Docket: 2017-221(IT)G

BETWEEN:

JEREMY LEONARD,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

BETWEEN:

Docket: 2017-219(IT)G

CAROL TENNEY,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeals heard on June 28, 2019, at Winnipeg, Manitoba
and on October 3, 2019 at Ottawa, Ontario; and Written Submissions
received on July 15, 2020

Before: The Honourable Justice Don R. Sommerfeldt

Appearances:

Counsel for the Appellants:	Jeff D. Pniowsky, Matthew Dalloo
Counsel for the Respondent:	David Silver, David Grohmueller

JUDGMENT

The Appeals of both Appellants are (subject to paragraph 119 of the accompanying Reasons) allowed, with costs, and the reassessments issued by the Minister of National Revenue (the "Minister") to both Appellants are referred back

to the Minister for reconsideration and reassessment on the basis that, in 2011, Jeremy Leonard sustained a non-capital loss in the amount of $826,426.

If the Parties are unable to reach an agreement in respect of costs within 30 days of the date of this Judgment, the Appellants may, within the ensuing 30 days thereafter, file a written submission on costs, and the Respondent shall thereafter have yet a further 30 days to file a written response. Any such submissions shall be limited to five pages in length. If, within the applicable time limits, the Parties do not advise the Court that they have reached an agreement and no submissions are received from the Parties, one set of costs (adjusted to recognize the need for a separate Notice of Appeal for each Appellant), in accordance with the Tariff, shall be awarded to the Appellants (to be apportioned between them as they so determine).

Signed at Edmonton, Alberta, this 30th day of April 2021.

"Don R. Sommerfeldt"

Sommerfeldt J.

Citation: 2021 TCC 33
Date: 20210430
Docket: 2017-221(IT)G

BETWEEN:

JEREMY LEONARD,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

Docket: 2017-219(IT)G

BETWEEN:

CAROL TENNEY,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Sommerfeldt J.

I. INTRODUCTION

[1] These Reasons pertain primarily to the Appeals instituted by Jeremy Leonard in respect of reassessments (the "Reassessments") issued to him by the Canada Revenue Agency (the "CRA") on behalf of the Minister of National Revenue (the "Minister") in respect of the 2011, 2012, 2013 and 2014 taxation years. The 2011 Reassessment disallowed a claimed non-capital loss (the "Loss") in the amount of $1,472,006,[1] which Mr. Leonard had reported on his income tax

[1] The Loss, according to Mr. Leonard, was derived from the transactions that are described below and that relate to various loan transactions and sales transactions that were denominated in US currency. In reporting those transactions for Canadian income tax purposes, Mr. Leonard treated the Canada-US exchange rate as being at par; see Exhibit AR-1, vol. 1, tab 4, p. 54. It appears that the Crown does not disagree with the "at-par" exchange rate used by Mr. Leonard. In these Reasons I will use the same amounts that

return for 2011. The Reassessments for 2012, 2013 and 2014 disallowed the carry-forward of portions of the Loss.

[2] Ms. Tenney is the spouse of Mr. Leonard. On her 2011 income tax return she had claimed a spousal amount in respect of Mr. Leonard as well as a transfer of unused personal credits from Mr. Leonard to her. In addition, in that income tax return, she indicated that the amount of the family income, for the purposes of the Canada Child Tax Benefit (the "CCTB") was $45,942. By reason of the disallowance of the Loss, which Mr. Leonard had reported for 2011, the CRA recalculated the family income as $496,733, which meant that Ms. Tenney no longer qualified for the CCTB. At the outset of the hearing, and again when making oral submissions, counsel for the Parties acknowledged that the determination of the outcome of Mr. Leonard's Appeals will automatically determine the outcome of Ms. Tenney's Appeal.

II. **ISSUES**

[3] In his Notice of Appeal, Mr. Leonard alleged that, during the relevant taxation years, he carried on the business of acquiring mortgages and lending money, and that the Loss was realized in the course of that business. Alternatively, Mr. Leonard alleged that any transaction giving rise to the Loss was an adventure in the nature of trade.[2]

[4] In his opening statement at the hearing, counsel for Mr. Leonard advised the Court that Mr. Leonard was, for the purposes of these Appeals, abandoning the argument that the Loss arose in the course of a business of lending money. Counsel also advised that the only position being advanced by Mr. Leonard at the hearing

---

were used in the documents and in the oral evidence given at the hearing. To the extent that those amounts pertain to transactions that occurred in Hawaii, it must be remembered that the amounts are actually denominated in US currency (which the Parties apparently consider to have been equivalent to Canadian currency at the time of those transactions).

[2] Mr. Leonard's Notice of Appeal uses the term *adventure in the nature of trade*. The term used in the ITA (as defined in paragraph 6 and footnote 4) is *adventure or concern in the nature of trade*. For instance, see subsection 10(1.01) and the definition of "business" in subsection 248(1) of the ITA (although the marginal note for subsection 10(1.01) uses the abbreviated term *adventures in the nature of trade*). For brevity, in these Reasons I too will use the abbreviated term *adventure in the nature of trade*, but it should be understood that, in so doing, I am referring to the actual term, i.e., *adventure or concern in the nature of trade*.

was that the transaction in question (the "Transaction") was an adventure in the nature of trade.[3]

[5] Accordingly, as listed in the order in which they will be considered, the fundamental issues in respect of these Appeals are:

(a) If there was a loss, was it a capital loss or a loss incurred in respect of an adventure in the nature of trade (i.e., a non-capital loss)?

(b) Was there a loss, and, if so, did Mr. Leonard realize the Loss in 2011, and what was the amount of the Loss?

III. **FACTS**

[6] Mr. Leonard is an entrepreneur. He is a resident of Canada for the purposes of the *Income Tax Act* (the "ITA").[4] He has homes in both Alberta and Hawaii. Through corporate entities, he carries on business in Alberta, Hawaii and Brazil.

[7] In approximately 2004 or 2005, Mr. Leonard became acquainted with Brian Anderson, who was a real estate developer carrying on business in Hawaii (and perhaps elsewhere). From time to time, over the course of the next five or so years, Mr. Leonard loaned money to Mr. Anderson and may have made equity investments in some of Mr. Anderson's developments. Sometime before 2009, Mr. Anderson acquired two adjoining lots (the "Lots") in the Kukio community in Hawaii. One of the Lots, designated as "Lot B-3," had a house constructed on it. The other Lot, which was designated as "Lot B-2," was undeveloped. Mr. Leonard described Lot B-2 as bare lava rock. Both Lots were subject to mortgages to secure debts owed by Mr. Anderson to the Central Pacific Bank. The mortgage (the "Mortgage") in respect of Lot B-2 secured a debt (the "Debt") that was evidenced by a promissory note (the "Note")[5] and that related to a loan in the amount $1,500,000, which Mr. Anderson had borrowed from City Bank on December 20,

---

3 *Transcript*, vol. 1, p. 14, line 21 to p. 15, line 4. See also *Transcript*, vol. 1, p. 52, lines 10-22. In these Reasons, I use the term "Transaction" to refer to all of Mr. Leonard's dealings with the Mortgage, the Note and the Debt (as those three terms are defined in paragraph 7 below).

4 *Income Tax Act*, RSC 1985, c. 1 (5th Supplement), as amended.

5 Exhibit AR-1, vol.1, tab 10, p. 136-138.

2004. Sometime thereafter, City Bank merged into Central Pacific Bank (the "Bank").[6]

[8] The economic downturn of 2008 had a serious impact on Mr. Anderson, who apparently was heavily leveraged. Mr. Leonard stated that he understood that Mr. Anderson had judgments against him aggregating approximately $40,000,000. It was Mr. Leonard's understanding that Mr. Anderson was unable to repay all of his debts.

[9] As Mr. Anderson was in default in respect of the Debt secured by the Mortgage on Lot B-2, the Bank commenced foreclosure proceedings on April 6, 2009 in respect of the Mortgage. The Bank did not commence foreclosure proceedings in respect of the mortgage on Lot B-3.[7]

[10] After defaulting in April 2007 in the repayment of a $1,500,000 loan that Mr. Leonard had made to Mr. Anderson in December 2006,[8] Mr. Anderson approached Mr. Leonard with a deal whereby Mr. Leonard could obtain the Lots at a discount, as a means of making amends for Mr. Anderson's failure to repay the 2006 loan.[9] Mr. Leonard subsequently contacted the Bank to express an interest in acquiring the Lots. He then negotiated an arrangement with the Bank, pursuant to which it was arranged that he would, as he thought, acquire both Lots at a price of $5,700,000, using funds to be loaned to him by the Bank. It appears that, for its purposes, the Bank allocated $4,400,000 of the total price to Lot B-3 (i.e., the Lot with a house constructed on it) and $1,300,000 to the Mortgage, the Note and the Debt (which pertained to Lot B-2).[10] Mr. Leonard understood that the amount of the Debt was originally $1,500,000, but the price payable by Mr. Leonard to the

---

6 See Exhibit AR-1, vol. 1, tab 4(2), p. 63, and tab 10, p. 136. The transactional and foreclosure documents that were put into evidence indicate that the Debt was owed, and the Mortgage was granted, by Brian Anderson, individually and as trustee of the Brian A. Anderson Revocable Living Trust, and by Joan Anderson, individually and as trustee of the Joan G. Anderson Revocable Living Trust. For brevity and convenience, I will refer collectively to the debtors and mortgagors simply as "Mr. Anderson" (as was generally done by counsel and Mr. Leonard during the hearing).

7 *Transcript*, vol. 1, p. 68, lines 7-10.

8 This was a different loan from that which was lent by City Bank to Mr. Anderson on December 20, 2004.

9 *Transcript*, vol. 1, p. 59, line 16 to p. 61, line 20.

10 Exhibit AR-1, vol. 1, tab 2, p. 15 (handwritten note).

Bank in respect of the Mortgage, the Note and the Debt was, apparently during negotiations with Mr. Leonard, reduced by the Bank to $1,300,000.[11]

[11] Subsequently, after the Bank and Mr. Leonard had settled on the terms of their arrangement, a meeting was scheduled among Mr. Leonard, Mr. Anderson and the Bank's representative. At that meeting, Mr. Anderson expressed displeasure with the price put on the two Lots. He was of the view that the price should have been greater.[12]

[12] The transaction among Mr. Leonard, Mr. Anderson and the Bank was documented in such a manner that Mr. Leonard acquired Lot B-3 from Mr. Anderson, and he acquired the Mortgage, the Note and the Debt from the Bank. The key transactional document relating to the transaction between Mr. Leonard and the Bank was an Assignment of Mortgage, Security Agreement and Financing Statement (the "Assignment"), dated effective as of June 24, 2009.[13] The significant operative portions of the Assignment read as follows:

> KNOW ALL MEN BY THESE PRESENTS:
>
> That the CENTRAL PACIFIC BANK … hereinafter called the "Assignor", in consideration of the sum of TEN DOLLARS ($10.00) and other good and valuable consideration to it paid by JEREMY PAUL LEONARD, … hereinafter called the "Assignee", the receipt whereof is hereby acknowledged, does hereby sell, assign, transfer, set over and deliver unto the Assignee, its successors and assigns, the mortgage hereinafter described, together with the promissory note and the debts thereby secured, and together also with all the right, title and interest of the Assignor in and to the property more particularly described in said mortgage, to-wit:
>
> That certain Mortgage, Security Agreement and Financing Statement dated December 20, 2004, made by BRIAN A. ANDERSON, as Trustee of the Brian A. Anderson Revocable Living Trust dated September 18, 2001, and JOAN G. ANDERSON, as Trustee of the Joan G. Anderson Revocable Living Trust

---

11 Exhibit AR-1, vol. 1, tab 2, p. 11 (handwritten note) & 13-14. On page 2 of the Assignment (Exhibit AR-1, vol. 1, tab 2, p. 11), as defined in paragraph 12 below, there is a statement indicating that the Mortgage secured the principal amount of $1,500,000, and next to that statement is a handwritten annotation that reads "see Note." At the bottom of that page there is another annotation that reads "Note: In final negotiations with the bank this was reduced to $1,300,000.00." See also *Transcript*, vol. 1, p. 64, line 26 to p. 65, line 1; and p. 65, lines 27-28.

12 *Transcript*, vol. 1, p. 105, lines 23-27.

13 Exhibit AR-1, vol. 1, tab 2, p. 10-12.

> dated September 18, 2001, as Mortgagor, in favor of City Bank, whose successor in merger is CENTRAL PACIFIC BANK, as Mortgagee, securing the principal amount of $1,500,000.00, and recorded in the Bureau of Conveyances of the State of Hawaii as Document No. 2004-264058.
>
> TO HAVE AND TO HOLD the same unto the Assignee, its successors and assigns, forever.
>
> This assignment is without recourse, except as to the warranties hereinafter provided. The Assignor does hereby covenant to and with the Assignee, its successors and assigns, that the Assignor is the lawful owner and holder of the above-mentioned promissory note and mortgage; and that the Assignor has good right to sell, transfer and assign the same as aforesaid.[14]

It is interesting that, in the warranties set out in the last paragraph quoted above, reference is made only to the Note and the Mortgage, but not to the Debt.

[13] To finance the purchase of Lot B-3 from Mr. Anderson and the purchase of the Mortgage, the Note and the Debt from the Bank, Mr. Leonard borrowed $5,700,000 from the Bank, pursuant to a Term Loan Agreement dated June 24, 2009.[15] That agreement did not allocate the $5,700,000 among Lot B-3, the Mortgage, the Note and the Debt.[16] The Final Buyer Statement issued by the escrow agent, Title Guaranty Escrow Services, Inc., on June 28, 2009 in respect of the sale of Lot B-3 to Mr. Leonard (which closed on June 26, 2009), shows that the price was $4,400,000.[17] As it is my understanding that Mr. Leonard used only borrowed money to purchase Lot B-3, the Mortgage, the Note and the Debt, it follows that the amount that he paid to the Bank for the Mortgage, the Note and the Debt was $1,300,000 (i.e., $5,700,000 − $4,400,000). This is consistent with subsection 4.15 of the Term Loan Agreement between the Bank and Mr. Leonard, which provided that, if Lot B-2 were to be sold to a third party as a result of the foreclosure auction, Mr. Leonard was required to make a principal payment to the Bank in an amount equal to the proceeds of the foreclosure auction up to a

---

14 *Ibid*, p. 10-11. As a copy of the Mortgage was not put into evidence, it is not altogether clear whether the phrase *Mortgage, Security Agreement and Financing Statement* referred to a single document or to three separate documents. However, a Memorandum in Support of Motion (Exhibit AR-1, vol. 1, tab 4(2), p. 63) states, "The Note is secured by that certain Mortgage, Security Agreement and Financing Statement dated December 20, 2004 (hereafter "Mortgage") …," which causes me to think that the Mortgage, Security Agreement and Financing Statement was a single document.

15 Exhibit AR-1, vol. 3, tab 50, p. 861.

16 *Transcript*, vol. 1, p. 74, lines 10-14; and p. 149, line 4 to p. 150, line 4.

17 Exhibit AR-1, vol. 2, tab 22, p. 555.

maximum amount of $1,300,000.[18] The price allocation of $1,300,000 for the Mortgage, the Note and the Debt is also consistent with the handwritten note at the bottom of the second page of the Assignment granted by the Bank to Mr. Leonard on June 24, 2009,[19] with the handwritten note at the bottom of a Loan Statement issued by the Bank to Mr. Leonard showing a payment due date of July 25, 2009,[20] and with an undated table showing the original amounts of two loans, described as Loan #1 and Loan #2, as being $1,300,000 and $4,400,000 respectively (for a total of $5,700,000).[21]

[14] Mr. Leonard stated that he acquired the Debt at a discount from the Bank.[22] However, the amount of the discount is not readily ascertainable in a straightforward manner. In a letter dated July 31, 2015, which was attached to Mr. Leonard's Notice of Objection,[23] and in a letter dated August 24, 2016,[24] both of which were written by Mr. Leonard's accountants to the CRA, those accountants stated that, on June 24, 2009, Mr. Leonard purchased the Note and the Mortgage for a price of $1,487,551. In their letter of August 24, 2016, the accountants also stated that the amount owing under the Note on June 24, 2009 was US$1,606,528.65. To substantiate the amount paid for the Mortgage and the Note, the accountants referred to a particular document that accompanied the letter of July 31, 2015. That document was a Loan Modification Agreement, dated June 29,

---

18 Exhibit AR-1, vol. 3, tab 50, p. 871.

19 Exhibit AR-1, vol. 1, tab 2, p. 11. See footnote 11 above.

20 Exhibit AR-1, vol. 1, tab 2, p. 15. The handwritten note at the bottom of the particular Loan Statement begins with the words "Made up of 2 purchases," below which is a column of three amounts, the first of which is $4,400,000 (which pertains to the purchase of Lot B-3), the second of which is $1,300,000 (which is described as "CPB [presumably Central Pacific Bank] / B. Anderson mortgage"), and the third of which is $5,700,000 (being the total of the first two amounts).

21 Exhibit AR-1, vol. 1, tab 2, p. 14. I do not put any significant weight on this document, as it is in a format similar to, and seems likely to have the same unknown authorship as, three other tables that were entered as Exhibit R-1 for identification, as Mr. Leonard did not know with certainty who had drafted those tables, although he thinks that they were likely drafted by his US lawyer or his Canadian accountants. See *Transcript*, vol. 1, p. 97, line 4 to p. 100, line 19.

22 *Transcript*, vol. 1, p. 40, lines 26-28; p. 61, lines 12-20; p. 64, lines 12-15; and p. 64, line 21 to p. 65, line 18. While Mr. Leonard testified that he acquired the Debt at a discount, he did not provide any specific evidence expressly stating the precise amount that he paid for the Debt or calculating the amount of the discount at which he acquired the Debt.

23 Exhibit AR-1, vol. 1, tab 4, p. 53. In this letter the amount is shown as $1,487,551.

24 Exhibit AR-1, vol. 1, tab 11, p. 152. In this letter the amount is shown as US$1,487,551.03. Although the Crown has admitted that the letter is an authentic document, it has not admitted the truth of the contents of the letter.

2010, among the Bank, Mr. Leonard and Pacific Pump & Power, Inc. (which was one of Mr. Leonard's corporations).[25] In actuality, that document stated that, as of June 29, 2010, Mr. Leonard was indebted to the Bank in the principal amount $1,487,551.03, but the document said nothing about the amount paid by Mr. Leonard to acquire the Mortgage and the Note.

[15] As indicated, in the above-mentioned letter of August 24, 2016, from Mr. Leonard's accountants to the CRA, the accountants stated that the amount owing under the terms of the Note when Mr. Leonard acquired the Mortgage and the Note (i.e., June 24, 2009) was US$1,606,528.65.[26] I think that this amount is derived from a table on the fourth page of a Memorandum in Support of Motion, dated October 15, 2009 and filed by Mr. Leonard's attorneys with the Circuit Court of the First Circuit of the State of Hawaii (the "Circuit Court"), in respect of the foreclosure proceedings against Mr. Anderson.[27] That table shows that the unpaid principal amount of the Debt was $1,497,657.53,[28] with interest from an unspecified date to June 24, 2009 in the amount of $108,871.12, resulting in a total of $1,606,528.65.[29]

[16] To summarize, the above-mentioned documents indicate that, on June 24, 2009, Mr. Leonard acquired the Mortgage, the Note and the Debt from the Bank at a discount of $306,528.65 (i.e., $1,606,528.65 − $1,300,000.00).

[17] After acquiring the Mortgage, the Note and the Debt from the Bank, Mr. Leonard did not attempt to sell or assign the Mortgage, the Note or the Debt to anyone else.[30]

[18] Given that he had acquired the Mortgage, the Note and the Debt at a discount, it seems that, notwithstanding that he thought that ultimately he would likely acquire Lot B-2 through the foreclosure process, Mr. Leonard was also

---

25 Exhibit AR-1, vol. 1, tab 4(1), p. 56. Although she was not a party described in the opening paragraph of the Loan Modification Agreement, Ms. Tenney signed that Agreement as a mortgagor.

26 Exhibit AR-1, vol. 1, tab 11, p. 152.

27 Exhibit AR-1, vol. 1, tab 4(2), p. 64.

28 See also the Third Note Modification Agreement, dated June 28, 2007, between Mr. Anderson and the Bank (Exhibit AR-1, vol. 2, tab 21, p. 549); and Working Paper 1000, dated February 3, 2015, attached to the CRA's letter of February 20, 2015 to Mr. Leonard (Exhibit AR-1, vol. 2, tab 17, p. 466).

29 The table also shows two other amounts that are not relevant here.

30 *Transcript*, vol. 1, p. 85, lines 13-15; and p. 92, line 9 to p. 93, line 23.

aware of the possibility that, in the ensuing judicial sale, someone might bid enough for Lot B-2 to result in the Debt being repaid in full, resulting in a profit for him.[31]

[19] Mr. Leonard said that, in entering into the foregoing arrangement to acquire Lot B-3 from Mr. Anderson and the Mortgage, the Note and the Debt from the Bank, he understood that the actual fair market value of the Lots was greater than the amount that he had paid to acquire Lot B-3, the Mortgage, the Note and the Debt. Therefore, as another possibility, he anticipated that he would be able to realize a profit by acquiring Lot B-3 by purchase and Lot B-2 by foreclosure, and then reselling the Lots.[32]

[20] After completing the transactions to acquire Lot B-3, the Mortgage, the Note and the Debt, Mr. Leonard was surprised to realize that his ability to sell Lot B-2 would be delayed until such time as the foreclosure proceedings came to a formal conclusion. In Hawaii, this required the holding of a judicial sale, which was to be conducted by public auction.

[21] On October 7, 2009, Mr. Leonard was substituted as the real party in interest in the foreclosure.[33] On October 15, 2009, a decree of foreclosure was filed in the Circuit Court.[34] However, it was not until mid-2011 that the judicial sale was completed.

[22] The judicial sale occurred by means of a public auction near the flagpole in front of the local courthouse. The date of the auction was not put into evidence; however, it seems that it would have been sometime after October 15, 2009 (which was the date when the Decree of Foreclosure was filed) and January 3, 2011 (which was the date of filing an Order granting Mr. Leonard's Motion for Confirmation of Sale, Allowance of Costs, Commissions and Fees and Directing Conveyance, Writ of Possession and Deficiency Judgment).[35] Mr. Leonard attended the auction. He stated that approximately 12 other people were also there. When the bidding opened, Mr. Leonard was surprised that no one bid in respect of

---

31 *Transcript*, vol. 1, p. 42, lines 9-23.

32 *Transcript*, vol. 1, p. 41, lines 6-7, 9-14 and 17-21; p. 44, lines 7-9; p. 62, lines 14-15; p. 63, lines 23-27; p. 69, lines 4-7; and p. 71, lines 5-7.

33 Exhibit AR-1, vol. 1, tab 4(2), p. 62, fn. 1.

34 A copy of the decree of foreclosure was not put into evidence. However, references to the decree of foreclosure are found in Exhibit AR-1, vol. 2, tab 27, p. 564; vol. 3, tab 48, p. 829; and tab 49, p. 839.

35 Exhibit AR-1, vol. 2, tab 27, p. 563-565; and vol. 3, tab 49, p. 839-840.

Lot B-2. He decided to start the bidding. In determining how much to bid, he testified that he was aware at the time of the auction that no property in Kukio had previously sold for anything less than $1,000,000.[36] However, he did not have that much liquidity; therefore, he made an opening bid of $500,000. To his surprise, no one else bid at the auction, with the result that Lot B-2 was sold to him for $500,000.[37] The judicial sale closed, and title to Lot B-2 was transferred to Mr. Leonard, effective as of June 20, 2011.[38]

[23] While Mr. Leonard was testifying, it became apparent that he did not have a proper understanding of the judicial sale process. In his testimony, he stated that, if someone else at the auction had bid $500,001, he would not have made an additional bid, because he did not have sufficient funds to pay anything more than $500,000 for the property. It appears that he was not aware that, if he were the successful bidder, whatever amount he might pay for Lot B-2 (less expenses, and limited by the outstanding amount of the Debt) would come back to him as the holder of the Mortgage, the Note and the Debt.

[24] A second misunderstanding that Mr. Leonard had was that he expected and hoped that someone would bid approximately $2,200,000 for Lot B-2, as he testified that he understood that the entire amount paid by a third party for Lot B-2 would go to him. He was not aware that, if anyone had paid more than $1,972,252.63 (i.e., the amount payable in respect of the Debt on June 20, 2011),[39] the excess would have been paid to Mr. Anderson.

[25] After the judicial sale, Mr. Leonard was in shock.[40] He testified that he was aware that he owed $5,700,000 to the Bank and he had expected to net approximately $2,200,000 from the judicial sale.

[26] Mr. Leonard realized that, in order to repay the Bank, it would be necessary for him to sell Lot B-2 as soon as possible. Accordingly, he met with Carrie

---

36 *Transcript*, vol. 1, p. 42, lines 14-17; and p. 88, lines 9-10. I think that the word *before* on p. 88, line 10 should be *below*, or the word *before* should be followed by the word *below*.

37 *Transcript*, vol. 1, p. 41, line 23 to p. 42, line 28.

38 Exhibit AR-1, vol. 1, tab 4(6), p. 107; and vol. 3, tab 49, p. 838-842.

39 Exhibit AR-1, vol. 2, tab 30, p. 578.

40 *Transcript*, vol. 1, p. 42, lines 26-28; and p. 83, lines 15-16.

Nicholson, a prominent and successful real estate agent in Hawaii, and arranged to have Lot B-2 listed for sale.[41]

[27] Lot B-2 did not sell. Eventually the listing expired, whereupon Mr. Leonard relisted the property.[42] In 2015, in order to reduce the monthly association fees that he was paying for property maintenance, Mr. Leonard arranged to have Lots B-2 and B-3 combined.[43] As of the commencement of the hearing, Lot B-2 (now combined with Lot B-3) had still not been sold.

[28] As part of the foreclosure proceedings, a deficiency judgment (the "Deficiency Judgment"), in the amount of $1,472,006.44, was filed in the Circuit Court, apparently on or after May 16, 2011, in favour of Mr. Leonard against Mr.

---

41 *Transcript*, vol. 1, p. 43, lines 2-4. Mr. Pniowsky (counsel for Mr. Leonard) apparently was of the understanding a few weeks before the commencement of the hearing that the Crown did not accept that Mr. Leonard had listed Lot B-2 for sale. Mr. Pniowsky suggested to Mr. Silver (counsel for the Crown) that they telephone Ms. Nicholson and have her corroborate that Lot B-2 had been listed for sale. Mr. Silver (as was his right) declined to participate in a telephone conversation with Ms. Nicholson. Accordingly, on June 14, 2019 (two weeks before the scheduled commencement of the hearing), Mr. Pniowsky filed a notice of motion and supporting affidavit with the Court, requesting an adjournment and an order to take the commission evidence in Hawaii of Ms. Nicholson. The Chief Justice denied the request for the adjournment and directed that the motion be heard at the commencement of the hearing. At the commencement of the hearing, Mr. Pniowsky stated that he wanted to hold the motion in suspension until after Mr. Leonard had testified. After Mr. Leonard's testimony, I heard the motion. The notice of motion indicated that Ms. Nicholson's testimony was required only to prove that Lot B-2 had been listed for sale. During his direct examination, Mr. Leonard testified that he had arranged for Lot B-2 to be listed for sale. During cross-examination, Mr. Silver did not ask Mr. Leonard any questions about the listing. During the hearing of the motion, Mr. Silver stated that he was not disputing that Lot B-2 had been listed for sale. Accordingly, I advised Mr. Pniowsky that I was making a finding of fact that Lot B-2 had been listed for sale, such that there was no need to obtain the corroborating evidence of Ms. Nicholson to the same effect. The jurisprudence has set out four criteria to be met by a party seeking commission evidence (see *Sackman v. The Queen*, 2011 TCC 492, ¶7; *GlaxoSmithKline v. The Queen*, 2005 TCC 621, ¶12; and *MNR v. Javelin Foundries & Machine Works Ltd.*, [1978] CTC 597, 78 DTC 6408 (FCTD), ¶13). The second criterion is that there be an issue that the Court should try. As I had determined, as a finding of fact, that Lot B-2 had been listed for sale, there was no longer an issue for the Court to try in respect of this point. Therefore, I dismissed the motion, with costs in the cause.

42 While there was no admissible evidence in this regard, it is my understanding that this was done strategically in order to restart the count of the number of days, during the current listing, that Lot B-2 had been listed for sale.

43 *Transcript*, vol. 1, p. 43, vol. 1, lines 6-19; and Exhibit AR-1, vol. 3, tab 48, p. 822.

Anderson.[44] Mr. Leonard testified that he has not recovered anything in respect of the Deficiency Judgment, although he never expected to, given the extent of the numerous debts owed by Mr. Anderson to a multitude of creditors. During cross-examination, Mr. Leonard stated that he has not forgiven the Debt, at least in writing. He did not explain what he meant by that qualification. In other words, I was left wondering whether he had orally forgiven the Debt, but there was no evidence in this regard.

IV. **POSITIONS OF THE PARTIES**

A. Mr. Leonard

[29] It is the position of Mr. Leonard that, in his dealings with the Mortgage, the Note, the Debt and Lot B-2, he was participating in an adventure in the nature of trade.[45] His counsel asserted that Mr. Leonard bought the Mortgage, the Note and the Debt for $1,487,551,[46] thinking that "lots of people were going to bid on" Lot B-2 at the auction and that he would make a profit, given that the outstanding amount of the Debt (i.e., principal and accrued interest) was greater than the amount that he had paid for the Mortgage, the Note and the Debt.[47] As it turned out, no one (other than himself) bid for Lot B-2, with the result that, in his view, in 2011 he sustained the Loss in the amount (as calculated by his accountants) of $1,472,006.[48]

---

44 *Transcript*, vol. 1, p. 84, lines 20-28; and Exhibit AR-1, vol. 2, tab 27, p. 562-566. This copy of the Deficiency Judgment was neither dated nor signed. The first full paragraph on p. 565 indicates that the Order granting the Motion for the Deficiency Judgment was filed on May 16, 2011. The recitals to the Commissioner's Deed, dated June 9, 2011, pursuant to which the Commissioner who conducted the judicial sale conveyed title to Lot B-2 to Mr. Leonard, suggest that the Deficiency Judgment was an integral part of the entire foreclosure and judicial sale process, and that the Motion for the Deficiency Judgment and other relief was apparently filed on January 3, 2011. See Exhibit AR-1, vol. 3, tab 49, p. 840, third recital on that page.

45 *Transcript*, vol. 1, p. 15, lines 2-4.

46 Notice of Appeal in Appeal No. 2017-221(IT)G, filed January 11, 2017, ¶5; and *Transcript*, vol. 1, p. 15, lines 8-12. As indicated in paragraphs 10 and 13 above, the documentary evidence indicates that Mr. Leonard paid only $1,300,000 for the Mortgage, the Note and the Debt.

47 *Transcript*, vol. 1, p. 15, lines 12-13.

48 Notice of Appeal, *supra* note 46, ¶8; and *Transcript*, vol. 1, p. 15, line 14 to p. 17, line 10. Initially, Mr. Leonard's accountants reported the $1,472,006 Loss as a bad debt, deductible under paragraph 20(1)(p) of the ITA. Subsequently, Mr. Leonard abandoned

[30] It seems that counsel for Mr. Leonard takes the position that the amount paid by Mr. Leonard to acquire the Mortgage, the Note and the Debt was an outlay or expense that was deductible in computing Mr. Leonard's income for 2011. In the written submissions of counsel for Mr. Leonard, that position was stated as follows:

> The nature of the outlay is the only remaining issue as defined in the pleadings.
>
> If the outlay in issue was for the purpose of earning income from a business (an adventure in the nature of trade) it is deductible from income pursuant to s. 18(1)(a) of the *Act*. As the sum total of such expenses exceeds income for the year there will be a loss carried pursuant to s. 111 of the *Act*…. If the outlay, which indisputably occurred, was made for securing a profit rather than as a long term investment, it is deductible from income in the year. This is trite, immutable law of taxation in Canada. Only a finding of additional income earned in the year can offset or reduce a loss in that year. The Crown is not saying other income in that year has offset this loss….
>
> … the only issue before this court: whether the (admitted) outlay was made to earn a profit.[49] [*Footnote omitted*.]

B. The Crown

[31] The Crown submits that Mr. Leonard did not participate in an adventure in the nature of trade and that, when he acquired the Mortgage, the Note and the Debt from the Bank, his objective was, by means of the judicial sale, to acquire Lot B-2 and hold it as a long-term investment. For instance, during oral argument, counsel for the Crown made the following statements:

> … the Appellant purchased the note and mortgage with the intention of obtaining title to the underlying real property.[50]
>
> … the intention wasn't to get rid of this property by way of foreclosure. It was -- the intention was to buy that property out of foreclosure and to control that process and -- in an effort to gain title to the underlying property.[51]

---

that argument and took the position in his Notice of Appeal that he had incurred a loss in his money-lending business or in an adventure in the nature of trade. As mentioned above, at the commencement of the hearing, counsel for Mr. Leonard abandoned the money-lending-business argument.

49 Written submissions by counsel for Mr. Leonard, dated July 15, 2020, p. 1-2 & 3.

50 *Transcript*, vol. 2, p. 32, lines 18-20.

51 *Transcript*, vol. 2, p. 40, lines 15-19.

> … the transaction was about the real property. The mortgage was a part, a feature, a tool, a method of acquiring this.[52]
>
> This wasn't an investment in a mortgage. This was an acquisition of real property.[53]

[32] The Crown takes the position that Mr. Leonard did not incur the Loss in 2009 or 2011, given that he continues to own Lot B-2 (which is now consolidated with Lot B-3) and he still holds the Deficiency Judgment relating to the principal and interest owed in respect of the Debt (less the proceeds of the judicial sale).

[33] The Crown's position is, in part, represented by several of the assumptions made by the Minister when reassessing Mr. Leonard, as set out in paragraph 12 of the Reply:

> In determining the appellant's [i.e., Mr. Leonard's] tax liability for the 2011, 2012, 2013 and 2014 taxation years, the Minister made the following assumptions of fact: …
>
> > z) it was not the appellant's intention to trade, resell or re-assign the promissory note and mortgage at the time when he acquired it through assignment;
> >
> > aa) the appellant's intention at the time of acquiring the promissory note was to purchase and hold it, and proceed with the foreclosure of the Kukio 15B-2 Property to realize a profit on the Kukio 15B-2 Property;
> >
> > bb) the appellant's intention was to hold the Kukio 15B-2 Property for long-term investment purposes, awaiting an appreciation of its value;
> >
> > cc) the appellant's intention was not to make a profit on the promissory note itself by collecting interest generated from it or by trading it; …
> >
> > gg) the appellant's intention in purchasing the promissory note was investment-related; …
> >
> > mm) the appellant was not engaged in an adventure in the nature of trade….[54]

---

52 *Transcript*, vol. 2, p. 102, lines 18-20.

53 *Transcript*, vol. 2, p. 109, lines 23-24.

54 Reply in Appeal No. 2017-221(IT)G, filed May 15, 2017, ¶12z)-cc), gg) & mm). The phrase "…to realize a profit…" in subparagraph 12aa) seems somewhat at odds with the investment intention assumed in some of the other subparagraphs.

[34] Notwithstanding the position taken by the Crown (as summarized above), in paragraph 1 of the Reply, the Crown admitted paragraph 8 of Mr. Leonard's Notice of Appeal, which reads as follows:

> 8. As a result of the Transaction [defined in paragraph 5 of the Notice of Appeal as Mr. Leonard's purchase of the Note for $1,487,551], the Appellant incurred a total loss of $1,472,006 (the "Loss").[55]

During his opening statement at the hearing, counsel for the Crown qualified that admission by indicating that the Crown was merely acknowledging that the amount of the reported Loss, as calculated by Mr. Leonard, was $1,472,006, but the Crown was not admitting that Mr. Leonard was entitled to deduct the Loss.[56]

C. Applicable Law

[35] The resolution of these Appeals may require an analysis of the nature of a mortgage, the legal procedures pertaining to a foreclosure and a judicial sale, and the effect of obtaining a deficiency judgment. The transactions which are the subject of these Appeals took place in Hawaii; however, neither party adduced any expert evidence concerning the laws of Hawaii.

[36] If a party fails to adduce expert evidence to describe the operation of a foreign law, the concept of *lex fori* (i.e., the law of the forum, or the law of the jurisdiction where the case is pending)[57] will apply, with the result that the Canadian court hearing the matter should "act as if the foreign law is the same as its own law, unless the law is of a local or regulatory nature."[58] Thus, if the applicable foreign law is not satisfactorily proven, the law is assumed to be the same as the law of the province where the trial is held.[59] This principle extends to a statute of general application that is part of the law of the forum.[60]

---

55 As will be discussed below, it is my view that the evidence does not support Mr. Leonard's assertion that the amount of the Loss was $1,472,006.

56 *Transcript*, vol. 1, p. 30, line 4 to p. 32, line 22.

57 Bryan A. Garner (editor), *Black's Law Dictionary*, 10th ed. (St. Paul: Thomson Reuters, 2014), p. 1049.

58 *Club Intrawest v. The Queen*, 2016 TCC 149, ¶74-75; *reversed on other grounds*, 2017 FCA 151. See also *Bui v. The Queen*, 2013 TCC 326, ¶10; *Eidsvik v. The Queen*, 2006 TCC 253, ¶33; and *Yoon v. The Queen*, 2005 TCC 366, ¶12-17.

59 *Wabush Iron Company Limited v. The Queen*, 2009 TCC 239, ¶58-59.

60 *Backman v. The Queen*, [1999] 4 CTC 177, 99 DTC 5602 (FCA), ¶38-40; and *Oloya v. The Queen*, 2011 TCC 308, ¶20-23.

[37] Counsel for the Crown took the position that, in the absence of expert evidence of Hawaiian law, the principle of *lex fori* should apply. As the evidentiary portion of the hearing took place in Winnipeg, counsel for the Crown submitted that Manitoba law should be applied by the Court. Counsel for Mr. Leonard made no submissions concerning the choice of law or the principle of *lex fori*.

D. Inapplicable Statutory Provisions

[38] Counsel for both parties have acknowledged that neither section 79.1 of the ITA[61] nor section 16 of *The Mortgage Act* (Manitoba)[62] was applicable to the transactions that are the subject of these Appeals.

V. **ANALYSIS**

A. Adventure in the Nature of Trade or Investment

[39] The first issue in these Appeals raises the question of whether, in acquiring the Mortgage, the Note and the Debt and in his subsequent dealings therewith (including the foreclosure, the judicial sale, the acquisition of Lot B-2 and the Deficiency Judgment), Mr. Leonard was making an investment or engaging in an adventure in the nature of trade. In other words, were his transactions on capital account or on income account? As recently stated by Justice Hogan in *Paletta*, the determination of whether a gain or a loss is on capital account or income account is a question of fact.[63] Like Justice Hogan, I will use the approach and the summary of the factors, as set out in *Friesen*,[64] that are typically used to determine whether a transaction involving real estate is an adventure in the nature of trade or a capital transaction.

---

61 If section 79.1 of the ITA were to be applicable, paragraph 79.1(7)(a) would deem Mr. Leonard to have disposed of the Debt in 2011, which would be relevant in determining whether there was a loss and whether it was realized in 2011.

62 Section 16 of *The Mortgage Act*, CCSM c.M200, contains a "seize or sue" provision, which could, depending on the circumstances, have resulted in an extinguishment of the Note, the Debt and the Deficiency Judgment, which would be relevant in determining whether the Note and the Debt were disposed of in 2011 and whether the Loss (if any) was realized by Mr. Leonard in 2011.

63 *Paletta et al. v. The Queen*, 2019 TCC 205, ¶273.

64 *Friesen v. The Queen*, [1995] 3 SCR 103.

[40] In *Friesen*, Justice Major stated, "The concept of an adventure in the nature of trade is a judicial creation designed to determine which purchase and sale transactions are of a business nature and which are of a capital nature."[65] He then noted the importance of there being a "scheme for profit-making" in these terms:

> The first requirement for an adventure in the nature of trade is that it involve a "scheme for profit-making". The taxpayer must have a legitimate intention of gaining a profit from the transaction.[66]

Borrowing from an Interpretation Bulletin issued by the predecessor of the CRA, Justice Major then listed four factors to be considered "to determine whether a transaction involving real estate is an adventure in the nature of trade creating business income or a capital transaction involving the sale of an investment[,]"[67] as follows:

> Particular attention is paid to:
>
> (i) The taxpayer's intention with respect to the real estate at the time of purchase and the feasibility of that intention and the extent to which it was carried out. An intention to sell the property for a profit will make it more likely to be characterized as an adventure in the nature of trade.
>
> (ii) The nature of the business, profession, calling or trade of the taxpayer and associates. The more closely a taxpayer's business or occupation is related to real estate transactions, the more likely it is that the income will be considered business income rather than capital gain.
>
> (iii) The nature of the property and the use made of it by the taxpayer.
>
> (iv) The extent to which borrowed money was used to finance the transaction and the length of time that the real estate was held by the taxpayer. Transactions involving borrowed money and rapid resale are more likely to be adventures in the nature of trade.[68]

[41] A precursor to the above list was set out in the *Happy Valley Farms* case. In that case, after considering previous cases that had determined whether a particular transaction was an adventure in the nature of trade, Justice Rouleau enumerated several tests that had been used by the courts, as follows:

---

65 *Ibid*, ¶15.

66 *Ibid*, ¶16. See also *Canada Safeway Limited v. The Queen*, 2008 FCA 24, ¶41.

67 *Friesen, supra* note 64, ¶17.

68 *Ibid*, ¶17. See also *Paletta, supra* note 63, ¶274. As stated by the Supreme Court in *Friesen*, the above list of factors was taken from Interpretation Bulletin IT-218R (1986).

> Several tests, many of them similar to those pronounced by the Court in the *Taylor* case, have been used by the courts in determining whether a gain [or a loss] is of an income or capital nature. These include:
>
> 1. *The nature of the property sold*. Although virtually any form of property may be acquired to be dealt in, those forms of property, such as manufactured articles, which are generally the subject of trading only are rarely the subject of investment. Property which does not yield to its owner an income or personal enjoyment simply by virtue of its ownership is more likely to have been acquired for the purpose of sale than property that does.
>
> 2. *The length of period of ownership*. Generally, property meant to be dealt in is realized within a short time after acquisition. Nevertheless, there are many exceptions to this general rule.
>
> 3. *The frequency or number of other similar transactions by the taxpayer*. If the same sort of property has been sold in succession over a period of years or there are several sales at about the same date, a presumption arises that there has been dealing in respect of the property.
>
> 4. *Work expended on or in connection with the property realized*. If effort is put into bringing the property into a more marketable condition during the ownership of the taxpayer or if special efforts are made to find or attract purchasers (such as the opening of an office or advertising) there is some evidence of dealing in the property.
>
> 5. *The circumstances that were responsible for the sale of the property*. There may exist some explanation, such as a sudden emergency or an opportunity calling for ready money, that will preclude a finding that the plan of dealing in the property was what caused the original purchase.
>
> 6. *Motive*. The motive of the taxpayer is never irrelevant in any of these cases. The intention at the time of acquiring an asset as inferred from surrounding circumstances and direct evidence is one of the most important elements in determining whether a gain is of a capital or income nature.[69]

[42] In reviewing the various factors that the courts have identified, I will follow the organizational structure set out in *Friesen*, and will then comment briefly in respect of the additional factors identified in *Happy Valley Farms*.

---

[69] *Happy Valley Farms Ltd. v. MNR*, [1986] 2 CTC 259, 86 DTC 6421 (FCTD), ¶14. See also *Atlantic Packaging Products Ltd. v. The Queen*, 2020 FCA 75, ¶35.

(1) Intention[70]

[43] At the hearing, there was some uncertainty as to whether Mr. Leonard, in his transaction with the Bank, intended to acquire the Mortgage encumbering Lot B-2 and then, by means of the judicial sale, hopefully obtain, from a third-party bidder, repayment in full of the Note and the Debt,[71] or intended to bid himself at the judicial sale and ultimately acquire title to Lot B-2, after which he would sell Lot B-2 for a profit. Examples of his description of his intention are set out and discussed in the ensuing paragraphs.

[44] During his direct examination, Mr. Leonard explained how he came to acquire the Mortgage and how he hoped to make a profit, as follows:

> Q. Now, what brought you to this –– this particular transaction in issue?
>
> A. … And so that's how I knew about this gentleman [i.e., Mr. Anderson] and his property and it came available to buy it for less than the cost of the –– the bank debt on the property and I thought that was very attractive.
>
> Q. … So you –– you bought a mortgage?
>
> A. Okay. Yeah, this –– this mortgage specifically was being held by a bank called the Central Pacific Bank and at that time they were under duress and had a great deal of trouble and they needed to clean up their books. So I met with the Central Pacific Bank and they offered to sell me this mortgage for below –– below the cost and it was secured by a property and, as we discussed here already, it was already in foreclosure.
>
> This –– this property was not a property that was useful to be on. It was just bare lava rock. It wasn't possibly gainful or something that anyone would have without developing it fully. It was just bare lava rock. So the –– the only reason I wanted to buy this property was to resell it and –– or this mortgage was to resell it and to have –– have this –– make a profit because I was buying it for less –– well –– well below the property cost, which was actually tax appraised by the tax assessment people in –– in Kona for $4.4 million. And I was able to buy this property for less than $2 million, fully expecting to sell it for at least half of what the tax-assessed value was of 4.4 [million]. So I fully expected that I would be able to sell the mortgage, which in Hawaii can't be done, I found out after the

---

70 See *Friesen*, *supra* note 64, ¶17(i); and *Happy Valley Farms*, *supra* note 69, ¶14(6) & 15, in which Justice Rouleau uses *motive* and *intention* interchangeably.

71 Having acquired the Note and the Debt at a discount, full repayment of the Note and the Debt would have resulted in a profit for Mr. Leonard.

> fact, until you actually have an auction on the property. And I fully expected that property would sell for somewhere in the neighbourhood of 50 percent of the tax-assessed value, which would have been 2.2 million, which would have been –– I –– I understood would –– would give me that profit….[72]
>
> I happened to know at the time that there had never been a property sold at Kukio, this place where this property was, for less than a million dollars, never in the history so far, and so I felt very comfortable putting in a bid for $500,000, with actually zero expectation that there wouldn't be more bids, and then I was excited to have the property bid up in the auction environment and I was expecting it would be bid up to 2.2 million or somewhere near half the tax-assessed value of the property.[73]

While Mr. Leonard stated that he hoped to make a profit by reselling the Mortgage,[74] the above testimony also suggests that, as an alternative, he thought that the profit might come from the acquisition and subsequent sale of Lot B-2.[75]

[45] At one point in his cross-examination, Mr. Leonard indicated that he purchased the Mortgage and the Debt as a means to acquire Lot B-2:

> Q. But he [i.e., Mr. Anderson] was in financial distress and not paying his debts by 2009, correct?
>
> A. I understand that was the case.
>
> Q. And my understanding is essentially Mr. Anderson came to you with a deal to obtain these two –– we'll call them the Kukio properties; is that –– you know what I'm referring to, the two parcels?
>
> A. Yes.
>
> Q. He felt –– or he suggested to you that you could have them at a discount to essentially, well, make a profit, partially to make amends for the failure to pay that loan back; correct?
>
> A. I –– I don't think –– I mean that was his suggestion that it would be useful for him. From –– from his perspective, he had a debt with the Central Pacific Bank that he wanted to get paid off and was happy to not have those properties and also not have that debt.

---

72 *Transcript*, vol. 1, p. 40, line 2 to p. 41, line 21.
73 *Transcript*, vol. 1, p. 42, lines 14-23.
74 *Transcript*, vol. 1, p. 41, lines 7-8 & 14-15.
75 *Transcript*, vol. 1, p. 41, lines 6-7, 8-14 & 17-21.

Q. And owe that debt to you instead?

A. No, that –– he wouldn't owe that debt to me. I would purchase the debt from the Central Pacific Bank and purchase the mortgage, which I did, and they –– they just freed Brian Anderson from that debt because I purchased the debt from the Central Pacific Bank.

Q. You purchased the debt?

A. Purchased the mortgage and I purchased the property.

Q. And when you purchase a debt, someone owes you the money under that debt; correct? I mean that's what debt is, it's a right to collect money from someone else. It's something someone owes you, correct?

A. I –– I purchased a mortgage that was in foreclosure and the reason the Central Pacific Bank sold it to me is because it was an uncollectible debt. They had already determined that. So it wasn't –– it wasn't collectible from anyone except by going through the foreclosure process and selling the property, which is –– I didn't realize when I purchased it, it was going to be such a difficult process in Hawaii because I think it's much easier in Canada, but that was the –– that was the intention, to get the money from the property.

Q. And you knew at the time you entered this transaction the assessed value of the subject property –– we often call it the property. There's two Kukios, but the one related to the mortgage, you knew that was assessed by property taxes at over $4 million; correct?

A. That –– that's correct.

Q. So you expected by entering this transaction you could sell the property, both of them, but specifically the one under the mortgage, at a profit?

A. That's correct and everybody that was party to this also thought that would be the case.

Q. And although you made some comments about it being bare land, you'd also made some comments about the value of these properties always being quite high. So you knew that this, even though it was bare lava rock, was quite valuable property; correct?

A. Right….[76]

---

[76] *Transcript*, vol. 1, p. 61, line 4 to p. 63, line 5. Some of the comments in this statement suggest that Mr. Leonard was not aware of all the legal consequences of his purchase of

It is curious that the Minister seemed to question Mr. Leonard's profit-seeking intention, yet several of the questions asked by counsel for the Crown in the above exchange seemed to suggest, if not actually acknowledge, that the Crown thought that Mr. Leonard intended to make a profit by acquiring, and then selling, the two Lots.[77]

[46] Further testimony showing that Mr. Leonard intended ultimately to acquire both Lots and then, in selling them, to make a profit, is set out in the following exchange during cross-examination:

> Q. And so you entered this transaction, and I think it's conceded, with no intention of ever — I shouldn't say that. You didn't expect that the Andersons would be paying monthly interest payments or anything like that on this loan?
>
> A. No. No, absolutely not. I — I expected I'd sell these properties promptly at a very significant discount to the market because I bought well below what I thought the market price was. That was the intention.
>
> Q. And at the time when you're making this transaction and signing the documents, you essentially believed you were buying two properties. You did not believe you were buying debt at the time?
>
> A. I knew — I knew I was buying a mortgage that would turn into that, sure. It would end up with me owning two properties. That's — that's what this would lead to.
>
> Q. I'm going to again suggest that, at this point in time, you only thought you were buying two properties? I'm going to ask you to think very careful (sic) about that answer. So what was your intention at the time you purchased — you entered this transaction? You believed you were buying two properties, not debt and a property; correct?
>
> A. No, you're just — you're just mincing words. I had to buy the mortgage that was in foreclosure. I knew that was happening and that would lead to me owning the property, so I would buy two properties, that's true. By buying the mortgage and by buying the property, then I would own those two properties.[78]

---

the Debt. In particular, he did not appreciate that the Bank had actually assigned the Debt to him, with the result that thereafter Mr. Anderson owed the Debt to him.

77 *Transcript*, vol. 1, p. 61, lines 13-14; p. 62, lines 16-20 & 23-25; and p. 63, lines 1-4.

78 *Transcript*, vol. 1, p. 68, line 18 to p. 69, line 21. The reference to "(sic)" in the third question in this exchange is found in the *Transcript*.

The first question and answer in the above exchange indicated that Mr. Leonard did not expect to receive "monthly interest payments or anything like that" from the Andersons in respect of the Debt. This is more consistent with an adventure-in-the-nature-of-trade intention, rather than an investment intention, on the part of Mr. Leonard.

[47] The cross-examination of Mr. Leonard further explored his intention in the following exchange:

> Q. To clarify, your intention entering this transaction was to own two properties; correct?
>
> A. No, my intention entering this transaction was to make money, make profit for my foundation.
>
> Q. We're not disputing ultimately, at the end of the transaction, you hoped to make a profit. I'm saying when you entered the transaction with the Canadian [*sic*] Pacific Bank to acquire the debt and all these other things, you were trying to buy two Kukio properties for resale, regardless that you lived on them? That was what you were doing, correct?
>
> A. Sure.[79]

Again, the Crown seems to acknowledge that Mr. Leonard's intention in entering into the transaction as a whole was to make a profit, albeit by selling the two Lots (rather than by selling Lot B-3, and by selling the Mortgage, the Note and the Debt or obtaining repayment of the Debt).

[48] As part of its own case, at the hearing, the Crown read into evidence two questions and their answers from the examination for discovery of Mr. Leonard, essentially as follows:

> 349: Q. And what was your understanding, like when you did purchase the promissory note and mortgage, what was your understanding of what it was worth, when it was purchased by you?
>
> A. My agreement, as we've already said on the record, was to purchase the 15B-3 and 15B-2 for a total of $5.7 million. At that time, they were one purchase for me. They weren't split up into two separate things that I –- so it was $5.7 million. I didn't know which one was attributed to which.

---

[79] *Transcript*, vol. 1, p. 71, lines 3-15.

> 350: Q. So, you weren't sure what the value –- you didn't look at it and go, oh, I'm buying this promissory note and mortgage for this price, you know, I'm getting a deal because I'm paying this and it should be worth this? It wasn't –- that's not how you regarded it?
>
> A. I regarded it that the total price for what I was paying is significantly less than the total value that I would be able to reap by selling those assets.[80]

The above excerpt highlights Mr. Leonard's scheme for profit-making.

[49] In order to determine the intention of Mr. Leonard when he purchased the Mortgage, the Note and the Debt, I must do more than simply consider the oral assertions that he made about his intent. In *Ludco Enterprises*, Justice Iacobucci stated:

> In the interpretation of the Act, as in other areas of law, where purpose or intention behind actions is to be ascertained, courts should objectively determine the nature of the purpose, guided by both subjective and objective manifestations of purpose….[81]

In other words, as Justice Côtй stated, in her dissenting reasons in *MacDonald*, "intent is a question that requires an assessment both of the taxpayer's subjective intention and of the presence or absence of objective manifestations of that intention."[82]

[50] The excerpts from Mr. Leonard's testimony, as quoted above, contain a number of statements of his subjective intention. However, they also reference objective manifestations of that intention, such as the following facts:

---

80 Transcript of the Examination for Discovery of Mr. Leonard, p. 132, line 12 to p. 133, line 6. The foregoing excerpt from that Transcript was filed with the Court at the hearing; see subsection 100(3.1) of the *Tax Court of Canada Rules (General Procedure)*. There are slight variations between the questions and answers reported in the Transcript of the Examination for Discovery and the manner in which those questions and answers were read into evidence at the hearing; see *Transcript*, vol. 1, p. 149, line 19 to p. 150, line 19. Those variations were minor and do not affect the substance of the questions or answers.

81 *Ludco Enterprises Ltd. et al. v. The Queen*, [2001] 2 SCR 1082, 2001 SCC 62, ¶54. See also *Symes v. The Queen*, [1993] 4 SCR 695, at 736; and *MacDonald v. The Queen*, 2020 SCC 6, ¶22 (*per* Justice Abella); and ¶54-55 (*per* Justice Côtй, in dissent).

82 *MacDonald, ibid*, ¶56.

(a) Lot B-2 (which was the subject of the Mortgage) was undeveloped (i.e., bare lava rock).

(b) Mr. Anderson was no longer making monthly interest payments in respect of the Debt.

(c) The Bank had determined that the Debt was uncollectible.

(d) When the Bank offered to sell the Mortgage, the Note and the Debt to Mr. Leonard, the Debt was in default and the Mortgage was in foreclosure.

(e) The Bank offered to sell the Mortgage, the Note and the Debt to Mr. Leonard at a price less than the Bank's cost and the face amount of the Debt.

(f) Based on the history of previous sales of real property in the Kukio community, Mr. Leonard anticipated that Lot B-2 would be sold at the auction for "somewhere in the neighbourhood of 50 percent of the tax-assessed value, which would have been [$]2.2 million…."

(g) The price paid by Mr. Leonard for the Mortgage, the Note and the Debt was significantly less than the assessed value of Lot B-2 for property tax purposes.

[51] In addition to the above objective manifestations of Mr. Leonard's intention, other objective manifestations are set out below in the discussion of the other *Friesen* and *Happy Valley Farms* factors.

[52] The dispute concerning Mr. Leonard's intention did not focus so much on whether he intended to make a profit or not, but rather on whether the source of the profit in respect of Lot B-2 would be a sale of that Lot or a repayment or disposition of the Debt secured by the Mortgage in respect of that Lot, as evidenced by the following exchange during cross-examination:

> MR. SILVER: Your Honour, I would submit that [i.e., the acquisition of Lot B-2] was the exact intent. This was only ever a means, a facility to acquire the property. It was always contemplated that the appellant would buy it out of foreclosure and that's how he would profit. There's no doubt that he bought it because he thought it was worth more. There's no doubt he entered the transaction because he thought he could make some money off an undervalued or distressed property. The point is there was never an intention to profit off the mortgage. That simply was a means, a mechanism to acquire the property.

> MR. LEONARD: Your Honour, that's just –– I really did go to the flagpole [i.e., the site of the public auction of Lot B-2] to see who was going to buy the property and I thought it would sell for about $2.2 million. I did not have $2.2 million. I couldn't possibly have bought the property for more than I had bought the mortgage for. I fully expected I would make a profit at that time. That was my intention regardless of what this guy says. That really is what –– what I was trying to do here and I did not have the funds to do anything different.[83]

[53] It is my understanding that the Crown does not dispute that Mr. Leonard had a profit-making intention when he entered into the transaction with the Bank,[84] but the Crown submits that Mr. Leonard intended to make a profit only by selling Lot B-2, and not by receiving repayment, or disposing, of the Mortgage, the Note and the Debt that he had acquired from the Bank as a preliminary step to acquiring Lot B-2.[85] Given that Mr. Leonard knew, when he acquired the Mortgage, the Note and the Debt at a discount, that the Debt was in default and the Mortgage was in foreclosure, and given that he did not expect to receive any interest from Mr. Anderson in respect of the Debt, it is my view that a continuing profit-making intention pervaded the entire Transaction, from the acquisition of the Mortgage, the Note and the Debt from the Bank to the completion of the judicial sale and the listing of Lot B-2 for sale. It does not make sense that Mr. Leonard would have had an investment intention or an on-account-of-capital intention when he acquired the Mortgage, the Note and the Debt, but then formulated a profit-making intention when he acquired Lot B-2.

[54] I accept Mr. Leonard's assertion that, when he acquired the Mortgage, the Note and the Debt from the Bank, his objective was to make a profit, by either:

a) continuing the foreclosure proceedings and arranging for the judicial sale of Lot B-2 in the hope that someone else would bid and pay a price greater than the amount that Mr. Leonard had paid to acquire the Mortgage, the Note and the Debt and preferably greater than $1,972,252.63, which was the total of the principal, unpaid interest and foreclosure-related expenses in respect of the Debt (this scenario is referred to as "Alternative A"); or

b) bidding himself in the judicial sale, and if he happened to be the successful bidder, leading to his acquisition of Lot B-2, subsequently selling it at an

---

83 *Transcript*, vol. 1, p. 82, line 9 to p. 83, line 1.

84 *Transcript*, vol. 1, p. 71, lines 8-9; and p. 82, lines 10-17.

85 *Transcript*, vol. 1, p. 82, lines 17-19.

amount greater than his cost thereof (this scenario is referred to as "Alternative B").

At the time of acquiring the Mortgage, the Note and the Debt from the Bank, Mr. Leonard had no way of knowing which of those two alternatives would unfold, as that was dependent on whether, and how much, anyone would bid in the judicial sale. In my view, Mr. Leonard was motivated by a profit-making intention in respect of the entire Transaction, including its two alternative paths. It would not make sense for him to have had an investment intention for Alternative A, but a profit-making intention for Alternative B.

[55] As the Supreme Court stated in *Friesen*, "An intention to sell the property for a profit will make it more likely to be characterized as an adventure in the nature of trade."[86] It is my understanding of the evidence that Mr. Leonard intended to dispose of the Mortgage, the Note and the Debt for a profit (assuming that someone bid an amount greater than what Mr. Leonard had paid for the Mortgage, the Note and the Debt) or to sell Lot B-2 for a profit (assuming that he acquired Lot B-2 in the judicial sale). In either case, his intention to realize a profit suggests to me that, rather than making an investment, he participated in an adventure in the nature of trade.

(2) Nature of Business[87]

[56] In his Notice of Appeal, Mr. Leonard stated that he "is highly experienced in, and has a history of providing loans and entering into real estate transactions."[88] In his Notice of Appeal, Mr. Leonard also stated that he "carries on the business of acquiring mortgages and lending money" or, alternatively, his "activities in acquiring mortgages and lending money constitute[d] an adventure in the nature of trade."[89] During cross-examination, Mr. Leonard acknowledged that for much longer than 12 years, "lending and investing is also something that [he has done] … for business."[90] However, it appears that, before purchasing the Mortgage, the Note and the Debt from the Bank in 2009, Mr. Leonard had not previously

---

86 *Friesen*, *supra* note 64, ¶17(i).

87 See *Friesen*, *supra* note 64, ¶17(ii); and *Happy Valley Farms*, *supra* note 69, ¶14(3).

88 Notice of Appeal, *supra* note 46, ¶3.

89 *Ibid*, ¶12.

90 *Transcript*, vol. 1, p. 48, lines 15-22.

purchased distressed debt,[91] other than a possible distressed-debt transaction involving the Edgewater Casino in Vancouver.[92]

[57] In his Notice of Appeal, Mr. Leonard further stated that his purchase of the Note "was effected in the course of [his] business or constituted an adventure in the nature of trade."[93] As noted above, at the commencement of the hearing, counsel for Mr. Leonard advised the Court that, although Mr. Leonard makes loans and is a very experienced businessperson, he was no longer arguing that he had incurred the Loss "pursuant to a business of lending loans."[94]

[58] Concerning the nature of Mr. Leonard's business, it is my understanding that the business activity that has occupied most of his time and attention during his career has been autonomous dredging, commercial diving, and pumping and barging operations for mine sites, to mitigate the problem of mine tailings and toxic waste, without putting people at risk.[95] It is the position of the Crown that Mr. Leonard's purchase of the Mortgage, the Note and the Debt, at a time when the Debt was in default and the Mortgage was in foreclosure, was unlike anything that Mr. Leonard had previously done, such that the purchase could not be viewed as something that he did in the course of his regular business.[96]

[59] In *Friesen*, Justice Major indicated that the more closely a taxpayer's business is related to the type of transaction in which the gain or loss arose (for instance, a real estate transaction in *Friesen*, a distressed-debt transaction here), the more likely it is that the profit or loss will be on income account rather than capital account.[97] In *Happy Valley Farms*, Justice Rouleau noted that, if there has been a series of similar transactions over a period of years, or if there were several similar transactions all at about the same time, a presumption arises that there has been a dealing in respect of the particular type of property.[98] While Mr. Leonard had participated in a lending and investing business for more than 12 years,[99] and had made 13 loans between 2005 and 2017,[100] it seems that, with the possible

---

91 *Transcript*, vol. 1, p. 91, lines 12-18.
92 *Transcript*, vol. 1, p. 91, line 12 to p. 92, line 7.
93 Notice of Appeal, *supra* note 46, ¶13.
94 *Transcript*, vol.1, p. 14, lines 23-25.
95 *Transcript*, vol.1, p. 39, lines 11-15; and p. 47, lines 20-23.
96 *Transcript*, vol. 1, p. 53, lines 21-25.
97 *Friesen*, *supra* note 64, ¶17(ii).
98 *Happy Valley Farms*, *supra* note 69, ¶14(3).
99 *Transcript*, vol. 1, p. 48, lines 17-22.
100 *Transcript*, vol. 1, p. 58, lines 1-4.

exception of the Edgewater Casino transaction, the purchase of the Mortgage, the Note and the Debt in 2009 may have been his first distressed-debt transaction. Therefore, this factor does not point to a transaction on income account, and may well point to a transaction on capital account.

(3) Nature and Use of Property[101]

[60] The property that was the subject of the Transaction was the Mortgage, the Note and the Debt (more specifically, distressed debt). There may be a suggestion that Lot B-2 should be considered as the property in question; however, as Mr. Leonard still owns Lot B-2, I do not propose to consider it in this analysis.

[61] The Debt had gone into default and the Bank had commenced foreclosure proceedings in respect of the Mortgage, before Mr. Leonard purchased the Mortgage, the Note and the Debt.[102] When Mr. Leonard purchased the Mortgage, the Note and the Debt, he did not expect that Mr. Anderson would make the monthly interest payments or pay any other amount in respect of the Debt.[103] Rather he expected that it would be necessary for him to sell the Mortgage, the Note and the Debt, or Lot B-2, if he hoped to make a profit.[104] With respect to the criterion of "use of the property," Mr. Leonard did not actually use the Mortgage, the Note or the Debt, although he did continue with the foreclosure proceedings in respect of the Mortgage.

[62] In discussing this factor (i.e., the nature of the property) in *Happy Valley Farms*, Justice Rouleau stated, "Property which does not yield to its owner an income or personal enjoyment simply by virtue of its ownership is more likely to have been acquired for the purpose of sale than property that does."[105] As it was highly unlikely that Mr. Leonard would receive interest or other investment income by holding the Mortgage, the Note and the Debt, this factor points toward the transaction being on income account, rather than capital account.

(4) Borrowed Money and Length of Ownership[106]

(a) Borrowed Money

---

101 See *Friesen, supra* note 64, ¶17(iii); and *Happy Valley Farms, supra* note 69, ¶14(1).
102 *Transcript*, vol. 1, p. 40, line 19 to p. 41, line 1; and p. 62, lines 6-11.
103 *Transcript*, vol. 1, p. 68, lines 18-23.
104 *Transcript*, vol. 1, p. 68, lines 20-27.
105 *Happy Valley Farms, supra* note 69, ¶14(1).
106 See *Friesen, supra* note 64, ¶17(iv); and *Happy Valley Farms, supra* note 69, ¶14(2).

[63] Mr. Leonard paid $5,700,000 for Lot B-3, the Mortgage, the Note and the Debt. The entire price was paid using money that he had borrowed from the Bank. In other words, Mr. Leonard did not put any of his own money into the Transaction.

[64] In *Friesen*, Justice Major indicated that transactions involving borrowed money are more likely to be adventures in the nature of trade.[107] Hence, this factor suggests that Mr. Leonard participated in an adventure in the nature of trade.

(b) Length of Ownership

[65] Mr. Leonard held the Mortgage from June 24, 2009 until the judicial sale closed on June 20, 2011. Given the nature of foreclosure proceedings in Hawaii, I do not consider this two-year period of ownership to be lengthy.

[66] Determining the length of ownership of the Debt is more involved, and requires consideration of the Deficiency Judgment. The gross proceeds of the judicial sale were in the amount of $500,000 (i.e., the amount bid and paid by Mr. Leonard). After taking into consideration the interest that had continued to accrue in respect of the Debt and the costs of the foreclosure and the judicial sale, there was a deficiency in the amount of $1,472,006.44.[108] Subsequently (likely in May 2011), Mr. Leonard obtained the Deficiency Judgment against Mr. Anderson, in the amount of $1,472,006.44.[109] Mr. Leonard never did collect any money in respect of the Deficiency Judgment, and may possibly have still held the Deficiency Judgment at the time of the hearing.[110] Assuming that the Deficiency Judgment represented the Debt, Mr. Leonard's ownership of the Debt could be described as indefinite.

[67] There was no evidence concerning the length of Mr. Leonard's ownership of the Note.

[68] Notwithstanding the delay that Mr. Leonard encountered in bringing the foreclosure to a conclusion, his expectation had been to promptly realize proceeds

---

107 *Friesen, supra* note 64, ¶17(iv).
108 Exhibit AR-1, vol. 2, tab 28, p. 572.
109 Exhibit AR-1, vol. 2, tab 27, p. 562-566; *Transcript*, vol. 1, p. 84, lines 20-28.
110 *Transcript*, vol. 1, p. 85 lines 16-21.

in respect of the Mortgage, the Note and the Debt or, alternatively, in respect of Lot B-12.[111]

[69] As stated by Justice Major in *Friesen*, a likely indicator of an adventure in the nature of trade is a rapid resale of the property in question. That did not happen here, although Mr. Leonard tried and hoped that it would have happened, so I consider this to be a neutral factor, which does not point toward, or away from, an adventure in the nature of trade.

(5) Work Expended[112]

[70] The evidence did not disclose any work or effort expended by Mr. Leonard to put the Mortgage, the Note and the Debt into a more marketable condition after he acquired it. In fact, during cross-examination, Mr. Leonard acknowledged that, after acquiring the Mortgage, the Note and the Debt, he did not attempt to assign or sell them to anyone else,[113] although he did talk about the Mortgage, the Note and the Debt with a group of acquaintances, but without actually asking if any of them wanted to buy the Mortgage, the Note and the Debt.[114]

[71] The only thing that Mr. Leonard did to realize a return in respect of the Mortgage, the Note and the Debt was to continue with the foreclosure proceedings, which ultimately culminated in the closing of the judicial sale in June 2011. Therefore, this factor is not indicative of dealing or trading in distressed debt.

[72] For the sake of completeness, it should be mentioned that, in 2015, Mr. Leonard, with governmental approval, consolidated Lot B-2 and Lot B-3.[115] The primary reason for combining the two Lots was to reduce the monthly maintenance fees, although he also thought that, as he had not been able to sell the two Lots separately, perhaps if he were to combine them into a larger property, he might be able to sell it.[116] However, as Mr. Leonard, at the time of the hearing, still owned the two Lots (albeit combined into a single lot), no profit or loss had yet been realized from any adventure in the nature of trade in respect of the Lots.

---

111 *Transcript*, vol. 1, p. 68, lines 23-24.

112 See *Happy Valley Farms*, *supra* note 69, ¶14(4).

113 *Transcript*, vol. 1, p. 85, lines 13-15.

114 *Transcript*, vol. 1, p. 92, line 9 to p. 93, line 23.

115 Exhibit AR-1, vol.3, tab 48, p. 819-826; and *Transcript*, vol. 1, p. 88, line 26 to p. 89, line 2.

116 *Transcript*, vol. 1, p. 43, line 6 to p. 44, line 22.

(6) Circumstances Responsible for Disposition[117]

[73] As noted in the preceding paragraph, as of the date of the hearing, there had not yet been a disposition of combined Lots B-2 and B-3. While there was not an actual sale of the Mortgage, the Note and the Debt, as noted below, there was a disposition of the Mortgage when it was cancelled (on the closing of the judicial sale). As that disposition was not the type of sale contemplated by Justice Rouleau when he enumerated the applicable tests in the *Happy Valley Farms* case, nothing further needs to be said about this particular factor, as it points in neither direction.

(7) Weighing of Factors

[74] Summarizing the above discussion, the following factors indicate that the Transaction was on income account:

(a) Mr. Leonard's stated intention was to make a profit, by one of two alternatives, i.e., either:

(i) acquiring the Mortgage, the Note and the Debt and then, at the judicial sale, realizing an amount greater than his cost of the Mortgage, the Note and the Debt, or

(ii) after acquiring the Mortgage, the Note and the Debt, purchasing Lot B-2 at the judicial sale, and later selling it for a profit.

The surrounding circumstances (such as Mr. Leonard's expectation that the judicial sale would close sooner than it did, his listing of Lot B-2 with a real estate agent shortly after the auction, and the facts described in paragraph 50 above) were consistent with his stated intention. In his mind, he had formulated a scheme for profit-making.

(b) The nature of the Mortgage, the Note and the Debt (i.e., distressed debt that was in default, with no expectation of interest being paid, and the Mortgage already in foreclosure) point to income account, rather than capital account.

---

117 *Happy Valley Farms, supra* note 69, ¶14(5).

(c) Mr. Leonard's use of borrowed money to pay the entire price to purchase the Mortgage, the Note, the Debt and Lot B-3 is indicative of an adventure in the nature of trade.

[75] The factors suggesting that the Transaction may have been on capital account were:

(a) The dissimilarity between Mr. Leonard's dredging business and the acquisition of the Mortgage, the Note and the Debt are not supportive of the Transaction being on income account.

(b) As Mr. Leonard did not expend any work or effort to put the Mortgage, the Note and the Debt or Lot B-2 into a more marketable condition (other than combining Lots B-2 and B-3), the factor described as "work expended" does not indicate that the Transaction was on income account.

[76] The following factors do not clearly point in either direction:

(a) With respect to the length of ownership, the fact that Mr. Leonard presumably still holds the Deficiency Judgment and still owns Lot B-2 (which is now combined with Lot B-3) suggests that the Transaction was on capital account.[118] However, shortly after the auction, Mr. Leonard took steps to sell Lot B-2, which suggests that the Transaction was on income account. Therefore, this is a neutral factor.

(b) As the Mortgage was discharged and cancelled by operation of law, as part of the foreclosure and judicial sale proceedings, and as Mr. Leonard continues to hold the Deficiency Judgment and Lot B-2, the factor described as "circumstances responsible for disposition" is not applicable.

[77] The factors described in paragraph 74 above outweigh the factors described in paragraph 75 above. The factors described in paragraph 76 above do not affect the analysis.

[78] Based on my understanding of the evidence, although Mr. Leonard seemed to have misunderstood some of the technicalities of the foreclosure process, he nevertheless had a scheme for profit-making, which is the first requirement for an adventure in the nature of trade. In addition, after weighing the above factors, I

---

[118] There was no evidence as to whether Mr. Leonard continued to hold the Note after the Deficiency Judgment was obtained.

have come to the conclusion that Mr. Leonard's acquisition of the Mortgage, the Note and the Debt and his subsequent efforts to realize a profit were part of an adventure in the nature of trade (on income account), and not an investment (on capital account). However, it remains to be determined whether Mr. Leonard incurred the Loss, and, if so, in what amount.

B. Realization of the Loss

(1) Amount of the Loss

[79] It is the position of Mr. Leonard that he realized a Loss in the amount of $1,472,006.[119] As noted above, the Crown has admitted the amount of the Loss.[120] However, as also noted above, I do not believe that the evidence supports that amount of the Loss.

[80] Given that this Court has a statutory mandate to confirm or vary an assessment, based on the facts, whether proven or admitted, this Court is not required to follow the principle applied in civil proceedings to the effect that an admission is binding on the party which gave it. Thus, while this Court will not generally look behind a formal admission by a party, this Court is not bound by an admission that is shown, through properly tendered evidence, to be contrary to the facts.[121] In other words, a judge of this Court should not turn a blind eye on evidence placed before him or her.[122] Accordingly, where an admission is

---

119 Notice of Appeal, *supra* note 46, ¶8.

120 Reply, *supra* note 54, ¶1.

121 *Paletta*, *supra* note 63, ¶102 & 105-106.

122 *Hammill v. The Queen*, 2005 FCA 252, ¶29-32; and *Fiducie Alex Trust v. The Queen*, 2014 FCA 123, ¶9.

contradicted by the evidence, the admission should be regarded as having been made in error.[123]

[81] It is my understanding that the amount paid by Mr. Leonard for the Mortgage, the Note and the Debt was $1,300,000. Pursuant to the judicial sale, Mr. Leonard received net proceeds in the amount of $472,746.74 (i.e., the judicial sale price of $500,000 less expenses of $27,253.26).[124] Accordingly, but subject to the ensuing analysis, the amount of the Loss (if it was actually realized and if there was a disposition of the Mortgage, the Note and the Debt) was $827,253.26 (i.e., $1,300,000 − $472,746.74).[125]

(2) Deductibility of the Outlay

[82] As noted above, counsel for Mr. Leonard has taken the position that the amount paid by Mr. Leonard to acquire the Mortgage, the Note and the Debt was an "outlay … for the purpose of earning income from a business (an adventure in the nature of trade) [such that] it is deductible from income pursuant to s.18(1)(a) of the *Act*."[126] I disagree with that position for two reasons. First, paragraph 18(1)(a) of the ITA does not permit an outlay to be deducted. Rather, paragraph 18(1)(a) imposes a restriction on the deductibility of an outlay or expense, unless the outlay or expense was made or incurred for the purpose of gaining or producing income from a business (which includes an adventure in the nature of trade) or from property.[127] To determine whether an outlay or an expense is deductible, one turns to subsection 9(1) of the ITA, and its reference to *profit*, which, in general terms, is determined as "gross revenues minus any expenses incurred to earn them,"[128] and which is normally calculated in accordance with "'well accepted principles of business (or accounting) practice' or 'well accepted

---

123 *Wardean Drilling Company Limited v. MNR*, [1978] CTC 270, 78 DTC 6202 (FCA), ¶11 & footnote 1. See also *McKervey v. MNR*, [1992] 2 CTC 2015, 92 DTC 1570 (TCC), ¶21.

124 Exhibit AR-1, vol. 2, tab 28, p. 570-571; and tab 30, p. 578.

125 As explained below, I have concluded that Mr. Leonard disposed of only the Mortgage, and not the Note or the Debt, with the result that the actual amount of the Loss was different than that shown in the sentence connected to this footnote.

126 Appellant's submissions, *supra* note 49, p. 1, third paragraph.

127 *Symes, supra* note 81, at 721-722; *Daley v. MNR*, [1950] CTC 254, [1951] 1 DLR 529 (Exch.), ¶5; *The Royal Trust Company v. MNR*, [1957] CTC 32, 57 DTC 1055 (Exch.), ¶23; *Lacroix v. The Queen*, 2013 TCC 312, ¶9; and Edwin C. Harris, *Canadian Income Taxation*, 4th ed. (Toronto: Butterworth, 1986), p. 189.

128 *Lacroix, ibid*, ¶9.

principles of commercial trading'."[129] Second, the outlay paid by Mr. Leonard was not a business expense, but rather, was the price that he paid to acquire the Mortgage, the Note and the Debt. In other words, it was the cost to Mr. Leonard of acquiring the Mortgage, the Note and the Debt. It is relevant in calculating profit or loss, but, in and of itself, the outlay alone does not create a loss. This was explained by Justice Major in *Friesen* as follows:

> Reduced to its simplest terms, the income or profit from the sale of a single item of inventory by a sales business is the ordinary tracing formula calculated by subtracting the purchase cost of the item from the proceeds of sale. This is the basic formula which applies to the calculation of profit before the value of inventory is taken into account….[130]

Justice Major then went on to set out the following formula for determining the profit from the sale of a particular item of inventory:

> Income = Profit = Sale Price – Purchase Cost[131]

(3) The Realization Principle

(a) Legal Principles

[83] An adventure in the nature of trade, by its nature, contemplates the rule sometimes referred to as the realization principle. In *Friesen*, Justice Major stated:

> The concept of an adventure in the nature of trade is a judicial creation designed to determine which purchase *and sale* transactions are of a business nature and which are of a capital nature.[132] [*Emphasis added*.]

Later in his reasons, Justice Major made reference to "the general principle that neither profits nor losses are recognized until realized."[133]

---

129 *Symes*, *supra* note 81, p. 723, ¶43; and *Canderel Limited v. The Queen*, [1998] 1 SCR 147, ¶31. See also *Daley*, *supra* note 127, ¶5; and *Royal Trust*, *supra* note 127, ¶27.

130 *Friesen*, *supra* note 64, ¶21. Subsection 10(1.01) of the ITA provides that, in the context of an adventure in the nature of trade, property described in an inventory is to be valued at the cost at which the taxpayer acquired it, meaning that the usual practice, under subsection 10(1) of the ITA, of valuing inventory at the lower of cost and fair market value, is not available in this situation. See *Grant v. The Queen*, [2000] 2 CTC 2587, 2000 DTC 1985 (TCC), ¶11.

131 *Friesen*, *supra* note 64, ¶21.

132 *Ibid*, ¶15.

In dissenting reasons, Justice Iacobucci described the realization principle in these terms:

> Probably the key taxation principle relevant to the case at bar is the realization principle, which provides that, in the computation of income from an adventure in the nature of trade, gains or losses must be realized in order for them to be included in the computation of income for tax purposes….[134]

In support of the above statement, Justice Iacobucci quoted the following statement by Professor Brian Arnold:

> One of the basic principles of income taxation is that appreciation or depreciation in the value of property is not taken into account in the computation of income until such appreciation or depreciation has been realized, usually by means of a sale.[135]

Justice Iacobucci went on to make the following observation:

> The importance of this [realization] principle is reflected in the fact that, whenever the *Income Tax Act* permits deemed dispositions at fair market value without actual realizations, it does so narrowly and in a highly circumscribed manner…. Exceptions from the realization principle are thus clearly stipulated and explicitly codified…. For the most part, the Act does not recognize "unrealized" or "paper" gains or losses….[136]

(b) Application

[84] It is the position of the Crown that, as Mr. Leonard still owned Lot B-2 (albeit combined with Lot B-3) at the time of the hearing, he had not yet incurred any loss in respect of Lot B-2. I concur with that position. In order to realize a loss in respect of an adventure in the nature of trade, a taxpayer must acquire a property and then subsequently dispose of it for proceeds less than its cost. There was not a disposition of Lot B-2 by Mr. Leonard in 2011.

---

133 *Ibid*, ¶45.

134 *Ibid*, ¶105.

135 *Ibid*, ¶107, quoting Brian J. Arnold, *Timing and Income Taxation: The Principles of Income Measurement for Tax Purposes* (Toronto: Canadian Tax Foundation, 1983), p. 333. See also *Shepp v. The Queen*, [1999] 1 CTC 2889, 99 DTC 510 (TCC), ¶66.

136 *Friesen, supra* note 64, ¶108.

[85] While there had not been a disposition of Lot B-2 prior to the hearing, it is necessary to determine whether, on the facts set out above, there was a disposition of the Mortgage, the Note or the Debt in 2011.

[86] Dealing first with the Mortgage, subparagraph (b)(i) of the definition of "disposition" in subsection 248(1) of the ITA states that "'disposition' of any property … includes … any transaction or event by which, … where the property is a … mortgage, … the property is in whole or in part redeemed, acquired or cancelled…." It is my understanding that the title that Mr. Leonard obtained to Lot B-2, as a result of the judicial sale, was not encumbered by the Mortgage.[137] Thus, by reason of the foreclosure and the judicial sale, the Mortgage was cancelled. By reason of the cancellation of the Mortgage, Mr. Leonard was deemed to have disposed of the Mortgage in 2011.

[87] Although counsel for the Crown has acknowledged that, by reason of the foreclosure and the judicial sale, the Mortgage was discharged,[138] the Crown takes the position that there has been no disposition of the Debt, given that Mr. Leonard continues to hold the Deficiency Judgment.

[88] To facilitate my analysis of whether there was a disposition in 2011 of the Debt, in this portion of the Reasons I will refer to the Debt, as secured by the Mortgage and until the judicial sale, as the "Pre-Auction Debt." As well, I will refer to the debt (whether it constitutes the original Debt or a new debt), after the judicial sale and as ultimately represented by the Deficiency Judgment, as the "Post-Auction Debt."

[89] The position of the Crown was stated by counsel for the Crown in his opening statement as follows:

> The debt continues to exist…. The debt is no longer secured, but it has been converted into a judgment and a judgment is an asset.[139]

---

137 The list of encumbrances in Exhibit "A" attached to the Commissioner's Deed, whereby Mr. Leonard obtained title to Lot B-2, does not make any reference to the Mortgage; see Exhibit AR-1, vol. 3, tab 49, p. 845-848.

138 *Transcript*, vol. 1, p. 25, lines 26-27 ("… the mortgage is discharged…."); and vol. 2, p. 115, lines 7-9 ("Mortgage is gone. We all know that…. Security is discharged from the property.")

139 *Transcript*, vol. 1, p. 26, line 8-9 & 11-12.

In other words, the Crown takes the position that the Pre-Auction Debt and the Post-Auction Debt are the same debt.

[90] In the *General Electric Capital* case, the Federal Court of Appeal confirmed that, where there are substantial changes to the fundamental terms of a debt obligation, the result may be the creation of a new obligation.[140] More specifically, in that case the Court stated:

> 14. The fundamental terms of the promissory notes in question were
>
> (a) the identity of the debtor;
> (b) the principal amount of the note;
> (c) the amount of interest under the note; and
> (d) the maturity date of the note.
>
> 15. In the present case, all but one of these fundamental terms were changed. By way of example, in Note number four the maturity date was changed from August 9, 1985 to March 15, 1987, the principal amount of the note was changed from $15,000,000.00 to $13,855,819.00, and the interest rate was changed from 13.25% to 15.95%. The other notes have comparable changes. These represent substantial changes to fundamental terms of the obligations and have the effect of materially altering the terms of the original promissory note.
>
> 16. I am of the view that when it can be said that substantial changes have been made to the fundamental terms of an obligation which materially alter the terms of that obligation, then a new obligation is created within the meaning of subpara. 212(1)(b)(vii) of the Act. In my opinion, the Trial Judge did not commit an overriding or palpable error when, on the evidence before him he found, as a fact, that the changes were sufficiently fundamental as to bring into existence a new obligation.[141]

[91] In discussing this same concept, the trial judge in the *General Electric Capital* case stated:

> The evidence clearly shows that the original notes were so materially altered by the agreements of February 18, 1985, as to result in completely new obligations pursuant to paragraph 212(1)(b)(vii) of the Act. Most significantly, the rate of interest of each note was changed, so that the net return to the holder of each note

---

140 *General Electric Capital Equipment Finance Inc. v. The Queen*, 2001 FCA 392, ¶14-16; leave to appeal to the SCC denied, October 3, 2002, 302 NR 194 (note).

141 *Ibid.* The decision in *General Electric Capital* has been criticized; see Monica Biringer, "Current Cases – When Is an Obligation New?" (2001) 9:4 *Corporate Finance*, 906-910 (pages 14-17 in the stand-alone version of this publication).

> after payment of withholding taxes, was equal to the rate of interest set out in the note. In addition, the maturity date of each note was changed as was the principal amount of each note. In other words, the effect of the February 18, 1985 agreement between [the parties thereto] was to change the interest rate, the manner of calculating the interest rate, the parties and the maturity date of each note. The only reasonable conclusion is that the changes to the obligations and to the notes underlying them constitute the creation of a new obligation within the meaning of that term as it is used in paragraph 212(1)(b) of the Act.[142]

[92] In *General Electric Capital*, the Federal Court of Appeal took guidance from its decision in *Wiebe*,[143] summarized in these terms:

> Some guidance can be obtained from the decision in *Wiebe* … where this Court held that fundamental changes to a stock option agreement which substantially affected the basic elements of the agreement were inconsistent with the continuing existence of that agreement.[144]

In other words, the Federal Court of Appeal indicated that fundamental changes to the basic elements of an agreement may, depending on all the circumstances, indicate that the original agreement no longer continued to exist. In *Wiebe*, the Federal Court of Appeal noted that new conditions, which substantially affected the basic elements of earlier purported stock option agreements, represented fundamental changes in the rights granted by the agreements. The Court stated:

> Changes as fundamental as this are inconsistent with the continuing existence of the alleged prior stock option agreement; rather they represent a whole new agreement.[145]

Hence, where a new debt obligation is created by reason of substantial changes having been made to the fundamental terms of a prior debt obligation, it might follow that there was a disposition of the prior debt obligation.[146]

---

142 *General Electric Capital Equipment Finance Inc. v. The Queen*, [2000] 4 CTC 82, 2000 DTC 6513 (FCTD), ¶6. See also *Gillette Canada Inc. v. The Queen*, [2001] 4 CTC 2884, 2001 DTC 895 (TCC), fn 18, *affirmed*, 2003 FCA 22.

143 *Wiebe et al. v. The Queen*, [1987] 1 CTC 145, 87 DTC 5068 (FCA).

144 *General Electric Capital*, *supra* note 140, ¶13.

145 *Wiebe*, *supra* note 143, ¶3.

146 By reason of the decision that I have made concerning my analysis of the factors identified in *General Electric Capital*, as set out below, I do not need to make a definitive decision in these Reasons as to whether that case is limited to the principle relating to the creation of a new debt obligation, or whether it extends to a corresponding reciprocal principle relating to the disposition of the prior debt obligation.

[93] In order to ascertain whether the Pre-Auction Debt and the Post-Auction Debt constituted the same debt obligation, or whether there was a disposition of the Pre-Auction Debt, I will consider the four fundamental terms identified in the *General Electric Capital* case.

(i) Identity of the Debtor

[94] The Note showed the debtors as being:

> … BRIAN A. ANDERSON, individually and as Trustee of the Brian A. Anderson Revocable Living Trust dated September 18, 2001, and JOAN G. ANDERSON, individually and as Trustee of the Joan G. Anderson Revocable Living Trust dated September 18, 2001 (collectively "Borrower"), jointly and severally,….[147]

[95] The Deficiency Judgment described the debtors as follows:

> Brian Anderson, Individually [*sic*] and as Trustee of the Brian A. Anderson Revocable Living Trust dated September 18, 2001, and Joan Anderson, individually and as Trustee of the Joan G. Anderson Revocable Living Trust dated September 18, 2001….[148]

[96] Apart from the omission of middle initials in the names of the individual debtors, the description of the debtors in the Deficiency Judgment is the same as in the Note.

(ii) Principal Amount

[97] The original principal amount of the Pre-Auction Debt was $1,500,000.[149] When Mr. Leonard acquired the Pre-Auction Debt, the amount of principal then outstanding was $1,497,657.53.[150]

---

147 Exhibit AR-1, vol. 1, tab 10, p. 136. A copy of the Mortgage was not put into evidence; therefore, I am somewhat uncertain as to the precise way in which the debtors (i.e., the mortgagors) were shown in the Mortgage. However, it is likely safe to assume that the debtors were described in the Mortgage in a manner similar to that set out in either the Note or the Deficiency Judgment.

148 Exhibit AR-1, vol. 2, tab 27, p. 563.

149 Exhibit AR-1, vol. 1, tab 10, p. 136.

150 See the Third Note Modification Agreement, dated June 28, 2007 (Exhibit AR-1, vol. 2, tab 21, p. 549); CRA's Working Paper 1000, dated February 3, 2015 (Exhibit AR-1, vol.

[98] When the Deficiency Judgment was granted, the principal amount of the Post-Auction Debt was $1,472,006.44.[151] Hence, the principal amount of the Post-Auction Debt was $25,651.09 (i.e., $1,497,657.53 − $1,472,006.44) less than the principal amount of the Pre-Auction Debt. This was not a large difference, but it was a difference nevertheless. However, I do not view the difference in the principal amount as being indicative of a new debt obligation, as the decreases in the principal amount of the Post-Auction Debt arose by reason of repayments of principal (either voluntarily or by reason of the judicial sale), and the increases in the principal amount may be traced back to the Note, which stated that the holder was entitled to recover enforcement and collection costs.[152]

(iii) Amount of Interest

[99] The Note provided that interest thereunder was to accrue at a floating rate of 1.5% above City Bank's Base Rate, which was defined as being the same rate as the Low New York Prime Rate published in the West Coast Edition of the *Wall Street Journal*.[153] The Note further provided that, if the principal amount thereof was not paid when due, the rate of interest was to be increased by an additional 5% above the otherwise applicable interest rate.[154]

[100] In the course of the foreclosure proceedings, the amount of principal, interest and other fees owing under the Mortgage and the Note was expressed in this manner:

Principal Balance	$1,497,657.53
Interest to 6/24/09[155]	108,871.12
Interest from 6/25/09 to 9/30/09[156]	24,372.81

2, tab 17, p. 466); and Memorandum in Support of Motion (in the foreclosure proceedings) (Exhibit AR-1, vol. 1, tab 4(2), p. 64).

151 See the Deficiency Judgment (Exhibit AR-1, vol. 2, tab 27, p. 566).

152 Exhibit AR-1, vol. 1, tab 10, p. 137.

153 Exhibit AR-1, vol. 1, tab 10, p. 136. The Note also provided for an alternate method of calculating the Base Rate if the above method was not feasible. In addition, the Note further provided for a second alternate method of calculating the Base Rate if the first alternate method was not available.

154 *Ibid*, p. 137.

155 June 24, 2009 was the date on which the Mortgage, the Note and the Pre-Auction Debt were assigned by the Bank to Mr. Leonard.

156 September 30, 2009 appears to be the date as of which accrued interest was calculated for the purpose of preparing the Memorandum in Support of Motion for Summary Judgment

Other Fees	2,000.00
TOTAL:	$1,632,901.46

> plus interest which continues to accrue at the per diem rate of $246.19 for each day from September 30, 2009 together with reasonable attorneys' fees and costs.[157]

According to my calculations, the per diem interest amount of $246.19 corresponds to an annual simple interest rate of approximately 6% (i.e., $246.19 × 365 × 100 ÷ $1,497,657.53).[158] The Deficiency Judgment provided that the per diem rate of interest for each day from June 21, 2011 (which was the date on which the judicial sale closed and title to Lot B-2 was transferred to Mr. Leonard) until entry of the Deficiency Judgment was to be $246.19 (i.e., the amount shown above), with statutory post-judgment interest at a rate of 10% per annum accruing thereafter.[159]

[101] Hence, once the Deficiency Judgment was entered with the Circuit Court, there appears to have been an increase in the interest rate.

(iv) Maturity Date

[102] The first paragraph of the Note, which was dated December 20, 2004, stated that the maturity date of the Pre-Auction Debt was June 20, 2006.[160] The Third Note Modification Agreement, which was dated June 28, 2007 but was effective as of May 31, 2007, extended the maturity date from May 31, 2007 (which presumably resulted from a previous extension or extensions made by the Note Modification Agreement dated July 31, 2006 and/or the Second Note Modification Agreement dated March 29, 2007, neither of which was put into evidence) to November 30, 2007, with an option for a further extension to May 31, 2008, provided that the Pre-Auction Debt was not in default.[161] By the time Mr. Leonard acquired the Pre-Auction Debt on June 24, 2009, the extended maturity date had long since passed.

---

and a decree of foreclosure, which Memorandum was signed on October 15, 2009. See Exhibit AR-1, vol. 1, tab 4(2), p. 61-72.

157 Exhibit AR-1, vol. 1, tab 4(2), p. 64.

158 An annual interest rate of 6% seems a bit low, particularly given the provision in the Note that provided for an additional 5% of interest to be charged in the event of a default.

159 Exhibit AR-1, vol. 2, tab 27, p. 566.

160 Exhibit AR-1, vol. 1, tab 10, p. 136.

161 Exhibit AR-1, vol. 2, tab 21, p. 550, ¶II.A.1(i) & (iii).

[103] The Deficiency Judgment does not show a maturity date. As the Pre-Auction Debt was already well past its maturity date when it was assigned to Mr. Leonard, I do not consider the absence of a maturity date in respect of the Post-Auction Debt as being a significant factor in this analysis.

(c) Resolution

[104] As indicated above, the *General Electric Capital* case identified four fundamental terms of a debt obligation, i.e., the identity of the debtor, the principal amount, the amount of interest and the maturity date. Of those four terms, the only term that was significantly different in respect of the Post-Auction Debt, than in respect of the Pre-Auction Debt, was the amount of interest. The identity of the debtor did not change. While the principal amount of the Post-Auction Debt was slightly less than the principal amount of the Pre-Auction Debt, the various items that contributed to that difference (such as debt repayments and collection expenses) were items that were built into the terms and conditions of the Pre-Auction Debt. As explained above, the maturity date was not a significant factor in this analysis.

[105] Having compared the terms of the Pre-Auction Debt and the terms of the Post-Auction Debt, I am of the view that the Post-Auction Debt did not represent the creation of a new obligation, with the result that there was not a disposition in 2011 of the Pre-Auction Debt. In other words, the Pre-Auction Debt and the Post-Auction Debt were the same debt obligation, to which I will refer hereafter (as I did initially) as the "Debt."

[106] It is my understanding that Mr. Leonard does not disagree with my view that there was not a disposition in 2011 of the Debt. In his written submissions, Mr. Leonard's counsel stated that the CRA's Interpretation Bulletin IT-448, entitled *Dispositions – Changes in Terms of Securities*, and principles of deemed disposition have no bearing on Mr. Leonard's Appeals.[162]

[107] There was no evidence or submissions as to whether there was a disposition of the Note *per se*. At times during the proceedings and in some of the documents,

---

[162] Appellant's submissions, *supra* note 49, p. 4. Interpretation Bulletin IT-448 has been archived by the CRA.

the terms *Note* and *Debt* were used interchangeably or in a manner suggesting that the Note and the Debt were coterminous. For instance, the warranties provision in the Assignment merely warranted that the assignor was the lawful owner and holder of the Note and the Mortgage, without making any reference to the Debt.[163] Similarly, the Memorandum in Support of Motion filed in the Circuit Court in respect of the foreclosure proceedings stated, "The Note is secured by that certain Mortgage, Security Agreement and Financing Statement dated December 20, 2004…."[164] Consequently, I will decide this matter on the basis that there was no disposition of the Note or the Debt in 2011.

(4) Calculation of Loss on Disposition of Mortgage[165]

[108] As explained above, in 2011 Mr. Leonard disposed of the Mortgage, but not the Note or the Debt. It therefore becomes necessary to ascertain whether the disposition of the Mortgage resulted in a gain or a loss. That, in turn, requires a determination of the cost to Mr. Leonard of the Mortgage and his proceeds of disposition.

[109] There was no specific evidence as to the amount paid by Mr. Leonard to acquire the Mortgage *per se*.[166] However, the evidence indicated that Mr. Leonard paid $1,300,000 for the Mortgage, the Note and the Debt together and that he received net proceeds in the amount of $472,746.74 from the judicial sale.[167]

[110] There was no evidence as to the manner in which the cost and the judicial sale proceeds are to be allocated among the Mortgage, the Note and the Debt. Accordingly, I have been guided by section 68 of the ITA, the relevant portion of which reads as follows:

---

163 Exhibit AR-1, vol. 1, tab 2, p. 11.

164 Exhibit AR-1, vol. 1, tab 4(2), p. 63.

165 The manner in which I have resolved these Appeals (i.e., by concluding that Mr. Leonard disposed of the Mortgage for a proportion of the net proceeds of the judicial sale) was not argued by either party. It is my view that the facts established by the evidence and the legal principles applicable thereto properly support the approach that I have taken. Furthermore, I note that in *Ferronnex Inc. and Quincaillerie Brassard Inc. v. MNR*, [1991] 1 CTC 2330, 91 DTC 559 (TCC), ¶65, Justice Tremblay stated, "The Court is never bound by the parties' legal arguments. It is always free to allow or dismiss an appeal on the basis of a legal argument that the parties have ignored or at least failed to make."

166 See paragraphs 10 and 13-16 above.

167 See paragraph 81 above.

> 68. If an amount received or receivable from a person can reasonably be regarded as being in part the consideration for the disposition of a particular property of a taxpayer, …
>
> (a) the part of the amount that can reasonably be regarded as being the consideration for the disposition shall be deemed to be proceeds of disposition of the particular property irrespective of the form or legal effect of the contract or agreement, and the person to whom the property was disposed of shall be deemed to have acquired it for an amount equal to that part;….[168]

[111] When the Bank sold the Mortgage, the Note and the Debt to Mr. Leonard on June 24, 2009 for $1,300,000, by reason of paragraph 68(a) of the ITA, the part of that amount that could reasonably be regarded as being the consideration for the disposition of the Mortgage was deemed to be the Bank's proceeds of disposition of the Mortgage, and Mr. Leonard was deemed to have acquired the Mortgage for an amount equal to that part. Similarly, the part of that amount that could reasonably be regarded as being the consideration for the disposition of the Note and the Debt was deemed to be the Bank's proceeds of disposition of the Note and the Debt, and Mr. Leonard was deemed to have acquired the Note and the Debt for an amount equal to that part. Thus, it becomes necessary to determine a reasonable allocation of the $1,300,000 consideration between the Mortgage on the one hand and the Note and the Debt on the other.

[112] There was no specific evidence that expressly addressed such allocation; however, Mr. Leonard did provide evidence concerning Mr. Anderson's unfavourable financial situation. During cross-examination, Mr. Leonard testified that, in April 2007, Mr. Anderson stopped paying interest on a particular loan that had been made to him by Mr. Leonard in 2006 and that subsequently became uncollectible. Mr. Leonard was aware that the world financial crisis between 2007 and 2009 had affected mortgages and real property in the United States.[169] By 2009, Mr. Anderson was in financial distress and not paying his debts.[170] Mr. Leonard understood that in 2009 or thereabouts Mr. Anderson had judgments, with an aggregate amount in excess of $40,000,000, against him.[171] The Bank sold the Mortgage, the Note and the Debt to Mr. Leonard because the Debt was

---

168 In 2009 the opening word of section 68 of the ITA was *Where*, rather than *If*. Section 68 was amended in 2013, with retroactive effect to February 27, 2004, so as to replace *Where* with *If*, as shown above.

169 *Transcript*, vol. 1, p. 60, lines 4-24.

170 *Transcript*, vol. 1, p. 61, lines 4-6.

171 *Transcript*, vol. 1, p. 67, lines 20-21.

uncollectible.[172] Consequently, when Mr. Leonard purchased the Mortgage, the Note and the Debt, he did not expect that Mr. Anderson would pay monthly interest payments or anything like that in respect of the Debt.[173] When Mr. Leonard purchased the Mortgage, the Note and the Debt from the Bank, the Mortgage was already in foreclosure.[174] Thus, it is my view that on June 24, 2009 the fair market value of the Mortgage was substantially greater than the fair market value of the Note and the Debt.[175]

[113] It is my understanding that the Crown is not suggesting that the Note or the Debt had any value. In his opening statement, counsel for the Crown stated:

> Now, I appreciate the facts are –- and they're not in dispute –- *no one was going to pay that debt*, but the legal effect of that in the *Act* has to be dealt with….
>
> That's our submission and that's what we will prove on the evidence because there was never an intention to profit on this debt. *This debt was never going to pay anything close to face value, especially in the circumstance,* but the whole purpose of entering the transaction was to acquire very valuable property in the context of the 2009 world financial crisis when assets were going below value….
>
> Whether the appellant subjectively and –- and factually knew this note –- *this promissory note post-mortgage and this deficiency judgment post-mortgage are worthless*, I don't doubt. I don't doubt that subjective understanding. We'll hear a lot of evidence that the appellant was quite familiar with the debtor's situation and this wasn't a surprise to him….[176] [*Emphasis added*.]

[114] My view that most of the consideration paid by Mr. Leonard to the Bank should be allocated to the Mortgage is consistent with the Crown's theory of the case. During oral submissions, counsel for the Crown stated:

---

172 *Transcript*, vol. 1, p. 62, lines 8-11.

173 *Transcript*, vol. 1, p. 68, lines 20-23.

174 *Transcript*, vol. 1, p. 62, lines 6-7.

175 A further point to note is that Mr. Leonard understood that many judgments had been granted against Mr. Anderson in favour of other creditors before Mr. Leonard obtained the Deficiency Judgment, such that Mr. Leonard considered that the Deficiency Judgment was not of any value (*ibid*, p. 85, lines 6-8). Although the Deficiency Judgment was obtained in 2011, such that Mr. Leonard's comment was not necessarily applicable to 2009, the comment does give some indication as to the continuing extent of Mr. Anderson's financial difficulties.

176 *Transcript*, vol. 1, p. 27, lines 7-10; p. 28, lines 4-11; and p. 33, lines 18-24.

> … the *viva voce* evidence of the Appellant, though contradictory at times, when viewed in its entirety demonstrates that the Appellant purchased the note and mortgage with the intention of obtaining title to the underlying real property….[177]
>
> The debt was a throw-away. It was thrown in here by the bank and they weren't worried about it, they weren't going to go for it….[178]
>
> Now, with regard to the documentary evidence that this Court has available to it, it also demonstrates that the purchase of the loan was only a part of a global transaction to acquire real property….[179]
>
> It just illustrates this confusion that comes from the Appellant's evidence and even from his counsel that the transaction was about the real property. The mortgage was a part, a feature, a tool, a method of acquiring this….[180]

[115] Although there was no expert valuation evidence presented at the hearing, given the circumstances described in the factual evidence that was provided, particularly the financial distress in which Mr. Anderson found himself in 2009, the Bank's inability to collect the Debt, necessitating the commencement of foreclosure proceedings in respect of the Mortgage, the recognition that the continuation of the foreclosure proceedings was the only viable method for the Bank initially (or Mr. Leonard subsequently) to recover anything in respect of the Note or the Debt, and the understanding that, apart from Lot B-2, which was subject to the Mortgage, no other assets of Mr. Anderson were available to satisfy the Note or the Debt, it is reasonable to allocate almost all of the consideration (i.e., $1,300,000) received by the Bank to the Mortgage, with only a nominal portion of that consideration being allocated to the Note and the Debt. In numerical terms, it is reasonable to allocate 99.9% of the consideration to the Mortgage, and 0.1% of the consideration to the Note and the Debt. Therefore, I am of the view that $1,298,700, (i.e., 99.9% of $1,300,000) should be allocated to the Mortgage, and $1,300 (i.e., 0.1% of $1,300,000) should be allocated to the Note and the Debt.

[116] It is also my view that, to achieve symmetry, the same proportion (i.e., 99.9%) that was used to allocate the purchase consideration to the Mortgage should also be used to allocate a portion of the proceeds of the judicial sale to the

---

177 *Transcript,* vol. 2, p. 32, lines 16-20.

178 *Transcript,* vol. 2, p. 53, lines 19-22.

179 *Transcript,* vol. 2, p. 67, lines 2-5.

180 *Transcript,* vol. 2, p. 102, lines 16-20. In fairness, counsel for the Crown also stated, "There was no thought about this mortgage being the investment. It was, by his [Mr. Leonard's] own admission –- it wasn't worth much." See *Transcript,* vol. 2, p. 110, lines 6-8.

Mortgage. As the net proceeds of the judicial sale were $472,746.74 (i.e., the judicial sale price of $500,000 less expenses of $27,253.26), the amount of Mr. Leonard's proceeds of disposition in respect of the Mortgage was $472,273.99 (i.e., 99.9% of $472,746.74), which I have rounded to $472,274.

[117] Using the formula set out by Justice Major in *Friesen*, as shown in paragraph 82 above, Mr. Leonard's loss in respect of the disposition of the Mortgage is calculated as follows:

> Income = Profit = Sale Price − Purchase Cost
>
> Income = $472,274 − $1,298,700
>
> Income = −$826,426

Accordingly, I am of the view that the amount of the Loss sustained by Mr. Leonard on the disposition of the Mortgage in 2011 was $826,426.

VI. **CONCLUSION**

[118] I have concluded that, in 2011, Mr. Leonard disposed of the Mortgage, in the context of an adventure in the nature of trade, resulting in a non-capital loss in the amount of $826,426.[181] Subject to the next paragraph, Mr. Leonard's Appeals are allowed and the Reassessments are referred back to the Minister for reconsideration and reassessment in accordance with the finding set out in the preceding sentence.

[119] When Mr. Leonard filed his 2011 income tax return, he showed the amount of the Loss as $1,472,006, which is significantly greater than the amount of the Loss that I have calculated. Mr. Leonard applied portions of the Loss, as calculated by him, to his 2012, 2013 and 2014 taxation years. As I do not have any information concerning the amounts that would otherwise be Mr. Leonard's income for 2011, 2012, 2013 and 2014, the Parties will need to determine the extent to which the Loss in the amount of $826,426 may be applied in respect of those four taxation years.

---

[181] The result in these Appeals will be tempered by the income tax consequences whenever Mr. Leonard eventually disposes of Lot B-2, as any gain or loss in respect of that disposition will be calculated by reference to an initial cost to Mr. Leonard of Lot B-2 of $499,500 (i.e., 99.9% of $500,000, and not $1,300,000).

[120] As the amount of the Loss (i.e., $826,426) is greater than the amount of the family income (i.e., $496,733) recalculated by the CRA for the purposes of Ms. Tenney's CCTB for 2011, her Appeal is allowed, with costs.

[121] As Mr. Leonard was successful in proving that in 2011 he engaged in an adventure in the nature of trade and that he incurred the Loss, he is entitled to costs. However, as the amount of the Loss is approximately 56% of the amount claimed on his 2011 income tax return, he was only partially successful, which may be a relevant factor to consider in determining the amount of his costs. If the Parties are unable to reach an agreement in respect of costs within 30 days from the date of the Judgment pertaining to these Appeals, Mr. Leonard and Ms. Tenney may, within the ensuing 30 days thereafter, file a written joint submission on costs, and the Crown shall thereafter have yet a further 30 days to file a written response. Any such submissions shall be limited to five pages in length. If, within the applicable time limits, the Parties do not advise the Court that they have reached an agreement and no submissions are received from the Parties, one set of costs (adjusted to recognize the need for a separate Notice of Appeal for each Appellant), in accordance with the Tariff, shall be awarded to Mr. Leonard and Ms. Tenney together (to be apportioned between them as they so determine).

Signed at Edmonton, Alberta, this 30th day of April 2021.

"Don R. Sommerfeldt"

Sommerfeldt J.

CITATION:	2021 TCC 33
COURT FILE NOS.:	2017-221(IT)G, 2017-219(IT)G
STYLE OF CAUSE:	JEREMY LEONARD AND HER MAJESTY THE QUEEN and CAROL TENNEY AND HER MAJESTY THE QUEEN
PLACES OF HEARING:	Winnipeg, Manitoba and Ottawa, Ontario
DATES OF HEARING:	June 28, 2019 and October 3, 2019
DATE OF SUBMISSIONS:	July 15, 2020
REASONS FOR JUDGMENT BY:	The Honourable Justice Don R. Sommerfeldt
DATE OF JUDGMENT:	April 30, 2021

APPEARANCES:

Counsel for the Appellants:	Jeff D. Pniowsky, Matthew Dalloo
Counsel for the Respondent:	David Silver, David Grohmueller

COUNSEL OF RECORD:

For the Appellant:

Name:	Jeff D. Pniowsky, Matthew Dalloo
Firm:	Thompson Dorfman Sweatman LLP

For the Respondent:	Nathalie G. Drouin Deputy Attorney General of Canada Ottawa, Canada