Citation: 2009 TCC 214
Date: 20090617
Docket: 2008-1488(IT)I

BETWEEN:

HAROLD CILEVITZ,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

AMENDED REASONS FOR JUDGMENT

Angers J.

These Amended Reasons for Judgment is issued in substitution for the Reasons for Judgment dated May 26, 2009.

[1] Harold Cilevitz is appealing his 2004 assessment made under the *Income Tax Act* (the "*Act*"). In his 2004 income tax return, he claimed an allowable business investment loss (ABIL) to which the Minister of National Revenue (the "Minister") claims he is not entitled as the loss was not one contemplated by paragraph 39(1)(*c*) of the *Act* in that the appellant failed to demonstrate that in the said taxation year he had incurred a capital loss within the meaning of paragraph 39(1)(*b*) of the *Act*.

[2] The appellant and one Haygo Demirion met at a jewelry show in 1999. They decided to go into business together with the intent of importing certain brands of watches for resale in Canada. They incorporated a company (1403762 Ontario Ltd.) and began operating under the business name and style D.G.I. Each held 50 per cent of the company's shares. A bank account was also opened for the company.

[3] On April 18, 2000, the appellant made an advance of $25,000 to D.G.I. The advance was made by way of a cheque payable to D.G.I. A second advance, of $1,000, was made by the appellant on August 11, 2000, also by cheque payable to D.G.I. The appellant testified that, in addition, he made cash advances to D.G.I.

totalling $6,000, but he informed the court that he did not seek an ABIL for that amount, thereby reducing his ABIL claimed to $13,000 (half of his business investment loss of $26,000) for his 2004 taxation year.

[4] There were no written loan agreements between the appellant and D.G.I. nor was there any agreement as to interest. The appellant testified that an oral agreement was reached and that it was simply that the loan was to be paid back with interest once the company achieved profitability. Shortly thereafter, the appellant became uncomfortable with his new partner and he eventually left D.G.I. in 2001, after nine months, and transferred his shares to Haygo Demirion. At that time, Mr. Demirion had informed the appellant that his nephew would be joining D.G.I.

[5] In the two years following his departure, the appellant made attempts to recover the advances. He met Mr. Demirion from time to time and they had discussions about repayment of the loan, but nothing came of these discussions. The appellant knew that D.G.I. was not making any money and he was informed that Mr. Demirion had left Canada for the U.S. in 2002. In his attempts to collect his money, the appellant spoke with Mr. Demirion's bookkeeper and accountant and was told that there was no money in D.G.I.'s bank account. He also consulted a lawyer and was told that the cost of pursuing the matter further would range between $5,000 and $10,000. Knowing there was no money in D.G.I.'s account, the appellant did not pursue that avenue. Moreover, the appellant suspected that D.G.I. never really operated the business, as the brands of watches it intended to import were not sold in Canada and Mr. Demirion's nephew never did join D.G.I.

[6] It was in 2004 that the appellant determined that his loan would never be repaid and claimed the business loss. Records at the Canada Revenue Agency indicate that D.G.I. (the numbered corporation) was incorporated but no T-2 return or financial statements were ever filed with the Agency.

[7] A letter dated December 11, 2007 from Mr. Demirion to the Canada Revenue Agency confirmed that no consideration was paid or would be paid for the transfer of the shares from the appellant to himself and, in paragraph 2, he said the following with regard to the appellant's advances to D.G.I.:

> 2. The shareholder loan of approximately $32,000 was not repaid **nor** will ever be repaid. This was agreed to by both parties. When the shareholder loan was given to the company, a verbal agreement to pay back the shareholder loan with interest was entered into once the company achieved profitability. When Harold Cilevitz sold, assigned and transferred his shares to Haygo Demirian, the

> shareholder loan was discussed and the outcome was that it was never going to be repaid. This was agreed to by both parties.

[8] In order to claim a business investment loss, the taxpayer must establish on a balance of probabilities that there was a debt, that it was incurred for the purpose of gaining or producing income, that D.G.I. was an eligible small business corporation in 2004 and that the debt became bad in 2004.

[9] The evidence presented by the appellant is sufficient to permit me to conclude on a balance of probabilities that there was an advance made by the appellant to D.G.I. whose amount was the value of the two cheques totalling $26,000. There was no determined date as to when the advance was to be repaid nor how it was to be repaid and no interest rate was agreed to. The appellant did expect that the advances would be repaid but his former partner indicated that the loan was to be paid back with interest once D.G.I. achieved profitability, which would definitely make the time of repayment very uncertain. These uncertainties make it difficult to conclude that even though advances were made, a debt actually existed when the advances were made.

[10] That same difficulty also rests with the second issue as to whether the advance was made for the purpose of producing income. No interest rate was agreed to. The only possible income for the appellant would be his entitlement to dividends.

[11] The other difficulty for the appellant lies in his failure to establish on a balance of probabilities that D.G.I. was a small business corporation as defined in subsection 248(1) of the *Act*. The definition reads as follows:

> **"small business corporation",** at any particular time, means, subject to subsection 110.6(15), a particular corporation that is a Canadian-controlled private corporation all or substantially all of the fair market value of the assets of which at that time is attributable to assets that are
>
> (*a*) used principally in an active business carried on primarily in Canada by the particular corporation or by a corporation related to it,
>
> (*b*) shares of the capital stock or indebtedness of one or more small business corporations that are at that time connected with the particular corporation (within the meaning of subsection 186(4) on the assumption that the small business corporation is at that time a "payer corporation" within the meaning of that subsection), or
>
> (*c*) assets described in paragraphs (*a*) and (*b*),

> including, for the purpose of paragraph 39(1)(*c*), a corporation that was at any time in the 12 months preceding that time a small business corporation, and, for the purpose of this definition, the fair market value of a net income stabilization account shall be deemed to be nil.

[12] A Canadian-controlled private corporation and an active business carried on by a corporation are defined in subsection 125(7) of the *Act* as follows:

> Definitions — In this section,
>
> "**active business carried on by a corporation**" means any business carried on by the corporation other than a specified investment business or a personal services business and includes an adventure or concern in the nature of trade;
>
> "**Canadian-controlled private corporation**" means a private corporation that is a Canadian corporation other than
>
> (*a*) a corporation controlled, directly or indirectly in any manner whatever, by one or more non-resident persons, by one or more public corporations (other than a prescribed venture capital corporation), by one or more corporations described in paragraph (*c*), or by any combination of them,
>
> (*b*) a corporation that would, if each share of the capital stock of a corporation that is owned by a non-resident person, by a public corporation (other than a prescribed venture capital corporation), or by a corporation described in paragraph (*c*) were owned by a particular person, be controlled by the particular person, or
>
> (*c*) a corporation a class of the shares of the capital stock of which is listed on a prescribed stock exchange.

[13] Very little is known about the numbered corporation. We do know it was incorporated with the intent to import certain brands of watches for sale in Canada and that the appellant and Mr. Demirion were equal shareholders. What we do not know is its business history and evolution and whether or not it actually operated. The numbered corporation has not filed any tax returns or produced any financial statements and the evidence seems to show that none of the watches that were intended to be imported were ever sold in Canada. There is no evidence indicating that the business was actually active and operating and controlled by the resident persons.

[14] These final conclusions are sufficient to dispose of this appeal. On the issue of whether the appellant took all reasonable steps in these circumstances to collect his advances, the evidence discloses that the appellant conducted an investigation into the corporation's ability to pay, his chance of success in recovering the advances, and the cost of legal action offering low potential for recovery, and that attempting to recover would be an exercise in futility. His decision to declare the loan bad may be reasonable in the circumstances. As for declaring the loan bad in 2004, that is questionable given the statement in Mr. Demirion's letter that it was understood at the time the shares were transferred in 2001 that the loan was not going to be paid back.

[15] The evidence is insufficient for me to allow an ABIL in these circumstances. The appeal is therefore dismissed.

Signed at Ottawa, Canada, this 17th day of June 2009.

Angers J.

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