SUPREME COURT OF NOVA SCOTIA
IN BANKRUPTCY AND INSOLVENCY

Citation: *Smith (re)*, 2021 NSSC 205

Date: 20210615
Docket: No. 43689
Registry: Halifax
Estate Number: 51-2461828

In the Matter of: The bankruptcy of Samuel Christian Smith

Judge: Raffi A. Balmanoukian, Registrar

Heard: March 5, 2021, in Halifax, Nova Scotia (by teleconference)

Counsel: Donald Leet, for the Trustee Powell Associates Ltd.
Maeve Baird, for Canada Revenue Agency
Samuel Christian Smith, for himself personally

Balmanoukian, Registrar:

[1] When I replayed the Court's Voxlog recording of this hearing, I noticed that I told Mr. Smith several times, "I can't give you an absolute discharge if I wanted to, and I don't want to." Having had the opportunity to reflect and conduct relevant research, that view – some might unflatteringly say "attitude" - remains intact.

[2] Mr. Smith's second bankruptcy, filed in January 2019, consists almost entirely of over two million dollars' debt to the Canada Revenue Agency.[1] Accordingly, s. 172.1 of the *Bankruptcy and Insolvency Act*, RSC 1985, c. B-3 (the "BIA") is engaged.[2]

[3] That section provides that when a debtor's "personal income tax debt," as defined therein, is more than $200,000 and more than 75% of the bankrupt's unsecured proven claims, the Court cannot grant an absolute discharge. It is further specifically directed to take into account four factors as outlined in s. 172.1(4), as well as such other considerations as may be relevant to the case at bar.

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[1] $2,325,191.23 according to the pre-bankruptcy notice of assessment; $2,325,254.98 according to the proof of claim, of which $1,213,056.27 is principal; the balance is penalties and interest. The 2019 pre- and post-bankruptcy NOAs showed nil income for that year. The total unsecured debts in the statement of affairs are listed at $2,345,123. The next largest listed creditor is $43,291.

[2] His first, in 1999, did not have meaningful tax debt.

[4] Mr. Smith's bankruptcy leaves those thresholds in the dust.

[5] Originally, CRA did not take an active role in the bankrupt's application for discharge, indicating to the Trustee on February 4, 2021 that it lacked financial information for Mr. Smith. As will appear, this shortcoming is entirely of Mr. Smith's making, and he should not benefit from it.

[6] Mr. Smith did not appear at the February hearing either, despite the Trustee having informed the Court on January 20, 2021 that "the Bankrupt has been advised of the hearing's location and time, as well as of his requirement to attend via conference call." (my emphasis). At my direction, both he and CRA did so when the matter returned to Court on March 5, 2021, and CRA filed an affidavit of Kate Lien (a CRA officer). Mr. Smith appeared by phone.

[7] It appears that Mr. Smith reported modest personal income for the 2011 through 2015 tax years, ranging from $10,483 to $33,977. In March, 2017, he was reassessed for substantially greater amounts, ranging from $351,453 to $681,950.

[8] On June 2, 2017 – that is, less than three months later, he quit claimed his interest in his only known meaningful asset, the matrimonial home; he did not enter into a separation agreement with his estranged spouse until November 2018;

it recites that the transfer is, among other things, in lieu of spousal support. It is assessed in 2021 for $167,000.[3]

[9] He filed for this bankruptcy in January 2019. That is about two months after "papering" the ostensible reason for the matrimonial home transfer two years before, which transfer was in turn on the heels of the tax reassessment. He did not report the transfer on his sworn statement of affairs.

[10] He also did not report a 25% interest in what was ultimately established to be a derelict property without realizable value.

[11] He did not report having "operated a business within the last five years" in answer to question 5 on his Form 79 statement of affairs, when in fact he did so, namely First Class Paving Inc. and First Class Contractors Limited. First Class Contractors Limited was indebted to CRA under various accounts for 2010-2014 for $443,141.01; First Class Paving Inc. was indebted to CRA, again under various accounts, for 2011-2016 for $1,625.818.41.

[3] Market evaluation submitted by Trustee.

[12] Mr. Smith did not object to or appeal the personal tax assessments. He did not pay anything on them. He appears to have worked for a family member for cash. He reported $1 in income for each of 2016 through 2019.[4]

[13] At the hearing, Mr. Smith asserted that he received the personal tax bill shortly after one or both of the corporate tax bills, saying they were "for exactly the same amount," took the view that these were really corporate rather than personal tax liabilities, and that the burden was on the Crown and that "they should have to explain where they got the debt from." When corrected on this point, he could provide no explanation (nor did he provide one to the Trustee), and said that he "can't remember the numbers back then" although we are speaking of reassessments from just on four years ago. The two corporate aggregates, although substantial, are neither identical to nor readily confused with the personal tax liability; Ms. Lien's affidavit makes it clear that these are separate accounts and not counted in Mr. Smith's "personal income tax debt" within the meaning of s. 172.1.

[14] He is now 59 years old and has no dependents.

[4] Lien affidavit, paragraphs 15-19, which was not challenged.

[15] He currently reports no income, and listed his occupation on his statement of affairs as "retired." At the hearing, he said he was not in fact retired but that he had been "doing nothing." That is, says he, "because of the bankruptcy;" he is living with (and, apparently, off of) relatives. He said he wants to "move on so I can get a job," and that he would do so "once I get a discharge." When I pointed out that he is not precluded from employment by reason of his bankruptcy, he said that you can only "make so much money" in the post-filing period before having to contribute to the estate. However, when pressed he denied that he was only interested in getting a job either after his discharge, or one that did not generate surplus income within the meaning of s. 68 of the BIA.

Law and Analysis

[16] I recently released *Re Sorochan*, 2021 NSSC 200, as an attempt to summarize much of the caselaw and "frequent flier" issues with respect to s. 172.1 BIA. I do not propose to engage in a lengthy exercise of quoting myself with approval, but shall merely incorporate those concepts and analyses in this case.

[17] In particular, I set out that the bankruptcy process is neither the manner nor forum in which to contest the validity of the tax assessment in issue. It is valid and

binding if an admitted proven claim and if there is no valid and subsisting tax appeal. That is the case here.

[18] As well, I discussed that the burden is on the high-tax-debt bankrupt to establish, to the Court's satisfaction on a civil standard, that they are an "honest but unfortunate debtor" and that the bankrupt has earned a discharge under conditions no more onerous than necessary in the circumstances of the case.

[19] I also reviewed the need to balance the significant rehabilitative elements of the BIA with the need for creditor protection and system integrity; and how this interfaces with the need for specific and general deterrence in tax-driven insolvencies from resiling from one's tax obligations.

[20] Further, I said that while the Court must consider the factors set out in s. 172.1(4) BIA when the section is triggered, it is also free to consider other relevant factors, including but not limited to those in s. 173.

[21] To be blunt, Mr. Smith appears to have a battle with truth. His submissions and responses ranged from the incredible to the farcical. His assertion, for instance, that the corporate debt somehow "migrated" to his personal account was roundly and completely refuted; his collateral attack on the validity of the assessment (and on whom the burden lay) was wrong in fact and law. His timeline

as to disposition of assets is convenient and even then was not disclosed under oath. His sworn answer to "business operations within five years of bankruptcy" is demonstrably wrong as well. As to his tax returns themselves, about all I can say in his favour is that they were filed. His reassessed income ranged from 32 to 55 times his declared net income.

[22] When confronted with the inimical consequences of the position that he would "go job searching" when (and apparently only when) he received his discharge and didn't need to pay anything into his estate, he backpedaled. His denial was malarkey.

[23] So, before turning to the four mandatory considerations in s. 172.1(4), I observe that Mr. Smith:

1. Obviously has (declared) assets below 50 cents on the dollar of unsecured liabilities and has not brought himself under the saving provision that he cannot "justly be held responsible" therefor, even if for such purposes one is most generous and ignores penalties and interest: s. 173(1)(a) BIA

2. Has omitted to keep relevant books of account given his complete inability to provide any kind of explanation for the substantial

discrepancies between reported and assessed income for 2011 through 2015; although s. 173(1)(b) refers only to the three years preceding bankruptcy (and is, strictly speaking, inapplicable), it will be recalled that Mr. Smith was reassessed in 2017 and filed his assignment in early 2019;

3. Has "failed to account satisfactorily for any loss of assets" – s. 173(1)(d) – the house transfer on the heels of the reassessment, the much-later "separation agreement," and the bankruptcy filing shortly after that separation agreement simply do not pass the smell test. Neither does his failure to disclose this (among other things) on his sworn statement of affairs;

4. Has previously been bankrupt: s. 173(1)(j);

5. Has failed to make an accurate statement of affairs: s. 158(d) and (e), and to make disclosure of dispositions/transfers at undervalue: s. 158(f) and (g).

[24] There may be other s. 173 and s. 158 factors. These are enough for now.

[25] I turn to the mandatory considerations of s. 172.1(4).

The circumstances of the bankrupt at the time the personal income tax debt was incurred: s. 172.1(4)(a)

[26] As I have noted, Mr. Smith asserted that the debts are actually corporate debts, and that these arose from "remittances not on time and accumulated," and were "only" a couple hundred thousand dollars. This is not the case; and even if it was, it is not an explanation of those egregious defaults either. He said that the debt was "re-allocated to him a month later." Once again, the inconvenient truth is that the numbers don't match and are clearly separate. On any kind of analysis, there was substantial underreporting and non-compliance, over a period of years. Although the assessments are binding, even if I were to be generous and say *arguendo* that they were off by, say, 90%, it means that he made between $35,000 and $68,000 while reporting $10,483 and $13,977 in the corresponding years. Less generously, it is manifest that he (directly or through his undisclosed companies - plural) made a substantial income and didn't pay his taxes.

The efforts, if any, made by the bankrupt to pay the personal income tax debt: s. 172.1(4)(b)

[27] These amounted to bupkis.

[28] Mr. Smith confirmed that his last payment was "four to five years ago," and the Lien affidavit confirms that although Mr. Smith was apparently "working for cash," he made no post-reassessment payments. Collection efforts came to naught. It appears his only financial response was to transfer title to the matrimonial home and to have no bank account at any major institution of whom CRA made inquiry.

Whether the bankrupt made payments in respect of other debts while failing to make reasonable efforts to pay the personal income tax debt: s. 172.1(4)(c)

[29] There was limited evidence on this point; Mr. Smith testified that not much else was paid in preference to the tax obligation (which raises the question of "where did the money go?"). He says he listed approximately $100,000 in other debt – the figure on the statement of affairs is actually $63,408; of this, $43,291 was to the next-highest creditor. The rest are well under $5,000 each.

[30] I do not have evidence that Mr. Smith did, or did not, prefer other creditors. However, given the level of income assessed and the lack of declared assets, it raises suspicions that Mr. Smith had an enviable level of consumption for several years, has undisclosed assets, or utilized his cash on hand in a manner that is not before the Court. Although again I emphasize that the assessment is binding, even

if it is wildly inaccurate it does not "jive" with the level of assets and non-tax liabilities I have before me.

The bankrupt's financial prospects for the future: s. 172.1(4)(d)

[31] As I have noted, Mr. Smith said that he would "go job searching," but despite his protestations to the contrary, I have no difficulty concluding that he will do so when and if it suits his purposes; he has no interest in yielding a dividend to creditors in even the most modest of fashions.

[32] I also have no difficulty concluding that Mr. Smith is quite capable of generating a significant income, also when it suits his purposes. He is middle-aged, without dependents, and has no impediments that were asserted to or evidenced to the Court.

Disposition

[33] As I have noted, s. 172.1 prohibits me from granting Mr. Smith an absolute discharge. It is up to him to demonstrate that the array of options available to me under s. 172.1(2) – namely, refusal, suspension, or other terms – are no more onerous than necessary to the facts of the case.

[34] He has, in what is restrained understatement, not done so. Nor has he rebutted the presumption that he is not an "honest but unfortunate debtor" and that his s. 173 "50 cents on the dollar" shortfall is not from circumstances for which he cannot justly be held responsible.

[35] I have no doubt that Mr. Smith has been, and perhaps remains, tax non-compliant. He did file his pre- and post-bankruptcy tax 2019 returns via the Trustee (as would be required to obtain a discharge), declaring nil or $1.00 income for both[5]. He declared the nominal dollar for 2016 through 2018[6]. At the time of hearing, the 2020 return was not yet due.

[36] He has not explained, at all much less satisfactorily, the substantial disconnect between assessed personal taxes and the lack of assets. His omissions on the statement of affairs are glaring and apparent. They border upon and perhaps cross over into outright perjury. He did not assert, nor did he manifest, any cognitive limitations that would put these discrepancies into any kind of innocent context.

[5] The Lien affidavit says $1.00 for 2019. The pre- and post-bankruptcy 2019 NOAs on file say $0
[6] Lien affidavit, para. 19.

[37] As I have said, I also have no doubt that Mr. Smith is underemployed by design and quite capable of making a decent living (or as he put it, having "a good paying job") when it suits him.

[38] In *Re Hover*, 2019 ONSC 6348, a second-time, 42 year old bankrupt engaged in significant under-reporting of income ($729,029 over three years); after imputing a level of income of around $70,000 per year, the Court ordered payment of $150,000 together with ancillary orders. Notably, Mr. Hover had significant medical limitations but had "many qualities of a successful and industrious entrepreneur" (para. 67).

[39] In *Re Schira*, 2014 SKQB 4, the bankrupt had earning potential of approximately $48,000 per year, but had an unspecified lower income.[7] In ordering an $18,000 payment over a maximum of 36 months on a tax debt of $364,106.65, Registrar Thompson explicitly took into account the bankrupt's potential as opposed to actual income.

[40] As I noted in *Sorochan*, a reasonable framework is what is achievable over a high tax debt bankrupt's medium (4-6 year) timeframe, after giving due

[7] It appears, given that he had no surplus income in the period following his 2012 filing and no dependents, that this was less than half his potential income, based on Directive 11-R2 as in effect for the applicable time.

consideration to the mandatory s. 172.1(4) factors and the other relevant facts of the case.

[41] I do not have adequate evidence of what Mr. Smith's potential "good paying job" would yield, should he deign to pursue one. I only am satisfied that having one is well within his grasp. I am also satisfied that given the amount of income attributed to him, the level and extent and duration of underreporting, lack of mitigating factors under s. 172.1(2), and tenuous relationship with candour, that a five year window is appropriate. The only reasons it is not longer are Mr. Smith's age and the fact that his first bankruptcy in 1999 was devoid of any meaningful tax liability. There should, however, be a "floor" to his obligation, given his demonstrated lack of motivation to contribute to his estate. If he chooses to remain unemployed or underemployed, his creditors should have a minimum return as a condition of Mr. Smith's discharge. I have also factored in the suspicious and undeclared transfer of property on the heels of the reassessment, and its "papering" through a separation agreement just before the bankruptcy filing.

[42] Lastly, I have not lost sight of the BIA's rehabilitative aspects. As I pointed out in *Sorochan*, however, part of that self-same rehabilitation is an appreciation that taxes are a perennial and lifelong reality and their honest filing and payment is an integral part of economic and financial rehabilitation. Mr. Smith's sense of

discharge entitlement needs a sharp and unequivocal reality check in that regard, and it should be for a sufficient period that he make his second exit from the bankruptcy process with that firmly in mind.

[43] I am therefore, in my discretion, ordering the following:

- Payment of 15% of Mr. Smith's T1 "line 15000" income, as well as 15% of any income generated from any entity with which he does not deal at arm's length (e.g. a company controlled by him or a non-arm's length party, or a proprietorship or partnership with which he is employed at non-arm's length) to the Trustee, not less than quarterly, for a period of five years from the date of this order; this shall not be less than $100,000. For clarity, the amount required to be paid into the estate shall be the greater of 15% of Mr. Smith's pre-tax income (and non-arm's length operations' pre-tax income) for the next five years, and $100,000.

- Filing, assessment, and payment of all relevant tax returns (including but not limited to income tax, HST, and payroll), and provision of same to the Trustee for the years 2021 through and including 2026, as and when due;

- In the event of an adverse reassessment of any such return by CRA, the same shall be disclosed to the Court; thereupon, the Court may if it deems fit,

modify the order pursuant to s. 187(5) BIA, or as otherwise within its jurisdiction;

- Delivery up to the Trustee of any present or pre-discharge property that is "property of the bankrupt" within the meaning of s. 67 of the BIA;

- Upon completion of all of the foregoing, Mr. Smith may make a further application for discharge.

[44] I appreciate that the effect of this decision is to extend the period of bankruptcy from early 2019 to at least some time in 2027, given the requirement for completion, evaluation, and if applicable payment of 2026's returns. It is a long time. Such is the price of deterrence from lack of candour and shameful tax practices, and on these facts in my view such is the proportionate means by which to balance rehabilitation with that deterrence and systemic integrity.

[45] The Trustee shall prepare the order for my review.

Balmanoukian, R.