Docket: 2009-2837(IT)I

BETWEEN:

RICHARD SWARBRICK,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeals heard on June 22, 2010, at Montreal, Quebec

Before: The Honourable Justice G. A. Sheridan

Appearances:

Counsel for the Appellant:	Marc-André Paquin
Counsel for the Respondent:	Simon-Nicolas Crépin

JUDGMENT

In accordance with the attached Reasons for Judgment, the appeals from the reassessments made under the *Income Tax Act* for the 2001, 2002 and 2003 taxations years are allowed, and the reassessments of the Minister of National Revenue are vacated.

Signed at Ottawa, Canada, this 26th day of November, 2010.

"G. A. Sheridan"

Sheridan J.

Citation: 2010TCC605
Date: 20101126
Docket: 2009-2837(IT)I

BETWEEN:

RICHARD SWARBRICK,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Sheridan, J.

[1] The Appellant, Richard Swarbrick, is appealing the reassessment of the Minister of National Revenue of his 2001, 2002 and 2003 taxation years. Following a net worth assessment of these years by the Minister of Revenue Quebec, the federal Minister reassessed to include unreported income of $17,424, $5,543 and $9,206 in 2001, 2002 and 2003, respectively. The Minister reassessed the 2001 and 2002 taxation years on December 24, 2007 beyond the normal reassessment period years under subsection 152(4) of the *Income Tax Act*; the 2001 taxation year was originally assessed on May 13, 2002; the 2002 taxation year, on April 28, 2003 for 2002. In respect of the 2003 taxation year, the Minister sent a notification that no tax was payable on April 14, 2004.

[2] The Minister also assessed penalties under subsection 163(2) of the *Act* for all three taxation years on the basis that the Appellant had filed false returns in circumstances amounting to gross negligence.

[3] The Minister's reassessment was based on the assumptions of fact set out in paragraph 8 of the Reply to the Notice of Appeal:

a) The MRQ had conducted an audit, using a cash flow method, of the Appellant for the taxation years within their program of "Indices des richesse", such program undertakes to evaluate the income of taxpayers where there are indications that the income as declared by a taxpayer does not reflect the lifestyle of the taxpayer;

b) Following the cash flow method the outflows of funds were determined as follows, per Annex as attached:

i) Personal expenses in the amounts of $16,372, $14,085 and $13,141 respectively for the 2001, 2002 and 2003 taxation years, such being based upon Statistics Canada amounts for a single person as the personal expenses as provided by the Appellant were not considered reasonable;

ii) NIL for any loan payments related to a residence, such decision being based upon the fact that the Appellant constructed his residence by himself and there was no evidence of any loan payments related thereto;

iii) Expenses for automobiles:

a) Payments made for the acquisition of a Jaguar CK8, $11,600, $17,400 and $17,400 respectively for the 2001, 2002 and 2003 taxation years;

b) Payments made for the acquisition of a Dolph 535S, $3,172 for the 2003 taxation year; and

c) $10,050 for the 2001 taxation year for the acquisition of the Jaguar CK8;

iv) Amounts paid for income tax, $11,409 and $3,169 respectively for the 2001 and 2002 taxation years;

v) Capital payments on a $25,000 loan in the amounts of $6,352 for each of the 2001, 2002 and 2003 taxation years;

c) Following the cash flow method the inflow of funds were determined in the following amounts, Annex attached.

i) Available income as per total income declared by the Appellant in the amounts of $38,359 and $67 for the 2001 and 2003 taxation yeas, and as filed with MRQ, $17,464 less a tax adjustment of $111 for the 2002 taxation year;

ii) GST and QST credits received by the Appellant in the amounts of $569 and $462 for the 2002 and 2003 taxation years respectively;

iii) Income tax refund from MRQ in the amount of $2,460 for the 2003 taxation years; and

iv) Non taxable income in the amounts of $17,541 and $27,870 respectively for the 2002 and 2003 taxation years, such amounts being salary insurance proceeds received by the Appellant.

9. In reassessing the Appellant beyond the normal reassessment period for the 2001 and 2002 taxation years the Minister considered:

a) The materiality of the additional amounts of income not reported representing 46% and 32% of the next income as declared by the Appellant;

b) The Appellant could not ignore that the outlays of funds to maintain his lifestyle and acquisition of assets, income taxes paid, and reimbursements of capital and interest paid on loans exceeded his incomes as declared.

10. In assessing the penalties pursuant to subsection 163(2) of the Act on the additional income, in the amounts of $17,424, $5,543, and $9,206 respectively for the 2001, 2002 and 2003 taxation years, the Minister considered:

a) The materiality of the additional amounts of income not reported representing 46%, 32% and [13.74%], respectively for the 2001, 2002 and 2003 taxation years, of the net income as declared by the Appellant;

b) The Appellant could not ignore that the outlays of funds to maintain his lifestyle and acquisition of assets, income taxes paid, and reimbursements of capital and interest paid on loans, exceeded his income as declared.

[4] The Appellant does not dispute that the banking and loan records[1] relied upon by the Minister reveal an overall discrepancy of approximately $32,000 between the amounts available to him in 2001, 2002 and 2003 and what he actually spent during those years. His position is, however, that such records do not take into account cash

[1] Exhibit A-6.

amounts kept in his home and upon which he drew, as necessary, to meet his financial needs. According to the Appellant, he had access to approximately $45,000 in cash made up of an advance on inheritance of $21,000 received from his father in late 1999[2] following the sale of the family home[3]; line of credit proceeds of $20,000; and personal loan proceeds of $4,000 advanced by the Bank of Montreal on February 16, 2000[4].

[5] In rejecting the Appellant's contentions, counsel for the Respondent referred the Court to *Lacroix v. Her Majesty the Queen*[5] in which the Federal Court of Appeal reviewed the law in respect of the onus and burden of proof borne by the parties in an appeal of a net worth assessment involving a reassessment beyond the normal reassessment period and the imposition of gross negligence penalties. Pelletier, J.A. held that the onus is on the taxpayer, not the Minister, to prove the source of the additional income identified by the net worth assessment; it remains for the Minister, however, to prove the existence of circumstances justifying the reassessment of otherwise statute-barred years and the imposition of penalties under subsection 163(2):

> What, then, of the burden of proof on the Minister? How does he discharge this burden? There may be circumstances where the Minister would be able to show direct evidence of the taxpayer's state of mind at the time the tax return was filed. However, in the vast majority of cases, the Minister will be limited to undermining the taxpayer's credibility by either adducing evidence or cross-examining the taxpayer. Insofar as the Tax Court of Canada is satisfied that the taxpayer earned unreported income and did not provide a credible explanation for the discrepancy between his ... reported income and his … net worth, the Minister has discharged the burden of proof on him within the meaning of subparagraph 152(4)(*a*)(i) and subsection 163(2).[6]

[6] In holding that on the evidence presented the Minister had satisfied the evidentiary burden imposed by these provisions, the appellate Court paid particular

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[2] Exhibits A-1 and A-2.

[3] Exhibit A-3.

[4] Exhibits A-4 and A-5.

[5] 2008 FCA 241. (F.C.A.).

[6] Above, at paragraph 32.

heed to the role of the trial judge in assessing the credibility of the evidence presented:

> The assessment of credibility is the task of the trial judge. There is nothing surprising in the fact that some evidence supports the version of the facts proposed by one party while other evidence undermines it. The trial judge is in a better position to assess the true value of these disparate elements and draw the proper conclusions. In the case at bar, the judge duly noted the evidence which the appellant raises but deemed it to be fabricated and dismissed it. There is nothing in the evidence or in the *Income Tax Act* …that would warrant this Court's intervention….[7]

[7] Given the Court's emphasis in *Lacroix* on the trial judge's assessment of credibility and the Crown's reliance on that case, it is useful to review some of the evidentiary weaknesses identified by Bédard, J.:

> [12] The assessment of the credibility of the appellant and of Mr. Pronovost have played an important role in my decision, given the almost complete lack of documentary or objective evidence as to how the appellant used the $500,000 in cash or where the $500,000 in cash allegedly held by Mr. Pronovost came from. I would like to point out that I attach little probative value to the testimonies of the appellant, his spouse and Mr. Pronovost. In this regard, I note at this point that courts are not required to believe witnesses, even if they are not contradicted. Their version may be implausible as a result of circumstances revealed by the evidence, or simply on the basis of common sense.
>
> [13] In addition to the implausibility of the appellant's story, I note that the explanation he gave during his testimony about how he used the $500,000 in cash allegedly loaned to him by Mr. Pronovost contradicted the answer given on this point on examination for discovery. I would point out that on discovery, the appellant answered that the $500,000 was essentially spent [TRANSLATION] "on renovations made to the properties". However, I note that the appellant testified that the $500,000 in cash had been used to pay off his line of credit, which had been used to purchase the properties and renovate them. I would also point out that the appellant's expert very clearly showed that the money from the loans made by Mr. Pronovost had not been used to renovate the buildings and that only part of this money was used to make down payments when the real estate was purchased. I also note that the appellant did not submit any documentary evidence showing that he had made several cash deposits (ranging from $4,000 to $5,000) to pay off his line of credit in full. I infer from this that this evidence would have been unfavourable to him.
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> [14] Besides the implausibility of Mr. Pronovost's story, I note that his answers were generally evasive, imprecise, ambiguous, elusive, equivocal, unintelligible and

[7] Above, at paragraph 8.

> laborious. The time he took to answer questions, his hesitations, his facial expression and his frequent memory gaps only added to my doubts about his credibility. Of course, the fact that the events took place several years ago may explain certain inaccuracies or memory gaps, but it is quite a stretch to accept this as a reason for his inability to tell Mr. Heppell and Mr. LeBlanc the amounts of the loans he allegedly made to the appellant. He could have occasionally substantiated his allegations and established his credibility with adequate and serious evidence, especially concerning the value of his assets, which apparently was $4 million when he made the loans, and concerning the advances repaid to him by his company. I note that these advances were allegedly used to make some of the loans to the appellant.
>
> [15] In any event, I am of the opinion that the whole story about the loans as told by the appellant, his spouse and Mr. Pronovost is implausible. I am also of the opinion that the note and the request for the repayment of the loan were written and signed after the beginning of the audit for the purpose of hiding the truth. I am also of the opinion that the payment in the amount of $430,000 was made for the same purpose.
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> [16] On this point, Mr. Pronovost's story about the rescue of his son, Patrice, who was then 16 years old, seemed to me to be simply implausible and not very credible. First of all, his testimony about the circumstances explaining how his son fell into the Richelieu River leave me perplexed to say the least. I also have a lot of difficulty imagining that a 16-year-old teenager whose fragile state was solely due to allergies could almost drown while the motor of the boat from which he fell was stopped. I find this story all the more implausible because Mr. Pronovost explained that he had not yet informed his spouse of the heroic act performed by the appellant to rescue their son, who died in 1997, I would point out. He did not tell this story because, according to him, he was afraid that his wife would accuse him of having been negligent during this incident.[8]

[8] Such deficiencies were not present in the present case. The Appellant and his brother, Terrance Swarbrick, testified at the hearing. Unlike the witnesses in *Lacroix*, the Appellant and his brother were, on balance, persuasive. Their evidence was direct and to the point, in no small part because the relevant transactions were much less intricate and better documented than in *Lacroix*. Another distinction is that no witnesses were called for the Respondent. While I understood counsel for the Respondent to say that the Crown's witness had become unavailable at the last minute, the fact remains that if, from the Minister's perspective, there was more to this story than met the eye, no such evidence was before the Court. There was also documentary evidence to corroborate the Appellant's claim of having received an inheritance payment from his father and to verify the existence of loans, loan payments and cash deposits (which the Appellant candidly admitted he had made).

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[8] 2007 TCC 376 at paragraphs 12-16. (T.C.C.).

Notwithstanding counsel for the Respondent's dim view of his money management style, the Appellant's direct evidence of his preference to keeping cash at home rather than relying on banks remained unshaken on cross-examination. I accept the Appellant's testimony that sometime in the 1980's he got into the habit of keeping cash at home; he took some pride in explaining that he had built his own home, complete with a hiding place for his money secure enough to withstand a fire, should it come to that. While somewhat eccentric, this practice is not unlawful. It renders more onerous, however, the Appellant's burden of proof.

[9] Turning, then, to a consideration of the sources of funds identified by the Appellant, in respect of the advance on inheritance, I am satisfied by the testimony of the Appellant, corroborated by his brother, the notarized letter from his father[9] and the real estate documents[10] regarding the sale of the family home, that the Appellant received $21,000 from that source in 1999. I also accept his evidence that rather than putting the money in a bank account, he kept in it a secure location in his home.

[10] The Appellant also claimed to have had access to $20,000 in cash taken from a line of credit established in anticipation of buying a replacement vehicle for his 1979 Fiat Spider. As it turned out, the purchase of the new vehicle was financed, as assumed by the Minister and corroborated by the bank statements in evidence[11]. This claim was unchallenged on cross-examination. The Appellant also said that at the request of the Bank of Montreal, he had taken out a personal loan for $25,000 on February 16, 2000. While no formal documents for the line of credit were in evidence, it is referred to in Exhibit A-5, the letter from the Bank of Montreal describing the $25,000 loan transaction (separately documented by promissory note[12]). According to that letter and the Appellant's testimony, the loan proceeds were immediately applied by the bank to pay off the existing line of credit of $20,000 and an overdrawn amount of $1,000 on the Appellant's personal account. That would have left $4,000 to be squirreled away at the Appellant's residence with his other funds; meanwhile, he was required to[13] (and did[14]) make monthly payments of

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[9] Exhibit A-2.

[10] Exhibit A-3.

[11] Exhibit A-6.

[12] Exhibit A-4.

[13] Exhibit A-4.

$529.33 on the personal loan. These payments were taken into account in the net worth assessment.

[11] The result is that as of 2001, the Appellant would have had approximately $45,000 in cash from non-taxable sources available to him during the taxation years under appeal. Applying the test in *Lacroix*, I am satisfied on a balance of probabilities that the Appellant has provided a credible explanation for the $32,000 discrepancy between reported income and his net worth. Accordingly, the Minister was not justified in reassessing beyond the normal reassessment period for 2001 and 2002 or in reassessing on unreported income of $9,206 in 2003. There being no basis for the amounts assessed, it follows that the imposition of gross negligence penalties was also unjustified.

[12] For the reasons set out above, the appeals of the 2001, 2002 and 2003 taxation years are allowed and the reassessments are vacated.

Signed at Ottawa, Canada, this 26th day of November, 2010.

"G. A. Sheridan"

Sheridan J.

[14] Exhibit A-6.

CITATION:	2010TCC605
COURT FILE NO.:	2009-2837(IT)I
STYLE OF CAUSE:	RICHARD SWARBRICK AND HER MAJESTY THE QUEEN
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APPEARANCES:

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