Docket: 2013-1829(IT)I

BETWEEN:

SYLVAIN DELISLE,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on June 9, 2015, at Québec, Quebec.

Before: The Honourable Justice Réal Favreau

Appearances:

Agent for the appellant:	Hélène Lamarche
Counsel for the respondent:	Simon Vincent

JUDGMENT

The appeal from a reassessment made by the Minister of National Revenue pursuant to the *Income Tax Act*, dated June 9, 2011, in respect of the appellant's 2007 taxation year is dismissed in accordance with the attached Reasons for Judgment.

Signed at Montréal, Canada, this 16th day of November 2015.

"Réal Favreau"

Favreau J.

Translation certified true
on this 28th day of December 2015
Janine Anderson, Translator

Citation: 2015 TCC 281
Date: 20151116
Docket: 2013-1829(IT)I

BETWEEN:

SYLVAIN DELISLE,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

REASONS FOR JUDGMENT

Favreau J.

[1] The appellant commenced an appeal before this Court, using the informal procedure, from a reassessment dated June 9, 2011, made by the Minister of National Revenue (Minister) pursuant to the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) as amended (Act), concerning the 2007 taxation year.

[2] In filing his tax return for the 2007 taxation year, the appellant claimed an allowable business investment loss (ABIL) in the amount of $21,457, that is to say, 50% of his business investment loss.

[3] Under the reassessment dated June 9, 2011, the Minister disallowed the ABIL of $21,457 claimed by the appellant.

[4] To determine the tax payable by the appellant for the 2007 taxation year, the Minister relied on the following findings and assumptions of fact:

> [TRANSLATION]
>
> (a) the appellant was the spouse of Hélène Lamarche at the time of the loan and still is today.
>
> (b) according to Quebec's enterprise register (CIDREQ system), Ms. Lamarche has been, to date, the sole shareholder of Épicerie-Boucherie Lam-Bher Inc.
>
> (c) Épicerie-Boucherie Lam-Bher Inc. was incorporated on April 26, 1988, under the *Companies Act*, Part 1A, CQLR, c. C-38, (company).

(d) the company retails food and food-related products.

(e) on January 4, 1997, the appellant and Ms. Lamarche signed a note payable in the amount of $20,000 for an investment in Ms. Lamarche's company, and no method of payment, due date or interest rate was specified.

(f) on January 5, 2004, the appellant and Ms. Lamarche signed a note payable in the amount of $12,000 for an investment in Ms. Lamarche's company, and no method of payment, due date or interest rate was specified.

(g) the company did not file a corporate tax return for the 2006 and subsequent taxation years.

(h) the business was sold to Ms. Lamarche's sister in 2007, which is not confirmed by a declaration in the CIDREQ system.

(i) the CIDREQ system does not contain any declaration of a bankruptcy.

(j) the Minister sent the appellant a notice of confirmation stating that he was disallowing the BIL in the amount of $42,914.

(k) the appellant did not acquire a debt from Lam-Bher.

(l) even if it is found that the appellant acquired a debt from Lam-Bher, the debt would not have been acquired for the purpose of gaining or producing income.

[5] Hélène Lamarche testified at the hearing and filed as Exhibit A-1 the private financing agreements dated January 4, 1997, and January 15, 2004, that she entered into with her spouse.

[6] Under the agreement dated January 4, 1997, Ms. Lamarche undertook to repay to the appellant the amount of $20,000, with interest, that he had paid her to invest in her company. The repayment deadline was flexible and 2% interest was to be added to the loan amount.

[7] Under the agreement dated January 15, 2014, Ms. Lamarche undertook to repay to the appellant the amount of $12,000, with interest, that he had paid her to invest in her company. The repayment deadline was to be set once Ms. Lamarche's business reached the break-even point. Interest at the rates in force at the time the loan was made was to be added to the total loan amount at the end of the repayment.

[8] Ms. Lamarche put in evidence the hypothecary loan taken out by her spouse at the Caisse populaire de Rivière-à-Pierre on October 30, 1996, in the amount of $20,000 with a five-year term and an interest rate of 8.125% as well as the personal loan taken out by her spouse at the same caisse populaire on October 21, 2003, in the amount of $12,000.

[9] Ms. Lamarche testified that her spouse had given her other advances, which were deposited into the company's bank account and totalled $20,572, during the period beginning August 26, 2004, and ending March 20, 2006. Ms. Lamarche did not provide explanations concerning the terms of repayment of those advances or the applicable interest rate, but specified that those advances came from an account that she held with her spouse and in which her spouse's pay was deposited.

[10] In her testimony, Ms. Lamarche put in evidence the proposal filed on March 1, 2006, with the official receiver pursuant to which unsecured creditors had to agree to accept $40,000 in full and final payment of the provable claims. The proposal trustee issued, on June 5, 2007, a certificate of full performance of the proposal, as deposited with the official receiver on March 1, 2006, and amended at the creditors' meeting on March 22, 2006, through which the trustee confirmed that the proposal had been completely performed effective June 5, 2007. In the context of that proposal in bankruptcy, the appellant filed a claim of $50,000 and received a payment of $7,085.98.

[11] Ms. Lamarche stated that her company had sold its immovables and assets for $172,000 to Épicerie-Boucherie Claire Lamarche Inc., a company that belonged to her sister and her sister's spouse. Of that amount, $109,000 was paid in cash at the time of the sale, on May 26, 2007, and $63,000 was seayable in 63 equal and consecutive monthly payments of $1,000 starting the day of the fifth anniversary of the sale, that is, on May 5, 2012, to August 5, 2017, the date on which any balance would become due and payable. The purchase price balance of $63,000 would not bear interest, but any payment not made by the due date would bear interest at a rate of 12% per year. According to Ms. Lamarche, her company never received the amount of $63,000 because the immovable and movable property that was acquired by "Épicerie-Boucherie Claire Lamarche Inc." was sold by judicial sale on November 3, 2008.

[12] In the financial statements of Épicerie-Boucherie Lam-Bher Inc. for the fiscal years ending April 30, 2004, and April 30, 2003, the loan of $20,000 from the appellant in 1997 and the loan of $12,000 from the appellant in 2004, that is, $32,000 in total, are recorded as notes payable, without interest and without a

planned repayment method. Ms. Lamarche explained that the purpose of this accounting presentation was to satisfy a Caisse populaire requirement for granting loans.

[13] The appellant also testified at the hearing and specified that he waited until 2007 to claim the loss on his loans because the sale price balance for the assets of "Épicerie-Boucherie Lam-Bher Inc.", in the amount of $63,000 would have been sufficient to pay back all of said company's debts.

Analysis

[14] At the outset of the hearing, the respondent admitted that the appellant had made loans of $20,000 and $12,000 to "Épicerie-Boucherie Lam-Bher Inc.", but the respondent did not admit the other advances from the appellant because they came from an account held jointly by the appellant and his spouse. Despite the admission by the respondent of the $20,000 and $12,000 loans, the respondent disallowed the ABIL because of confusion surrounding the interest payable on those loans. The agreements of January 4, 1997, and January 15, 2014, which were submitted by the appellant, included interest whereas the financial statements of "Épicerie-Boucherie Lam-Bher Inc." indicated no interest for those loans. According to the respondent, those loans were not made by the appellant for the purpose of gaining or producing income from a business or property.

[15] The relevant sections of the Act for determining entitlement to an ABIL are as follows:

> Subdivision c – Taxable Capital Gains and Allowable Capital Losses
>
> SECTION 38: Taxable capital gain and allowable capital loss
>
> For the purposes of this Act:
>
> . . .
>
> > (*c*) a taxpayer's allowable business investment loss for a taxation year from the disposition of any property is 1/2 of the taxpayer's business investment loss for the year from the disposition of that property.
>
> SECTION 39: Meaning of capital gain and capital loss
>
> (1) For the purposes of this Act:

. . .

(*c*) a taxpayer's business investment loss for a taxation year from the disposition of any property is the amount, if any, by which the taxpayer's capital loss for the year from a disposition after 1977

(i) to which subsection 50(1) applies, or

(ii) to a person with whom the taxpayer was dealing at arm's length

of any property that is

(iii) a share of the capital stock of a small business corporation, or

(iv) a debt owing to the taxpayer by a Canadian-controlled private corporation (other than, where the taxpayer is a corporation, a debt owing to it by a corporation with which it does not deal at arm's length) that is

(A) a small business corporation,

(B) a bankrupt (within the meaning assigned by subsection 128(3)) that was a small business corporation at the time it last became a bankrupt, or

(C) a corporation referred to in section 6 of the Winding-up Act that was insolvent (within the meaning of that Act) and was a small business corporation at the time a winding-up order under that Act was made in respect of the corporation,

SECTION 40: General rules

(2) Limitations. Nothwithstanding subsection 40(1),

. . .

g) a taxpayer's loss, if any, from the disposition of a property . . . to the extent that it is

. . .

(ii) a loss from the disposition of a debt or other right to receive an amount, unless the debt or right, as the case may be, was acquired by the taxpayer for the purpose of gaining or producing income from a business or property (other than exempt income) or as consideration

> for the disposition of capital property to a person with whom the taxpayer was dealing at arm's length,
>
> SECTION 50: Debts established to be bad debts and shares of bankrupt corporation
>
> 50. (1) For the purposes of this subdivision, where
>
> (*a*) a debt owing to a taxpayer at the end of a taxation year (other than a debt owing to the taxpayer in respect of the disposition of personal-use property) is established by the taxpayer to have become a bad debt in the year, or
>
> (*b*) a share (other than a share received by a taxpayer as consideration in respect of the disposition of personal-use property) of the capital stock of a corporation is owned by the taxpayer at the end of a taxation year and
>
> (i) the corporation has during the year become a bankrupt,
>
> (ii) the corporation is a corporation referred to in section 6 of the Winding-up Act that is insolvent (within the meaning of that Act) and in respect of which a winding-up order under that Act has been made in the year, or
>
> (iii) at the end of the year,
>
> (A) the corporation is insolvent,
>
> (B) neither the corporation nor a corporation controlled by it carries on business,
>
> (C) the fair market value of the share is nil, and
>
> (D) it is reasonable to expect that the corporation will be dissolved or wound up and will not commence to carry on business
>
> and the taxpayer elects in the taxpayer's return of income for the year to have this subsection apply in respect of the debt or the share, as the case may be, the taxpayer shall be deemed to have disposed of the debt or the share, as the case may be, at the end of the year for proceeds equal to nil and to have reacquired it immediately after the end of the year at a cost equal to nil.

[16] For taxpayers to be entitled to an ABIL, taxpayers must first establish that they suffered, in a given taxation year, a capital loss from the disposition of

property, and the loss must be a particular kind of loss, that is, a business investment loss.

[17] A business investment loss is the amount, if any, by which the taxpayer's capital loss for the year from a disposition after 1977 to which subsection 50(1) of the Act applies, or a debt by a Canadian-controlled private corporation that is a small business corporation.

[18] Subsection 50(1) of the Act sets out, in particular, that where a debt owing to the taxpayer at the end of a given taxation year is established by the taxpayer to have become a bad debt in the year, and the taxpayer elects in the taxpayer's return of income to have this subsection apply in respect of the debt, the taxpayer is deemed to have disposed of the debt for proceeds equal to nil and to have reacquired it immediately after the end of the year at a cost equal to nil.

[19] To be entitled to a BIL under sections 38 and 39 of the Act, the appellant must demonstrate that he suffered a capital loss from the disposition of a property. Pursuant to section 50 of the Act, a taxpayer is deemed to have disposed of a debt owing to the taxpayer at the end of the year for proceeds equal to nil if that debt is established to have become a bad debt in the year. For section 50 to apply, the debt must have existed at the end of the taxpayer's taxation year, that is, on December 31, 2007, in this case.

[20] To determine whether the debt owed to the appellant by the company still existed on December 31, 2007, the Court must determine when the company was discharged from its liability to pay back the advances from the appellant following the proposal in bankruptcy.

[21] The *Bankruptcy and Insolvency Act* (BIA) is silent as to when a debtor is discharged from his or her liabilities when a proposal in bankruptcy is accepted by the creditors. There are two views on this, and they are stated in paragraphs 34 to 37 of my decision in *Jacques St-Hilaire v. Her Majesty the Queen*, 2014 TCC 336, which I shall reproduce here:

> [34] In bankruptcies, the BIA is clear: the bankrupt debtor is released once the discharge order has been made. As the bankruptcy provisions of the BIA are to supplement, by analogy, the provisions relating to proposals in bankruptcy, some authors argue that the time of the partial discharge of a debt and partial release of the debtor under a BIA proposal is the time of the trustee's discharge order or the time the trustee issues a certificate that the proposal has been fully performed. This theory was accepted by the Federal Court of Appeal in *Rita Congiu* and

9100-7146 Québec Inc. v. The Queen, 2014 FCA 73, where the Court cited the following excerpt from the decision of the Court of Appeal of Québec dated February 7, 2014, in *Rita Congiu c. L'Agence du Revenu du Québec*, 2014 QCCA 242:

> [TRANSLATION]
>
> [42] The proposal in bankruptcy of [Canada inc.] may have had the effect of deferring the date on which [Canada inc.'s] debt became due, but it has not eliminated the debt. . . .

[35] The other prevailing theory is that the date of the debtor's partial release and that of the partial discharge of the initial debt under a BIA proposal is the date a court ratifies the proposal after it has been accepted by the creditors. This theory is based on, among other things, the remarks of Jacques Deslauriers in "La faillite et l'insolvabilité au Québec," Montréal: Wilson & Lafleur, 2004, at page 132, in which he argues that the date a debt is settled under a proposal in bankruptcy is not the date the court orders the discharge of the trustee:

> [TRANSLATION]
>
> (ii) Discharge of the debtor's debts
>
> The proposal can release the debtor from his or her debts. A proposal stipulating the payment of a certain percentage of the debts (e.g., 30%) will discharge the debtor for the balance if the proposal is accepted (subsection 62(2) BIA). . . .

[36] In their work entitled "Bankruptcy and Insolvency Law of Canada," 3rd ed. (revised), Vol. 2, Toronto: Carswell, at page 2-166, L.W. Houlden and G.B. Morawetz take a view similar to that of the author Deslauriers:

> When a proposal is accepted by creditors and approved by the court, the debtor receives the same relief as he or she would receive from a discharge from bankruptcy, i.e., a release of all debts and liabilities to unsecured creditors, except those listed in s. 178 . . . .

[37] In *Réal Martel v. Her Majesty the Queen*, 2010 TCC 634, Justice Boyle considered both theories and chose to adopt the opinions of Houlden and Morawetz and of Deslauriers, relying on the decision rendered in *Anderson v. Canadian Imperial Bank of Commerce (1999)*, 11 C.B.R. (4th) 157, by the Ontario Court of Justice, which has jurisdiction to apply the BIA in that province.

[22] In this case, the requisite majority of the creditors duly accepted the proposal in bankruptcy amended at the meeting of the creditors on March 22, 2006, and, on April 19, 2006, the Superior Court of Quebec (Commercial Division) sanctioned

and ratified for all legal purposes the decisions made by the creditors at the meeting on March 22, 2006, and declared that the amended proposal in bankruptcy bound each and every creditor of the debtor/proposing party. Consequently, "Entreprise-Boucherie Lam-Bher Inc." was discharged from the remaining debts and liabilities to its unsecured creditors on April 19, 2006. The remainder of the unpaid debt owed to the appellant was struck under the terms of the proposal in bankruptcy and ceased to exist. The appellant thus disposed of his debt for tax purposes in 2006. At the end of the 2007 taxation year, the company did not owe any debt to the appellant.

[23] Because the debt owed to the appellant no longer existed on December 31, 2007, section 50 of the Act cannot apply, and the appellant is not entitled to the business investment loss for the year 2007.

[24] Furthermore, the appellant was not entitled to claim, in 2007, a business investment loss with respect to the debt owing to him by "Épicerie-Boucherie Lam-Bher Inc." as a Canadian-controlled private corporation that was a small business corporation because he disposed of his debt in 2006 and not in 2007, under the proposal in bankruptcy. At the end of the 2006 taxation year, only the balance of $7,085.98 was owing to the appellant under the proposal in bankruptcy.

[25] For these reasons, the appeal is dismissed.

Signed at Montréal, Canada, this 16th day of November 2015.

"Réal Favreau"

Favreau J.

Translation certified true
on this 28th day of December 2015
Janine Anderson, Translator

CITATION:	2015 TCC 281
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APPEARANCES:

Agent for the appellant:	Hélène Lamarche
Counsel for the respondent:	Simon Vincent

COUNSEL OF RECORD:

For the appellant:

Name:

Firm:

For the respondent: William F. Pentney
Deputy Attorney General of Canada
Ottawa, Canada