



Ottawa, Monday, May 12, 1997

Appeal No. AP-93-093

IN THE MATTER OF an appeal heard on September 11, 1996,
under section 81.19 of the *Excise Tax Act*, R.S.C. 1985, c. E-15;

AND IN THE MATTER OF a decision of the Minister of
National Revenue dated March 31, 1993, with respect to a notice
of objection served under section 81.15 of the *Excise Tax Act*.

BETWEEN

KOBETEK SYSTEMS LIMITED

Appellant

AND

THE MINISTER OF NATIONAL REVENUE

Respondent

DECISION OF THE TRIBUNAL

The appeal is dismissed.

Arthur B. Trudeau

Arthur B. Trudeau
Presiding Member

Lyle M. Russell

Lyle M. Russell
Member

Charles A. Gracey

Charles A. Gracey
Member

Michel P. Granger

Michel P. Granger
Secretary

UNOFFICIAL SUMMARY

Appeal No. AP-93-093

KOBETEK SYSTEMS LIMITED

Appellant

and

THE MINISTER OF NATIONAL REVENUE

Respondent

The appellant is a licensed wholesaler of computers and related software and equipment, located in Halifax, Nova Scotia. The appellant appealed a decision of the respondent which upheld an assessment against the appellant for unpaid taxes, penalty and interest, on the basis that the appellant incorrectly applied the blanket discount method of calculating its federal sales tax (FST) liability. The appellant has requested that the Tribunal allow it to calculate its FST liability for the audit period in question on the basis of the direct costing method of calculating FST liability. The appeal raises two issues: first, whether the Tribunal has jurisdiction to grant the relief requested by the appellant; and second, whether the appellant has proved that the respondent's assessment was incorrect.

HELD: The appeal is dismissed. The Tribunal agrees with counsel for the respondent that it does not have jurisdiction to direct the election and use of methods of calculation of FST liability in this case because these methods reflect policies set out in an excise memorandum. However, the Tribunal does have jurisdiction to decide whether the assessment itself was incorrect. As the appellant has agreed that there are no errors in the calculations underlying that assessment, it cannot be said that the appellant has established that the assessment was incorrect.

Places of Video Conference

Hearing: Hull, Quebec, and Dartmouth, Nova Scotia
Date of Hearing: September 11, 1996
Date of Decision: May 12, 1997

Tribunal Members: Arthur B. Trudeau, Presiding Member
Lyle M. Russell, Member
Charles A. Gracey, Member

Counsel for the Tribunal: Hugh J. Cheetham

Clerks of the Tribunal: Margaret Fisher and Anne Jamieson

Appearances: Sieg Deleu, for the appellant
Lyndsay K. Jeanes, for the respondent

Appeal No. AP-93-093

KOBETEK SYSTEMS LIMITED

Appellant

and

THE MINISTER OF NATIONAL REVENUE

Respondent

TRIBUNAL: ARTHUR B. TRUDEAU, Presiding Member
LYLE M. RUSSELL, Member
CHARLES A. GRACEY, Member

REASONS FOR DECISION

This is an appeal heard by way of video conference in Hull, Quebec, and Dartmouth, Nova Scotia, under section 81.19 of the *Excise Tax Act*¹ (the Act) from a decision of the Minister of National Revenue dated March 31, 1993.

The appellant is a licensed wholesaler of computers and related software and equipment, located in Halifax, Nova Scotia. In March 1991, the appellant was assessed unpaid taxes, penalty and interest in the amount of \$31,143.03, for the period from March 1, 1987, to August 31, 1990. The assessment related to the manner in which the appellant used the blanket discount method in calculating federal sales tax (FST) payable on its sales made during the period in question. The appellant objected to this assessment and, by notice of decision dated March 31, 1993, the respondent varied the assessment in part and determined that the amount owing as of the date of the assessment was \$28,010.86. On June 23, 1993, the appellant appealed this decision to the Tribunal and requested that it be assessed for the period in question on the basis of the direct costing method of calculating FST liability, as opposed to the blanket discount method.

This appeal raises two issues: first, whether the Tribunal has jurisdiction to grant the relief requested by the appellant; and second, whether the appellant has proved that the respondent's assessment was incorrect.

Mr. Sieg Deleu, President of Atlantis Kobetek Inc., appeared on behalf of the appellant. Atlantis Kobetek Inc. came into being as a result of a recent amalgamation between the appellant and Atlantis Microcomputer Inc. Mr. Deleu indicated that, during the period in question, he was unaware that there were two methods of calculating FST liability. He only found out about it after the audit was completed, from the auditor of the Department of National Revenue (Revenue Canada) who performed the audit leading to the assessment at issue. Mr. Deleu subsequently did calculations using the direct costing method and came to the view that the appellant had overpaid FST by approximately 60 percent during the period in question. In response to questions from the Tribunal during his testimony, Mr. Deleu confirmed that he was not challenging the actual calculations underlying the assessment at issue and that he had no problems with the calculations of those numbers.

In cross-examination, Mr. Deleu indicated that he may well have received an information package from Revenue Canada at the time that he received his wholesaler's licence which described the two methods of calculating FST liability. However, the pressures of being a small business were such that the appellant

1. R.S.C. 1985, c. E-15.

relied on the recommendation of Revenue Canada officials and used the blanket discount method. Mr. Deleu agreed that, since the assessment, he had not provided the respondent with any evidence to substantiate that the calculations in the assessment were wrong, because he agreed that they were correct under the blanket discount method.

In response to questions from the Tribunal, Mr. Deleu agreed that the calculations that he made using the direct costing method assume that the amount of tax payable by the appellant under this method would be the same amount as that payable by the appellant's supplier, not the amount payable on the appellant's purchase price from such supplier.

Counsel for the respondent called one witness, Mr. Robert Knickle, an auditor with Revenue Canada. Mr. Knickle performed the audit that led to the assessment at issue. He has been an auditor with Revenue Canada for 20 years. Mr. Knickle testified that, as a licensed wholesaler, the appellant was required to remit FST on all sales to non-exempt customers, using either method of calculating FST liability. These methods are set out in Excise Memorandum ET 201² (ET 201). Mr. Knickle stated that, under the blanket discount method, the licensed wholesaler essentially creates a statement of cost of goods sold, determines an average cost for its goods and then accounts for FST based on that average cost. He noted that, once taxpayers had opted for one method or the other, they were not permitted to use the other method selectively, but rather had to use the method chosen for the entire relevant time period.

With respect to the period in question, Mr. Knickle explained that the problem was that, in April 1986, the appellant determined a particular discount rate and then another higher one in May 1986. Thereafter, the appellant continued to use the May 1986 rate, without adjustment, for the rest of the audit period. The assessment at issue reflected the determination of the appellant's tax liability on the basis of the adjusted discount rate. This led to the appellant's FST remittance being lower than the appellant's actual liability. Turning to the manner in which Mr. Deleu used the direct costing method in calculations submitted with this appeal, Mr. Knickle agreed that Mr. Deleu's calculations may be wrong, more specifically, understated, to the extent that the appellant used the amount of FST that would be paid by its suppliers on taxable sales.

In cross-examination, Mr. Knickle did not agree with Mr. Deleu that he had initially told him that the amount assessed would be approximately \$600. In response to questions from the Tribunal, Mr. Knickle confirmed that the assessment related to the incorrect use of the blanket discount method during the period in question. He was also of the view that these two methods should yield essentially the same result in calculating the FST liability of a particular licensee. Mr. Knickle stated that the current ability of the respondent to waive penalty and interest in respect of the Goods and Services Tax (the so-called "Fairness Package") did not exist during the period in question or with respect to FST.

In argument, the appellant's representative referred again to his testimony and his explanation of why the appellant was asking the Tribunal to vary the assessment at issue. He added that, if the appellant had to pay the assessment, it might have to declare bankruptcy.

Counsel for the respondent first addressed the issue of whether the appellant has established that the respondent's assessment was incorrect. She referred the Tribunal to the testimony of Mr. Deleu in which he admitted that the manner in which the respondent had applied the blanket discount method was correct and submitted that there was no evidence to suggest that the respondent's calculations were in error. Counsel also submitted that, in light of the explanation of the two methods by Mr. Knickle, if the appellant had used the direct costing method correctly, the outcome would have been substantially the same. Furthermore,

2. *Licensed Wholesalers*, Department of National Revenue, Customs and Excise, September 29, 1989.

counsel submitted that there was no provision in the Act that would allow the appellant to retroactively change the method of calculation used for a specific time period.

With respect to the issue of the Tribunal's jurisdiction to vary the assessment at issue, counsel for the respondent submitted that the Tribunal does not have such jurisdiction because the election and use of methods of calculation are policies set out by the respondent in ET 201. In support of this position, counsel referred the Tribunal to its decision in *Electra Supply Inc. v. the Minister of National Revenue*.³ Counsel also submitted that the Tribunal has acknowledged that it lacks jurisdiction to waive penalty or interest imposed in accordance with the Act.⁴

The Tribunal agrees with counsel for the respondent that it does not have jurisdiction to change the applicable standard enunciated by the respondent in a particular excise memorandum, in this case ET 201. In this regard, the Tribunal adopts its reasoning set out in *Electra Supply* and, in particular, the distinctions referenced therein as to what is within and not within the Tribunal's jurisdiction in considering these matters. However, this does not mean that the Tribunal does not have jurisdiction to consider whether an assessment is incorrect or not. In considering that question, an appellant bears the burden of establishing that the assessment was incorrect. In this case, the appellant has not met that burden, in that it agreed with the calculations underlying the assessment at issue. With respect to the issue of interest and penalty, the Tribunal agrees with counsel for the respondent that the Tribunal has no jurisdiction to vary penalty and interest, except to the extent that an assessment, on which penalty and interest have been imposed, is itself varied.

Accordingly, the appeal is dismissed.

Arthur B. Trudeau
Arthur B. Trudeau
Presiding Member

Lyle M. Russell
Lyle M. Russell
Member

Charles A. Gracey
Charles A. Gracey
Member

3. Appeal No. AP-92-042, May 4, 1993.

4. Citing *Les Presses Lithographiques Inc. v. The Minister of National Revenue*, Appeal No. 2997, June 26, 1989.