Docket: 2012-2070(IT)I

BETWEEN:

ESMAIL HEMMATI,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on January 24, 2013, at Toronto, Ontario

Before: The Honourable Justice Valerie Miller

Appearances:

For the Appellant:	The Appellant himself
Counsel for the Respondent:	Suzanne Bruce

JUDGMENT

The appeal from the reassessments made under the *Income Tax Act* for the Appellant's 2005 and 2006 taxation years is allowed, without costs, and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that:

(a) in 2005, the Appellant's income is to be reduced by $10,373;
(b) in 2006, the Appellant's income is to be reduced by $1,084.83; and
(c) in 2006, the Appellant used his van 80% for business purposes.

Signed at Ottawa, Canada, this 22nd day of February 2013.

"V.A. Miller"

V.A. Miller J.

Citation: 2013TCC66
Date: 20130221
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BETWEEN:

ESMAIL HEMMATI,

Appellant,

and

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Respondent.

REASONS FOR JUDGMENT

V.A. Miller J.

[1] The Minister of National Revenue (the "Minister") reassessed the appellant's 2005 and 2006 taxation years as follows:

(a) The amounts of $12,477 and $12,304 were included in his income in the 2005 and 2006 taxation years respectively;
(b) The amount of $1,758 was disallowed as an expense for supplies in 2006;
(c) The expenses and capital cost allowance related to the business use of his vehicle were reduced from 80% to 50%.

[2] During the period, the Appellant operated two businesses as a sole proprietor. The Minister found that the Appellant had underreported income for each of the businesses. I will consider each business separately.

[3] The Appellant represented himself at the hearing with the assistance of an interpreter. He called two witnesses, his spouse, Hitomi Ikeda Hemmati and his friend, Mohammad Koosha. The Respondent did not call any witnesses.

Dundas West Food Mart

[4] The Appellant operated a grocery store called Dundas West Food Mart (the "Food Mart") from January 2004 until August 3, 2005. The Food Mart mainly sold meats but it also carried bread and dry goods for sale.

[5] In his 2005 income tax return, the Appellant reported that the Food Mart had an opening inventory of $9,450; purchases of goods for resale ("purchases") of $14,749; and, sales of $39,127. During the audit, the Appellant presented documents which showed that his purchases were actually $ 31,309. The auditor accepted these documents. However, she assumed that if the Appellant's purchases were greater than he had reported, his sales must have been greater than reported. The auditor assumed that the Appellant had underreported his sales. Using the industry average (67.1%) for the "cost of goods sold as a percentage of sales", she estimated that the Appellant had sales of $66,060. The auditor then calculated that the Appellant had not reported income of $10,373 from the Food Mart.

[6] It was the Appellant's position that he had reported his sales correctly from the cash register tapes. He incurred numerous losses which led to his closing the business in August 2005. The Appellant stated that the main reasons he suffered losses at the Food Mart were that he purchased too many goods for sale and his business was located in a poor neighbourhood. He testified that he could not sell all of the meat products he had purchased with the result that many pounds of meat spoiled and he had to throw them out. Some of his dry goods such as the walnuts spoiled and he disposed of them. Unfortunately, he did not weigh the spoilage or keep a record of the spoilage.

[7] Both Hitomi Ikeda Hemmati, the Appellant's spouse, and Mohammad Koosha, his friend, corroborated the Appellant's testimony that he had to dispose of goods which had spoiled. Mr. Koosha was aware of the business at the Food Mart because he lived in a basement apartment in the store and he visited the Appellant in the store each day.

[8] It was the Appellant's evidence that this was the first time he had operated a grocery store and he made many mistakes. Foremost among those mistakes was the location he chose to operate his store. He found that he had opened his store in a financially distressed neighbourhood. By 2005, he knew that he could not continue to operate the Food Mart and he closed the business on August 3, 2005.

[9] The Appellant submitted that if the Food Mart had the sales which the auditor had estimated, he would not have closed his business. He closed the business precisely because his expenses exceeded his sales.

[10] I found the Appellant's evidence to be credible. He stated that, contrary to the Minister's assumption, he did have books and records. He had invoices from his suppliers, bank receipts, a ledger book and cash register tapes. It is my view that exhibit R-1 filed by counsel for the Respondent confirmed this portion of the Appellant's testimony.

[11] The Appellant fully explained why he had failed to report all of his purchases in his 2005 income tax return. His failure to claim all of his purchases was to his detriment. He stated that he had actually incurred a loss whereas he had reported a net business income of $911 from the Food Mart.

[12] The unreported income calculated by the Minister was an estimate established using an industry average for meat markets for 2006. There was no explanation as to how this average was established or how it related to the Appellant's business in 2005.

[13] I accept the Appellant's evidence that the Food Mart was in a loss situation in 2005 and he closed the business when he concluded that the business was unsustainable. I also accept that the sales for the Food Mart were correctly reported in the Appellant's 2005 income tax return.

Arc Home

Income and Expenses

[14] Commencing October 2005, the Appellant provided repair and renovation services for residential and commercial buildings. He operated as a sole proprietor under the name of Arc Home and he was paid by cash or cheque for his services.

[15] At the audit stage of this appeal, the Minister determined that the Appellant had underreported his income from Arc Home in 2005 and 2006 and had overstated his expenses in 2006.

[16] The Minister completed a bank deposit analysis of the Appellant's bank accounts and found that the Appellant had unexplained bank deposits of $2,104.06 and $12,303.70 for 2005 and 2006 respectively.

[17] It was the Appellant's position that in 2005 he deposited the amount of $2000 in his bank account from cash which he kept in his home. The sources of the cash were his family in Iran and his spouse's family in Japan. However, he stated that he did not have the documentation to substantiate his testimony and he accepted the Minister's calculation of his income from Arc Home for 2005.

[18] For the 2006 taxation year, the Appellant explained that various deposits in his bank account were not business income but were reimbursements for materials which he had picked up for his clients. In support of his testimony, he submitted cheques and emails from third parties. The total amount on these documents was $7,999.19.

[19] It is my view that the Appellant has established that a deposit of $360 into his account on October 30, 2006 was the repayment of a loan and not business income. I have also accepted that the amounts of $108, $500 and $116.83 were not business income in 2006 but were repayments for materials purchased for his clients. A review of exhibit R-1 showed that the Appellant did not claim an expense for these materials. It is my view that an email without supporting documents from a third party was insufficient to establish that the amount of $6,914.36 was not business income.

[20] In 2006, the Appellant claimed an expense for supplies in the amount of $13,190.97. However, only the amount of $11,432.95 was supported by receipts and the Minister disallowed the difference of $1,758.02.

[21] The Appellant stated that he accepted the Minister's calculation for the supplies expense.

[22] I realize that the Appellant had just started his business in 2005 but when a taxpayer decides to operate a business, he/she must keep detailed records to substantiate the income earned and the expenses claimed against that income: *Njenga v. R.*, [1997] 2 C.T.C. 8 (FCA).

Use of Vehicle

[23] The Appellant purchased a van in 2006 which he used for the Arc Home business. The Appellant claimed 80% business use of the van in 2006. The Minister allowed only 50% business use of the van because the Appellant did not provide a log to substantiate the business trips.

[24] I find that the Respondent attributed minimal business use to the Appellant's van. He was in a business that required him to use his van extensively. He testified that he used his van to travel to potential clients to give estimates for jobs and to pick up and deliver materials for the jobs he obtained.

[25] Although the Appellant did not keep a log of his business travel in 2006, I have been persuaded that he used his van 80% for business purposes.

Conclusion

[26] For all of the above reasons, the appeal is allowed on the following basis:

(a) in 2005, the Appellant's income is to be reduced by $10,373;
(b) in 2006, the Appellant's income is to be reduced by $1,084.83; and
(c) in 2006, the Appellant used his van 80% for business purposes.

Signed at Ottawa, Canada, this 22nd day of February 2013.

"V.A. Miller"

V.A. Miller J.

CITATION:	2013TCC66
COURT FILE NO.:	2012-2070(IT)I
STYLE OF CAUSE:	ESMAIL HEMMATI AND HER MAJESTY THE QUEEN
PLACE OF HEARING:	Toronto, Ontario
DATE OF HEARING:	January 24, 2013
REASONS FOR JUDGMENT BY:	The Honourable Justice Valerie Miller
DATE OF JUDGMENT:	February 22, 2013

APPEARANCES:

For the Appellant:	The Appellant himself
Counsel for the Respondent:	Suzanne Bruce

COUNSEL OF RECORD:

For the Appellant:

Name:

Firm:

For the Respondent:	William F. Pentney, Deputy Attorney General of Canada Ottawa, Canada