Docket: 2014-3040(IT)I

BETWEEN:

LISE GABOURY,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on July 15, 2015, at Montréal, Quebec.

Before: The Honourable Justice Dominique Lafleur

Appearances:

Agent for the appellant:	Jacques Dagenais
Counsel for the respondent:	Anne-Marie Boutin

JUDGMENT

The appeal from the reassessment made under the *Income Tax Act* for the 2008 taxation year is dismissed.

Signed at Ottawa, Canada this 1st day of October 2015.

"Dominique Lafleur"

Lafleur J.

Translation certified true
On this 10th day of November 2015
Margarita Gorbounova, Translator

Citation: 2015 TCC 235
Date: 20151001
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BETWEEN:

LISE GABOURY,

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and

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Respondent.

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REASONS FOR JUDGMENT

Lafleur J.

[1] The appellant has been a Court of Québec judge since 1996.

[2] In 2008, she received a retroactive salary payment of $153,375, as well as a sum of $25,473.02 from the government of Quebec (the Government); the Canada Revenue Agency (CRA) characterized the $25,473.02 as interest to be included in the appellant's income under paragraph 12(1)(*c*) of the *Income Tax Act* (the Act). The Government issued a T5 slip for the same amount characterizing it as interest from Canadian sources.

[3] The appellant disputes the fact that a part of that amount, namely, $22,290.49, representing the interest for the pre-judgment period, should be included in her income under the Act and argues that that amount represents non-taxable damages paid by the Government for failing to comply with its constitutional obligations.

I. Facts

[4] On March 21, 2001, in accordance with section 246.29 of the *Courts of Justice Act* (CJA) (R.S.Q., c. T-16), the Government appointed, for a three-year

term, the members of the judicial compensation committee for the Court of Québec and municipal courts, chaired by M.J. Vincent O'Donnell, Counsel. The mandate of the committee, referred to as the O'Donnell Committee, was, among other things, to assess whether the salary, pension plan and other social benefits of the Court of Québec judges were adequate; the assessment covered the period from July 1, 2001, to June 30, 2004.

[5] In September 2001, the O'Donnell Committee's report (the Report), given to Quebec's Minister of Justice, recommended, among other things, a 31% salary increase for 2001 so that the Court of Québec judges' salary would be $180,000 as of July 1, 2001, $182,000 as of July 1, 2002, plus the consumer price index (CPI) in effect at that time, and another $2,000 salary increase on July 1, 2003, plus the CPI in effect at that time.

[6] On October 18, 2001, the Report was tabled at the National Assembly.

[7] On December 13, 2001, the Government tabled with the National Assembly what would be its first response to the O'Donnell Committee's recommendations (the First Response), which rejected the recommendations in the Report, among other things, with respect to judges' remuneration, and proposed instead an 8% increase of said remuneration for 2001, a 2.5% increase for 2002, and 2% increase for 2003.

[8] On December 18, 2001, the National Assembly approved the First Response without amendment.

[9] In February 2002, the Court of Québec judges filed with the Superior Court a *sui generis* motion against the Quebec Attorney General and Minister of Justice to review the First Response and the National Assembly's resolution because, according to the moving party, the First Response and the National Assembly's resolution (and its follow-up order) were unlawful, lacked a rational basis and were unconstitutional in that they violated the CJA and infringed on judicial independence.

[10] In a judgment dated April 17, 2003 (No. 500-05-0703510926), the Honourable Jean Guibault, J.S.C., allowed the motion, stated that the First Response and the National Assembly's resolution approving it as well as any follow-up order were unconstitutional because they did not meet the standard of simple rationality, ordered the Government and the Minister of Justice to follow and to implement without delay all of the recommendations in the Report and

stated that the Government and the Minister of Justice had to pay to each of the Court of Québec judges in office during the relevant period the difference between the salary that they should have been paid under his judgment and their salary during that period, with interest at the legal rate from the date the amounts were owing until the date of judgment.

[11] In a judgment dated May 31, 2004 (No. 500-090013406-038), the Quebec Court of Appeal dismissed the Government's appeal, but did, however, amend the date from which interest had to be calculated, namely, February 2002, when the Government would have been able to pay the amounts owing had its response to the O'Donnell Committee's recommendations been positive, namely, seven months after the start of the new remuneration period that had begun on July 1, 2001.

[12] On July 22, 2005,[1] the Supreme Court of Canada dismissed the Government's appeal (the Appeal). The country's highest court confirmed that the First Response did not comply with the simple rationality standard with which the Government's responses must comply because the Government did not provide any rational reasons justifying the rejection of the recommendations in the Report. However, the Supreme Court found as follows with respect to the appropriate remedy:

> 44. In light of these principles, if the commission process has not been effective, and the setting of judicial remuneration has not been "depoliticized", then the appropriate remedy will generally be to return the matter to the government for reconsideration. If problems can be traced to the commission, the matter can be referred back to it. Should the commission no longer be active, the government would be obliged to appoint a new one to resolve the problems. Courts should avoid issuing specific orders to make the recommendations binding unless the governing statutory scheme gives them that option. This reflects the conclusion in *Mackin v. New Brunswick (Minister of Finance)*, [2002] 1 S.C.R. 405, 2002 SCC 13, that it is "not appropriate for this Court to dictate the approach that should be taken in order to rectify the situation. Since there is more than one way to do so, it is the government's task to determine which approach it prefers" (para. 77).
>
> . . .

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[1] *Provincial Court Judges' Assn. of New Brunswick v. New Brunswick (Minister of Justice); Ontario Judges' Assn. v. Ontario (Management Board); Bodner v. Alberta; Conférence des juges du Québec v. Quebec (Attorney General); Minc v. Quebec (Attorney General)*, 2005 SCC 44, [2005] 2 S.C.R. 286.

> 171. For these reasons, we would dismiss the Attorney General's appeals with costs. However, those portions of the orders below which are not in accordance with these reasons must be set aside and the matter must be remitted to the Government and the National Assembly for reconsideration in accordance with these reasons. . . .

[13] The Supreme Court noted that, although the judicial compensation committees' recommendations were not binding, the purpose of putting the committees in place was to effectively settle the issue of judicial salaries and other related issues.

[14] Following the Supreme Court judgment, the Government therefore tabled a second response (the Second Response) to the Report on March 22, 2006. On April 5, 2006, the National Assembly passed a resolution confirming the Second Response.

[15] The Court of Québec judges filed with the Superior Court a second [TRANSLATION] "*sui generis* motion in the nature of an evocation of a government decision and of a National Assembly resolution and in the nature of an injunction to compel the implementation of the O'Donnell report of the judicial compensation committee for the Court of Québec and municipal courts".

[16] On June 4, 2007, the Honourable Justice Claude Auclair of the Superior Court allowed the motion and ordered the Government to implement the O'Donnell Committee's recommendations by September 1, 2007, at the latest, and to pay interest at the legal rate starting on February 1, 2002, until the payment date (the Auclair judgment). Justice Auclair acknowledged that the Supreme Court had established the principle that a court dealing with a judicial review should not intervene and that an appropriate remedy is generally to refer the matter back to the Government for reconsideration. However, since this is an exceptional situation, the judge therefore disregarded this general principle in rendering his decision.

[17] The Government did not appeal the Auclair judgment. Rather, the Government implemented the recommendations in the Report and paid interest at the legal rate starting on February 1, 2002, on the difference between the salary actually received by the judges and that proposed in the Report.

II. Issue

[18] It must be determined whether the amount of $22,290.49 received by the appellant during the 2008 taxation year must be included in her income under the Act.

III. Parties' positions

[19] The appellant included in her income the amount of interest thus received and deducted $22,290.49 as non-taxable interest, because, according to her, that amount was paid by the Government as non-taxable damages for failing to comply with its constitutional obligations regarding the appellant. That amount represents interest calculated on an amount equal to the difference between the salary recommended in the Report and the salary actually received by the appellant for the period from February 1, 2002, to June 4, 2007, that is, the date on which the Auclair judgment was rendered.

[20] The respondent is of the view that the $22,290.49 represents interest that is fully taxable under paragraph 12(1)(*c*) of the Act. If that is not the case, the amount then represents damages the tax treatment of which follows the treatment of the principal, that is, the salary paid retroactively, in accordance with the *surrogatum* principle, and, therefore, that amount is also fully taxable.

IV. The Act and analysis

[21] Paragraph 12(1)(*c*) of the Act reads as follows:

> 12. (1) There shall be included in computing the income of a taxpayer for a taxation year as income from a business or property such of the following amounts as are applicable
>
> . . .
>
> (c) subject to subsections (3) and (4.1), any amount received or receivable by the taxpayer in the year (depending on the method regularly followed by the taxpayer in computing the taxpayer's income) as, on account of, in lieu of payment of or in satisfaction of, interest to the extent that the interest was not included in computing the taxpayer's income for a preceding taxation year;

[22] The word "interest" is not defined in the Act; the ordinary meaning of this word as defined in dictionaries as well as its definition by the courts must therefore be examined.

[23] According to *Le Petit Robert de la langue française* (2015 edition) the word "intérêt" is defined as "la somme qui rémunère un créancier pour l'usage de son argent par un débiteur pendant une période déterminée".

[24] According to the *Oxford Dictionary of English*, the word "interest" is defined as "money paid regularly at a particular rate for the use of money lent, or for delaying the repayment of a debt".

[25] Justice Reed concluded in *Brenda J. Miller v. The Queen*, (1986) 1 F.C. 382, that, in order for an amount to be reported as interest within the meaning of the Act: (1) it must be calculated on a day-by-day accrual basis; (2) it must be calculated on a principal sum or a right to a principal sum; and (3) it must be compensation for the use of the principal sum or the right to the principal sum.

[26] Justice Reed cited the comments of Justice Rand in *Reference as to the Validity of Section 6 of the Farm Security Act, 1944 of Saskatchewan*, [1947] S.C.R. 394, at pages 411 and 412:

> The Defendant relies on Mr. Justice Rand's definition of interest in *Reference re Validity of Section 6 of the Farm Security Act, 1944, of the Province of Saskatchewan,* [1947] S.C.R. 394 at pp. 411-412 for this contention:
>
> > Interest is, in general terms, the return or consideration or compensation for the use or retention by one person of a sum of money, belonging to, in a colloquial sense, or owed to, another. There may be other essential characteristics but they are not material here.
> >
> > The relation of the obligation to pay interest to that of the principal sum has been dealt with in a number of cases...from which it is clear that the former, depending on its terms, may be independent of the latter, or that both may be integral parts of a single obligation or that interest may be merely accessory to principal.
> >
> > But the definition, as well as the obligation, assumes that interest is referrable to a principal in money or an obligation to pay money. Without that relational structure in fact and whatever the basis of calculating or determining the amount, no obligation to pay money or property can be deemed an obligation to pay interest.

> I do not find Mr. Justice Rand's comments go so far as the Defendant contends. Those comments to me merely say that in determining whether a certain amount is interest it is crucial to consider to what it relates. If it is paid in reference to "a principal in money or an obligation to pay money" then a relational structure exists which indicates that the sum is interest. In the present case the sum was paid in reference to a principal sum – that part of the Plaintiff's salary to which she had become entitled during the 1980 year but which had not been paid to her during that time. In my view Mr. Justice Rand's decision does not address the issue raised by the Defendant.

[27] Thus, for an amount to be characterized as interest, among other things, a principal, a right to a principal or a debt must exist. The other criteria for the definition of interest are not at issue in this case.

[28] In this case, is the Government in debt to the judges of the Court of Québec (including the appellant) and, if so, when did the debt come into existence?

[29] The appellant is of the view that no amount of money was owed to her before July 3, 2007, on which date the Government agreed to pay the judges in accordance with the Report's recommendations. The appellant considered this to be a third response to the Report, and because the Government never made this third response, the Court of Québec judges were not entitled to a salary increase.

[30] However, I cannot agree with the appellant's argument.

[31] The Supreme Court found in the Appeal, *supra*, that the litigation before the Quebec courts regarding the First Response to the Report resulted in the quashing of the First Response. It stated the following:

> 152. The outcome of the litigation in the Quebec courts was that the Response was quashed. The Superior Court and the Court of Appeal held in their judgments that the Response did not meet the test of rationality. The Government would have been required to implement the O'Donnell Committee's first 11 recommendations if the judgments had not been appealed to our Court.

[32] The quashing of the First Response also resulted in the quashing of the National Assembly's resolution approving the First Response and any orders related to it.

[33] Thus, if we apply the Supreme Court's reasoning, the Second Response and the National Assembly's resolution approving it were also quashed given that, on

June 4, 2007, the Honourable Justice Claude Auclair of the Superior Court found them to be unconstitutional in the Auclair Judgment.

[34] In addition, it cannot be claimed that the fact that the Government decided to implement the Report's recommendations in July 2007 represented a third response. The Government is not obliged to provide responses to judicial compensation committees' reports; it can simply table the report at the National Assembly within the time limit prescribed by the CJA. Sections 246.43 and 246.44 of the CJA provide as follows:

> Chapter T-16
>
> *COURTS OF JUSTICE ACT*
>
> 246.43. The committee shall make a report to the Government containing the recommendations it considers appropriate. The report must be filed within six months from the date on which the committee members were appointed or, where the committee exercises its functions under the third paragraph of section 246.29, within six months from the date on which the proposed change was submitted to the committee.
>
> Tabling. The Minister of Justice shall table the report in the National Assembly within 10 days of receiving it if the Assembly is sitting or, if it is not sitting, within 10 days of resumption.
>
> 246.44. The National Assembly may approve, amend or reject some or all of the committee's recommendations, by way of a resolution stating the reasons on which it is based. The Government shall take, with diligence, the necessary steps to implement the resolution in accordance with this Act or the Act respecting municipal courts (chapter C-72.01).
>
> Alternate implementation.
>
> If the National Assembly fails to adopt a resolution on or before the thirtieth day of sitting following the day on which the committee's report is tabled, the Government must take, with diligence, the necessary steps to implement the recommendations in accordance with this Act or the Act respecting municipal courts.
>
> [Emphasis added.]

[35] Under section 246.44 of the CJA, if the National Assembly does not adopt the resolution on the 30th day of sitting following its tabling, the Government must take, with diligence, the necessary steps to implement the recommendations.

[36] In this case, the Report was tabled at the National Assembly in October 2001. Since the First Response and the Second Response did not meet the rationality standard, they are null as are the National Assembly's resolutions approving them and any orders related to them. Given the provisions of section 246.44 of the CJA, the Government had to implement the recommendations in the Report with diligence after the time limit of 30 days following the tabling of the Report in October 2001.

[37] Therefore, I find that the Government was in debt to the Court of Québec judges (including the appellant) as of the end of 2001 or early 2002, and the debt represented the difference in salary between the judges' salary set out in the Report and that actually paid by the Government. My finding is also consistent with the findings in the Auclair judgment, which ordered that the amounts owed to the Court of Québec judges be repaid:

> [TRANSLATION]
>
> 152. DECLARES that the Government of Quebec and the Minister of Justice must reimburse and pay each of the judges concerned, who served as judges at any time during the period between July 1, 2001, and today, including adjustments for those who held an administrative office, the amount representing the difference between the salaries to be paid under this judgment and the amount of their salaries during that period, with interest at the legal rate starting in February 2002 and until the payment date.
>
> [Emphasis added.]

[38] I must now determine whether the interest paid to the appellant by the Government on the Government's debt to her should be included in her income.

[39] In *Eaton v. Canada*, [2008] F.C.J. No. 687, the Federal Court of Appeal found that the interest paid in relation to a retroactive salary increase granted as part of pay equity was taxable as interest.

[40] In *Montgomery v. Canada* [2007] 5 CTC 2081, Justice Woods of our Court had to determine whether an amount characterized as interest by the CRA constituted interest under the Act. The appellant in that case received a retroactive salary payment with interest on wages paid retroactively as part of a pay equity dispute. Justice Woods found that interest thus paid was interest from property (the property being the right to fair compensation) under the Act and that the meaning of the word "interest" in paragraph 12(1)(*c*) should not be limited to situations involving the borrowing of money (para. 21).

[41] In *Coughlan v. Canada*, [2001] T.C.J. No. 449, Judge Bowie of our Court had to determine the nature of an amount received as pre-judgment interest. He quoted Justice Rand in *Farm Security Act* in order to determine the meaning of the word "interest". He also referred to *Huston, Whitehead and Whitehead v. M.N.R.*, 61 DTC 1233, in which the nature of interest paid under legislation compensating Canadians for the loss of property located abroad during World War II had to be determined. Judge Bowie made the following comments with respect to *Huston*:

> 15 In *Huston, Whitehead and Whitehead v. M.N.R.*, Thurlow J. had to consider whether "interest" paid under the *War Claims Regulations* fell within the provisions of paragraph 6(1)(*b*), the predecessor to the present paragraph 12(1)(*c*). Those Regulations made provision for the payment of compensation to persons for loss of property as a result of World War II. The Regulations specifically provided that they conferred no right of payment; they simply gave authority to make a discretionary payment from the War Claims Fund. They also provided that "interest ... may be paid ...". After considering *Riches v. Westminster Bank*, *Glenboig Union Fireclay Ltd. v. C.I.R.*, *C.I.R. v. Ballantyne* and *Simpson v. Executors of Bonner Maurice*, Thurlow J. concluded that the real question to be decided is "... whether the amounts in question are of an income or a capital nature". He concluded that in the case before him, the amounts awarded as interest, along with the compensation, were not of an income nature and, therefore, were not interest within the meaning of section 6 of the *Income Tax Act*. This was so because no principal sum was owing to the Appellants at any time. They had no right to compensation, and they sustained no loss of revenue for which they could be entitled to either damages or compensation. *Bellingham v. The Queen* is another case which demonstrates that not all statutory interest payments are received on income account. Under subsection 66(4) of the *Alberta Expropriation Act*, the Land Compensation Board may award "additional interest" along with the compensation and interest otherwise payable, if the expropriating authority's proposed payment to an expropriated owner is less than 80% of the amount the Board awards for compensation. The Federal Court of Appeal held that this "additional interest", being in the nature of a penalty imposed on the authority, does not assume the character of income in the hands of the owner.

[42] Judge Bowie found that the pre-judgment interest that was awarded as interest on wrongfully withheld determined amounts rather than as incremental damages had the character of income and was taxable under paragraph 12(1)(*c*) of the Act.

[43] In my view, in light of the above decisions, the amount of $22,290.49, the tax treatment of which is at issue in this case, is interest within the meaning of the Act and must therefore be included in the appellant's income under

paragraph 12(1)(*c*) of the Act for the 2008 taxation year. In addition, no deduction in this regard is allowed in computing the appellant's income under the Act.

[44] Even if the $22,290.49 were determined to not constitute "interest" within the meaning of the Act, but rather constituted damages paid to the appellant by the Government, I am of the view that, based on the *surrogatum* principle, that amount should be added to the appellant's income for the 2008 taxation year as special damages awarded to compensate the appellant for not being paid the additional salary provided in the Report during the period from July 1, 2001, to June 30, 2004. Thus, since the unpaid salary is a taxable salary under section 5 of the Act, the damages compensating the appellant with respect to that salary should receive the same tax treatment and are thus taxable under the Act.

[45] In *Cloutier-Hunt v. Canada*, 2007 TCC 345, the Court had to determine the nature of an amount received as interest as part of a retroactive salary payment made as pay equity. Justice Webb stated the following:

> 6. Even if the amount were to be construed as damages, the question would then become whether the amount would still be included in income. In *Transocean Offshore Limited v. R.*, 2005 FCA 104, [2005] 2 C.T.C. 183, 2005 DTC 5201, Sharlow J.A. of the Federal Court of Appeal stated as follows:
>
> > For the purposes of Part I of the *Income Tax Act*, the answer to that question requires the application of a judge-made rule, sometimes called the "*surrogatum* principle", by which the tax treatment of a payment of damages or a settlement payment is considered to be the same as the tax treatment of whatever the payment is intended to replace.
>
> 7. Even if the amount described as "interest" were to be construed as damages, the application of the *surrogatum* principle would require that the tax treatment of the amount paid as damages should be the same as the payment it is intended to replace. In any event, I do not find that the amount described as "interest" was paid as damages as paragraph 10 of the Orders issued by the CHRT clearly states that interest is to be paid and the amount in question is the amount paid as the interest as provided in the Orders of the CHRT.

[46] As mentioned above, the appellant stated that the Government paid her interest to compensate her for a tort, namely, the unconstitutional actions taken by the Government in drafting the First Response and the Second Response. Thus, applying the principle in *Ahmad v. Canada*, [2002] T.C.J. No. 471, the appellant is of the view that the amounts representing pre-judgment interest are not taxable. However, I am of the view that that decision does not apply to this case because

that case dealt with damages claimed for inducement to breach a contract of employment and thus a tort, including pre- and post-judgment interest; Judge Miller of our Court found that they were general damages resulting from a tort, not from a contract, and that the pre-judgment interest was part of the damages and was not taxable under paragraph 12(1)(*c*) of the Act. In this case, the Government did not commit a tort; it did not meet the rationality standard in its First Response and Second Response. This cannot, in my opinion, be characterized as a tort.

[47] I am also of the view that the purpose of the $22,290.49 was not to compensate the appellant for general damages, that is, damages for physical or psychological pain and suffering, which would normally not be taxable.[2]

[48] For all these reasons, this appeal is dismissed.

Signed at Ottawa, Canada this 1st day of October 2015.

"Dominique Lafleur"

Lafleur J.

Translation certified true
On this 10th day of November 2015
Margarita Gorbounova, Translator

[2] *Morency v. Canada*, 2003 TCC 633, affirmed on appeal by the Federal Court of Appeal 2005 FCA 16.

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APPEARANCES:

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Counsel for the respondent:	Anne-Marie Boutin

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