5) Notwithstanding subsection (4), there shall not be included in computing the income of a taxpayer, for the purpose of any reassessment, additional assessment or assessment of tax, interest or penalties under this Part that is made after the expiration of 4 years from the day referred to in subparagraph (4)(a)(ii), any amount

...

(b) in respect of which the taxpayer establishes that the failure so to include it did not result from any misrepresentation that is attributable to negligence, carelessness or wilful default or from any fraud in filing a return of his income or supplying any information under this Act, and

...

This means that if the taxpayer can prove (and he has the burden of proof here) with respect to any year or years more than four years prior to the reassessment where the original assessment has been reopened by virtue of subsection 152(4), that his failure to include any particular item of income was not due to negligence, carelessness, or wilful default or fraud, then such items should not be included in the reassessed income. While there was some discussion of this subsection during the case, I understand the plaintiff's position to be that he is not asserting that any particular item of income during the years 1972-75 should be exempted from inclusion in the reassessment for this reason. He relies on his position, instead, that the defendant has not met the burden of proof required by subsection 152(4) and therefore no item of income during this period can be reassessed. I will therefore not deal further with subsection 152(5).

(3) *Amount of unreported income* — After some months and years of discussion between Revenue Canada and the taxpayer's representatives, the difference between them has been considerably narrowed with respect to the amount of income which the taxpayer failed to report during the six-year period 1972-77. The defendant says that amount is $330,934. The plaintiff has admitted that $283,501 of income was unreported. For 1978 the defendant reassessed the plaintiff's income by adding $17,456.77 which is also challenged by the plaintiff. The issue here, apart from the question of whether any reassessment could be made in 1980 with respect to any period more than four years prior to the reassessment (see (1) above), is whether I consider that the plaintiff has met the burden of proof placed on him to overcome the presumption that normally applies as to the correctness of the Minister's reassessments. This will require examination of each of the items in question in relation to the evidence.

(4) *Imposition of penalties* — In 1978, subsection 163(2) of the *Income Tax Act* provided:

> (2) Every person who, knowingly, or under circumstances amounting to gross negligence in the carrying out of any duty or obligation imposed by or under this Act, has made, or has participated in, assented to or acquiesced in the making of, a statement or omission (in this section referred to as a "false statement") in a return, certificate, statement or answer (in this section referred to as a "return") filed or made in respect of a taxation year as required by or under this Act or a regulation, is liable to a penalty of 25% of the amount, if any, by which
>
> (a) the tax for the year that would be payable by him under this Act if his taxable income for the year were computed by adding to the taxable income reported by him in his return for the year that portion of his understatement of income for the year that is reasonably attributable to the false statement
>
> exceeds
>
> (b) the tax for the year that would have been payable by him under this Act had his tax payable for the year been assessed on the basis of the information provided in his return for the year.

This subsection was amended both before and after this date, but the essential language remained the same for the purposes of this case.

These provisions mean that the 25 per cent penalty can only be applied if it is shown that the taxpayer "knowingly, or under circumstances amounting to gross negligence" has made a "false statement" in a return or has somehow participated or acquiesced in the making of that statement. By virtue of subsection 163(3) "the burden of establishing the facts justifying the assessment of the penalty is on the Minister". It will be noted that for the penalty to be applicable there appears to be a higher degree of culpability required, involving either actual knowledge or gross negligence, than is the case under subsection 152(4) for reopening assessments more than four years old where mere negligence seems to be sufficient. The jurisprudence under these subsections will be examined more fully later. It may be noted at this point that, as I understand it, the parties are in agreement that the amounts which would be subject to penalties, if subsection 163(2) is applicable, for the years 1972-78 inclusive would be $283,448. The particulars year by year are set out in Exhibit D-54.

(5) *Partnership* — The taxpayer contends that during the years 1972-78 the income attributed to him was in fact the income of a partnership between himself and his wife so that the income should be equally attributable to his wife.

Background

The taxpayer, Lucien Venne was 49 years old at the time of the trial, having been born in Timmins. He grew up speaking French at home and learned English from his friends. He went to school for eight years and completed grade 5. The school used French as the language of instruction. He says that he can read and write both English and French and not very well in either case. He left school at fourteen and went to work in garages. In 1962 he went into a garage business with his brother Roger. There he says Roger looked after the business affairs and he was involved with the mechanical and service end of the business. In 1967 he sold his share to Roger for $17,000.

It is appropriate to note at this point that Lucien Venne was married in 1955. He and his wife Grace both testified that prior to marriage they had each developed the habit of keeping their savings in cash at home. At the time of their marriage they pooled their financial resources, some $3,000 in cash, which they kept at home. They continued to add to it through savings which they accumulated at the rate of about $1,000 a year. In 1965 Mr Venne bought a seond-hand safe of sizable proportions — some four feet high and two feet wide — in which they thereafter kept the cash they had at home. When Mr Venne received a cheque for $16,000 with respect to the sale of his share of the business to his brother in 1967, he cashed the cheque and also put this money in the safe at home. There was much other evidence of the comings and goings of cash in and out of this safe but save for one or two further incidents I need not go into these details.

When he sold his share of the garage business to his brother, Mr Venne then leased a service station from Shell Oil. In 1968 he bought the building adjacent to the Shell station, paying $16,000 for it. He and his wife sold their house on Bannerman Street and moved into the upstairs apartment in that building, using the lower floors for the business. From these modest beginnings in 1967-68 Mr Venne developed a very successful business known as the Shell Clinic and Luke's Sports and Marine. It had substantial gross sales, reaching as high as $595,000 in 1975. Through much of this period the Vennes lived on the business premises and Mrs Venne often assisted in the business. In particular she balanced the cash at the end of each day and made bank deposits. The service station was operated seven days per week. In early 1976 Mr Venne sold this business for $190,000 plus the value of the inventory. Thereafter he opened another business of his own which was incorporated in 1978 as Luke Venne Enterprises Limited. It is apparently a wholesale marine and snowmobile business. This business was started on property on McBride Street bought by the Vennes in 1973 as a home, at which time they had moved out of the business building on Algonquin Street and rented out the apartment there.

During the period in question, from 1971 to at least 1977 (the period covered by the "net worth" statement prepared by the defendant and not, in this respect, disputed by the plaintiff) the other important source of income for Mr Venne apart from his business was mortgage interest. Starting with the remnants of a mortgage which they had taken in 1968 when they sold their house on Bannerman Street, he had by 1977 over $150,000 in mortgages. The largest part of this latter figure apparently came from moneys received on the sale of the business in 1976. Failure to declare large amounts of interest from some of these mortgages as income was one of the major factors in the reassessments by the defendant.

Also of interest is the succession of bookkeepers or accountants whom Mr Venne employed over the years in question. It appears that at the time of the commencement of operation of the Shell station and of the Sports and Marine business on Algonquin Street a Mr St-Jacques was employed as a bookkeeper. He set up for Mr Venne a system of recording sales and inventory which Mr Venne continued to employ through at least two successive bookkeepers, Mr Kelly and Mr Barnes. Mr Kelly, who succeeded Mr St-Jacques, indicated by 1972 that to carry on with Mr Venne's bookkeeping he would have to double his fee. At that point Mr Venne instead hired Mr Barnes, also a bookkeeper. Mr Venne insists that this was not done to save money as he never even inquired from Mr Barnes how much he would charge. In 1978, some time after it became known to Mr Venne that Mr Barnes was himself the object of legal proceedings with respect to income tax, Mr Venne switched to a chartered accountant, Mr Charette, to look after his accounting. In 1979 he engaged a different chartered accountant, Mr Dobson, whose firm of Dobson and Reid subsequently undertook extensive work to produce proper financial statements for the years in question and to represent Mr Venne's interest *vis-à-vis* the Department of National Revenue which was by this time conducting an investigation with respect to Mr Venne's income tax.

It appears that a relatively simple method of record-keeping was used at the service station and marine business which Mr Venne operated from 1967 to 1976. All sales, cash or charge, were punched into a cash register. There were sales receipts covering items sold and work orders with respect to service work done at the service statement. Major bills were paid by cheque, or in the case of payment for deliveries of gasoline supplies, through use of credits based on gasoline bought by customers with credit cards. Some small expenses were paid in cash. At the end of each month usually Mr Venne, or sometimes Mrs Venne, would take the copies of all receipts, work orders, cash register tapes, and cheque stubs for the month to the bookkeeper who was, during the years in question here, Mr Barnes. At the end of the year the Vennes would take inventory and also provide that information to Mr Barnes. According to Mr Venne, Mr Barnes would then prepare the income tax return which Mr Venne would in due course sign.

Central to Mr Venne's position now is the proposition that he was not personally responsible for the many errors committed by Mr Barnes in the completion of these income tax returns. Mr Venne testified that he found it almost impossible to understand income tax returns, that successive bookkeepers tried to explain these matters to him but he found them almost entirely incomprehensible. He insisted that he signed the forms without verifying the information in them or indeed without understanding its purport. He even testified that he had not noticed until the trial that, because of the wording of the income tax form, when he signed such a form he was thereby certifying the truth of the information in the form. Counsel for the plaintiff also sought to introduce evidence to demonstrate Mr Barnes' general incompetence although I refused to admit most of this evidence. It was in my view essentially opinion evidence being proffered by a witness who was not, because of a failure by the plaintiff to comply with rule 482, entitled to testify as an expert.

Conclusions

(1) *Power to reassess for more than four years* — I have concluded that the plaintiff here has made misrepresentations attributable to neglect or carelessness and therefore it is open to the Minister to reassess his tax for the taxation years 1972, 1973, 1974, and 1975.

I am satisfied that it is sufficient for the Minister, in order to invoke the power under subparagraph 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 neglect" must mean, particularly when combined with other grounds such as "carelessness" or "wilful default" which refer to a higher degree of negligence or to intentional misconduct. Unless these words are superfluous in the section, which I am not able to assume, the term "neglect" involves a lesser standard of deficiency akin to that used in other fields of law such as the law of tort. See *Jet Metals Products Limited* v *MNR*, [1979] CTC 2738; 79 DTC 624 at 2755 [636-37].

The plaintiff devoted a good deal of effort during the trial to demonstrating that his bookkeeper during these years, Mr Barnes, was grossly negligent or incompetent or both. To be sure, there is ample evidence to suggest that Mr Barnes did not do an adequate job of preparing the plaintiff's tax returns. In some cases this worked against the interests of the taxpayer and cannot be assumed to have reflected his true wishes. Further, I am satisfied from the evidence that many of the subtleties of income tax law and of accounting were beyond the understanding of the taxpayer.

Nevertheless, there are two salient forms of evidence which have convinced me that the taxpayer did not exercise reasonable care in the completion and filing of his income tax returns and that this negligence resulted in misrepresentations being made in the returns.

First, there is ample evidence that the taxpayer did not read his returns before signing them. He admitted this on several occasions: see the examination for discovery of the plaintiff, questions 124, 420, 608, 740, and 859. There was also a specific admission by him with respect to one of the years in question, 1973, that he had not read the return: see examination for discovery of the plaintiff, question 420. While one cannot expect a person with the plaintiff's limited education and limited experience with accounting matters to understand fully the details of a tax return, in my view he cannot absolve himself from all responsibility by hiring what he now says to be a patently inadequate bookkeeper and leaving matters entirely in the latter's hands. See for example *Howell* v *MNR*, [1981] CTC 2241; 81 DTC 230 at 2243-44 [233]. Secondly, the errors in the income tax returns should have been sufficiently obvious that a reasonable man of even limited education and experience, especially one who was apparently a very successful businessman and investor, should have noticed.

This conclusion is based partly on the magnitude of the unreported income during the years 1972-1975. In 1972 the plaintiff reported income of $9,248. He now admits that there was further unreported income in that year of $12,962 (see Exhibit D-44). The Minister estimates the amount of unreported income in 1972 to be $13,042, and I accept the evidence of Mr Panella, special investigator for the Department of National Revenue, on this point (see Exhibit D-50 and transcript pages 34-36). For the taxation year 1973 the total income reported by the taxpayer was $8,594. He now admits that there was further unreported income in the amount of $49,391 for that year. The Minister has estimated the unreported income of the taxpayer that year to have been an even further $19,500, for a total unreported income of $68,891. I need not decide for this purpose whether I accept the Minister's figure. For the taxation year 1974, the total income reported by the taxpayer was $13,546. He now admits that there was $2,305 of income unreported. The Minister has assessed the unreported income at $39,804 which includes a sum of $30,000 that will be referred to later (see transcript pages 39-43). In 1975, the taxpayer reported income of $26,148. He now admits that there was further unreported income in the amount of $65,735. The Minister essentially agrees with the latter figure although he estimates the amount as being $20 more, namely $65,755. I think it is apparent from the order of magnitude of these amounts of unreported income, even (with the exception of 1974) as estimated by the taxpayer, that a reasonable taxpayer would have suspected that there was something deficient in the income tax returns which he was signing during this period.

As for 1974, there was at least one example of a flagrant oversight which would have been perceived by a moderately competent businessman who by this time had learned of the profitability of lending money on mortgages. It appears that during 1974 he had earned interest of $1,083.03 on a mortgage he held from a Robert Fournier. The plaintiff admitted that none of this amount was shown on his income tax return (see examination for discovery of plaintiff, question 427) although his attention could readily have been drawn to the fact that interest was taxable by the entry in his income tax return of an amount of "interest in investment income" of $481.92 which apparently reflected amounts of interest shown on T-5 slips with respect to other interest earnings.

Further, the plaintiff should have been led to question the modest income which he was reporting having regard to the steady growth in his bank accounts. From the end of 1971 to the end of 1972, his cash in bank grew from $7,706 to $16,031, while his total income reported for 1972 was $9,248. At the end of 1973 his cash in bank had grown to $34,614, while his reported income for 1973 was $8,594. By the end of 1974 his cash in bank had grown to $57,881 while he reported income that year of $13,546. At the end of 1975 his cash in bank had grown to $123,215 while he reported income that year of $26,148. Assuming that throughout this period he was spending several thousand dollars at least for the living expenses of himself and his family these sizable net accretions in his bank accounts should have at least led him to question his bookkeeper.

It is admitted by the plaintiff (see Exhibit D-44) that there were these substantial misrepresentations of income during the years 1972-1975 and indeed thereafter in 1976 and 1977. I am satisfied that these misrepresentations were attributable to neglect on the part of the plaintiff within the meaning of subparagraph 152(4)(a)(i) of the *Income Tax Act* because the plaintiff did not make any effort to question and supervise aspects of his income tax returns which he was clearly able to do. He ignored the deficiencies in those returns which would have been obvious to him had he made a serious effort to ensure their accuracy. I therefore find that it was open to the Minister by his reassessment of September 3, 1980, to reassess the plaintiff's income tax for the years 1972-1975.

(2) *Exclusion of certain income from such extended reassessment* — As noted earlier, the plaintiff did not seek to rely on paragraph 152(5)(b) of the *Income Tax Act* in order to show that the failure to report any particular item of income or to report it accurately during 1972-75 occurred without negligence, etc, and since I have found against him on that question and no case has been made for the exclusion of any particular item of income under paragraph 152(5)(b) the Minister can assess tax on all unreported items of income including those unreported in taxation years 1972-1975.

(3) *Amount of unreported income* — Having concluded that it is open to the Minister to assess additional income tax in all of the years in question, there remain some items of income which are in dispute.

For the years 1972-1977 the defendant says that the unreported income totals $330,934. The plaintiff admits that for that period the unreported income was $283,501. I will deal with the particular items where there is disagreement.

For 1972, the defendant assessed the unreported income at $13,042, $80 more than admitted by the plaintiff. The plaintiff has not demonstrated, as is his responsibility, that the defendant is in error and I therefore accept the defendant's assessment.

With respect to 1973, the plaintiff admits to $49,391 in unreported income whereas the defendant says the correct figure is $68,891. The difference of $19,500 is based on the assumption that deposits totalling this amount which were made to the plaintiff's bank account in July, 1973, by Mrs Venne represented income which was not otherwise reported. Copies of the deposit slips were entered as Exhibit D-10. The plaintiff and his wife gave various explanations about the origins of this cash but the common thread running throughout, which I accept, was that the money came from the safe which the plaintiff had in his home. I believe that, from the evidence of Mr and Mrs Venne and their daughter Pat, it is sufficiently established that there was a safe and that substantial amounts of cash were kept in it. The defendant tried to link somehow all of this money with a gap which existed in the tapes of the business for July 24, 1973, suggesting that certain business income had been deleted from the tapes in this manner. I was satisfied with the plaintiff's explanation of the gap in the tapes as being the result of the repair and servicing of the machine. (See transcript pages 893-97). I am also satisfied that all or most of the $19,500 in question with respect to 1973 had its origin in savings effected by Mr and Mrs Venne since their marriage in 1955. Both Mr and Mrs Venne testified that they had a few thousand dollars in savings at the time of their marriage and that they had put aside something in the order of one thousand dollars per year since that time, all of this money being kept in the safe at home. While a further approximately $16,000 resulted from the sale by the plaintiff to his brother of his share in Venne Auto Sales (see Exhibit D-2), a similar amount would have been paid out in 1968 when the Vennes bought property adjacent to the Shell Station and incorporated it in their business activities. It is consistent with the evidence and quite credible that a further $19,500 in cash remained in the safe in July, 1973 when Mrs Venne deposited the money in the bank, apparently in order to enable them to write a cheque for the purchase of the property on McBride Street to which they moved that year. I think the plaintiff has therefore met the burden of proof in this respect and I therefore find that the plaintiff's 1973 income should be reassessed on the basis of his own admission that there was unreported income in the amount of $49,391 rather than the $68,891 previously assessed by the defendant.

With respect to 1974, the plaintiff admits to unreported income of $2,305 whereas the defendant has assessed the unreported income as being $39,804. The higher assessment of the defendant is explained by the evidence of its witness, Mr Panella, at 40-43 of the transcript. I accept the defendant's position that there should be an addition to the income of $8,000 based on an error in the net worth with respect to the cost of land, and the reduction of $500 based on an error of the net worth concerning mortgages receivable. This leaves the amount of $30,000 which was deposited in the plaintiff's account on August 15, 1974 by Mrs Venne. (See Exhibit D-11). The defendant assumed that this represented income otherwise unreported by the plaintiff. The plaintiff and his wife have explained that this money also came from the safe. Further they say that the large quantity of cash that was in the safe which, according to them, was all intermingled regardless of source, came in part from a sum of $36,000 or $37,000 given to the Vennes for safekeeping in November, 1972, by Mrs Venne's mother, Mrs Cunningham. Mr Cunningham had died in October, 1972. He had died while in his sixties, having been retired a number of years from his employment as a miner due to ill health. The Cunninghams lived in a rented one-bedroom house in South Porcupine. They did not own a car and spent very little money, according to Mr Venne. According to the evidence of Mr and Mrs Venne (see transcript 935-37, 1093-1105, 1175-82), Mrs Cunningham said that she and her husband had kept this money in a trunk and that she was nervous about having it in the house after her husband had died. Knowing that the Vennes had a safe, Mrs Cunningham asked them to keep the money for her. Further, the Vennes said that they never counted the money to be sure exactly how much had been given to them for safekeeping, nor did they keep it separate and apart in the safe. They testified in effect that the money had been mixed with their own and used for a variety of purposes including investing in mortgages from which Mr Venne collected the interest. When Mrs Cunningham died, in January, 1980, the money simply remained with the Vennes. There was no will and no letters of administration. Both the Vennes indicated quite clearly that they had not divided the money with other members of the family, namely Mrs Venne's two sisters and two brothers. Nor did they advise the other members of the family of the fact that they had this amount of money in safekeeping for Mrs Cunningham although there was some suggestion that the brothers and sisters were aware that the Vennes were keeping some money for her. I am unable to accept this account as the source of a sufficient amount of cash to provide the $30,000 deposited in the bank on August 15, 1974. In my view it defies credibility. First, it is quite improbable that the Cunninghams who lived extremely modestly would have accumulated such a sum of money or would have kept it in such a way as to forego earning any interest on it, even simple savings account interest. There was some evidence that an unspecified portion of the money had come from an inheritance from Mrs Cunningham's uncle, although no details were provided. But even if the Cunninghams had such money, which is not otherwise relevant to this case, I am unable to accept that the money was turned over to the Vennes and handled by them on the terms which they described. First, it is incredible that no one, neither Mrs Cunningham nor either of the Vennes ever counted the money which was being turned over to them temporarily for safekeeping. This is particularly unlikely as the money was supposedly put in the safe without any identification and without being kept separate from the money of the Vennes. It is also difficult to believe that during the remaining eight years of her life Mrs Cunningham neither required any of this money nor did she apparently tell her other children of the amount involved. Nor was any question raised by any member of the family after her death. It is particularly hard to believe that the Vennes would not feel some obligation to share this knowledge, and perhaps some of the money, with Mrs Venne's brothers and sisters after the death of Mrs Cunningham. It is also notable that when Mr Panella, the special investigator from Revenue Canada, questioned Mr Venne in May, 1979 about sources of cash other than business no mention was made of this alleged, not inconsiderable, sum of $36,000 or $37,000. The explanation based on Mrs Cunningham as the source was not offered until the time of the examination for discovery of the plaintiff in October, 1982. (See transcript 41-43). There was no corroboration of the evidence of Mr and Mrs Venne on the existence of the Cunningham money or its amount. The only evidence offered by the plaintiff in this respect was the testimony of his daughter Patricia Hamelin who simply testified as to the existence of the safe and that she once saw cash in it. She could not specify when this happened. She said she had never used the safe and she never counted the cash in it nor did she estimate how much cash was in it. On cross-examination she agreed that in 1972 she would have been about 14 years old. This evidence was in no way helpful to corroborate the source or quantity of the alleged Cunningham money. I therefore do not accept that this money was the source of unexplained infusions of cash such as the deposit by Mrs Venne on August 15, 1975 of $30,000. I therefore confirm the assessment by the defendant of the plaintiff's income for 1974.

With respect to 1975, the taxpayer admits that there was unreported income in the amount of $65,735. The defendant says the correct amount is $65,755. According to Mr Panella this reflects a typographical error. This was not refuted by the plaintiff and I therefore confirm the assessment made by the defendant for 1975.

With respect to 1976 the plaintiff admitted unreported income of $98,797 whereas the defendant assessed it at only $98,496. The plaintiff, has, understandably, not demonstrated an error in the defendant's assessment and I therefore accept the latter.

Similarly, with respect to 1977, the plaintiff admitted unreported income of $54,311 whereas the defendant asserted that the amount was only $52,399. I therefore confirm the assessment of the defendant.

With respect to 1978 there was no admission by the plaintiff as to unreported income. In its notice of reassessment of September 3, 1980 the defendant reassessed the plaintiff's income at an amount $17,456.77 higher than that reported, of which one item was unreported interest in the amount of $8,408. It appears now that the parties agree that this particular item should instead be $7,175. (See Exhibits D-44, D-54; transcript 51, 1069-70). The plaintiff has not otherwise demonstrated any error in the defendant's reassessment and I therefore confirm the latter subject to the agreed reduction from $8,408 to $7,175 with respect to unreported interest.

(4) *Imposition of penalties* — As noted earlier, in order for the defendant to levy penalties under subsection 163(2) of the *Income Tax Act* it is necessary that the taxpayer have "knowingly, or under circumstances amounting to gross negligence ... participated in, assented to or acquiesced in the making of" a false statement in a return, etc. The similar language of subsection 56(2) of the former *Income Tax Act* was interpreted by Cattanach, J in *Udell* v *MNR*, [1969] CTC 704; 70 DTC 6019. In that case a farmer had retained a certified public accountant to prepare his income tax returns. The accountant made several errors in different taxation years in the process of transposing figures from the taxpayer's account books to his working papers. In some of the years in question the accountant signed the returns on behalf of the taxpayer before they were seen by the later and in other years the taxpayer reviewed them first and then signed them. He apparently did not notice any errors. The Minister of National Revenue assessed penalties with respect to these errors. In interpreting the language now found in subsection 163(2) of the present *Income Tax Act*, Cattanach, J said, at 713-14 [6025-25]:

> Accordingly there remains the question of whether or not section 56(2) contemplates that the gross negligence of the appellant's agent, the professional accountant, can be attributed to the appellant. Each of the verbs in the language "participate in, assented to or acquiesced in" connotes an element of knowledge on the part of the principal and that there must be concurrence of the principal's will to the act or omission of his agent, or a tacit and silent concurrence therein. The other verb used in section 56(2) is "has made". The question, therefore, is whether the ordinary principles of agency would apply, that is, that what one does by an agent, one does by himself, and the principal is liable for the actions of his agent purporting to act in the scope of his authority even though no express command or privity of the principal be proved.
>
> In my view the use of the verb "made" in the context in which it is used also involved a deliberate and intentional consciousness on the part of the principal to the act done which on the facts of this case was lacking in the appellant. He was not privy to the gross negligence of his accountant. This is most certainly a reasonable interpretation.
>
> I take it to be a clear rule of construction that in the imposition of a tax or a duty, and still more of a penalty if there be any fair and reasonable doubt the statute is to be construed so as to give the party sought to be charged the benefit of the doubt.

In coming to this interpretation the learned judge had regard to the fact that the subsection in question is a penal provision and it must be interpreted restrictively so that if there is a reasonable interpretation which will avoid the penalty in a particular case that construction should be adopted. He concluded that the erroneous information in the returns was not included with the knowledge of the taxpayer nor could the gross negligence of the accountant be attributed to him.

It is also important to keep in mind in applying this subsection that by subsection 163(3) the burden of proof is on the defendant in justifying the assessment of a penalty.

I have come to the conclusion that the defendant has not sufficiently proven that the misstatements were made "knowingly" by the plaintiff in his tax returns for the years in question. I should note here, as it is relevant to the whole question of the application of penalties under subsection 163(2), that there seems to be a certain element of subjectivity recognized in the case law with respect to assessing the knowlege or gross negligence of a taxpayer with respect to misstatements in his return: see, eg, *Howell* v *MNR*, (*supra*), at 2245 [234]; *Joris* v *MNR*, [1981] CTC 2596; 81 DTC 470 at 2598 [472]. The taxpayer here is a man with a grade five education, working and paying taxes in a language which is not his first language nor that in which he was educated, a man who is more at ease in a garage than in an office. Not only do these factors militate against a finding that the misstatements in his return were made knowingly by him, but also his entire course of conduct is not consistent with that of a person who had deliberately set out to conceal large amounts of taxable income. He kept what appear to be quite complete records of sales in his business, then turned these over to his bookkeeper. As far as one can judge from the evidence, all or most of the revenues from the business were deposited in the bank where the moneys could readily be traced. He also lodged all but one or two of the mortgages on which he lent money with banks and trust companies which kept careful records of the income earned from these "escrow mortgages". It is unlikely that a person planning to conceal income would have handled his affairs in this manner. Further it is hard to believe that he was consciously and effectively supervising his bookkeepers since a number of the errors made in his returns were to his disadvantage, even though more of them were to his advantage. I am therefore not able to conclude that the misstatements in the returns were made "knowingly" by the plaintiff.

With respect to the possibility of gross negligence, I have with some difficulty come to the conclusion that this has not been established either. "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. I do not find that high degree of negligence in connection with the misstatements of business income. To be sure, the plaintiff did not exercise the care of a reasonable man and, as I have noted earlier, should have at least reviewed his tax returns before signing them. A reasonable man in doing so, having regard to other information available to him, would have been led to believe that something was amiss and would have pursued the matter further with his bookkeeper.

With respect to business income, I can more readily recognize that effective surveillance would have been difficult for the plaintiff and would have involved him making and reviewing numerous computations of revenues, expenditures, assets, and liabilities. In other words the errors in business income, small in some years but very substantial in others, would not necessarily have "sprung out" at a person of the taxpayer's background and abilities. While it may have been naive for him to trust his bookkeeper as knowing more about such matters than he did, I do not think it was gross negligence for him to fail to challenge the bookkeeper with respect to the business computations. However egregious the errors committed by the bookkeeper in this respect, it is quite conceivable that theyd were not in fact noticed by the plaintiff and his neglect in not noticing them fell short of constituting gross negligence. For other examples of such a situation see *MNR* v *Weeks*, [1972] CTC 60; 72 DTC 6001; *Mark* v *MNR*, [1978] CTC 2262; 78 DTC 1205; *Snelgrove* v *MNR* [1979] CTC 2938; 79 DTC 780; *Morgan et al* v *MNR*, [1973] CTC 2192; 73 DTC 146.

With respect to most of the unreported interest income, however, I have more difficulty avoiding the conclusion that the plaintiff was grossly negligent. His position is essentially that prior to 1976 (when very little interest income was earned), he did not know that interest was taxable. Commencing with the 1976 taxation year, he became aware that it was but he believed that the only portion of interest which was taxable was that which was included in a T-5 form. (See transcript pages 955-56, 966, 980, 1002, 1003, 1024, 1045). As mentioned above, most of the mortgages on which the plaintiff earned interest were lodged with the Ontario Trust Company, the Bank of Nova Scotia, or the Canada Trust Company. In most of the years in question these institutions issued T-5 slips to the plaintiff with respect to interest earned on his accounts in those institutions but these slips did not include interest collected by them on his behalf on the escrow mortgages which they held for him. At the same time however the plaintiff appears to have kept careful records at home concerning these mortgages, recording each month the amount of principal and interest paid and the balance still owing. (See eg, Exhibits D-15, D-28 to 31). There was apparently further confusion caused in 1976 by the fact that after the sale of his business the plaintiff had a certificate of deposit at the Bank of Nova Scotia on which over $12,000 of interest was credited to him in 1976, but no T-5 was issued by the bank for that. Although in that year the plaintiff declared interest and other investment income in the amount of $15,419 which included other sources of interest covered by T-5s in the amount of $2,276, it was not clear whether the remaining $13,000 declared by him was with respect to the interest from the certificate of deposit or to interest from mortgages from which the plaintiff had also earned a somewhat similar amount. I can only conclude that the plaintiff knew, or was readily able to ascertain, how much interest income he was earning year by year from mortgages and from bank accounts, trust company accounts, certificates of deposit and like instruments. This was not a difficult concept and well within the plaintiff's abilities which, the evidence demonstrates, easily included the addition of sums and the calculation of interest. His explanation for not reporting all his interest income, however, is that he was not concerned about possible discrepancies between the amount of interest he knew, or could ascertain, that he was earning, and the amount reported in his income tax returns, because he thought the T-5 issued by the banks and trust companies was the governing instrument indicating how much of the interest was taxable. That he might have reached such conclusion is not completely improbable because taxpayers have long been confused by a complex system of taxation in which the taxable amount from certain sources does not always correspond to the amount actually received.

It is difficult to decide whether a mistake such as this is one of fact or of law. If his mistake was in thinking that the T-5s from the banks and trust companies accurately recorded all interest income relevant to completion of his tax returns, perhaps it could be seen as a mistake of fact. If his mistake was in thinking that interest from the "escrow mortgages" was not taxable, this could more readily be seen as a mistake of law. I am not sure that it matters which kind of a mistake is involved. After reviewing a number of previous decisions on subsection 163(2) or its predecessors I have been unable to find any clear authority on whether a mistake of law is a defence to the application of penalties thereunder. I am inclined to think that it can be, depending on the circumstances and the state of understanding of the taxpayer. 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 subsection 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. The section has in the past been applied subjectively to taxpayers, taking into account their intelligence, education, experience, etc, and I believe this implies that an ignorance of the law which is not unreasonable for the particular taxpayer in question and the particular circumstances may be acceptable as a defence to the application of penalties. On this basis, and having regard to the fact that the onus is on the Minister to prove that the penalty should be applied, I find the evidence ambiguous and therefore conclude that the penalty should not be applied even in respect of the unreported income from interest.

I have therefore reached the conclusion that penalties under subsection 163(2) may not be assessed on the unreported amounts of income arising during the years 1972 to 1978 inclusively.

(5) *Partnership* — In his pleadings the plaintiff claims that in the taxation years 1972 to 1978 income attributed to him was in fact income earned by himself and his wife in partnership and thus the income was equally attributable to his wife. There is no evidence to substantiate this allegation.

During the years in question the plaintiff filed his income tax returns on the basis of a sole proprietorship and claimed his wife as a dependant (see Exhibit D-45). Dealer leases and sales contracts, insurance certificates and an agreement with Shell for business and property management, all connected with the business, were in the name of the plaintiff alone (see Exhibits D-33 to D-41). The dissolution of the proprietorship of Luke's Sport and Marine was signed by him alone (Exhibit D-42). The new business, Luke Venne Enterprises Limited was subsequently incorporated by him alone (see Exhibit D-44).

The plaintiff stressed that the property at 181 Algonquin which was adjacent to the Shell Clinic and which was bought by the Vennes in 1969 was registered in their joint names. He further contends that the value of the land and buildings which the plaintiff sold in 1976 with the sale of the business represented $127,000 of the $190,000 sale price. Therefore interest earned from the reinvested proceeds of the sale of the land and buildings should be attributed equally to Mr and Mrs Venne. The evidence shows however that the building at 181 Algonquin was purchased with money received by the plaintiff from the sale to his brother of his share of Venne Auto Sales (see transcript 1193). That partnership interest in Venne Auto Sales was in his name alone (see Exhibit D-2). One can only assume that the premises at 181 Algonquin were put in the joint names of husband and wife because it was to be their home as well as part of their place of business. Viewing the evidence as a whole there is no substantial evidence of any partnership agreement between Mr and Mrs Venne. This is perhaps another example of the plaintiff's limited understanding of business and taxation matters but, given the fact that there was never any suggestion in the income tax returns of the existence of a partnership nor in any other documents where one might expect to see it, I cannot find any basis on which to declare now that one half of the plaintiff's income was in fact the income of his wife. While Mrs Venne said in her evidence that she considered herself to be a partner (see transcript 1192) it is clear from the context that she was speaking of a partnership of husband and wife in which she contributed what she could — and it was very considerable — to the success of the business. Rightly or wrongly, she had felt that to be her duty. She said they had never discussed the division of profits between them. She obviously assumed that she would also benefit from whatever profits her husband might make from the business and that she would contribute to it what she could. But there was no suggestion of any formal division of that income.

I therefore do not accept the plaintiff's allegation that a partnership existed in the sense that one half of the income should now be ascribed to Mrs Venne.

Considering that success has been divided in this case no costs will be awarded.