Date: 20001103

CORAM: DÉCARY J.A.

LÉTOURNEAU J.A.

NOËL J.A.

Docket: A-758-98

BETWEEN: **HER MAJESTY THE QUEEN**

Appellant

AND:

LOUISE MARCOUX-CÔTÉ

Respondent

_ _

Docket: A-759-98

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

ALAIN CÔTÉ

Respondent

Hearing held at Québec, Quebec, on Thursday, October 19, 2000

Judgment delivered at Ottawa, Ontario, on Friday, November 3, 2000

REASONS FOR JUDGMENT BY: LÉTOURNEAU J.A.

CONCURRED IN BY: DÉCARY J.A.

NOËL J.A.

Date: 20001103

CORAM: DÉCARY J.A.

LÉTOURNEAU J.A.

NOËL J.A.

Docket: A-758-98

BETWEEN: **HER MAJESTY THE QUEEN**

Appellant

AND:

LOUISE MARCOUX-CÔTÉ

Respondent

_ _

Docket: A-759-98

BETWEEN:

HER MAJESTY THE QUEEN

Appellant

AND:

ALAIN CÔTÉ

Respondent

.

REASONS FOR JUDGMENT

LÉTOURNEAU J.A.

Did Judge Garon (now Chief Judge) of the Tax Court of Canada err in holding that the respondents were entitled to a tax credit for charitable gifts under section 118.1 of the *Income Tax Act* (the Act)? Did he err in determining the fair market value of the gifts for purposes of calculating the deduction permitted by the Act? Was he correct in imposing the penalty prescribed by subsection 163(2) of the Act on the respondents?

These are the three questions that were submitted to us, the first by way of appeal by Her Majesty the Queen and the two others by way of cross-appeal by the respondents. The two appeals and cross-appeals in these cases were heard together with the appeals and cross-appeals in the Duguay (A-756-98 and A-757-98) and Langlois (A-760-98 and A-761-98) cases. They were argued on the basis of a number of questions common to all, while bearing in mind certain factual differences.

The facts

Mr. and Mrs. Côté are members of a group of several people who had dealings with Marc Levert, the founder and principal shareholder of the Galerie des Maîtres Anciens Inc. in Québec. Mr. Levert would sell works of art (paintings) to his clients, usually for 25% of the appraised value, and they would then give the works of art to charitable organizations identified and chosen by Mr. Levert. It was Mr. Levert who looked after finding and choosing

the charitable organizations to which he gave the gifts. For this purpose, he acted as agent of the donors. He also appraised the property that was donated and provided the receipts that were needed for obtaining the tax credit. In addition, Mr. Levert acted as agent for the charitable organizations. As such, he received the gifts intended for them, resold the gifts immediately and gave the organizations only a minute share--between 4% and 10%-- of the sale proceeds.

In a judgment of the Superior Court of Quebec, criminal division, dated February 28, 1994, Mr. Levert was found guilty of destroying records for the 1984, 1991 and 1992 taxation years. On March 17, 1995, the Court of Québec, penal division, also found him guilty of tax evasion for the 1984 to 1988 taxation years. This judgment was confirmed by the Superior Court on January 11, 1996. Last, on April 7, 1997, Mr. Levert pleaded guilty, in relation to the present cases, to charges of conspiring to evade payment of taxes and enabling taxpayers, including the respondents, to evade payment of taxes in the amount of $110,000 for the 1986 to 1988 taxation years. He was sentenced to imprisonment for ten months. A probation order was also made prohibiting him from acting directly or indirectly as an appraiser, promoter, broker or consultant in connection with gifts of works of art to non-profit organizations, for a period of two years.

The respondents bought and transferred property over a five-year period beginning in 1986. For 1988, 1989 and 1990, Mr. Côté donated property which was routinely valued at $11,000 and his wife donated property valued at $2,750. The purchase price paid by the respondents corresponded to 25% of the appraised value of the paintings determined by Marc Levert. No purchase invoice was issued and the respondents refused to provide Revenue Canada with proof of purchase or payment.

Only the 1988, 1989 and 1990 taxation years are at issue. In fact, the respondents were reassessed for 1986 and 1987, as the Minister of National Revenue disputed the fair market value assigned to the gifts by Mr. Levert. The respondents objected to the reassessment but later withdrew their objections.

Despite the reassessment, the respondents continued to make gifts during the years at issue.

Were the respondents entitled to the tax credit for charitable gifts?

The Tax Court of Canada Judge applied the principles set out in the Civil Code of Lower Canada, in particular articles 755 and 776 which, at the time, governed the making of gifts. He held that the essential conditions for a gift to exist had been met: intent to give, delivery of the property and acceptance by the donee. Relying on the decision of this Court in *The Queen* v. *Friedberg*, 92 DTC 6031, he held that even though obtaining a tax advantage was the principal motivation of the respondents in this case, that did not nullify the donors' intent to give. He also was of the view that obtaining a receipt from the charitable organization could not be viewed as consideration that would eliminate the gratuitous and liberal nature of the transaction.

In the end, he concluded that the subject-matter of the gifts was identified clearly enough, and he was satisfied that they became the property of the charitable organizations which issued the receipts for tax purposes.

In my view, the judge directed himself properly as to the legal principles that apply to this case. I am also not persuaded that he erred in applying those principles to the facts before him. Accordingly, I would dismiss the appeal with costs.

Did the judge err in determining the fair market value of the items donated?

By way of cross-appeal, the respondents submit that, in determining the fair market value of the property, the judge put too much emphasis on auction prices for these items and that he systematically disregarded their retail prices in art galleries. They also submit that he ignored the objective criteria on which Mr. Levert relied to establish the appraised values.

Counsel for the respondents suggested that we do a fresh determination of the fair market value, based on an average of the appraised value shown on the receipt, the value of similar goods at auction, and the retail price paid by purchasers at a gallery.

In my view, the calculation suggested by counsel for the respondents is not appropriate in this case, and there is no reason to proceed otherwise than the Trial Judge did: for many of the paintings there was no gallery market; the circumstances surrounding the transactions were at the very least strange and unique, not to say suspicious, by any yardstick, and the prices were routinely inflated. These factors make any standard or principle of general application such as is suggested by the respondents inappropriate.

Accordingly, the Judge had to assess the fair market value of the property at issue on the basis of its distinctiveness and its specific characteristics. "Fair market value" means the value obtained in a normal market, that is, a market which is not disturbed by unusual economic factors and where vendors, ready but not too anxious to sell, meet with purchasers ready and able to purchase: *Attorney General of Alberta* v. *Royal Trust Co.* [1945] S.C.R. 267, at page 288. In order to determine fair market value, the Judge used various methods: he relied at times on the testimony of expert witnesses, at other times on the fact that the property itself, at auction, could not even fetch a reserve price well below the appraised value submitted by the respondents, at other times on the prices actually paid at auction for works for which there was no market other than auctions, at other times on prices actually paid for works by the same artist that were comparable in size, subject matter and time period, and at other times on the sale or buy-back price of property that was immediately resold at auction by the donee. The judge took into account the relevant market where supply and demand operated and where the work could have been sold, or in fact, was resold shortly thereafter: his approach cannot be criticized.

For example, in 1988, Mr .Côté bought a painting from Mr. Levert by the artist Ludger Larose depicting the funeral of a young girl in Venice. He obtained an appraisal from Mr. Levert in the amount of $11,000. This painting belonged to Thomas Kramer who had purchased it in 1983 for $1,200 (see the testimony of Mr. Kramer, file A-759-98, appeal book, vol. IV, pages 769-771).

In early 1986, Mr. Kramer offered to sell the painting to the Musée du Québec for $5,000. His offer was rejected by the acquisitions committee. He came back in August of the same year, offering to donate the painting to the Musée in return for a receipt for income tax purposes. On December 19, the acquisitions committee again refused the painting because

it did not meet the three criteria for acquisitions established by Musée officials, namely, the quality of the work itself, what interest the work held as compared to the artist's body of work, and what interest the work held as compared to the entire collection owned by the Musée (*id.*, at pages 739-746). Mr. P. L'Allier, the Musée du Québec's curator, stated that the main reason for refusing the painting related to the quality of the work in aesthetic terms, as the painter was an artist who had difficulty incorporating the representation of people into a given composition (*id.*, pages 752-756).

After the Musée officials refused the painting, Mr. Kramer put it up for sale at Encans Pinneys for a minimum price of $2,000. The auctioneer, Mr. D. Kelsey, estimated it to be worth between $2,500 and $3,000. The painting was sold in December 1987 for $2,200 (see the testimony of Mr. Kramer and Mr. Kelsey, appeal book, vol. IV, at pages 772-75 and 946-47). It is worth noting that it was bought back by the same Mr. Levert, for less than the price for which he had sold it to Mr. Côté ($2,750), after providing him with an appraisal of $11,000. Under the circumstances, it seems to me that the value of $2,200 assigned by the judge reflects the fair market value.

The judge was also sensitive to the limits set by the experts regarding the factors used by Mr. Levert in his appraisals. By way of example, according to the testimony of Mr. Harvey, Mr. Gagnon and Mr. Rinfret, the prices in the Guide Vallée, which Mr. Levert relied on heavily in doing his appraisals, did not represent actual sale prices, but rather prices displayed for the purpose of publicizing the artists mentioned in it. Those prices are calculated by the square inch, based on the size of the painting, and do not take into account important factors that influence fair market value, such as the period when the painting was done, the artist's subject and the quality of the painting (see Côté, file A-759-98, vol. VIII, at page1968, vol. XI, at pages 2610-11, 2848-57, 2867-69 and vol. X, at pages 2508-16).

The judge had the delicate and very difficult task of determining the fair market value of the gifts acquired and resold by Mr. Levert on the auction market, for which the respondents did not provide any retail gallery sale invoice. The judge did a conscientious job of this for each of the properties, referring to the evidence before him. I do not see any error in his approach that would warrant our intervention. Accepting the evaluation method proposed by the respondents would amount to reasoning in the abstract and ignoring both the evidence and the judge's analysis of it. I would dismiss the first ground of the cross-appeal.

Was the judge correct in imposing the penalty prescribed in subsection 163(2) of the Act?

Subsection 163(2) imposes a penalty on every person who knowingly or under circumstances amounting to gross negligence makes or participates in, assents to, or acquiesces in the making of, a false statement or omission in a return in respect of a taxation year. More specifically, it reads:

163. (2) Faux énoncés ou omissions

Toute personne qui, sciemment ou dans des circonstances équivalant à faute lourde dans l'exercice d'une obligation prévue à la présente loi ou à un règlement d'application,, fait un faux énoncé ou une omission dans une déclaration, un formulaire, un certificat, un état ou une réponse - appelé "déclaration" au présent article - rempli ou produit, pour une année d'imposition conformément à la présente loi ou à un règlement d'application, ou y participe,

y consent ou y acquiesce est passible d'une pénalité égale, sans être inférieure à 100$, à 50% du total:

a) de l'excédent éventuel

(i) de la fraction de l'excédent éventuel de l'impôt qui serait payable par cette personne pour l'année en vertu de la présente loi qui est en sus du montant qui serait réputé par le paragraphe 120(2) payé au titre de cet impôt pour l'année, s'il était ajouté au revenu imposable déclaré par cette personne dans la déclaration pour l'année la partie de son revenu déclaré en moins pour l'année qu'il est raisonnable d'attribuer au faux énoncé ou à l'omission et si son impôt payable pour l'année était calculé en soustrayant des déductions de l'impôt payable par ailleurs par cette personne pour l'année, la partie de ces déductions qu'il est raisonnable d'attribuer au faux énoncé ou à l'omission,

sur

(ii) la fraction éventuelle de l'impôt qui aurait été payable par cette personne pour l'année en vertu de la présente loi qui est en sus du montant qui aurait été réputé par le paragraphe 120(2) payé au titre de cet impôt pour l'année, si l'impôt payable pour l'année avait fait l'objet d'une cotisation établie d'après les renseignements indiqués dans la déclaration pour l'année;

[...]

163. (2) False statements or omissions

Every person who, knowingly, or under circumstances amounting to gross negligence in the carrying out of any duty or obligation imposed by or under this Act, has made or has participated in, assented to or acquiesced in the making of, a false statement or omission in a return, form, certificate, statement or answer (in this section referred to as a "return") filed or made in respect of a taxation year as required by or under this Act or a regulation, is liable to a penalty of the greater of $100 and 50% of the total of

(a) the amount, if any, by which

(i) the amount, if any, by which
(A) the tax for the year that would be payable by the person under this Act exceeds
(B) the amount that would be deemed by subsection 120(2) to have been paid on account of the person's tax for the year
if the person's taxable income for the year were computed by adding to the taxable income reported by the person in the person's return for the year that portion of the person's understatement of income for the year that is reasonably attributable to the false statement or omission and if the person's tax payable for the year were computed by subtracting from the deductions from the tax otherwise payable by the person for the year such portion of any such deduction as may reasonably be attributable to the false statement or omission

exceeds

(ii) the amount, if any, by which(A) the tax for the year that would have been payable by the person under this Act

exceeds

(B) the amount that would have been deemed by subsection 120(2) to have been paid on account of the person's tax for the year

had the person's tax payable for the year been assessed on the basis of the information provided in the person's return for the year,

...

The Trial Judge found that the respondents were extremely reckless or at least grossly negligent in respect of their tax obligations. He described several facts which led him to make this finding:

In light of all the evidence, I have been persuaded by the appellants' behaviour that they were extremely reckless or at least grossly negligent in respect of their tax obligations. It seems to me that, particularly after Mr. Côté's meeting with Revenue Canada's investigators, the appellants should have reconsidered their position in relation to the tax authorities. They should have wondered about the true nature of the arrangements pursuant to which they were obtaining tax receipts for amounts four times higher than the prices of the works of art they had just acquired. That fact alone-- the fact that there was so great a difference between the prices paid by the appellants for the paintings and the amounts that appeared on the tax receipts, which supposedly represented the market value of the paintings at the same point in time--leads me to believe that the appellants knew or ought to have known, if they had been mindful of their tax obligations, that the amounts indicated on the receipts were greatly inflated or excessive and did not represent the market value of the paintings in question. Mr. Levert's role at every stage of these transactions should have raised serious suspicions in their minds. The fairly passive role of the charities to which the works of art were given should have prompted the appellants to be careful. The facts that the charities were for all practical purposes chosen by Mr. Levert and that the appellants displayed a total lack of interest, as donors, in the organizations that received their gifts are also strange and unusual aspects of the transactions in question. Generally speaking, the appellants' failure to co-operate with the tax authorities when they were asked to provide proof of purchase and payment documents regarding the works of art in question also persuades me that they may have thought their conduct was not beyond reproach.

All these facts were put into evidence and I agree with both his interpretation of the facts and the finding that he made.

Counsel for the respondents maintained that his clients could not be criticized for continuing to make gifts after being reassessed for 1986 and 1987. Referring to *Hudson Bay Mining and Smelting Co.* v. *R.*, [1986] 1 C.T.C. 414, affirmed by this Court with respect to the dismissal of the penalty, [1989] 2 C.T.C. 309, he argued that a mere disagreement with the tax authorities does not justify the imposition of the penalty prescribed in subsection 163(2). He added that his clients had certainly not been negligent, and on the contrary, had been doubly vigilant after being alerted by Revenue Canada that Mr. Levert's appraisals were inflated and did not reflect fair market value.

With respect, I believe, on the one hand, that the respondents' conduct revealed much more than a mere disagreement with the tax authorities and, on the other hand, that their alleged vigilance is not supported by the evidence regarding what they did during the taxation years at issue.

Revenue Canada informed the respondents in 1987 that the appraisals submitted by Mr. Levert in 1986 and 1987 were inflated. In fact, the value of the property donated in 1986 was reduced by 78% (see the testimony of Mr. Demers, appeal book, vol. IV, at page 848). The respondents recognized this by withdrawing their objection. What do they do in 1988? They engage in fresh dealings with the same Mr. Levert, in the same context where he again acts as agent for both the donors and the donee, and they do nothing to verify the appraisals of $11,000 and $2,750 that he provides to them.

If only the year 1988 were at issue, it could perhaps be argued that there is room for doubt. But what do the respondents do in 1989 and 1990, after being reassessed and receiving a serious warning as to the accuracy of the appraisals they were providing in support of their request for a tax credit? They again purchase from Mr. Levert, and curiously, always at a price corresponding to 25% of the appraised value, and they do not question in any way the appraisal that he gives them. Under these circumstances, it is difficult not to conclude that they were wilfully blind and grossly negligent within the meaning of subsection 163(2). I would dismiss the second ground of the cross-appeal.

For the reasons stated, I would dismiss the appeal and the cross-appeal with costs.

Gilles Létourneau

J.A.

"I concur.

Robert Décary J.A."

"I concur.

Marc Noël J.A."

Certified true translation

Mary Jo Egan, LLB