Docket: 2007-4165(IT)G

BETWEEN:

KAREN FAITH PEARSON,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

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Appeal heard on June 8, 2009, at Kamloops, British Columbia

By: The Honourable Justice Campbell J. Miller

Appearances:

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|---|---|
| For the Appellant: | The Appellant herself |
| Counsel for the Respondent: | Nadine Taylor Pickering |

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**JUDGMENT**

The appeal from the assessment made under section 160 of the *Income Tax Act*, notice of which is dated March 22, 2007, and bears number 38982, is dismissed, with costs.

Signed at Vancouver, British Columbia, this 23rd day of June, 2009.

"Campbell J. Miller"

C. Miller J.

Citation: 2009 TCC 338
Date: 20090623
Docket: 2007-4165(IT)G

BETWEEN:

KAREN FAITH PEARSON,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

**REASONS FOR JUDGMENT**

Miller J.

[1] Mr. Paul Pearson ran a successful trade show business during the 1990s and into the new century. As a result of a Canada Revenue Agency (CRA) audit, he became liable to the Government of Canada for close to $1 million in early 2004. He struggled to keep the business afloat. His daughter, the Appellant Karen Pearson, assisted her father in 2004 with the business for which he said he paid her $600 every two weeks. Over and above that were cheques to her of approximately $27,000 in that year, which both father and daughter claim were for Mr. Pearson's business or personal needs, and not for the benefit of the Appellant herself. The Appellant has been assessed pursuant to section 160 of the *Income Tax Act* on the basis that Mr. Pearson transferred this property, the $27,000, to her for no consideration, and that she is therefore jointly and severally liable for her father's tax liability up to the amount transferred.

[2] What are the circumstances surrounding Ms. Pearson's cashing of $27,000 of cheques made out to her by her father in 2004? One must go back a few years to 1993 when Mr. Pearson started his business of operating log home trade shows. He ran the shows in Canada and the United States. He hired commissioned salesmen to get exhibitors, and he paid the salesmen a 20% commission, or in the case of Mr. Scott, who testified, 20 or 25% depending on the size of the contract he obtained. Mr. Pearson paid his salesmen every Friday in cash. He or his receptionist would go to the bank to get the cash. The business appeared to be successful.

[3] In 2003, CRA conducted an audit of Mr. Pearson, leading to a possible reassessment of over $1 million. Mr. Pearson and CRA reached an agreement in February 2004 on a liability of approximately $936,000, CRA having allowed some expenses and dropping gross negligence penalties. Mr. Pearson looked to new ways to earn income. He attempted to get into the log home building magazine business and hired his daughter, the Appellant, to assist in that regard throughout 2004. On Examination for Discovery, Ms. Pearson could not correctly recall the name of the magazine in question. Mr. Pearson claims he paid his daughter $600 every two weeks, amounts which she did not report on her 2004 tax return. Records of these payments were not accounted for on a review of his bank account, though he claimed he maintained a separate U.S. account, the records of which were not before me. Also, in a letter of February 2007 addressed to whom it may concern, Mr. Pearson indicated “Karen did not work for me in 2004”.

[4] Mr. Pearson had less sales staff in 2004, but still indicated he paid them by cash. Mr. Scott, one of the salesmen, confirmed that is how he got paid in 2004. He also testified that he felt Ms. Pearson did most of the banking. She testified that in 2004, it was more convenient for her to go to the bank than for her father to go. She also testified that she may have kept the odd small amount of cash. Mr. Pearson claimed that while he went to the bank perhaps 20 times in 2004, he was not comfortable doing so and would rather his daughter went. The reason for this discomfort was that Mr. Pearson had been charged with a sexual offence that had been well publicized in the Kamloops media. He had served time many years previously for sex-related offences and had been on probation. Although he was acquitted of the more recent offence, he clearly felt the stigma and animosity of the community. He did, however, still get out and about in the community in 2004 as he had to do so for business purposes. He claims it was this embarrassment that was more the cause for sending his daughter to the bank. He maintained that the $27,000 cash that his daughter received was returned to him to cover business expenses, including salesmen’s commissions as well as his own personal expenses, which included feeding his cocaine and alcohol problem. The CRA claims payments to Karen started days after Mr. Pearson’s agreement with them concerning his tax liability, and that payments were to shift potential collectible funds from him to his daughter.

[5] The Crown seeks support for their position from the fact that Ms. Pearson and her partner only reported approximately $12,000 of income in 2004, though this does not include the approximate $14,000 she allegedly received as wages from her father,

and that the couple's living expenses would have far exceeded this income. The Crown asks where else would Ms. Pearson have got money to live.

[6] My impressions from Mr. Scott's testimony was that he and Mr. Pearson had an off-on relationship, but more importantly played fast and loose with rules and regulations, admitting they would drive under the influence, drive without a license and change GST numbers on documents. Life and business appear to have been something of a lark. Mr. Pearson earned some considerable money, did not pay the requisite taxes and declared bankruptcy. The CRA are now looking to the daughter to recover a small fraction of her father's debt.

[7] Ms. Pearson testified that she did not know in 2004 that her father owed the CRA about $1 million. Whether she did or did not should make no difference to the application of subsection 160(1) of the *Income Tax Act* which reads:

> 160(1) Where a person has, on or after May 1, 1951, transferred property, either directly or indirectly, by means of a trust or by any other means whatever, to
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> (*a*) the person's spouse or common-law partner or a person who has since become the person's spouse or common- law partner,
>
> (*b*) a person who was under 18 years of age, or
>
> (*c*) a person with whom the person was not dealing at arm's length,
>
> the following rules apply:
>
> (*d*) the transferee and transferor are jointly and severally liable to pay a part of the transferor's tax under this Part for each taxation year equal to the amount by which the tax for the year is greater than it would have been if it were not for the operation of sections 74.1 to 75.1 of this *Act* and section 74 of the *Income Tax Act*, chapter 148 of the Revised Statutes of Canada, 1952, in respect of any income from, or gain from the disposition of, the property so transferred or property substituted therefor, and
>
> (*e*) the transferee and transferor are jointly and severally liable to pay under this Act an amount equal to the lesser of
>
> (i) the amount, if any, by which the fair market value of the property at the time it was transferred exceeds the fair market value at that time of the consideration given for the property, and
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> (ii) the total of all amounts each of which is an amount that the transferor is liable to pay under this *Act* in or in respect of

> the taxation year in which the property was transferred or any preceding taxation year,
>
> but nothing in this subsection shall be deemed to limit the liability of the transferor under any other provision of this Act.

[8] Before addressing the section 160 requirements, I want to briefly address the motivation of the Pearsons and, hand-in-hand with that, their credibility. As I indicated previously, my impression of Mr. Pearson was of someone not diligent in abiding by rules, and arranging his affairs with little regard to the details of accurate accounting and reporting. I do not reach this view from his criminal background, but from his approach to commerce generally; for example, underreporting, limited documentation and cash dealings. I add to this impression, his contradictory statements; for example, his February 2007 correspondence definitely stating his daughter did not work for him versus his trial evidence that he paid her $600 every two weeks for working on a magazine. I garnered little comfort from Ms. Pearson's evidence from discovery that she could not correctly recall the name of the magazine of which her father considered her the publisher. Further, the fact that she never reported the $14,000 she received as wages adds to my suspicion as to what arrangement really existed between father and daughter. My concern with their testimony is again engaged when I hear that they are close, but not so close that dad would not reveal to his daughter a $1 million CRA liability, especially as that was purportedly the trigger for getting a magazine going: an attempt to raise funds to pay off this debt.

[9] Also, Ms. Pearson, in first describing why she did the banking, suggested it was because it was more convenient for her, with no real explanation as to the inconvenience to Mr. Pearson, other than it was sometimes hot and he was a big man. Yet Mr. Pearson's whole thrust in this regard was his wanting to stay out of the public eye due to the sexual offence charges. However, he did still go to the bank and did many other transactions clearly indicating he was out and about in the community.

[10] The only arms-length employee to be called as a witness, Mr. Scott, was not a strong corroborative force, suggesting that comments about Mr. Pearson being a thief were to be taken lightly and using fictitious GST numbers was just a joke. No, the conclusion I reach with respect to the Appellant's witnesses is not a favourable one. So where matters hang in the balance, I tip the balance against the Pearsons.

[11] I turn now to the requirements of the application of section 160:

(i) a transfer of property;

(ii) the transferor and transferee are not dealing at arm's length;

(iii) no consideration or inadequate consideration flowing from the transferee to the transferor; and

(iv) the transferor must be liable to pay an amount under the *Act* in and only in respect of the year the property was transferred or any preceding year.

[12] As was the case in *Gambino v. Canada*,[1] requirements two and four have been met and requirements one and three are in dispute.

(i) *Was there a transfer of property?*

[13] If I conclude that Ms. Pearson had control over the cheques that she received from Mr. Pearson, and subsequently the cash obtained from cashing those cheques, then there has been a transfer of property. Even, according to comments of the Federal Court of Appeal in the case of *The Queen v. Livingston*,[2] if I found that she only got those funds as trustee for her father, there would still have been a transfer. It was not argued she was a bare trustee. Could she have endorsed a cheque to a third party? Could she have pocketed some of the cash? I believe she could have, and indeed, she acknowledged she could take a small amount if needed, for example, for groceries. But further, and more significantly, Ms. Pearson has not proven to me on balance that she did return all the funds to her father. This is where credibility comes into play. When I look at the minimum earnings Ms. Pearson and her partner had in 2004 and I assess the veracity of the Pearson story, I simply cannot conclude that on balance she returned all funds to her father. Indeed, I am satisfied she did not. She may have returned some, but I have no way to determine how much, and it is for her to satisfy me on that score. This is not a situation where I can with any basis in fact divide the amount between her and her father.

[14] But even if I found she did return the monies to her father, did she do so as she was simply his agent, akin to an arm's length employee conducting her employer's banking? The stories from the Pearsons are just not cohesive enough for me to find

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[1] 2008 TCC 601.

[2] 2008 FCA 89.

an agency arrangement: no employment contract, no banking documents, no trace of funds – just not enough.

(ii) *Did Mr. Pearson provide adequate consideration for the cheques?*

[15] It was on this basis that Justice Boyle decided *Gambino* in favour of the taxpayer. Ms. Gambino cashed her incapacitated son's disability cheques and brought the cash back to him. Justice Boyle concluded:

> 31 I accept that Mrs. Gambino intended to and did oblige herself to bring the cash from the cashed cheques promptly back to her son. I also accept that Mrs. Gambino intended for her son to repay the $500 she had loaned him. I accept that she did not understand her son was intending to make a gift to her of any of the amounts. I am satisfied that there was consideration as that term is used in section 160 for all amounts that briefly passed through her hands. I am also satisfied that her commitment to do that, or in any event, her actually doing that, was at the time of the transfer of the endorsed cheques to her.

[16] Somewhat to my surprise, Respondent's counsel suggested this was wrongly decided, implying that the clear wording of section 160 had been met, and that the Court ruled from sympathy in the *Gambino* situation. Such a strict interpretation by the Crown would not only lead to excessively harsh results, it would lead to broader collection powers than section 160 was ever intended to provide. No, *Gambino* was wisely decided. There was consideration flowing from mother to son in the form of an obligation to return the full amount. I have not been convinced the same obligation existed in the case before me. As I have already indicated, Ms. Pearson may have returned some cash, though I have concluded that it is unlikely she returned it all. And if she did not return it all, did she breach an obligation to do so or was there simply no obligation. Drawing from my earlier views on Mr. Pearson's commercial practices, I find there was no obligation that could justify a finding that Ms. Pearson provided adequate consideration. Maybe she would return some, maybe she would not. Maybe she did, maybe she did not. Too many maybes and not enough credible concrete evidence. On balance, I find there was no adequate consideration. Thus all four requirements of section 160 have been met and Ms. Pearson is indeed jointly and severally liable for the cash she received from the father.

[17] The appeal is dismissed, with costs.

Signed at Vancouver, British Columbia, this 23rd day of June, 2009.

"Campbell J. Miller"

C. Miller J.

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| CITATION: | 2009 TCC 338 |
| COURT FILE NO.: | 2007-4165(IT)G |
| STYLE OF CAUSE: | KAREN FAITH PEARSON and<br>HER MAJESTY THE QUEEN |
| PLACE OF HEARING: | Kamloops, British Columbia |
| DATE OF HEARING: | June 8, 2009 |
| REASONS FOR JUDGMENT BY: | The Honourable Justice Campbell J. Miller |
| DATE OF JUDGMENT: | June 23, 2009 |

APPEARANCES:

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| For the Appellant: | The Appellant herself |
| Counsel for the Respondent: | Nadine Taylor Pickering |

COUNSEL OF RECORD:

For the Appellant:

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| Name: | N/A |
| Firm: | |

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| For the Respondent: | John H. Sims, Q.C.<br>Deputy Attorney General of Canada<br>Ottawa, Canada |