Date: 20090123

Docket: A-480-07

Citation: 2009 FCA 19

CORAM: **DÉCARY J.A.**
NOËL J.A.
BLAIS J.A.

BETWEEN:

177795 CANADA INC.

Appellant

and

HER MAJESTY THE QUEEN

Respondent

Hearing held at Montréal, Quebec, on January 15, 2009.

Judgment delivered at Ottawa, Ontario, on January 23, 2009.

REASONS FOR JUDGMENT BY: NOËL J.A.

CONCURRED IN BY: DÉCARY J.A.
BLAIS J.A.

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REASONS FOR JUDGMENT

NOËL J.A.

[1] This is an appeal from a decision by Justice Lucie Lamarre of the Tax Court of Canada (the TCC judge), confirming the assessment of the Minister of National Revenue (the Minister) pursuant to the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) (the Act) for the appellant's 1992 taxation year.

[2] The appellant is a corporation which, during the 1992 taxation year, operated a company under the name of Sofati Ltée. (Sofati). At issue is the appellant's right to claim a loss of about

US$16 000 000 incurred in 1988 and to deduct the balance of it in computing its income for the 1992 taxation year. The loss in question was allegedly the result of the operation of a business by a partnership of which the appellant had been a member.

FACTS

[3] The facts underlying the appeal were set out in a partial agreement, which was reproduced by the TCC judge in her reasons. The TCC also heard the testimony of Michel Gaucher, the appellant's president, and Nancy Orr, who was Sofati's vice-president at the time and also in charge of its finances. Both were involved in the negotiation of the transactions that allegedly made it possible for the appellant to become a member of the partnership that generated the loss.

[4] The loss in question dates back to 1988 and stems from Preston Parkway Joint Venture (PPJV), a partnership established under the *Partnership Act* of the state of Texas, of which the appellant became a member on December 1, 1987.

[5] On November 30, 1987, PPJV's only asset and only purpose was a rental property, Sherry Plaza, which had been built a number of years earlier for the cost of US$32 000 000 and which, on November 30, 1988, had a market value of US$16 000 000.

[6] Before December 1, 1987, the members of PPJV were Louis G. Reese Inc. (Reese) and Preston Parkway Development Company (PPDC), two American companies whose interests in the partnership were 99% and 1% respectively.

[7] On December 1, 1987, the Bank of New York, which held a mortgage on Sherry Plaza, bought Sherry Plaza at auction for US$16 000 000. As the building had been acquired by PPJV for US$32 000 000, the sale resulted in a loss of US$16 000 000, which was recorded in PPJV's financial statements for the fiscal year ending December 31, 1987.

[8] PPJV was informed for the first time on October 12, 1987, that the real property would be seized and sold if it defaulted on the mortgage payment. It was also informed at least 21 days prior to the date of the seizure that the property would be seized and sold.

[9] On November 16, 1987, when the appellant agreed to acquire Reese's and PPDC's interests in PPJV, it therefore knew that the company's only asset would be seized and sold on December 1, 1987.

[10] PPJV's constituting agreement provided that the sole purpose of the partnership was to develop a real estate project that eventually became Sherry Plaza. According to the terms of an amendment that is undated but that became effective on November 30, 1987, the original agreement was amended to allow for the pursuit of other ventures.

[11] On December 15, 1987, the agreement under which Reese and PPDC transferred their interests to Sofati and its sister company Westmount Park Towers Inc. (WPTI) was signed. Reese first assigned its 99% interest to the appellant and WPTI in respective shares of 99% and 1%, and PPDC then transferred its 1% interest to the appellant and WPTI in the same proportions, the whole retroactive to December 1, 1987.

[12] The only transaction made by PPJV under the control of the Canadian partners occurred in September 1989, when PPJV acquired a 1% interest in a project in Texas (the Highland Park Shopping Village) for US$175 000.

[13] In its return for the 1992 taxation year, the appellant deducted its share of the US$16 000 000 loss resulting from the sale of PPJV's real property in December 1987 in computing its income.

ASSESSMENT

[14] The Minister refused to carry over the loss on the ground that when the appellant purchased its share in PPJV, its intention was not to carry on business with a view to profit from the activities of PPJV. The appellant therefore did not become a member of that partnership within the meaning of the Act and therefore could not claim entitlement to the loss incurred by PPJV under section 96 of the Act.

[15] Alternatively, the Minister argued that, even if PPJV was a partnership in which the appellant participated, no loss was attributable to the appellant within the meaning of subsection 10(1) of the Act and section 1801 of the *Income Tax Regulations*, C.R.C., c. 945. More specifically, subsection 10(1) obliged PPJV to value Sherry Plaza according to its fair market value, namely US$16 000 000, such that no loss was made in the year of disposition.

[16] The Appellant objected to the assessment, which was later confirmed by the Minister on May 4, 2004. Consequently, the appellant turned to the TCC.

TCC JUDGMENT

[17] The TCC concluded that the American partners and the Canadian buyers had no common intention to carry on business with a view to profit. The essence of the TCC judge's reasoning can be found at paragraph 36 of her reasons.

> In my opinion, as in *Backman* [*v. Canada*, [2001] 1 S.C.R. 367, 2001 SCC 10], the Appellant did not prove that it agreed with the American partners to carry on business in common with a view to profit from the activities of PPJV. It is true that right before the repossession of the property by [the Bank of New York], the partnership contract was amended to provide for the possibility of investing in real property projects other than the Sherry Plaza, and that indeed, two years later, PPJV finally invested US$175,000 in a real property project it still has. However, considering the circumstances surrounding the entire transaction, those facts alone do not pursuade [*sic*] me that Louis G. Reese, PPDC and the Appellant had the intention to carry on business in common with a view to profit. In my opinion, that was the key element that had to be proven by the Appellant, which it failed to do.

[18] She added at paragraph 40:

> In this case, the only asset of PPJV was seized immediately after the retroactive withdrawal of the American partners. Even though the purposes of the partnership were amended prior to their withdrawal, I am satisfied that, in view of the evidence, neither Mr. Reese nor PPDC had an intention to carry on business in common with a view to profit with the Appellant and WPTI. Indeed, no investment was made with them after that. The objectives sought by the Appellant after the withdrawal of Mr. Reese and PPDC, and the time and money invested by the Appellant, were not to carry on the business operated by PPJV while it was under American control. . . .

[19] Having concluded that the appellant had not participated in the pursuit of a common purpose with Reese and PPDC, the TCC judge did not discuss the alternative argument raised by the Minister to justify the assessment.

ANALYSIS AND DECISION

[20] While recognizing that the TCC judge correctly identified the constituent elements of a partnership, the appellant alleges that she misapplied them (Appellant's Memorandum, paragraphs 29 to 67). The appellant also challenges a number of the conclusions drawn by the TCC judge (paragraphs 68 to 76). The questions raised are either questions of fact or questions of mixed fact and law. In either case, this Court cannot interfere in the absence of a palpable and overriding error (*Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235). In my humble opinion, it has not been shown that the TCC judge committed such an error.

[21] Among the arguments raised by the appellant, the only one that warrants closer examination is that the TCC judge should have determined whether Reese's and PPDC's involvement was necessary to ensure PPJV's continued existence (Appellant's Memorandum, paragraphs 33 and 54). The appellant argues that if the TCC judge had asked herself that question, she would have necessarily concluded that PPJV continued to exist with the appellant and WPTI as partners. According to the appellant, Reese's and PPDC's participation was in no way necessary to ensure PPJV's long-term survival (Appellant's Memorandum, paragraph 55).

[22] With respect, the TCC judge, after finding that the appellant had never had the common intention of operating PPJV with the American partners, did not have to take the analysis any further. In order to be entitled to the claimed loss, the appellant had to have participated as a partner in the partnership that generated the losses. The TCC judge did not rule out the possibility that the appellant could have created a new partnership with WPTI (Reasons, paragraph 37), but she concluded unequivocally that the appellant had never been part of the partnership that generated the losses.

[23] The evidence supports that conclusion. According to the evidence, the only building that was the objective of the business carried on by PPJV was sold on December 1, 1987. Only two weeks later, the appellant was awarded its share in the partnership. In that respect, the appellant greatly insisted on the fact that its admission into the partnership was retroactive to December 1 (Appellant's Memorandum, paragraphs 57 to 59). The appellant relies on the wording of the agreement, which stipulated as follows in its opening paragraph (Appeal Book, Vol. I, page 66):

> This assignment . . . is executed . . . on the fifteenth day of December, 1987, to be effective as of the first day of December, 1987 . . .

[24] That being said, the parties to that agreement do not specify that the contract reflects a verbal agreement entered into on an earlier date, as is commonly done. The parties simply agreed to make the agreement retroactive to December 1, 1987. This is what Ms. Orr's testimony reveals (Appeal Book, Vol. IV, page 699, lines 3 to 8). For his part, Mr. Gaucher stated that he did not know why the agreement was entered into retroactively (Appeal Book, Vol. IV, page 667, lines 6 to 10). Certainly, no one alleged that the agreement signed on December 15, 1987, reflected a verbal agreement entered into previously.

[25] Whether the appellant intended to operate PPJV with the American partners is a question of fact. The TCC judge found, among other things, that PPJV had disposed of the revenue-producing building when the appellant signed the December 15, 1987, agreement (Reasons, paragraphs 16 and 25). As the development and operation of that building was PPJV's only commercial activity, the TCC judge concluded that the appellant could not have intended to carry on PPJV's business with the American partners. The fact that the parties' agreement was retroactive clearly cannot remedy this defect.

[26] The attempts to involve Reese in the subsequent operations that the appellant was planning also failed to show that there was a common intention to carry on business (Reasons, paragraphs 27 and 28). Ultimately, the TCC judge concluded that the appellant had not succeeded in

demonstrating that, at some point in time, it had had the intention of carrying on business in common with the American partners. The evidence supported this conclusion.

[27] It is therefore not necessary to rule on the alternative argument raised by the Minister to justify the assessment. I would say, however, that it is doubtful that subsection 10(1) can apply notwithstanding subsection 10(2), as the Minister's counsel argues (Respondent's Memorandum, paragraph 39). In fact, subsection 10(1) sets out how inventory should be valued for the purpose of computing income for a given taxation year, and, according to the evidence, no inventory was owned by PPJV on December 31, 1987.

[28] For those reasons, I would dismiss this appeal with costs.

"Marc Noël"

J.A.

"I agree.
Robert Décary J.A."

"I agree.
Pierre Blais J.A."

Certified true translation
Johanna Kratz

FEDERAL COURT OF APPEAL

SOLICITORS OF RECORD

DOCKET:	A-480-07
(APPEAL FROM A JUDGMENT OF THE HONOURABLE MADAM JUSTICE LUCIE LAMARRE OF THE TAX COURT OF CANADA, DATED SEPTEMBER 27, 2007, DOCKET NO. 2004-3092(IT)G.)	
STYLE OF CAUSE:	177795 CANADA INC. and HER MAJESTY THE QUEEN
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DATE OF HEARING:	January 15, 2009
REASONS FOR JUDGMENT BY:	NOËL J.A.
CONCURRED IN BY:	DÉCARY J.A. BLAIS J.A.
DATED:	January 23, 2009

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