Docket: 2015-1026(IT)I

BETWEEN:

MARIE-PAULE D'AMOUR,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on October 7, 2016, at Montréal, Quebec

Before: The Honourable Justice Réal Favreau

Appearances:

For the appellant:	The appellant herself
Counsel for the respondent:	Marie-Claude Landry

JUDGMENT

The appeal from the reassessment made pursuant to the *Income Tax Act* dated November 3, 2008, respecting the 2005 taxation year is dismissed in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Canada, this 22nd day of January 2016.

"Réal Favreau"

Favreau J.

Translation certified true
on this 21st day of March 2016
Daniela Guglietta, Translator

Citation: 2016 TCC 18
Date: 20150122
Docket: 2015-1026(IT)I

BETWEEN:

MARIE-PAULE D'AMOUR,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

REASONS FOR JUDGMENT

Favreau J.

[1] This is an appeal under the informal procedure against a reassessment made under the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Suppl.), as amended, (the Act), dated November 3, 2008, in respect of the appellant's 2005 taxation year.

[2] Pursuant to the assessment dated November 3, 2008, the Minister of National Revenue (the Minister) disallowed the appellant's claim for an allowable business investment loss (ABIL) of $48,813, that is, 50% of a capital loss of $97,627.

[3] In making and confirming the reassessment, the Minister relied on the following assumptions of fact:

> [TRANSLATION]
>
> (a) Since March 20, 2002, the appellant is the sole owner of a building located at 121 Principale Street in St-Sauveur (the immovable);

(b) the rental income from the immovable declared by the appellant and assessed by the Minister for the year in issue is as follows:

Gross rental income	$18,000
Net rental income	$5,613

(c) since July 5, 2002, the appellant is the sole shareholder, secretary and treasurer of 9133-6503 Québec Inc. (hereinafter the company), whose fiscal year-end is February 28 of each year;

(d) the company's main activity was the operation of a restaurant located at 121 Principale Street in St-Sauveur;

(e) the restaurant was operated by the company until August 2003;

(f) as of August 2003, the appellant rented the immovable to 9132-1596 Québec Inc.;

(g) as of August 2003, the company was no longer in operation;

(h) on or about December 20, 2005, the appellant sold the immovable and gave all of the company's assets to 9132-1596 Québec Inc.;

(i) the capital gain from the disposition of the immovable declared by the appellant and assessed by the Minister is as follows:

Proceeds of disposition	$325,000
Less: adjusted cost base and expenditures	$233,292
Capital gain	$91,708
Taxable capital gain	**$45,854**

(j) the company was dissolved on December 5, 2006;

(k) in filing her tax return for the 2005 taxation year, the appellant claimed an ABIL of $48,813 ($97,627 x 50%);

(l) the appellant did not make advances to the company totalling $97,627.

[4] Ms. D'Amour testified at the hearing and provided information regarding the nature of the work performed to transform what used to be a convenience store that had been closed for six years into a four-star restaurant. She admitted all the assumptions of fact on which the Minister relied, except the assumptions regarding the proceeds of the disposition of the immovable located at 121 Principal Street in Saint-Sauveur (the immovable) which, according to her, were supposed to be $320,000 rather than $325,000 and regarding the advances totalling $97,627 that she allegedly made to 9133-6503 Québec Inc. (the company), which operated the restaurant. Ms. D'Amour's spouse was the restaurant's head chef.

[5] Ms. D'Amour acquired the immovable on March 20, 2002. It was an old building with a convenience store adjacent to the house. Access to the convenience store from inside was through the house's laundry room.

[6] On July 5, 2002, Ms. D'Amour incorporated the company "Restaurant Trattoria D'Amore Saint-Sauveur-Des-Monts Ltée" under Part 1A of Quebec's *Companies Act* which, on September 15, 2003, became the company following an amendment to its articles. The company's fiscal year-end was February 28 of each year and its main activity was the operation of the restaurant.

[7] The renovations were completed over the summer and the restaurant opened its doors on September 1, 2002. In her testimony, Ms. D'Amour stated that she paid the costs of the renovations from her personal bank accounts. Ms. D'Amour adduced in evidence the following documents:

- excerpts from her bank accounts with notes explaining what the amounts spent were used for;

- a list of expenditures incurred in 2002 for the restaurant including names of suppliers, amounts claimed by each of them, payment dates and amounts paid, with a copy of underlying invoices attached;

- the company's unaudited financial statements prepared by Marcel Dulude, a chartered accountant, namely, (i) an opening balance sheet as of September 1, 2002, showing capital totalling $88,203 ($51,422 for furniture and equipment and $36,726 for leasehold improvements) and an amount of $98,845 owing to the director without interest, or terms of

repayment; (ii) a balance sheet as of September 30, 2002, and (iii) complete financial statements as of February 28, 2003, showing capital of $85,440 and an amount of $97,627 owing to the director;

- the company's unaudited financial statements as of February 28, 2005 with comparable figures as of February 28, 2004, prepared by Les Entreprises Michel Lafond Enr., which indicate capital in the amount of $86,500 as the sole asset and an amount of $97,038 owing to the director as the sole liability. These financial statements indicate that the company has conducted no business over the year and has been inactive since February 28, 2003;

- the renovation permit dated July 18, 2002, from the municipality of the Village of Saint-Sauveur-Des-Monts sought by Ms. D'Amour for the authorization of work estimated at $100,000 and to be undertaken from July 22, 2002, to August 15, 2002.

[8] Unfortunately for the appellant, her spouse became ill and the restaurant was closed in August 2003. The company ceased operation and the appellant leased the immovable by notarial lease to 9132-1596 Québec Inc., a company owned by Luc Mannella. Said company continued to operate the restaurant. The lease in question was registered on September 11, 2003, but was not filed in evidence.

[9] Exasperated by numerous requests from the company lessee of the immovable and its shareholder to carry out repairs to the immovable, the appellant finally decided to sell the immovable on or about December 20, 2005, to the company "Gestion immobilière desma inc.," a company apparently affiliated with 9132-1596 Québec Inc. and controlled by Luc Mannella, and to transfer to it all of the company's assets. The notarial deed of sale dated December 20, 2005, was not entered into evidence but the sale price indicated in the land register is $325,000.

[10] Ms. D'Amour submits that the proceeds of disposition of the immovable were $320,000 rather than $325,000 because a few days before the sale the company and 9132-1596 Québec Inc. entered into a transaction within the meaning of the *Civil Code of Québec*, confirmed by the Court of Québec, under which the parties agreed to settle the dispute out of court. The substance of the dispute arose out of a promise between the parties to purchase the immovable for the amount of $325,000 subject to a structural inspection of the immovable commissioned by Luc Mannella. He asked for a $5,000 reduction in the selling price because support beams had to be cut to get a refrigerator into the basement.

[11] Pursuant to the transaction, 9132-1596 Québec Inc. agreed, *inter alia*, to pay $320,000 in trust to a notary to be applied against the purchase price of the immovable, and the money could not be released until the deed of sale was published and filed in the land register without prejudicial entry.

[12] Despite the fact that said transaction occurred on December 16, 2005, the notarial deed of sale appears to have specified that the selling price of the immovable was $325,000 based on the entry in the land register entered into evidence by the respondent.

[13] The appellant filed her income tax return for the 2005 taxation year reporting the following:

(a) Gross rental income of $18,000 and net rental income of $5,613;

(b) a capital gain from the disposition of the immovable in the amount of $91,708, namely, proceeds of disposition of $325,000 less an adjusted cost base and selling expenses totalling $233,292;

(c) a business investment loss in the amount of $48,803, that is, 50% of the advances made to the company totalling $97,627.

[14] On December 5, 2006, the company was dissolved. The appellant confirmed in her testimony that the company's income tax returns for the 2002 to 2005 taxation years were not were not filed with the Canada Revenue Agency (the CRA).

Relevant Statutory Provisions

[15] The relevant provisions 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

Notwithstanding 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,

is nil.

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.
>
> *248(1)* ***small business corporation***, at any particular time, means, subject to subsection 110.6(15), a particular corporation that is a Canadian-controlled private corporation all or substantially all of the fair market value of the assets of which at that time is attributable to assets that are
>
> (*a*) used principally in an active business carried on primarily in Canada by the particular corporation or by a corporation related to it,
>
> (*b*) shares of the capital stock or indebtedness of one or more small business corporations that are at that time connected with the particular corporation (within the meaning of subsection 186(4) on the assumption that the small business corporation is at that time a ***payer corporation*** within the meaning of that subsection), or
>
> (*c*) assets described in paragraphs (a) and (b),
>
> including, for the purpose of paragraph 39(1)(c), a corporation that was at any time in the 12 months preceding that time a small business corporation, and, for the purpose of this definition, the fair market value of a net income stabilization account shall be deemed to be nil; (*société exploitant une petite entreprise*)

Analysis

[16] The respondent submits that there was no debt owing to the appellant by the company in the amount of $97,627. I respectfully disagree with this interpretation of the facts. In my view, the appellant demonstrated with supporting documentary evidence that she did incur and pay expenses for the renovations and fit-up of the restaurant. That is not where the problem lies.

[17] Rather, the problem resides in the fact that the appellant did not dispose of her debt in 2005. The debt continued to exist until the company was dissolved in 2006. As a result, the appellant could not be entitled to an ABIL in 2005.

[18] Since the appellant did not enter into evidence her income tax return for the 2005 taxation year, she was unable to demonstrate that she elected to apply the provisions of subsection 50(1) of the Act to a debt that has become a bad debt in the year. Said election probably should have been made in respect of the 2003 taxation year following the closure of the restaurant.

[19] Even if the appellant were considered to have disposed of her debt in 2005, the appellant would not have been able to claim an ABIL because the company was not, in 2005 and 2004, a small business corporation; the company ceased to carry on business effective August 2003.

[20] As of August 2003, all or substantially all of the fair market value of the company's assets were not attributable to assets used principally in an active business carried on by the company itself or by a corporation related to it.

[21] Finally, it should be noted that the debt owing by the company was not acquired for the purpose of gaining or producing income from a business or property. As indicated in the company's opening balance sheet as of September 1, 2002, and financial statements as of February 28, 2003, the amount owed to the director did not include interest or terms of repayment. The appellant did not present evidence to the contrary. In such a case, paragraph 40(2)(*g*) of the Act deems a loss from the disposition of a property to be nil.

[22] As for the proceeds of disposition of the immovable, it should be noted that the appellant herself reported the capital gain realized on the sale of the immovable using proceeds of disposition of $325,000. The appellant could not be unaware that she only received $320,000 pursuant to the transaction entered into a few days before the sale.

[23] The transaction, which was confirmed by the Court of Québec, did not specify what the immovable had to be sold for, but did specify the payment terms for the amount of $320,000 to which the appellant was entitled and the steps required for the parties to grant each other full and final acquittance.

[24] Without the benefit of having seen the notarial deed of sale of the immovable, I can only assume that the sale was made at the price of $325,000 but that the appellant only received in cash the amount of $320,000. The $5,000 shortfall must have been applied to compensate the purchaser or persons related to the purchaser for the reduction in value of the immovable that occurred as the direct result of the structural inspection of the immovable.

[25] In any event, the notarial deed of sale is an authentic act that is proof of its contents. The only way to challenge the validity of an authentic act is by improbation. None of this was done by the appellant. Consequently, the appellant cannot contradict what is set out in the deed of sale. The proceeds of disposition of the immovable must therefore be $325,000.

[26] For these reasons, the appellant's appeal is dismissed.

Signed at Ottawa, Canada, this 22nd day of January 2016.

"Réal Favreau"

Favreau J.

Translation certified true
on this 21st day of March 2016
Daniela Guglietta, Translator

CITATION:	2016 TCC 18
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PLACE OF HEARING:	Montréal, Quebec
DATE OF HEARING:	October 7, 2015
REASONS FOR JUDGMENT BY:	The Honourable Justice Réal Favreau
DATE OF JUDGMENT:	January 22, 2016

APPEARANCES:

For the appellant:	The appellant herself
Counsel for the respondent:	Marie-Claude Landry

COUNSEL OF RECORD:

For the appellant:

Name:

Firm:

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