

Ottawa, Friday, October 27, 1995

Appeal No. AP-93-382

IN THE MATTER OF an appeal heard on May 15, 1995, 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 November 26, 1993, with respect to a notice of objection served under section 81.15 of the *Excise Tax Act*.

BETWEEN

SKYWOOD P.V.C. EXTRUSION INC.

Appellant

AND

THE MINISTER OF NATIONAL REVENUE

Respondent

DECISION OF THE TRIBUNAL

The appeal is allowed in part.

Lyle M. Russell
Lyle M. Russell
Presiding Member

Charles A. Gracey
Charles A. Gracey
Member

Robert C. Coates, Q.C.
Robert C. Coates, Q.C.
Member

Michel P. Granger
Michel P. Granger
Secretary

UNOFFICIAL SUMMARY

Appeal No. AP-93-382

SKYWOOD P.V.C. EXTRUSION INC.

Appellant

and

THE MINISTER OF NATIONAL REVENUE

Respondent

This is an appeal under section 81.19 of the Excise Tax Act of an assessment of the Minister of National Revenue dated November 8, 1989, for federal sales tax that was neither charged nor collected on sales of polyvinyl chloride plastic siding during the period from December 1, 1985, to July 31, 1989.

***HELD:** The appeal is allowed in part. With respect to all but the sales to Armoral Inc., the Tribunal is not persuaded that the appellant was incorrectly assessed for unpaid federal sales tax, interest and penalty. In the Tribunal's view, the evidence introduced by the appellant did not show that the sales were exempt from federal sales tax under subsection 50(5) of the Excise Tax Act as sales to manufacturers or wholesalers of partly manufactured goods. Moreover, the exemption under Part XVIII of Schedule III to the Excise Tax Act for "Energy Conservation Equipment" was repealed effective July 1, 1985, and could not, therefore, have applied to the sales at issue, as contended by the appellant. Accordingly, the Tribunal dismisses that portion of the appeal concerning the assessment for federal sales tax on the sales to D. Brown Ltd., Kento Ltd., Manac Inc., Stevenson Enterprises and Sikora Windows.*

With respect to the assessment for federal sales tax on sales to Armoral Inc., the Tribunal is of the view that the appellant was incorrectly assessed, as Armoral Inc. never paid the appellant for these sales, and the amounts owing were written off by the appellant as bad debts.

The Tribunal refers the assessment back to the respondent to be revised to take into account the respondent's concessions, the appellant's withdrawal of its claim relating to Debbra Herrman and the Tribunal's finding that the appellant was incorrectly assessed for federal sales tax in respect of the sales to Armoral Inc.

*Place of Hearing: Ottawa, Ontario
Date of Hearing: May 15, 1995
Date of Decision: October 27, 1995*

*Tribunal Members: Lyle M. Russell, Presiding Member
Charles A. Gracey, Member
Robert C. Coates, Q.C., Member*

Counsel for the Tribunal: Shelley Rowe

Clerk of the Tribunal: Anne Jamieson

*Appearances: John Nassar, for the appellant
Susan Tataryn, for the respondent*

Appeal No. AP-93-382

SKYWOOD P.V.C. EXTRUSION INC.

Appellant

and

THE MINISTER OF NATIONAL REVENUE

Respondent

TRIBUNAL: LYLE M. RUSSELL, Presiding Member
CHARLES A. GRACEY, Member
ROBERT C. COATES, Q.C., Member

REASONS FOR DECISION

This is an appeal under section 81.19 of the *Excise Tax Act*¹ (the Act) of an assessment of the Minister of National Revenue dated November 8, 1989, for federal sales tax (FST) that was neither charged nor collected on sales of polyvinyl chloride plastic siding during the period from December 1, 1985, to July 31, 1989. The assessment was for the amount of \$47,548.52 plus \$23,027.64 for interest and penalty. The appellant served a notice of objection stating that the auditor could not understand its records due to poor bookkeeping and did not, therefore, take into account bad debts, goods returned, exempt sales and cash discounts. The appellant also provided corrected invoices with FST exemption certificate numbers. The respondent's decision states that the documentation provided by the appellant was inconclusive.

Although the sales at issue involve 10 of the appellant's customers, that is, Armoral Inc., Debbra Herrman, D. Brown Ltd., HC Products Ltd., Kento Ltd., Manac Inc., Overhead Door of Sioux City, Stevenson Enterprises, Sertapak Inc. and Sikora Windows, at the hearing, several issues relating to the sales where either withdrawn by the appellant's representative or conceded by counsel for the respondent. In particular, counsel for the respondent conceded that the appellant was incorrectly assessed for FST on sales to Armoral Inc. (invoice nos. 1255, 1260, 1275, 1359 and 1360), HC Products Ltd. (invoice no. 1353), Overhead Door of Sioux City (invoice no. 1760) and Sertapak Inc. (invoice no. 1379). The appellant withdrew the portion of the appeal relating to sales to Debbra Herrman (invoice no. 1700).

With respect to the remaining sales at issue, other than the sales to Armoral Inc., namely, those to D. Brown Ltd., Kento Ltd., Manac Inc., Nu-Shade Patio Rooms and Sikora Windows, the appellant's representative argued that the appellant was incorrectly assessed for FST on these sales, as the purchasers were manufacturers that held FST exemption certificates entitling them to purchase goods without paying FST. He further argued that some of the sales were exempt from FST under the "energy saving program" which exempts from tax certain goods as listed in Part XVIII of Schedule III to the Act.

The appellant's representative testified that it was the appellant's practice to seek signed FST exemption certificates from the companies with which it did business. However, for the transactions at issue, the relevant documentation could not be found. He explained that this was caused, in part, by the mismanagement of Mr. Merrill Machan who was General Manager of Skywood P.V.C. Extrusion Inc. from August 8, 1983, to February 19, 1987. Mr. Machan did not always charge FST when required, did not

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

obtain the requisite documentation and did not maintain proper records. Mr. Machan was dismissed from the company for, among other things, his mismanagement of the company.

Mr. Zaki Nassar, the owner of Skywood P.V.C. Extrusion Inc., testified that, based on his personal knowledge, each of the sales for which the appellant was assessed unpaid FST was to companies that were manufacturers and which have since declared bankruptcy, namely, Manac Inc., D. Brown Ltd. and Kento Ltd.

The appellant's brief included copies of invoices and letters which, the appellant's representative submitted, showed that purchases by the companies at issue were exempt from FST. There was a copy of an invoice to Manac Inc. dated July 5, 1990, which has the following stamped onto it: "We certify that the goods ordered (imported) hereby are to be used in, [w]rought into or attached to taxable goods for sale." This statement is followed by Federal No. S-0109124-04 and Provincial No. 805-MT OS36-1 and is initialled "MR." The brief included an undated letter from Sikora Windows which provides the following: "We certify that the goods ordered/purchased hereby are to be used in, wrought into, or attached to taxable goods for sale" and cites "Federal Sales Tax License Number S 2070688." Mr. Nassar submitted that this letter was provided in 1987. There is also an invoice to Sikora Windows dated January 22, 1990, which refers to this licence number. Finally, there is an unsigned document from Nu-Shade Patio Rooms, received by facsimile from "Stevenson_Ent," that provides as follows: "We certify that the goods which will be purchased from you during the period from April 88 to April '89 are to be used in, wrought into, or attached to taxable goods for sale" and cites "Licence Number S 3615606." Both the appellant's representative and Mr. Nassar submitted that Stevenson Enterprises owned Nu-Shade Patio Rooms and that the latter was an operating name used by the former.

In addition, at the hearing, the appellant's representative introduced, as an exhibit, a letter dated July 6, 1984, from the Department of National Revenue (Revenue Canada) to Mr. Nassar, which provides that Celuka Siding does not qualify for exemption from FST under the scope of the provisions of section 5 of Part XVIII of Schedule III to the Act for "thermal insulation materials designed exclusively for insulation of buildings ..." but rather attracts federal sales tax at the current lower rate of 5% under the provisions of section 11 of Part I of Schedule V to the Act for '... siding.'

With respect to the sales to Armoral Inc., the appellant's representative testified that the appellant sold goods to Armoral Inc., but that the invoices for the sales were unpaid and that the majority of the goods were returned and could not be resold, as they were customized. The appellant's brief included copies of letters dated June 8 and 10, 1987, in which the appellant requests payment for the goods, as well as invoices. The representative submitted that the appellant treated the amounts unpaid by Armoral Inc. as bad debts and argued that the appellant should not have been assessed for FST in respect of these amounts. He also stated that the Tax Court of Canada, in a recent decision,² recognized that amounts unpaid by Armoral Inc. were bad debts for income tax purposes.

Mr. John Sooran, an auditor with Revenue Canada, testified that, in the course of his audit, the appellant provided him only with incomplete sales invoices and bank statements for the transactions at issue

2. *Skywood PVC Extrusion Inc. v. Her Majesty the Queen*, unreported, File No. 94-1856(IT)I, May 11, 1995.

and did not provide him with any books of account or records. Moreover, he was unsuccessful in his attempts to obtain additional information.

Mr. Sooran stated that there are two types of licences, an “S” licence, for a manufacturer, and a “W” licence, for a wholesaler. With respect to each of the companies at issue, Mr. Sooran explained why, in his view, the companies were not manufacturers. He further explained that the fact that some of them may have had an FST exemption number would not, in and of itself, indicate that they purchased goods on a tax-exempt basis. Referring specifically to the documents provided by the appellant, Mr. Sooran indicated that they were insufficient. In particular, he noted that the purchase order from Manac Inc. related to a period subsequent to the audit. There was no information provided to show that Stevenson Enterprises was operating under the FST licence issued to Nu-Shade Patio Rooms. Finally, the exemption certificate for Sikora Windows is not dated.

Mr. Sooran explained that the “energy saving program,” which exempts from tax certain goods as listed in Part XVIII of Schedule III to the Act, was not in effect during the period covered by the audit, as the relevant provisions of the Act were repealed effective July 1, 1985. Moreover, Mr. Sooran confirmed that, during the relevant period, the rate of FST for goods mentioned in Schedule V to the Act, later Schedule IV, was 8 percent and not 5 percent, as believed by the appellant.

Based on the description in the appellant’s brief that the primary business for Armoral Inc. is the distribution to lumber yards and other retail stores, Mr. Sooran opined that Armoral Inc. is not a manufacturer. With respect to the amounts unpaid by Armoral Inc. and the returned goods, Mr. Sooran stated that, had he known of this at the time of his audit, he would have advised the appellant that it was entitled to write off the amounts as bad debts in its financial statements and that, once written off, it could claim a refund if it applied within two years of the date on which the amounts were written off. He also stated that, had he known about the debt at the time of the audit and had the debt been written off, he would have excluded that amount from the assessment.

The appellant’s representative argued, based on Mr. Sooran’s testimony, that an FST exemption certificate is not always required for a taxpayer to be exempt from charging and collecting FST and that it depends upon the situation and the reasonableness of the circumstances. He submitted that the documents provided, as well as Mr. Nassar’s testimony, show that it was reasonable for the appellant not to charge or collect FST on the sales at issue, as the customers to which the goods were sold were manufacturers and held FST exemption certificates.

In the case of the sales to Armoral Inc., the appellant’s representative argued that, since the goods were never paid for and some of the goods were returned and the amounts owing to the appellant were written off as bad debts, the appellant should not be assessed for FST, interest or penalty in respect of those sales.

Counsel for the respondent submitted that the documentation provided by the appellant in the audit was clearly insufficient and inconclusive to warrant any major changes in the assessment. She contended that the exemption provisions in the Act are to be strictly construed and that the appellant must show every constituent element necessary. In her view, what Mr. Sooran stated in his testimony was that an FST exemption certificate is readily accepted by Revenue Canada and that, in cases where a certificate is

not available, Revenue Canada will look to other evidence to see if the goods were sold to a licensed manufacturer or wholesaler and were, thus, sold for FST-exempt purposes. Speaking to the sales at issue, she submitted that the documents provided by the appellant showed only that the companies held FST exemption certificates, but did not show that the specific goods sold were to be used for FST-exempt purposes. Moreover, for those companies for which the appellant was not able to produce any documentation, counsel submitted that there was no proof that the sales were to licensed manufacturers or wholesalers.

With respect to the sales to Armoral Inc., counsel for the respondent submitted that, pursuant to section 50 of the Act, the appellant was required to levy and remit FST on the sale price of the goods, since it had not demonstrated that the sales fell into the specific circumstances, when FST is not payable, listed under subsection 50(5). She submitted that section 68.15 provides for a refund of FST remitted in respect of amounts which have become bad debts, provided the amounts have been written off as bad debts and the taxpayer applies for a refund within two years after the end of the fiscal year during which the debts were written off. However, the appellant did not avail itself of this remedy.

With respect to all but the sales to Armoral Inc., the Tribunal is not persuaded that the appellant was incorrectly assessed for unpaid FST, interest and penalty. Pursuant to section 50 of the Act, FST is to be imposed, levied and collected on the sale price of goods produced or manufactured in Canada payable by the producer or manufacturer at the time when the goods are delivered to the purchaser or at the time when the property in the goods passes, whichever is the earlier. Subsection 50(5) sets out a number of circumstances when FST is not payable. Paragraph 50(5)(a) refers to goods sold by a licensed manufacturer to another licensed manufacturer if the goods are partly manufactured goods. Paragraph 50(5)(d) refers to goods sold by a licensed manufacturer to a licensed wholesaler otherwise than for his own use or for rental to others. In the Tribunal's view, the evidence introduced by the appellant does not show that the sales at issue meet the requirements of the provisions of paragraph 50(5)(a) or (d).

The Tribunal notes that the exemption for "Energy Conservation Equipment" under Part XVIII of Schedule III to the Act was repealed by subsection 51(10) of *An Act to amend the Excise Tax Act and the Excise Act and to amend other Acts in consequence thereof*³ which came into effect on July 1, 1985, prior to the period at issue. Therefore, the sales at issue were not exempt from FST on the basis that the goods were exempt as energy conservation equipment, as contended by the appellant.

Accordingly, the Tribunal dismisses that portion of the appeal concerning the assessment for FST on the sales to D. Brown Ltd., Kento Ltd., Manac Inc., Stevenson Enterprises and Sikora Windows.

Finally, with respect to the sales to Armoral Inc., the Tribunal is of the view that the appellant was incorrectly assessed for unpaid FST and allows that portion of the appeal relating to these sales. The Tribunal is persuaded by the evidence that the sale and delivery of the goods to Armoral Inc. were not successfully concluded. Moreover, the auditor stated that, had he known that the amounts had been written off as bad debts, he would not have included those amounts in the assessment.

3. S.C. 1986, c. 9.

The Tribunal refers the assessment back to the respondent to be revised to take into account the respondent's concessions, the appellant's withdrawal of its claim relating to Debbra Herrman and the Tribunal's finding that the appellant was incorrectly assessed for FST in respect of the sales to Armoral Inc.

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