Docket: 2017-961(IT)I

BETWEEN:

MARTHE GAUDETTE,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on June 12, 2018, in Sherbrooke, Quebec.

Before: The Honourable Justice Réal Favreau

Appearances:

For the Appellant:	The Appellant herself
Counsel for the Respondent:	Grégoire Cadieux

JUDGMENT

The appeal from the reassessment under the *Income Tax Act* dated February 3, 2017, for the Appellant's 2014 taxation year is allowed and the reassessment is referred to the Minister of National Revenue for reconsideration and reassessment in order to award the Appellant the amount of $116,277 granted by the Minister as a business investment loss for her 2014 taxation year as per the attached reasons for judgment.

Signed at Montreal, Canada, this 30th day of October 2018.

"Réal Favreau"

Favreau J.

Citation: 2018 TCC 208
Date: 20181030
Docket: 2017-961(IT)I

BETWEEN:

MARTHE GAUDETTE,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

REASONS FOR JUDGMENT

Favreau J.

[1] Ms. Marthe Gaudette is appealing a reassessment made by the Minister of National Revenue (the "Minister") under the *Income Tax Act* R.S.C. (1985), c. 1 (5th Supp.), as amended (the "Act"), dated February 3, 2017, regarding the Appellant's 2014 taxation year.

[2] Under the reassessment of February 3, 2017, the Minister denied the Appellant the $430,000 amount that she had claimed as a business investment loss (hereinafter "BIL") for her 2014 taxation year.

[3] The amount claimed as a BIL arises from the following loans made by the Appellant to the corporation *L'Agora, Recherches et Communications Inc*. (hereinafter the "Corporation") during the 1996 to 2000 taxation years, totalling $305,000.

Date	Amount
1996-11-28	$50,000
1997-07-29	$25,000
1997-08-27	$25,000
1998-06-15	$25,000
1998-09-01	$10,000

1998-12-11	$20,000
1999-01-26	$10,000
1999-03-12	$20,000
1999-06-21	$20,000
1999-10-28	$15,000
1999-12-16	$25,000
2000-01-14	$40,000
2000-01-18	$20,000
Total	$305,000

[4] At the stage of opposing the initial assessment of June 11, 2015, for the 2014 taxation year, the Appellant confirmed that her BIL was $305,000, not $610,000 as reported, and she requested an additional amount of $125,000 in connection with a loan that she had made to the Corporation on October 6, 2005.

[5] The Minister denied the loss claimed as a BIL because the loans made by the Appellant to the Corporation did not involve any interest or repayment terms and because the Corporation had not had any revenue-generating activities for several years.

[6] At the hearing, Counsel for the Respondent acknowledged the existence of the Appellant's debt to the Corporation and acknowledged that it became a bad debt in 2014.

[7] Ms. Gaudette testified at the hearing and explained the circumstances around the granting of loans to the Corporation. She worked for about 20 years in the field of primary, secondary and college education and for 5 years in Quebec's Ministry of Education doing, among other things, text editing of school programs. She has been retired since 1978 and receives a pension income based on her years of work as an employee of the Government of Quebec.

[8] Over the course of her working life and during her retirement, in other words for over 50 years, Ms. Gaudette has made numerous stock transactions that have enabled her to accumulate a significant amount of capital. The earnings made in the stock market enabled Ms. Gaudette to make the loans and margin loans to the Corporation whose cause she had taken up. Her motivation was to help combat the ignorance that is the source of all ills on earth.

[9] The Corporation publishes a quarterly Quebec magazine established in 1993 called *L'Agora* and, since 1998, has been running an online encyclopedia called the *Encyclopédie de l'Agora*.

[10] The Corporation's shareholders are Mr. Jacques Dufresne and his spouse, Ms. Hélène Laberge, who hold 55% and 45%, respectively, of the capital stock of the Corporation.

[11] Ms. Gaudette acknowledged that the loans she had made to the Corporation between 1996 and 2000 in the amount of $305,000 were without interest or repayment terms and that she had no documentation showing that the amounts advanced were loans to the Corporation.

[12] The above-mentioned fund transfers were made by personal cheques from Ms. Gaudette made out to Hélène Dufresne or Hélène Laberge, in other words by cheques made out to the Appellant drawn on her margin account and endorsed by the latter for depositing into the bank account of Jacques Dufresne and Hélène Laberge. In fact, the amounts thus advanced by Ms. Gaudette were never recorded in the Corporation's books.

[13] Ms. Gaudette had to pay interest on the withdrawals from her margin account, but she has never received any principal or interest repayments from the Corporation.

[14] According to the correspondence between Ms. Gaudette and Mr. Jacques Dufresne, it appears that the Corporation's shareholders considered Ms. Gaudette to be a generous patron of the work of *L'Agora, Recherches et Communications Inc.* Also, Ms. Gaudette acknowledged performing services for the Corporation for four years doing text editing for the encyclopedia and for two years as the person in charge of the library that the Corporation opened in North Hatley, without receiving any pay.

[15] Regarding the $125,000 loan made by Ms. Gaudette to the Corporation on October 6, 2005, Ms. Gaudette demonstrated that:

a) Mr. Jacques Dufresne and Ms. Hélène Laberge had signed an acknowledgement of debt on behalf of the Corporation in the amount of $125,000;

b) that loan bore an interest rate of 6% per year that could be renewed annually at the prime rate in effect plus one percent (1%) and was repayable via monthly payments of $940, starting December 1, 2005;
c) that loan was entered as long-term debt on the Corporation's financial statements and,
d) the outstanding balance on that loan was $116,277 at August 31, 2014, the end of the Corporation's fiscal year.

[16] Ms. Gaudette also demonstrated that she had retained the services of a lawyer for obtaining repayment of the principal of the loans totalling $305,000, as well as the balance of the principal of the $125,000 loan and the outstanding interest on that loan.

[17] The Respondent denied the deduction of a BIL on the $305,000 loaned by the Appellant because those loans were not made to the Corporation for the purpose of earning property income pursuant to subparagraph 40(2)(g)(ii) of the Act. However, the Respondent conceded at the hearing that the $125,000 loan made by the Appellant in 2005 to the Corporation had been for the purpose of earning property income and, therefore, allowed the deduction of a BIL on the unpaid balance of the loan at December 31, 2014, in the amount of $116,277.

[18] The relevant provisions of the Act for determining entitlement to a BIL are reproduced below:

Sub-division c - Taxable Capital Gains and Allowable Capital Losses

For the purposes of this Act,

[…]

(c) a taxpayer's allowable business investment loss for a taxation year from the disposition of any property is 1/2 of the taxpayer's business investment loss for the year from the disposition of that property.

Section 39: Meaning of capital gain and capital loss

For the purposes of this Act,

[…]

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

(i) to which subsection 50(1) applies, or
(ii) to a person with whom the taxpayer was dealing at arm's length of any property that is
(iii) a share of the capital stock of a small business corporation, or
(iv) a debt owing to the taxpayer by a Canadian-controlled private corporation (other than, where the taxpayer is a corporation, a debt owing to it by a corporation with which it does not deal at arm's length) that is

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

Section 40: General rules

(2) Limitations Notwithstanding subsection 40(1),

[…]

(g) a taxpayer's loss, if any, from the disposition of a property (other than, for the purposes of computing the exempt surplus or exempt deficit, hybrid surplus or hybrid deficit, and taxable surplus or taxable deficit of the taxpayer in respect of another taxpayer, where the taxpayer or, if the taxpayer is a partnership, a member of the taxpayer is a foreign affiliate of the other taxpayer, a property that is, or would be, if the taxpayer were a foreign affiliate of the other taxpayer, excluded property (within the meaning assigned by subsection 95(1)) of the taxpayer), to the extent that it is

[…]

(ii) a loss from the disposition of a debt or other right to receive an amount, unless the debt or right, as the case may be, was acquired by the taxpayer for the purpose of gaining or producing income from a business or property (other than exempt income) or as consideration for the disposition of capital property to a person with whom the taxpayer was dealing at arm's length,

Section 50: Debts established to be bad debts and shares of bankrupt corporation

(1) For the purposes of this subdivision, where

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

[19] To be able to deduct a BIL under sections 38 and 39 of the Act, the Appellant must demonstrate that she experienced a capital loss as a result of the disposition of property. Under section 50 of the Act, a taxpayer is deemed to have disposed of a debt owing to him or her at the end of the year for proceeds equal to nil if that debt is established to have become a bad debt in the year.

[20] In this case, only subparagraph 40(2)(g)(ii) of the Act comes into play here, and it is clear that the Appellant has never been a shareholder of the Corporation and never had any prospect of earning dividend income further to making the loans to the Corporation.

[21] *Byram v. Canada*, 1999 CanLII 7428(FCA) deals specifically with the application of subparagraph 40(2)(g)(ii) of the Act. The review required by that provision deals only with the purpose for which the debt was acquired, in other words for the purpose of earning income from a business or property.

[22] According to *Byram* cited above, the taxpayer does not have to directly earn income from the debt, but when the taxpayer does not hold shares in the debtor

corporation, the burden of demonstrating a sufficient nexus between the taxpayer and the dividend income is much higher.

[23] In this case, the loans were made without any documentation (loan agreement or note) and without specific terms and conditions regarding the annual interest rate, the duration of the loans, or the repayment terms. The Appellant does not know how the amounts that she loaned were used because they do not even appear on the Corporation's financial statements. Lastly, the Appellant did not take steps to recover the interest on those loans.

[24] Under the circumstances, I fail to see how I would be able to conclude that the Appellant could expect to earn income from the loans totalling $305,000 that she had made to the Corporation. Therefore, the Appellant is not entitled to the BIL deduction on the $305,000 loaned to the Corporation because that loss is deemed to be nil under subparagraph 40(2)(g)(ii) of the Act.

[25] For these reasons, the appeal is allowed and the reassessment is referred to the Minister for reassessment in order to award the Appellant the amount of $116,277 granted by the Minister as a BIL for her 2014 taxation year.

Signed at Montreal, Quebec, this 30th day of October 2018.

"Réal Favreau"

Favreau J.

CITATION:	2018 TCC 208
COURT FILE NO.:	2017-961(IT)I
STYLE OF CAUSE:	Marthe Gaudette and Her Majesty the Queen
PLACE OF HEARING:	Sherbrooke, Quebec
DATE OF HEARING:	June 12, 2018
REASONS FOR JUDGMENT BY:	The Honourable Justice Réal Favreau
DATE OF JUDGMENT:	October 30, 2018

APPEARANCES:

For the Appellant:	the Appellant herself
Counsel for the Respondent:	Grégoire Cadieux

COUNSEL OF RECORD:

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