Docket: 2003-4006(IT)G

BETWEEN:

HERON BAY INVESTMENTS LTD.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on February 25, 26 and 27, 2009, at Toronto, Ontario.

Before: The Honourable Justice Robert J. Hogan

Appearances:

Counsel for the Appellant:	William I. Innes Douglas Stewart Brendan Bissell
Counsel for the Respondent:	John Shipley Perry Derksen

JUDGMENT

The appeal of the August 14, 2003 reassessment for the Appellant's 1995 taxation year is dismissed, with costs, for the reasons attached hereto.

Signed at Ottawa, Canada, this 8th day of September 2009.

"Robert J. Hogan"

Hogan J.

Citation: 2009 TCC 337
Date: 20090908
Docket: 2003-4006(IT)G

BETWEEN:

HERON BAY INVESTMENTS LTD.,

Appellant,

and

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REASONS FOR JUDGMENT

Hogan J.

I. Introduction

[1] Heron Bay Investments Ltd. ("Heron Bay") loaned money to a related company in its 1994 fiscal year. For its 1995 taxation year, Heron Bay deducted the entire loan as a write-off for a doubtful debt under subparagraph 20(1)(*l*)(ii) or a bad debt under subparagraph 20(l)(*p*)(ii). That write-off is contested by the Minister.

II. Issues for Determination

[2] The issues for determination have to do with whether the three conditions prescribed in either subparagraph 20(1)(*l*)(ii) or subparagraph 20(1)(*p*)(ii) of the *Income Tax Act* (the "*ITA*") have been met and are as follows:

(a) Does the Appellant's ordinary business include the lending of money?
(b) Was the loan made in the ordinary course of the Appellant's moneylending business? and
(c) Was the loan established to be doubtful under subparagraph 20(1)(*l*)(ii) or uncollectible under subparagraph 20(1)(*p*)(ii)?

The Appellant contends that all of the conditions have been satisfied. Not surprisingly, the Respondent alleges the opposite.

III. Factual Background

A. *Background and General Business Practices of the Conservatory Group of Companies*

[3] The late Ted Libfeld was a holocaust survivor who immigrated to Canada at the end of the war with nothing more than his personal belongings. He went on to build a very successful real estate firm, first with partners and later with his four sons. For the last 50 years, the Conservatory Group of Companies has carried on the business of real estate development, from commercial buildings to condominiums and residential housing in the Greater Toronto Area. In addition, in later years the Conservatory Group provided mortgages to third-party purchasers in connection with its real estate business and invested large amounts of surplus funds in commercial paper.

[4] The Conservatory Group is now run by Ted's four sons: Sheldon, Jay, Mark and Corey.

[5] Heron Bay is one of the oldest corporations in the Conservatory Group. Heron Bay's business activities include the purchase and development and subsequent sale of real property. It also loans money to related entities. Heron Bay builds residential homes on its own and in partnership or through joint ventures with other corporations within the Group. In the taxation years under review, it operated its business as a merchant real estate developer, performing sales, marketing and design functions. It left the risky business of home building to third-party builders. The common shares of Heron Bay are owned equally by the four brothers. Sheldon Libfeld is, and was during the relevant years, the president and secretary of Heron Bay.

IV. The Acquisition of the Frost Farm

A. *Runnymede Development Corporation Ltd.*

[6] Runnymede Development Corporation Ltd. ("Runnymede Development") carries on the business of real estate development in the Greater Toronto Area.

B. *First Right of Purchase*

[7] By memorandum of agreement dated April 14, 1988, Runnymede Development granted Ted Libfeld in Trust a first right to purchase any future residential building lots owned by Runnymede in the town of Ajax.

[8] In the early 1990s, Runnymede announced that it was ready to sell certain land known as the "Frost Farm", Group I and Group II lots. Potential purchasers, including Rosehue Downs Development Inc. and Burlmarie Developments Inc., both members of the Conservatory Group, expressed interest in the Group I and Group II lots.

[9] There was some disagreement as to the interpretation of the "first right to purchase" enjoyed by Ted Libfeld in trust. Mr. Libfeld understood that he enjoyed a "right of first refusal" such that Runnymede would have to present an executed offer, whereupon Mr. Libfeld would have the right to match the offer and purchase the lots. Runnymede understood the term to mean that it could present an offer to Mr. Libfeld for acceptance within a reasonable time ("right of first purchase"), failing which Runnymede could sell the lots at an equal or better price. A right of first refusal would have greater value to the Conservatory Group than a right of first purchase as, in the long run, it would dissuade third parties from bidding for the properties.

[10] During the dispute over the interpretation of the term "first right of purchase", Runnymede presented offers to Libfeld's lawyer, who was to confirm that these offers were made by *bona fide* third parties. Neither Mr. Libfeld nor Jack Feintuch, the executive vice-president of Runnymede, could recall the outcome of the referral to Libfeld's lawyer.

[11] Despite Runnymede's denial that there was a binding agreement of purchase and sale with respect to the Group I lots, Mr. Libfeld took the position that there was a binding agreement and threatened legal action on the basis of a right of first refusal.

[12] With the agreement of both parties, the issue of the scope of the right of first purchase and other unrelated issues were taken to arbitration. At a cost of $5 million, Runnymede, obtained, *inter alia*, a release with respect to Libfeld's right of first purchase and related right of joint venture. Mr. Feintuch testified that the release and the payment of the $5 million had nothing to do with the purchase price or the fair market value of the Frost Farm lots. The reduction in price was merely a mechanism for the payment of the $5 million for the release with respect to Libfeld's right of first purchase and the settlement of other, non-relevant, issues. Mr. Libfeld took the contrary view and alleged that part of the $5 million settlement award related to a

rebate on the purchase price of the Frost Farm. Mr. Libfeld felt that they had overpaid for the Frost Farm.

[13] The following members of the Conservatory Group executed agreements to purchase the Frost Farm lands from Runnymede as follows:

- 147 building lots for $11,764,000 by Rosehue Downs Development Inc. by agreement executed August 10 and 12, 1994;
- 142 building lots for $12,202,800 by Burlmarie Developments Inc. by agreement executed August 10 and 12, 1994.

[14] The transactions were structured using a long-form agreement of purchase and sale. Under such an arrangement, title does not pass until a sale to the ultimate homeowner occurs and payment has been made on a lot-by-lot basis. Only then, would the deed to the lot held by Runnymede be put directly in the homeowner's name. When a deposit is made for the property, there is no security given for the funds being advanced. The developer who puts the deposit down only obtains the right to build on and develop the lots.

[15] Contemporaneously with the above transactions, Marlo Developments Inc. ("Marlo"), another member of the Conservatory Group, acted as trustee for the Marlo joint venture in which Viewmark Homes Ltd. ("Viewmark Homes") holds a 95% interest and Shellfran Investments Ltd. holds the remaining 5% interest. Marlo agreed to purchase:

- 147 building lots for $12,000,000 from Rosehue Downs Development Inc. by agreement dated August 10, 1994;
- 142 building lots for $12,500,000 from Burlmarie Developments Inc. by agreement dated August 10, 1994.

[16] Heron Bay loaned Viewmark Homes a total of $3,770,000 from Heron Bay's investment in other real estate joint ventures [i.e. Viewmark Homes Ltd. (trustee)] during October to November 1994. This loan was to enable Marlo, on behalf of the joint venture, to acquire the property. The $3,770,000 represented nearly 100% of the deposit required for the leveraged acquisition of the Frost Farm lands from Burlmarie and Rosehue. The two properties purchased consist of an aggregate of 289 building lots (the "Property").

[17] By agreement dated November 30, 1994, Heron Bay confirmed advances totalling $3,770,000 to Viewmark Homes. The $3,770,000 debt was secured by a

promissory note to Heron Bay and by a pledge to Heron Bay of Viewmark Homes' investment interest in the Marlo joint venture. The terms of the loan were as follows:

- The principal balance and interest were repayable on demand.
- The loan was without recourse, which means that Heron Bay's sole recourse under the loan was against Viewmark Homes' interest in the Property (i.e. its 95% interest in the Marlo joint venture).
- The loan bore interest at 8% per annum.

V. Heron Bay's Tax Position

[18] By November 1994, Sheldon Libfeld was alleging that the fair market value ("FMV") of Viewmark Homes' interest in the Property had been determined to be less than its cost of the Property. In the course of dealing with the appraiser hired by the Appellant to value the properties, Sheldon Libfeld gave that appraiser information respecting property transactions in Whitby. Appraisals obtained at the request of Heron Bay put the FMV of the Property as at November 30, 1994 at no more than $17,235,000. That coupled with other encumbrances on the Property totalling $20,636,000, which ranked ahead of Heron Bay's claim, led to Heron Bay's determination that the value of the loan was nil. It should be noted that this occurred within a short period after the funds were first advanced.

[19] In computing its income tax for its 1995 taxation year, the Appellant claimed a deduction from income of the entire amount of the $3,770,000 loan on the basis that the loan had become a doubtful or bad debt at that time. No adjustment was made in the T2S(1) for tax purposes as, for accounting purposes, the deduction was entered on Heron Bay's profit and loss statement. It is Heron Bay's position that the loan was made in the ordinary course of its business, which included the lending of money, both of which are essential conditions to be met in order for a taxpayer to claim a deduction for a doubtful loan or bad debt.

VI. The Minister's Position

[20] The Minister suggests that at all material times the major business activity of Heron Bay was real estate and that the lending of money was not an integral part of its business operations, but merely part of an occasional investment of surplus funds, generally in the form of term deposits.

[21] The Minister also submits that the loan made by Heron Bay was outside the ordinary course of any moneylending business and was not consistent with Heron

Bay’s related-party transactions. In brief, Heron Bay made only two non-recourse loans and claimed a doubtful or bad debt deduction in respect of each of those two loans.

[22] Finally, the Minister contends that the evidence does not show that the loan was doubtful, uncollectible or bad.

VII. Rezoning Expenses

[23] Heron Bay incurred an expense of $89,799 for the rezoning of a parking lot on its 90 Dundas Street West property in Toronto so that the construction of a condominium building would be permitted. The parking lot portion of that property was treated by Heron Bay as part of its inventory. Heron Bay claims that the condominium sales did not take place, though, due to a decline in the condominium market. As a result, Heron Bay obtained an appraisal with respect to the property and on the basis of this appraisal, determined that the FMV attributable to the parking lot was less than the actual purchase price of the parking lot. While Heron Bay did not increase the portion of the Dundas Street property which it regarded as inventory by the amount of the expense incurred for the rezoning, it did deduct the $89,799 in computing its income for its 1995 taxation year. Heron Bay submits that claiming the expense in this fashion was the same as if the amount had been included in its inventory and a deduction taken in accordance with subsection 10(1) of the *ITA* since the fair market value of the inventory item was less than its cost.

[24] The Minister argues that no evidence was provided to substantiate the decline in value and submits that the parking lot was not inventory of Heron Bay and that Heron Bay accordingly had no basis for writing down its inventory under section 10(1) of the *ITA*. Rather, the Minister submits, the rezoning expense was an expenditure on account of capital, since it was a one-time expenditure for the purpose of bringing into existence an asset of permanent and enduring advantage, and thus the deduction thereof is prohibited by paragraph 18(1)(*b*) of the *ITA*.

VIII. Analysis

[25] Paragraph 20(1)(*l*) of the *ITA* as it applies to Heron Bay’s 1995 taxation year reads as follows:

> 20.(1) Notwithstanding paragraphs 18(1)(*a*), (*b*) and (*h*), in computing a taxpayer's income for a taxation year from a business or property, there may be deducted such

of the following amounts as are wholly applicable to that source or such part of the following amounts as may reasonably be regarded as applicable thereto:

. . .

(*l*) a reserve determined as the total of

(i) a reasonable amount in respect of doubtful debts that have been included in computing the income of the taxpayer for that year or a preceding taxation year, and

(ii) where the taxpayer is a financial institution (as defined in subsection 142.2(1)) in the year or a taxpayer whose ordinary business includes the lending of money, an amount in respect of properties (other than mark-to-market properties, as defined in that subsection) that are doubtful loans or lending assets that were made or acquired by the taxpayer in the ordinary course of the taxpayer's business of insurance or the lending of money or that were specified debt obligations (as defined in that subsection) of the taxpayer, equal to the total of

(A) the prescribed reserve amount for the taxpayer for the year, and

(B) in respect of doubtful loans or lending assets for which an amount was not deducted for the year by reason of clause (A) (in this clause referred to as the "loans", the lesser of

(I) a reasonable amount as a reserve for the loans in respect of the amortized cost of the loans to the taxpayer at the end of the year, and

(II) the product obtained when the total of

1. the part of the reserve for the loans reported in the financial statements of the taxpayer for the year that is in respect of the amortized cost to the taxpayer at the end of the year of the loans, and

2. the total of all amounts included under subsection 12(3) or paragraph 142.3(1)(*a*) in computing the taxpayer's income for the year on a preceding taxation year to the extent that those amounts reduced the part of the reserve referred to in sub-subclause 1.

is multiplied by one minus the prescribed recovery rate,

or such lesser amount as the taxpayer may claim where the lesser amount is the total of a percentage of the amount determined under clause (A) and the same percentage of the amount determined under clause (B);

[Emphasis added.]

[26] Subparagraph 20(1)(*l*)(i) is inapplicable in the present appeal. It allows the deduction of a reasonable reserve in respect of doubtful debts which have been included in computing income. The loan made to Viewmark Homes was made with after-tax funds and was not included by Heron Bay in the determination of its income.

[27] Subparagraph 20(1)(*l*)(ii) is relevant to the present appeal. The part that concerns us applies to doubtful loans or lending assets of taxpayers whose ordinary business includes the lending of money, where such doubtful loan were made or acquired in the ordinary course of the taxpayer's business of the lending of money.

[28] Clause 20(1)(*l*)(ii)(A) applies only to certain types of loans made by banks and is not applicable in the present appeal. Clause 20(1)(*l*)(ii)(B) provides for a general reserve and is relevant to the present appeal. This reserve is equal to the lesser of a reasonable reserve in respect of doubtful loans and the reserve amount entered on the financial statements. The Appellant relies on clause 20(1)(*l*)(ii)(B) to claim a deduction for the loan made to Viewmark Homes. It argues that the loan was doubtful at the end of its 1995 taxation year and that it meets all of the above conditions.

[29] The Appellant also relies on paragraph 20(1)(*p*). This provision allows a taxpayer to deduct the full amount of a loan that has been made where:

(a) the ordinary business of the taxpayer includes the lending of money;
(b) the taxpayer made the loan in the ordinary course of its business of lending money; and
(c) it has been established in the year by the taxpayer that the loan has become uncollectible.

[30] The conditions described in paragraphs (a) and (b) above are identical to those set out in paragraph 20(1)(*l*). The condition described in paragraph (c) above is different. Paragraph 20(1)(*l*) requires only that the debt be established as doubtful. Paragraph 20(1)(*p*) requires the debt to have become uncollectible in the year. This, obviously, is a more stringent standard. If the Appellant fails to establish that its loan to Viewmark Homes satisfies the two conditions in paragraph 20(1)(*l*) that are the same as those under paragraph 20(1)(*p*), it will also fail under paragraph 20(1)(*p*). The Appellant's counsel, Mr. Innes, directed his arguments at trial to the Appellant's case under paragraph 20(1)(*l*) in acknowledgment of the

fact that this was the easier of the two provisions to rely on to justify the Appellant's deduction of the Viewmark Homes loan.

A. *Whether Ordinary Business Includes Moneylending*

[31] The Minister submits that Heron Bay does not carry on the business of moneylending. The Minister argues that even though Heron Bay made loans, it did not act as a moneylender as that term is commonly understood, since Heron Bay did not seek to profit at all from the loans it made, because it either charged no interest or did not enforce the debt.[1]

[32] Determining whether or not a moneylending business exists is a question of fact. If it can be shown, after considering as a whole all the facts of the case, that there is a degree of system and continuity about the transactions, the existence of a moneylending business will be established.

[33] Case law which establishes the test set out above can be found in *Orban v. M.N.R.*, 54 DTC 148 (ITAB), a decision in which Mr. Fordham quoted old English cases on moneylending at pages 149-50:

> . . . In *Litchfield v. Dreyfus*, (1906) 1 K.B. 584, at p. 589, Farwell J., said:
>
>> But not every man who lends money at interest carries on the business of money-lending. Speaking generally, a man who carries on a money-lending business is one who is ready and willing to lend to all and sundry, provided that they are from his point of view eligible . . . **it is a question of fact in each case**.
>
> . . . In *Newton v. Pyke*, (1908) T.L.R. 127, at p. 128, Walton, J. states:
>
>> Whether a man was carrying on business as a money-lender must be, as was pointed out in *Litchfield v. Dreyfus*, a question of fact in each case. It seems impossible to lay down any definition or description which would be of much assistance, but I feel that it is not enough merely to shew that a man has on several occasions lent money at remunerative rates of interest; **there must be a certain degree of <u>system and continuity</u> about the transactions**.
>
> In *Nash v. Layton*, (1911) 2 Ch. 71, at p. 82, Buckley, L.J., said:

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[1] Respondent's Written Submissions, at paragraphs 24 and 25.

> Whether a man is a money-lender or not is an **investigation whether he has done such a succession of acts as that upon the facts proved by establishing that those acts were done** the Court arrives at the conclusion as matter of law that he falls within the definition of a money-lender.
>
> [Emphasis added.]

[34] It is true that in all three cases the effect of the *British Money-lenders Act, 1900* was under consideration, but in each of them the court concerned had, in addition, to deal with the subject of moneylending generally.

[35] In *R.S. Jackson Promotions Ltd. v. M.N.R.*, 85 DTC 145 (TCC), Sarchuk J. added the following at page 149:

> The presence or absence of any single factor referred to does not by itself establish whether that the appellant was not carrying on the business of money-lending. **It is the cumulative effect of this evidence that leads the Court to that conclusion** . . .
>
> [Emphasis added.]

[36] Furthermore, the Federal Court of Appeal stated in footnote 2 of *Loman Warehousing Ltd. v. Canada*, [2000] F.C.J. No. 1717 (QL):

> . . . the business of lending money under the Act extends not only to one who lends money to all who qualify in the conventional sense (see *Litchfield v. Dreyfus* (1906) 1 K.B. 584 at 589), **but would also include one who lends money on a regular and continuous basis over time to a limited group of borrowers for an arm's length consideration** . . .
>
> [Emphasis added.]

[37] The Minister submits that it is not sufficient to have interest income to prove that a moneylending business exists. The Minister argues that receiving interest from mortgages associated with the sale of property is not carrying on the business of a moneylender. Rather, it is the receiving of payment of the unpaid purchase price of property.[2] Furthermore, the Minister suggests that the lending activity is not being carried on with a view to profit because it involves a number of related-party transactions in which the Appellant borrows at 15% and lends at a lower rate, for example, 8%.[3]

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[2] Trial transcript, page 463, at lines 1-4.
[3] *Ibid*. at lines 5-6.

[38] Dealing with the first argument, I find it difficult to accept the suggestion that the receipt of interest relates only to the unpaid purchase price of property. The receipt of interest payments with respect to the mortgages associated with the sale of property implies that a loan was made to the purchaser in order to assist the purchaser in completing the purchase of the property. The loan is a separate transaction from the sale. Accordingly, when payments are made on the purchase price of a home, interest is charged on the portion of the loan that is outstanding.

[39] Regarding the second argument made by the Minister, it was suggested that Heron Bay did not act as a typical moneylender would since it did not lend with a view to profit, as Heron Bay borrowed at 15% but made loans on which it charged a lower percentage. This implies that a typical moneylender would borrow at a lower rate and lend out at a higher rate, thereby earning a profit in the form of the interest income from the spread between the two rates. While this is generally true, it is useful to point out that the 15% rate at which Heron Bay borrowed funds was on shareholder loans.[4] It is also important to note that a business can make loans from profits earned and retained in the business.

[40] Turning to the evidence appearing in the financial statements, it can be observed that interest income is broken down into several components on the Non-Consolidated Statement of Income[5] as follows:

Interest Earned from:	Year Ended: Aug 31/96	% of Total Interest	Year Ended: Aug 31/95	% of Total Interest
Mortgage	54,571	5.9%	64,607	6.1%
Term Deposits & T-Bills	55,885	6.0%	64,576	6.1%
Loans Receivable	822,040	88.1%	933,029	87.8%
Total Interest:	932,496	100%	1,062,212	100%

[41] From the above table, it is clear that for the fiscal years ended August 31, 1995 and 1996, interest income from mortgages and loans receivable made up a substantial portion of the interest income received. The interest on the loans receivable is explained in notes 4 and 5 to the financial statements dealing with interest earned on loans made to related parties.[6]

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[4] Appellant's Book of Exhibits, Tab 63, at pages 375-377.
[5] *Ibid.*, Tab 71, at page 462.
[6] *Ibid.* at pages 471-472.

[42] Mr. Libfeld stated that internal funds were used for lending within the group instead of relying on bank financing.[7] The funds were lent out to help other entities cover construction costs or cash requirements as necessary from time to time.[8] Eventually, when surplus funds become available, they are used to repay Heron Bay.[9] From 1992 onward, interest was normally charged on all loans.[10] Furthermore, there was evidence presented that showed the history of numerous loan transactions with individuals and related parties, including the amounts loaned, the interest rates charged over different periods of time, the payments made and the outstanding balances.[11] Along with the results reflected in the income statement, all these factors support the notion that there is a capacity to make a profit from such loans through the earning of interest income. While there may have been a few loans that bore no interest,[12] interest rates and the timing of interest payments are really terms of the loan that is negotiated between the parties. The fact remains that loans are commonly made by Heron Bay. Accordingly, after considering the factors above, it can be said that a certain degree of system and continuity does exist with respect to the transactions in question. This is similar to the situation in *Langhammer v. The Queen*, 2001 DTC 45 (TCC), a case in which Judge Rip (as he then was) found that loans were made for the purpose of earning interest income as opposed to income from property. Judge Rip found that continuity or system in the lending activities was established due to the fact that the loans were made for specific terms (in that case, three years or shorter) and the lender kept track of interest payment due dates and outstanding balances.

[43] In *Saltzman v. M.N.R.*, 64 DTC 259 (TAB), Mr. Saltzman provided money to a law firm that made mortgage loans on his behalf. After receiving interest, Mr. Saltzman proceeded to claim a reserve for doubtful debts in the same amount. Mr. Davis, Q.C. found that Mr. Saltzman was not in the business of moneylending because he lacked continuity or system in lending out his money. Mr. Saltzman just put in the money, but did not know who the borrowers were, what the exact nature and terms of the mortgages being issued were, or whether he had gotten any money back and knew little of how his money was invested. This can be contrasted to Heron Bay's case.

[44] Whether the loans are made to related parties or not, Heron Bay is not precluded from being a moneylender. In *576315 Alberta Ltd. v. Canada*, [2001]

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[7] Trial transcript, page 25, at lines 2-6.
[8] *Ibid.*, page 72, at lines 6-11.
[9] *Ibid.*, page 73, at line 9-11.
[10] *Ibid*, page 74 lines 9-14.
[11] Appellant's Book of Exhibits, Tabs 61-63.
[12] Appellant's Book of Exhibits, Tab 22.

T.C.J. No. 510 (QL), the corporate taxpayer made two loans to two different corporate entities. The first loan of $1.7 million was to finance four restaurants while the second loan of $325,000 was to enable a debtor to pay its bills. The Minister argued that the taxpayer had not established a systematic and continuous pattern of lending money, did not always collect interest on loans, did not hold itself out to the public as a moneylender, and made a number of loans to related persons or business associates. Nonetheless, Judge Bonner allowed the appeal in part by allowing a deduction related to the first loan since financing was part of the taxpayer's ordinary business and the lending done was part of that financing activity. The inference is that the fact that a loan is made to a related party does not preclude the related-party lender from being a moneylender.

[45] In *Rich v. The Queen*, 2003 DTC 5115 (FCA) (hereinafter "*Rich*"), Rothstein J.A. stated at paragraph 16 that while a non-arm's length relationship may justify closer scrutiny than arm's-length situations, a non-arm's length relationship alone, without more, cannot lead to a finding that the creditor did not act honestly and reasonably in determining the debt to be bad.

[46] I find that Heron Bay is in the business of moneylending since making loans is an integral part of its business and, as established above, there were both system and continuity in the making of the loans. Hence the purpose of the loans was not just the occasional investment of surplus funds. The factors indicating the existence of a moneylending business far outweigh any factors that suggest otherwise.

B. *Whether the Loan Was Made in the Ordinary Course of Business*

[47] In determining the treatment of the deduction under examination, the next question is whether the loan to Viewmark Homes was made by Heron Bay in the ordinary course of its business. As part of the Conservatory Group system, Heron Bay loaned money to related parties and did so on a rather regular basis. One might be tempted, at first blush, to conclude that because the loan to Viewmark Homes was made on income account, it follows that this loan was made in the ordinary course of the Appellant's moneylending activities. In my opinion, such an approach would confuse the proper fact-finding test of the first condition with the fact-finding enquiry needed to determine the second issue. By adding the word "ordinary" to the second condition, namely that the loan be made "in the ordinary course of the taxpayer's business . . . of lending . . . money", the legislator has indicated that the taxpayer must demonstrate not only that the loan was made in the course of the taxpayer's business, but also that it was made in the normal or regular ("ordinary") course of the taxpayer's business of lending money. In my opinion, the non-recourse feature of the

Viewmark Homes loan makes this loan stand out as an extraordinary transaction when compared to the other types of loans that are commonly made by the Appellant.

[48] The argument put forward by Heron Bay in this regard is based on the "normalcy" of the loan in question. It submits that the loan was made in connection with its overall profit-making scheme and was of a class of loan arrangement usually entered into by it. Heron Bay asserts as well that the loan was prompted by the ordinary business considerations that governed its making of loans.

[49] For a loan to fail this test, it would need to be extraordinary or "extracurricular" in some distinct fashion and different from activities carried on in the day-to-day operation of the business as an entity. The loan would need to appear as an aberration or an abnormality of some kind.

[50] As a preliminary noteworthy point, the wording used in paragraph 20(1)(*l*) is not "ordinary course of business", but "ordinary course of the taxpayer's business of . . . lending . . . money". I will, accordingly, consider Heron Bay's business and the types of loans it typically makes in order to determine whether the loan it made to Viewmark Homes was made in the ordinary course of its business.

[51] An instructive point of departure for the purpose analysis is to delineate the meaning and scope of the phrase "in the ordinary course of the taxpayer's business". This phrase is found in other provisions of the *ITA*, and has also been judicially considered in different contexts.

[52] Activity falling within "the ordinary course of business" involves repetition and continuity.[13] Factors considered in distinguishing between transactions on account of capital and transactions on income account are useful but not necessarily determinative.[14] Moreover, "[i]t is trite law that there is a rebuttable presumption that the income earned from anything that a corporation does within the limits of its corporate objects or enabling legislation is business income."[15] But this is not to suggest that anything done by a corporation under the umbrella of its corporate objects or enabling legislation is done in the ordinary course of business or in the ordinary course of that corporation's business "because Parliament has used the word 'ordinary'. The addition of the word 'ordinary' to the expression 'course of business'

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[13] Guy Fortin and Melanie Beaulieu, "The Meaning of the Expressions 'In the Ordinary Course of Business' and 'Directly or Indirectly'", in *Report of Proceedings of the Fifty-fourth Tax Conference*, 2002 Conference Report (Toronto: Canadian Tax Foundation, 2003) 36:1-60 at 36:2.
[14] *Ibid*., at 36:2.
[15] *Ibid*., at 36:7.

must have been intended to capture particular transactions and not just anything done by the corporation in its business."[16]

[53] The phrase was canvassed by Judge Rip (as he then was) in *British Columbia Telephone Company v. M.N.R.*, 86 DTC 1286 (TCC) in the context of former paragraph 20(1)(*gg*) dealing with inventory allowances. At page 1290, Judge Rip commented as follows, relying on international decisions:

> In a bankruptcy matter before the High Court of [Australia], Rich, J. wrote that for transactions to be considered in the ordinary course of business supposes "that according to the ordinary and common flow of transactions in affairs of business there is a course, an ordinary course. It means that the transaction must fall into place as part of the undistinguished common flow of business done; that it should form part of the ordinary business as carried on, calling for no remark and arising out of no special or particular situation": *Downs Distributing Co. Pty., Ltd. v. Associated Blue Star Stores Pty., Ltd. (In Liquidation)*, (1948), 76 C.L.R. 463, at page 477. Street, J., of the Supreme Court of New South Wales stated that "the transaction must be one of the ordinary day-to-day business activities, having no unusual or special features, and being such as a manager of a business might reasonably be expected to be permitted to carry out on his own initiative without making prior reference back or subsequent report to his superior authorities, such as, for example, to his board of directors.": *Re Bradford Roofing Industries Pty., Ltd.,* (1966) 84 W.N. (Pt. 1) (N.S.W.) 276 at page 285 . . . .
>
> [Emphasis added.]

[54] To similar effect is the discussion in *Highfield Corporation Ltd. v. M.N.R.,* 82 DTC 1835 (TRB), at page 1843, of the phrase "in the ordinary course of [the taxpayer's] business" in the moneylending context:

> . . . Since making a loan is the lending of money, it would seem to me that a loan made in the "ordinary course of business" would identify that transaction as part of the "ordinary business" of the taxpayer. For a loan to fall short of those parameters, it would need to be extraordinary or extracurricular in some distinct fashion and clearly different from the day-to-day operation of the business as an entity. It would appear as an aberration or an abnormality of some kind. Perhaps there is a bottom line consisting of a certain required frequency, or similarity of "loan" transactions below which it could not be said that they formed part of the ordinary business of the taxpayer. However, I am not faced with the problem of locating that "bottom line" in this appeal. The constant and consistent procedures adopted and followed by Highfield when making its investments make the particular loans in question "ordinary" in every aspect.

[16] *Ibid.,* at 36:7. But, see also *M.N.R. v. Kelvingrove Investments Ltd.,* 74 DTC 6357 (FCTD) at 6360, where it was found that loans were made "within the objects for which the respondent incorporated" and therefore "constituted the business in which the respondent was engaged."

[Emphasis added.]

[55] The phrase "in the ordinary course of the taxpayer's business" covers "the amalgam of day-to-day activities carried out with regularity and a degree of frequency by the management of the taxpayer in conducting the taxpayer's business, which may be contrasted with isolated transactions infrequently engaged in, including significant asset acquisitions or dispositions that are extraordinary events."[17]

[56] The "appropriate approach of interpretation should be the one that considers the specific characteristics and operating history of the particular business that included an impugned transaction."[18] Support for this approach is found in *Royal Bank v. Tower Aircraft Hardware* (1991), 3 CBR (3d) 60 (Alta. Q.B.), a decision in which the nature of past advances to shareholders was found by the court to be relevant in determining whether a subsequent shareholder advance was made in the ordinary course of business. Similarly, in *Can. Commercial Bank, etc.* (1986), 49 Alta. L.R. (2d) 58 (Alta. Q.B.) at 62, the court considered "what is ordinary in light of all the circumstances" in delineating the scope of ordinary course of trade. Both of these cases demonstrate that courts take into account the specific relationship of the parties in order to determine whether an impugned transaction was carried out in the ordinary course of business.[19]

[57] In *Industrial Investments Ltd. v. M.N.R.,* 73 DTC 118 (TRB), the appellant company loaned money to an affiliated company. No security or collateral was obtained and no interest was charged. The shareholders stated that the reason for proceeding in this manner was that they controlled the American company and the money would be repaid as soon as the funds became available from that company's business operations. The Board found that the loan was not made "in the ordinary course of business" by the Appellant and that it was more in the nature of an accommodation for an associate, or a capital investment.[20]

[58] Against this background, the determination of what falls within the scope of "ordinary", whether in terms of business generally or in the taxpayer's business specifically, becomes an exercise that is highly fact-specific. "Authorities generally agree that the expression ["in the ordinary course of business"] cannot be defined

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[17] Elizabeth J. Johnson and James R. Wilson, "Financing Foreign Affiliates: The Term Preferred Share Rules and Tower Structures" in "International Tax Planning," (2006), Vol. 54, No. 3, *Canadian Tax Journal*, 726-761 at 759.
[18] See above, note 13, Fortin and Beaulieu at 36:8.
[19] See above, note 13, footnote 35 at 36:42.
[20] See above, note 13, footnote 37 at 36:43.

with any precision in the abstract and that its proper interpretation will depend on the facts specific to each case."[21] The Supreme Court of Canada, for bankruptcy law purposes, in *Robitaille v. American Biltrite (Canada),* [1985] 1 S.C.R. 290, at 291 stated that "it is best to consider the circumstances of each case and to take into account the type of business carried on between the debtor and creditor" when determining what constitutes the ordinary course of the taxpayer's business.

[59] The Supreme Court approved the following passage from the Quebec Court of Appeal's majority decision in Pacific Mobile Corp. (In re): *American Biltrite (Canada) Ltée c. Robitaille,* [1982] C.A. 501 at 506:

> It is apparent from these authorities, it seems to me, that the concept we are concerned with is an abstract one and that it is the function of the courts to consider the circumstances of each case in order to determine how to characterize a given transaction. This in effect reflects the constant interplay between law and fact.

[60] Some of the judicial statements referred to above related to provisions of the *ITA* that are inapplicable in the instant appeal or to provisions of other statutes. This does not necessarily render inapplicable the judicial treatment of those provisions. Legislative drafters are understood to abide by the principle of uniformity of expression, so that each term has one and only one meaning.[22] Therefore, the same words appearing in a statute are to be given the same meaning.

> [I]t is a basic principle of statutory interpretation that where the same words are used in a statute, they are to be given the same meaning.
>
> In *Ainsworth Lumber Co. Ltd. v. The Queen*,[23] the court considered the issue of how to interpret the words used in the Act and adopted the following commentary:
>
>> [T]he third edition of *Driedger on the Construction of Statutes* at page 163 . . . says:
>>
>>> It is presumed that the legislature uses language carefully and consistently so that within a statute or other legislative instrument the same words have the same meaning.
>>>
>>> . . .
>
> In *R. v. Zeolkowski,* (1989) 61 D.L.R. (4th) 725, at 732 (S.C.C.), Sopinka, J. wrote:

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[21] *Ibid*., at 36:7.

[22] Pierre-André Côté, *The Interpretation of Legislation in Canada*, Second Edition (Québec : Les Éditions Yvon Blais Inc., 1991) at 279.

[23] 2001 DTC 496, at paragraphs 78-80 (TCC).

> Giving the same words the same meaning throughout a statute is a basic principle of statutory interpretation.

Driedger at page 475 reads:

> In preparing an enactment, the legislature is presumed to be aware of existing case law and to take that case law into account in drafting its provisions. Where words have been given a particular meaning in a case or series of cases, and those words are then used in legislation, the obvious inference is that the legislature intended to give the words the same established meaning.[24]

[61] The concept of "ordinary course" has also been addressed, in the term preferred share context, in relation to the provisions denying the intercorporate dividend deduction to specified financial institutions. The exception carved out of these denial provisions permits the intercorporate dividend deduction in connection with term preferred shares acquired outside the "ordinary course of [the] business" carried on by the taxpayer.

[62] The only reported case discussing the phrase "ordinary course of business" as used in subsection 112(2.1) of the *ITA* is *Société d'investissement Desjardins v. M.N.R.,* 91 DTC 393 (en.), 91 DTC 373 (fr.) (TCC). The Appellant in that case, a subsidiary of a financial institution (therefore a specified financial institution for the purposes of the said subsection), was established with a view to investing in Quebec businesses. In the course of a reorganization designed to give employees greater share ownership, the Appellant converted certain debentures of the Sico company into a separate class of shares. Shortly thereafter, one half of these shares were redeemed, giving rise to a deemed dividend that was deducted by the Appellant in accordance with subsection 112(1). The Minister in turn denied the deduction pursuant to subsection 112(2.1) of the *ITA*. The Appellant conceded that the shares in question constituted term preferred shares, but argued that subsection 112(2.1) did not apply given that the shares were not acquired in the ordinary course of its business.

[63] This Court allowed the appeal. Its findings were twofold. Firstly, it held that in determining if a term preferred share was acquired in the ordinary course of the business carried on by a specified financial institution, *all* of the circumstances surrounding the acquisition must be examined. It was found in this regard that the Appellant's acquisition of the particular shares did not take place in the ordinary

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[24] Brian R. Carr and Duane R. Milot in "Copthorne: Series of Transaction Revisited" in "Corporate Tax Planning", (2008), Vol. 56, No.1 *Canadian Tax Journal,* 243-268 at 262-263.

course of its investment business, but instead occurred only in response to outside pressures to carry out the reorganization.

[64] Secondly, the acquisition fell outside the Appellant's ordinary course of business because the short-term nature of the particular shares did not accord with the Appellant's general investment policy, which was to invest in medium- to long-term investments. In this respect, the Court adopted a narrow reading of the taxpayer's ordinary course of business, restricting it to those actions which the taxpayer customarily carries on. Rather than finding that the taxpayer's ordinary course of business was making investments, or even investing in Quebec businesses, it narrowed the focus even further, finding that the taxpayer's ordinary course of business was to hold medium- to long-term investments.

[65] The purpose of the "ordinary course" condition appears clear to me in the context of both the term preferred share rules and the provisions under consideration in the present case. In the context of the term preferred share rules, provision was made to allow a specified financial institution ("SFI") the benefit of an intercorporate dividend deduction that otherwise would be denied with respect to dividends received on "term preferred shares". To be eligible for this treatment the SFI must establish that the shares were not acquired in the ordinary course of its business.

[66] An SFI may be in the business of lending money to third parties. In this context it could subscribe for preferred shares that are, in substance, identical to unsecured debt issued by its client. The prohibition found in subsection 112(2.1) would then operate to deny a deduction for intercorporate dividends paid on such shares and the dividend paid on the shares would be taxed much in the same way as the interest would have been had the funds been loaned instead. On the other hand, if the same financial institution wanted to capitalize a subsidiary through an investment in preferred shares for a reason other than for its general business purpose of money lending or investing in shares of third parties, the shares might not be acquired in the "ordinary course of business" thus paving the way for an intercorporate dividend deduction. To benefit from the exception, the SFI must demonstrate that the investment in the preferred shares of its subsidiary is different from the third-party transactions that it enters into as part of its general business activities.

[67] The "ordinary course" condition found in paragraphs 20(1)(*l*) and (*p*) operates a little differently. Unlike the case of term preferred shares, where the condition operates as an exception to the general rule that disallows a deduction for the preferred share dividends, here the conditions must be met in order for a reserve or deduction for a doubtful loan or bad debt to be allowed.

[68] Those provisions recognize that although a taxpayer's ordinary business may include moneylending activities, in certain cases a loan may be made outside the taxpayer's ordinary course of business while still being a transaction on income and not capital account.

[69] I therefore turn now to the application of the foregoing interpretive principles and guidelines to the facts in the instant appeal. Heron Bay acted as "banker" for Conservatory Group member companies.[25] A taxpayer can be a moneylender or have moneylending activities as part of its ordinary business but make loans without this being done in the ordinary course of business. While Heron Bay regularly loaned money from its retained earnings to Conservatory Group member companies, often on non-commercial terms, such loans were not typically made on a non-recourse basis. The appellant company apparently made and received hundreds of loans between 1988 and 1995.[26] Only two such loans[27] made by Heron Bay, however, were without recourse: namely, the loan in dispute in the instant appeal and another one to Shellfran Investments, a Conservatory Group member company. Ultimately, both loans were written off as doubtful or bad debts on the strength of an appraisal obtained by Heron Bay. This fact is reflected in the question-answer sequence below from the cross-examination of Mr. Libfeld, found at page 135 of the trial transcripts, commencing at line 9:

> Q. . . . If you look at Tab 23 in the same Book of Documents, you will see a promissory note from Shelfran Investments?
>
> A. Yes.
>
> Q. And this promissory note was made without recourse?
>
> A. Yes.
>
> Q. If we look to every promissory note you have produced in these volumes, this is the only other note that was made without recourse. You understand that?
>
> A. Yes.
>
> Q. In this case, the taxpayer again obtained an appraisal, and again claimed a bad debt in respect of this particular transaction; is that not so, Mr. Libfeld?
>
> A. If you tell me so. . . .
>
> Q. You understood, I would suggest, that there was a benefit in writing down your inventory, to defer the taxation in respect to the borrowing company, and to claim a bad debt in the lending company.

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[25] See page 72, trial transcripts, lines 2-22.
[26] See Appellant's Book of Exhibits, Tab 61.
[27] See Appellant's Book of Exhibits, Tabs 23 and 45.

> And you could accomplish both of the things through the use of a non-recourse promissory note.
>
> You understood that, didn't you, Mr. Libfeld?
>
> A. Yes.

[70] Mr. Libfeld's answers to the above questions are revealing when considered in the context of his overall testimony. He testified that he believed Runnymede was not living up to the terms of the transaction negotiated with his late father. In his eyes, the Conservatory Group enjoyed a right of first refusal rather than a right of first purchase. A right of first refusal had greater value for the Conservatory Group as it required Runnymede to solicit *bona fide* offers from third parties. The Conservatory Group would have the opportunity to scrutinize the offers in deciding whether or not to exercise the right of first refusal. In brief, because Runnymede acted on the basis that its obligation was one resulting from the granting of a right of first purchase, Mr. Libfeld felt that the group may have been placed in the circumstance of having overpaid for the property.

[71] In that context, it is not unreasonable to believe that the related-party financing transactions were structured to allow of a double deduction if the Conservatory Group was to develop the land and incur a loss in the process. Mr. Libfeld acknowledges that he is familiar with the tax aspects of the transactions. First, the joint venturers, as the owners of the land, are entitled to write its value down to fair market value and claim a business loss, assuming they can demonstrate that the land had decreased in value. Second, by making the loan by Heron Bay to Viewmark Homes a non-recourse loan, Heron Bay increased the chances that it would be able to claim a reserve for a doubtful debt as Heron Bay would not have access to Viewmark Homes' other assets and investments.

[72] As noted earlier, Mr. Libfeld failed to persuade me that the loan was made non-recourse for commercial purposes. None of the other related-party loans made by Heron Bay had this limitation save for the other loan, to Shellfran Investments, in respect of which a doubtful debt deduction was also claimed.

[73] I do not find the mere fact that the Conservatory Group could benefit from a double deduction to be particularly offensive. Heron Bay would be entitled to a deduction provided that it met all of the conditions laid out in paragraphs 20(1)(*l*) or (*p*), which I do not believe it has done. In the present case, the specific terms and features of the non-recourse debt made it extraordinary and put it outside Heron Bay's ordinary course of business. This, in tandem with the non-arm's length relationship between Heron Bay and Viewmark Homes, as well as the fact that both

non-recourse loans were written off by Heron Bay as bad or doubtful debts, all suggests to me that something was going on, something outside the ordinary course of the taxpayer's business.

[74] Mr. Libfeld was given the opportunity during cross-examination to explain the underlying reason for making the loan to Viewmark Homes non-recourse. He stated, commencing at line 12 of page 134 of the trial transcript, that "to protect the interests of all the companies involved, we made it non-recourse . . .". To similar effect is the following question-answer sequence from the examination-in-chief of Mr. Libfeld, commencing at line 6 of page 67 of the trial transcript:

> Q. Could you tell us what security, if any, Heron Bay took with respect to this loan?
>
> A. Heron Bay took Viewmark's interest in Marlo as security for this loan.
>
> Q. Was there any other form of recourse?
>
> A. No.
>
> THE COURT: I would like to ask the witness a question.
>
> We are dealing with related companies at this point. Without questioning your judgment, why would you make a non-recourse loan? What difference did it make, from a business or commercial standpoint?
>
> THE WITNESS: We wanted to protect corporations within the system.
>
> It would be beneficial to make it non-recourse, so if there was a problem with one of the other corporations, it wouldn't end up affecting it.
>
> . . .
>
> THE WITNESS: The commercial reason is to protect. If something happened, we wouldn't want people to be able to go through one company to another, to be able to realize on that loan.
>
> We didn't want to put Viewmark at risk, if something happened to Heron Bay.
>
> . . .
>
> THE WITNESS: . . . it is structured in a way that we protect the interest of the system, so to speak, in terms of not allowing one corporation to end up triggering a domino effect throughout the rest of the system.

[75] While a borrower may request that a loan be non-recourse for *bona fide* commercial reasons, I do not find Mr. Libfeld's explanation — namely the protection of Viewmark Homes' assets from Heron Bay — to be credible. Heron Bay often borrowed on a full recourse basis from corporations within the group and loaned on a

full recourse basis.[28] This included a loan from Viewmark Homes to Heron Bay in excess of $5 million.[29] The inference could thus be made that, but for the without a recourse restriction on the promissory note, Viewmark Homes would have had the capacity to satisfy the debt. That is, rather than loan the money, Heron Bay could, in my view, have instead repaid the loan it received. Heron Bay could have offset one loan against the other, were it not for the without-recourse element of the loan.

[76] Additionally, it does not appear from the evidence that Runnymede, the entity to which was owed a balance of sale price secured by the land, requested that the loan be made non-recourse. There is also no evidence that the banks lending to the Conservatory Group requested this feature. Generally speaking, unrelated creditors may demand subordination of related-party indebtedness to provide better security for their loans.

[77] In the end, I find that the loan was extraordinary and abnormal. It deviated from the types of loans that Heron Bay would generally make in the course of its business. This is particularly true if one bears in mind the interpretation to be given to the concept "ordinary course" pursuant to the decision of this Court in *Société d'investissement Desjardins*, above. The loan fails to fall into place as part of the undistinguished common flow of Heron Bay's business. It is clearly different from Heron Bay's day-to-day business and its practice of making full recourse loans. In the absence of any credible and convincing evidence to the contrary, I draw a negative inference from the circumstances presented to me: that is, the loan was made non-recourse to facilitate its earlier write-off.

[78] Considering the other with-recourse loans made back and forth between the related entities and the almost immediate bad debt claim with respect to the without-recourse loan, the assertion that the without-recourse feature was designed to protect the interests of Heron Bay from third parties is difficult to accept as an accurate and realistic portrayal of what was really occurring. The "ordinary course" requirement in paragraph 20(1)(*l*) serves to prohibit the doubtful debt reserve even in the case of persons that loan money as part of their business, unless the loan is made in the ordinary course of the taxpayer's business.

C. *Whether the Debt Was Doubtful or Bad*

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[28] See Appellant's Book of Exhibits, Tab 61, for a synopsis of Heron Bay's lending and borrowing activities.
[29] See trial transcript, page 179, commencing at line 6.

[79] The test for bad debts and doubtful debts was stated by Justice Reed in the decision *Coppley Noyes & Randall Ltd. v. Canada (M.N.R.)*, [1991] F.C.J. No. 347 (QL) (FCTD), in which she quoted paragraph 22 of Interpretation Bulletin IT-442 – Bad Debts and Reserve for Doubtful Debts, as follows:

> . . . For a debt to be classed as a **bad debt** there must be evidence that it has in fact become uncollectible. For a debt to be included in a **reserve for doubtful debts** it is sufficient that there be reasonable doubt about the collectibility of it. . . .
>
> [Emphasis added.]

[80] The question of when a debt is to be considered uncollectible is a matter of the taxpayer's own judgment as a prudent businessman (*Flexi-Coil Ltd. v. R.*, 1995 CarswellNat 1380, [1996] 1 C.T.C. 2941, at paragraph 22).

[81] In the case of doubtful debts on the other hand, "doubtful" means there must be some reasonable doubt as to the collectibility of the principal amount of the debt obligation. It is sufficient if there is some reasonable doubt as to the timeliness of payments. (Ryan Keey, Carol Klein Beernink and Joscelyn Affonso, eds., Canada Tax Service, vol. 4 (Toronto: Thomson Reuters Canada Limited, 2009), at 20-1406).

[82] Accordingly, the test appears to be more flexible for doubtful debts than for uncollectible debts. In *Highfield Corporation Ltd.*, above, Mr. Taylor confirms this by stating the following in his decision (paragraphs 34 and 35 CarswellNat, page 1847 DTC):

> . . . A "Reserve for doubtful debts" established under section 20(1)(l) of the Act would seem to leave with the taxpayer a much greater degree of flexibility in using business judgment with regard to the inclusion of amounts in such a reserve than is permitted to a taxpayer in claiming a deduction under section 20(1)(*p*) of the Act for a "bad debt". The term "doubtful debt" in itself can mean only what it says – the debt is owing and possible of collection, but that possibility is not sufficiently certain in the mind of the taxpayer that he wishes to be placed in the disadvantageous position of having to pay income tax thereon before that possibility has become more of a certainty.
>
> In effect, a taxpayer may be given a year's grace with the application of section 12(1)(*d*) of the Act serving to bring the reserve back into income in the following year, at which point he is presumably required or permitted to re-examine the situation and reserve against the amount again, or not do so depending on his business judgment then, and the situation at that time. Obviously if his original concern regarding collectibility has been ill-founded and the amount collected in the interim, it would be credited as income. Conversely, under section 20(1)(*p*) of the Act, it is necessary for the taxpayer to establish that the amount at issue is a "bad

> debt" – in simple language uncollectible. It has gone beyond any reasonable hope of recovery and is effectively worthless (not merely doubtful) as an asset. That, as I see it, requires considerably greater support for the claim than may be required under section 20(1)(l).
>
> [Emphasis added.]

[83] An honest and reasonable determination is needed in order to establish that the loan was bad (*Rich*, above, at paragraph 28). A reasonable determination will be based on a contextual review of all of the factors that come into play in the particular situation.

[84] Rothstein J.A. summarized the factors — similarly to those adopted in *Hogan v. M.N.R.,* 56 DTC 183 (ITAB) — that should be taken into account in determining whether a debt has become bad, at paragraph 13 of *Rich*:

> 1. the history and age of the debt;
> 2. the financial position of the debtor, its revenues and expenses, whether it is earning income or incurring losses, its cash flow and its assets, liabilities and liquidity;
> 3. changes in total sales as compared with prior years;
> 4. the debtor's cash, accounts receivable and other current assets at the relevant time and as compared with prior years;
> 5. the debtor's accounts payable and other current liabilities at the relevant time and as compared with prior years;
> 6. the general business conditions in the country, the community of the debtor, and in the debtor's line of business; and
> 7. the past experience of the taxpayer with writing off bad debts.
>
> This list is not exhaustive and, in different circumstances, one factor or another may be more important.

[85] At paragraph 14 of *Rich*, Rothstein J.A. went on to state:

> While future prospects of the debtor company may be relevant in some cases, the predominant considerations would normally be past and present. If there is some evidence of an event that will probably occur in the future that would suggest that the debt is collectible on the happening of the event, the future event should be considered. If future considerations are only speculative, they would not be material in an assessment of whether a past due debt is collectible.

[86] Rothstein J.A. confirms that there is no one specific factor that must be present for a debt to be classified as a bad debt. The uncollectibility of a debt is determined on the basis of the consideration of many factors. While *Rich* is a case that deals with

bad debts, the factors considered for bad debts also apply to determining whether debts are doubtful; it is simply a matter of adapting them to take into account the fact that for doubtful debts the threshold is lower, as the collectibility of the debt need only to be doubtful. (Interpretation Bulletin IT-442R at paragraphs 23 and 24).

[87] Heron Bay argues that the decision to write off the $3,770,000 loan receivable in its 1995 taxation year was a business judgment and as such should not be questioned as it was honestly and reasonably made[30] on the basis of the facts and the valuation of the asset at that point in time.[31] In the alternative, Heron Bay suggests that the write-off was valid because the loan was uncollectible.[32]

[88] Dealing with the doubtfulness issue first, I agree that a taxpayer is generally in the best position to determine whether a receivable from a client is doubtful or not. In this case, however, there are some questions that arise after consideration of the factors relevant to the situation.

[89] This is what emerges from the application of some of the factors listed in the *Rich* decision above:

D. *History and Age of the Debt*

[90] In considering the history of the debt written off, the time period between the date the loan was made (late in the 1994 fiscal year) and its write-off by Heron Bay in its year ended August 31, 1995, was short. During cross-examination, Mr. Libfeld confirmed that Heron Bay never made any demands on Viewmark Homes for repayment of the whole or any part of the debt.[33]

[91] It is important to note that it is unnecessary for a creditor to exhaust all possible recourses for collection. All that is required is an honest and reasonable assessment (*Rich*, above, at paragraph 15). Nonetheless, considering the fact that Heron Bay owns Viewmark Homes, the two entities were not dealing at arm's length, and accordingly, the write-off warrants closer scrutiny. As Justice Rothstein stated in the *Rich* decision at paragraph 16:

> . . . The non-arm's length relationship may justify closer scrutiny than in [arm's] length situations. But a non-arm's length relationship alone, without more, cannot

[30] Trial transcript, page 423, at lines 11-21.
[31] *Ibid.*, at lines 22-23.
[32] *Ibid.*, page 426, at line 17.
[33] *Ibid.*, page 178, at lines 9-13.

> lead to a finding that the creditor did not honestly and reasonably determine the debt to be bad.

[92] The additional factors that follow will reveal why closer scrutiny is warranted in this case.

E. *The Financial Position of the Debtor*

[93] There was no indication that Viewmark Homes was in financial difficulty. One example is that Viewmark Homes had sufficient funds to lend a substantial sum to Heron Bay. The Minister argued that the balance sheet for the year ended August 31, 1995 reflected a loan of $4,055,765 made by Viewmark Homes to Heron Bay during the year.[34] Another example shows that Viewmark Homes had $15,000,000 in current net assets for the 1996-1997 period of the joint venture, and that, in the 1997-1998 fiscal period of the joint venture, Viewmark Homes withdrew that same amount from its capital account.[35]

F. *Valuation Reports on the Value of the Land*

[94] Mr. David Atlin, the expert real estate appraiser for Heron Bay, determined the fair market value (FMV) of the 289 residential lots as at November 30, 1994 to be $19,000,000[36] and the value of the favourable financing terms that helped finance the purchase to be $3,563,255 for the buyer.

[95] Mr. John Davies, the expert appraiser for the Minister, valued the lots in separate parcels (one of 142 lots and the other of 147 lots). He confirmed that there would be no difference in the result of his appraisal if the lots were determined together (i.e. 289 lots).[37] Mr. Davies determined the fair market value of the land to be $22,160,000 in his January 21, 2009 amended report[38].

[96] Both Mr. Atlin and Mr. Davies used similar approaches in their valuation of the land, namely a direct comparative approach, which compares market evidence with the subject property using some standard unit of comparison. Mr. Atlin used price "per front foot", while Mr. Davies used price "per lot". Mr. Atlin testified that this particular difference, however, does not result in any material differences in the

[34] Appellant's Book of Exhibits, Tab 69, page 452.
[35] Trial transcript, pages 184-185.
[36] *Ibid.*, page 215, at line 15.
[37] *Ibid.*, page 342, at lines 3-4.
[38] *Ibid.*, page 383.

value of the land.[39] Also, neither appraiser disputed the facts themselves with respect to the property, that is, facts such as drainage issues, soil conditions, planning and zoning status, etc.[40] Furthermore, both appraisers agreed on the general performance of the market.

[97] During the trial, Mr. Atlin stated that the material differences between the two reports arise with respect to:

(a) financing and
(b) the size of the development as it affected absorption.[41]

[98] With respect to the financing element, Mr. Atlin noted that the subject property includes non-arm's length financing consisting of a one-year interest-free period[42] and a relatively low interest rate (prime + 1%) in relation to the loan-to-value ratio.[43] Mr. Atlin stated the loan-to-value ratio (i.e. the percentage of the purchase price which was financed) to be 85% for parcel 1 and 82.5% for parcel 2.[44] Mr. Atlin testified that favourable financing would drive up the price, but not the value. He noted that there is an important distinction between price and value.[45] The total price for the transaction was $24,400,000, which factored in the value of the interest-free period and the favourable interest rates. Mr. Atlin then assigned a total value of $3,536,255 to the favourable financing, which figure was made up of $1,762,144 for the smaller parcel and $1,774,111 for the other parcel. Subtracting the $3,536,255 (i.e. removing the impact of the financing) from the $24,400,000 provides the cash sale equivalent.[46] During cross-examination, Mr. Atlin agreed that there was no significant change in value between August and November 1994.[47]

[99] At this point it should be noted that Heron Bay's recourse to the joint venture's assets extended to both the land and the value of the favourable financing terms. Therefore, the disagreement between Mr. Davies and Mr. Atlin over how much of the value should be allocated to the favourable financing terms is irrelevant to the issue being considered as, whichever way the value is allocated, both assets support the loan debt owed by Viewmark Homes to Heron Bay. What separates the two

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[39] *Ibid.*, page 226, at lines 12-14.
[40] *Ibid.*, page 220, at lines 15-23.
[41] *Ibid.*, page 226, at lines 15-18.
[42] *Ibid.*, page 232, at lines 6-7.
[43] *Ibid.*, page 228, at lines 13-20; page 232, at lines 7-8; page 248, at lines 16-19.
[44] *Ibid.*, page 232, at line 1.
[45] *Ibid.*, page 230, at lines 6-8.
[46] *Ibid.*, page 269, at lines 1, 16-20.
[47] *Ibid.*, page 282, at lines 5-6.

experts is that, on the one hand, Mr. Atlin says that what was acquired by Viewmark Homes was worth $1.4 million less at year-end because of the absorption cost, while Mr. Davies disputes this finding.

[100] With respect to the size of the development, Mr. Atlin testified that there is a significant downward adjustment for purchasing in bulk as compared to buying small lots.[48] Mr. Atlin explained that in a purchase of 289 lots, one would benefit from economies of scale and thus the price would be reduced. Subtracting from the $20,400,000 purchase price a value of $1,400,000 for the absorption cost gives a cash equivalent fair market value of $19,000,000.[49] Mr. Atlin further stated that the intrinsic value of the land does not change.[50]

[101] Mr. Davies, on the other hand, arrived at a final figure of $23,966,800 in his June 18, 2008 report. Mr. Davies relied mainly on the purchase and sale agreements entered into between Runnymede and Burlmarie and Rosehue since, he testified, the actual prices paid for property best represent its market value.[51] Mr. Davies further confirmed that there was no discernable change in market conditions between August 1994, when the purchase and sale agreements were entered into, and November 1994.[52] His initial figure of $26,425,275 for the 289 lots in the same report, arrived at without the benefit of having the purchase and sale agreements available, was based on comparable properties for which interest-free periods of varying lengths were factored in.[53] Mr. Davies noted that all the comparables were inclusive of vendor take-back mortgages at similar rates of interest (9%), and very similar time periods, with the exception of the interest-free period.[54] Mr. Davies stated that the comparables were used to verify the price paid.

[102] The difference between Mr. Davies' initial report and his amended report dated January 21, 2009 was due to the fact that the interest-free periods of varying lengths were taken out[55] of the calculation in order to reduce all sales to a common basis. This was done because the transaction in Heron Bay's case had an interest-free period of one year only. After the interest adjustment, Mr. Davies testified, the total of $23,966,000 was allocated as follows: $22,160,000 for the land and $1,806,004 for

[48] *Ibid.*, page 240, at lines 8-10.
[49] *Ibid.*, page 270, at lines 23-25.
[50] *Ibid.*, page 266, at lines 14-15.
[51] *Ibid.*, page 350, at lines 23-24.
[52] *Ibid.*, page 352, at lines 11-25.
[53] *Ibid.*, page 355, at lines 2-3.
[54] *Ibid.*, page 363, at lines 13-16.
[55] *Ibid.*, page 355, at lines 12-13.

the interest benefit.[56] Also, another report, dated January 22, 2009, was made by Mr. Davies concerning offers he was asked to consider. Mr. Davies confirmed that these offers — from Coughlan, Fram, and a numbered company — gave further credibility to the opinion that the purchase and sale agreements were at market value.[57]

[103] With respect to adjustments for absorption, Mr. Davies testified that he understood Mr. Atlin to say that there was considerably more risk in purchasing a larger-sized property than a smaller one because of the length of time it took to absorb (or resell) the lots.[58] Mr. Davies stated that there was no attempt to sell the property as one parcel, rather, it was divided into two separate parcels. He further testified that an absorption adjustment was not warranted because larger builders were able to obtain significant cost saving benefits from purchasing a large number of lots, namely benefits, in terms of the bulk ordering of materials, sequentially moving from house to house, professional fees (e.g. design, legal), brokerage fees, and spreading the cost of a model home over a larger number of houses (cost and the fewer number of model homes needed).[59]

[104] Both appraisers agreed that there was no overall change in the market from August 1, 1994 to the date the write off was claimed by Heron Bay. Therefore, I find Mr. Davies' approach to be preferable because he relies on the actual arm's length sale in concluding that the value of Viewmark Homes' joint venture assets had not declined by the time Heron Bay claimed its write-off.

[105] If I was to accept Mr. Atlin's view, I believe a reasonable conclusion could be drawn that Heron Bay's cost of the loan was overstated at the outset and should be reduced pursuant to paragraph 69(1)(*a*) of the *ITA*.

[106] Paragraph 69(1)(*a*) provides that where a taxpayer acquires property from a person with whom that taxpayer was not dealing at arm's at an amount in excess of its fair market value at the time, the taxpayer's cost shall be deemed to be that fair market value. Heron Bay gave cash to Viewmark Homes, a non-arm's length party, in exchange for intangible property in the form of a loan receivable. On the face of it, paragraph 69(1)(*a*) could accordingly apply, resulting in no deduction as the cost of the non-recourse loan would be nil for Heron Bay. As Mr. Atlin testified that nothing had changed in the real estate market over the period in question, presumably the

[56] *Ibid.*, page 383, at lines 5-8.
[57] *Ibid.*, page 362, at lines 1-2.
[58] *Ibid.*, page 369, at lines 11-15.
[59] *Ibid.*, page 371.

absorption costs that he used to justify a decline in the value of the land likewise existed at the time of purchase. I recognize that the Respondent did not seek to pursue this point when I raised it at trial. However, I simply cannot ignore it if it is otherwise applicable.

[107] Soon after the loan was made, a valuation was performed, and then the entire write-off occurred. In fact, as noted earlier, the Appellant hired a valuator within 60 days of the first advance of funds. In the past, a similar loan by Heron Bay to Shellfran, a related entity, had been made, also on a non-recourse basis. After that loan was made, an appraisal was obtained and the loan was written off.[60] The non-recourse feature of the loan appears to have been added to facilitate the write-off.

[108] In any event, I find that Heron Bay is not entitled to the deduction claimed for all of the other the reasons noted earlier.

G. *The General Business Conditions in the Community*

[109] The expert appraisers for Heron Bay and the Minister both agreed on the performance of the general real estate market. In the late 1980s, the real estate market experienced very good economic performance. Then there was a downturn in the early 1990s, but by 1994 there were signs of recovery.[61]

H. *The Past Experience of the Taxpayer with Writing off Doubtful Debts*

[110] It is interesting to note that the loan from Heron Bay to Viewmark Homes was made on a non-recourse basis. Mr. Libfeld explained that the reason for this was protection: if something happened to Heron Bay, they did not want creditors to be able to go through Heron Bay to Viewmark Homes.[62] I did not find this explanation to be very credible. While there were many loans made by Heron Bay, only one other was made on a non-recourse basis, also to a related party.

[111] Overall, there are limits to how far deference will be given to business judgment. One case in which those limits would apply is where the business judgment was clearly unreasonable. As explained earlier, transactions between related parties may be subject to closer scrutiny. In *Flexi-Coil Ltd. v. R.,* above, affirmed [1996] 3 C.T.C. 57 (FCA), it was noted at paragraph 20:

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[60] *Ibid.,* page 156, at lines 11-15.
[61] *Ibid.,* page 221, at lines 2-24.
[62] *Ibid.*, page 68, at lines 15-18.

> . . . the supplier of goods is also the owner, financial backer and controller of the customer: it is in a position to influence how the business of the customer subsidiary is to be carried on, . . .

[112] And at paragraph 25 the following was stated:

> To my knowledge, the Act does not provide special rules for the determination when the debts owing by related parties are bad. Therefore, the rules applicable to arm's length traders should apply to those not dealing at arm's length. This does not mean that courts should not be vigilant in ensuring that the related creditor acted properly in determining that some debts had become uncollectible.

[113] In *Rich*, above, the taxpayer lent money to his son's corporation, which could not repay the loan. The taxpayer in *Rich* only held a 25% interest in his son's corporation. Both Heron Bay and Viewmark Homes were controlled by the Libfelds. Heron Bay also held an equitable interest in Viewmark Homes and thus Heron Bay owned both the debt and the equity, thereby making it easy to manipulate the terms of the loan. Accordingly, closer scrutiny is warranted. Considering all the above factors, I believe that Heron Bay took an early opportunity to write off this debt, a step that was not justifiable in the circumstances. Among the primary factors that stand out is the fact that little time elapsed between the loan and its write-off. There was no evidence provided that showed a change in circumstances between the time the loan was contracted and the date the write-off was claimed. In addition, the valuations provided at trial revealed that the difference between them as regards the value of the underlying property of the joint venture was small. Mr. Atlin, who testified on Heron Bay's behalf, split the value between land and favourable financing. The only decline in value was attributed to absorption. Mr. Davies, who testified for the Minister, relied mainly on the purchase and sale agreements to determine the value, as these provide the arm's length price. He relied on prices and offers for comparable properties to confirm that the recent arm's length price should be preferred.

[114] With respect to the alternative argument that the write-off was a bad debt, the criterion to be met, as established above, is that the debt has become uncollectible. The factors described earlier can also be used to assess the collectibility of the debt. Looking at all the factors as a whole, one must conclude that Heron Bay has not established that the loan was uncollectible. There is no evidence that the loan amount or part thereof, was uncollectible. Accordingly, the requirements of subparagraph 20(1)(*p*)(ii) have not been met either.

I. *Reasons re: Rezoning Expenses*

[115] The Respondent's position was that the rezoning expenses were capital in nature as they were a one-time expenditure incurred to clear the way for the development of a high-rise condominium that could be resold at a profit.

[116] Since no evidence on submissions were provided by Heron Bay on this matter, the appeal can be dismissed with regard to this issue. It would be useful nonetheless to just comment on the general principles related to the analysis of such an issue.

[117] The first question to be asked is whether an expenditure of this type is a current expense or a capital expense. The distinction is not necessarily clear. If it is determined to be a current expenditure, it is deductible in the year incurred. If it is determined to be a capital expense, the next question to answer is whether it is subject to capital cost allowance rules or whether it is an eligible capital expense. If the answer is neither, then it is considered "nothing" and no deduction is permitted on the amount of the expenditure (Tim Edgar & Daniel Sandler, *Materials on Canadian Income Tax* (Toronto: Carswell, 2005) at 486).

[118] The basic test for determining whether an expenditure is capital in nature or not is the enduring benefit test. The leading case on this had traditionally been the decision of the House of Lords in *British Insulated and Helsby Cables v. Atherton* [1926] A.C. 205 (HL), in which Viscount Cave held that (at pages 213-214):

> when an expenditure is made, not only **once and for all**, but with a view to bringing into existence an asset or an advantage **for the enduring benefit** of a trade, I think that there is a very good reason (in the absence of special circumstances leaning to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital
>
> [Emphasis added.]

[119] This standard rule was dealt a blow by the Supreme Court of Canada in a unanimous judgment rendered by Estey J. in *Johns-Manville Canada Inc. v. The Queen*, [1985] 2 C.T.C. 111, at 119, who quoted *Hallstroms Pty. Ltd. v. Federal Commissioner of Taxation* (1946) 72 C.L.R. 634, 648:

> *The solution to the problem is not to be found by any rigid test or description.* It has to be derived from many aspects of the whole set of circumstances some of which may point in one direction, some in the other. One consideration may point so clearly that it dominates other and vaguer indications in the contrary direction. *It is a commonsense appreciation of all the guiding features which must provide the ultimate answer.* Although the categories of capital and income expenditure are

> distinct and easily ascertainable in obvious cases that lie far from the boundary, the line of distinction is often hard to draw in border line cases; and conflicting considerations may produce a situation where the answer turns on questions of emphasis and degree. That answer: "depends on what the expenditure is calculated to effect from a practical and business point of view rather than upon the juristic classification of the legal rights, if any, secured, employed or exhausted in the process".
>
> [Emphasis added.]

[120] In essence, there is no hard and fast rule in determining whether as expenditure is income or capital in nature. Rather, a common-sense assessment of all the relevant facts is required.

[121] With respect to rezoning expenditures, *The Cadillac Fairview Corporation Limited v. The Queen*, 97 DTC 405 (TCC), provides some guidance on how zoning costs should be dealt with. In *Cadillac Fairview*, the corporate taxpayer incurred substantial expenses to obtain density rights (air space rights) in respect of a proposed building. The issue was whether the cost of obtaining zoning changes permitting a higher density in buildings which the Appellant proposed to build on land it owned in Toronto formed part of the cost of the land or of the buildings, or was an eligible capital expenditure. Judge Bowman (as he then was) stated the following at pages 413 and 414:

> . . . We may start from the proposition that <u>in the absence of legislative or other legal restrictions a landowner is free do to what it wants on its land</u>. It can farm it, build highrise apartments or office buildings, or build the Tower of Babel. Its rights inhere in the ownership of the land. **The exercise of those rights can, however, be restricted, regulated or prohibited by legislation**. In this case the authority having that jurisdiction is the province and it delegates the power to the municipal authorities.
>
> The power of municipal zoning is conferred upon the municipality by the *Planning Act*. Section 34 of the *Planning Act of Ontario* R.S.O. 1990, c. P-13 reads in part as follows:
>
> > (1) Zoning by-laws may be passed by the councils of local municipalities:
> >
> > 1. For prohibiting the use of land, for or except for such purposes as may be set out in the by-law within the municipality or within any defined area or areas or abutting on any defined highway or part of a highway.
> >
> > 2. For prohibiting the erecting, locating or using of buildings or structures for or except for such purposes as may be set out in the

by-law within the municipality or within any defined area or areas or upon land abutting on any defined highway or part of a highway.

3. For prohibiting the erection of any class or classes of buildings or structures on land that is subject to flooding or on land with steep slopes, or that is rocky, low-lying, marshy or unstable.

4. For regulating the type of construction and the height, bulk, location, size, floor area, spacing, character and use of buildings or structures to be erected or located within the municipality or within any defined area or areas or upon land abutting on any defined highway or part of a highway, and the minimum frontage and depth of the parcel of land and the proportion of the area thereof that any building or structure may occupy.

. . .

(3) The authority to regulate provided in paragraph 4 of subsection (1) includes and, despite the decision of any court, shall be deemed always to have included the authority to regulate the minimum area of the parcel of land mentioned therein and to regulate the density of development in the municipality or in the area or areas defined in the by-law.

The origin of that section is S.O. 1983, c. 1.

Presumably the zoning by-laws of Toronto were enacted by it under the authority of a predecessor to that section, possibly section 39 of the *Planning Act*, R.S.O. 1980, c. 379 which is substantially the same as that contained in R.S.O. 1990. **It is important to recognize that zoning does not constitute a conferral of a right but rather a restriction of the otherwise unlimited right of a landowner to do what it wishes with its land. It is less accurate to describe a change in zoning to allow a further use of land as the conferral of a right than to describe it as a lifting or relaxation of a restriction on the otherwise unrestricted use of the property**. It follows that the right to use property, whether restricted by zoning by-laws or not, is a right that inheres in the ownership of the property. It is part of the bundle of rights that a landowner has by reason of ownership of property. **The cost of a modification of the restrictions of the rights that a landowner has with respect to the use of land is a part of the cost of the land. The cost of lifting restrictions on the exercise of those rights clearly relates to the cost of the bundle of rights that ownership entails**. Density rights have to do with what the owner can do with the land. If a landowner is successful in improving the zoning of a parcel of land, and then sells it, it is inconceivable that the revenue authorities could demur at the inclusion of the cost of that rezoning in the cost of the land sold.

. . .

. . . **The cost of modifying rights relating to what one can do with land are [sic] in my view a cost attributable to the land. They inhere in the land, whether or**

> **not a structure is erected on the land. In this case the proposed Phase II has not been erected**. It requires something of a leap of faith to claim capital cost allowance under Class 3 on a building that does not exist and may never exist. The land however does exist, along with all of the rights that inhere in it. The rights do not exist independently of the ownership of the land. If the ownership of the land is transferred, the rights follow it.
>
> [Emphasis added.]

[122] In the present case, the property purchased by the Appellant consisted of an office building and surface parking lot. Rezoning was obtained with respect to the parking lot in order to permit the construction of a high-rise residential condominium building whose condominium units were to be sold. Unfortunately the condominium market declined and the sales contracts were terminated. At that point, Heron Bay obtained an appraisal with respect to the Dundas Street property and, on the basis of this appraisal, it was determined that the value of the portion of the property attributable to the parking lot was less than the actual purchase price of that portion of the land. Heron Bay submits in its notice of appeal that deducting the $89,799 rezoning cost as an expense was equivalent to that amount being added to its inventory and then a deduction being claimed pursuant to subsection 10(1) of the *ITA*, since the fair market value of that inventory item was less than its cost. Other than this statement, there were no submissions or evidence presented on this issue.

[123] The Respondent, in its written submissions, argued that the amount in question was a once-and-for-all expenditure which would bring into existence an asset of permanent and enduring advantage. The parking lot was capital property to the Appellant, and was operated as rental property. It was not inventory, nor was it treated as such by the Appellant. In any event, the case law referred to below will suggest that the rezoning expenses should be added to the cost of the land. As Judge Bowman (as he then was) stated in *Sun Life Assurance Co. of Canada v. Canada*, [1997] T.C.J. No. 446 (QL):

> 16 *Counsel for the appellant contended that the acquisition of the density rights bore directly on the economics of the operation in the sense that a larger building could be constructed and increased rents would be received*. This is, I think, evident from the memorandum quoted above. Counsel also contended that density rights and zoning by-laws have to do essentially with buildings. In support of this he pointed to the City of Toronto Official Plan in which a number of the definitions of density appear to focus on the size of building that may be put on a lot.
>
> 17 *I do not necessarily disagree with these observations but*, notwithstanding Mr. van Banning's very able argument, *I do not think that they are determinative of the issue. In analyzing the question one must determine the true nature of zoning*.

> While I have no reluctance about reconsidering my own judgment in Cadillac Fairview, or in distinguishing it, I am not persuaded that I reached the wrong conclusion in that case. Nor can I see any rational basis for reaching a different conclusion depending on whether a building is constructed on the land.
>
> 18 **I continue to be of the view that since zoning determines what a landowner can do with land it is an attribute of the land and that costs associated with obtaining a change in zoning are part of the cost of land. Density rights have to do with what an owner can do with land. They are, therefore, an integral component in the value of land. They exist independently of their exercise and independently of any present or future building. They would continue to exist even if the building were demolished and the land were left vacant or another building erected. In light of this, it cannot be said that they form part of the cost of this particular building**. The obtaining of higher zoning, or increased density rights, may well affect the economics of the intended commercial operation but this results from the fact that the landowner has obtained the right to do more with the land. On one view of the matter one could say that the cost of purchasing the land is an integral part of the economics of the proposed commercial operation yet one could not include the cost of the land in the cost of the building. Possibly one way of testing the conclusion would be to envision the situation where the previous owner, before selling the land to Sun Life, had negotiated with the church and, for a price, obtained a higher density or more favourable zoning and as a result charged a higher price for the land. The increased price for the land could not be attributed to the building even though, in a sense, it relates to the type of building that can be constructed on the land.
>
> [Emphasis added.]

[124] While we have not been provided with evidence as to the nature of the rezoning expenses incurred, it would follow from the Respondent's argument that no deduction is permitted because the expenditure was a payment on account of capital and therefore prohibited by paragraph 18(1)(*b*). Although the Respondent submits that the rezoning expenses should be included as part of the cost of the parking lot, it could be argued that the cost incurred for the rezoning should be added to the land, in light of the case law mentioned earlier. Since no arguments or evidence were presented by the Appellant in this regard, the appeal on this issue is dismissed.

VIII. <u>Conclusion</u>

[125] The appeal is dismissed. Under subparagraph 20(1)(*l*)(ii), Heron Bay qualifies as a moneylender as there is an established system and continuity to the loans it makes. It fails, however, to meet the ordinary-course-of-business condition because non-recourse loans are not the typical loans that Heron Bay makes. Finally, Heron

Bay did not exercise informed judgment in the circumstances and as a consequence failed to meet the reasonableness requirement of the provision. The debt had not been outstanding for long, and it has not been established that there were changes in circumstances that gave Heron Bay cause to doubt the collectibility of the debt. Furthermore, the valuation evidence provided revealed that the difference in the value of the property was small. Thus, in the absence of more cogent evidence, there is nothing to establish that the write-off was reasonable. The requirements under subparagraph 20(1)(*p*)(ii) have not been met either, as there was no evidence provided that the debt was uncollectible.

[126] The cases considered by the Court are cited in the Appendix.

Signed at Ottawa, Canada, this 8th day of September 2009.

"Robert J. Hogan"

Hogan J.

APPENDIX

CASES CONSIDERED BY THE COURT

576315 Alberta Ltd. v. R., 2001 CarswellNat 1727, 2001 DTC 776, [2001] 4 C.T.C. 2169 (Tax Court of Canada [General Procedure]) – referred to.

Ainsworth Lumber Co. v. R., 2001 CarswellNat 824, [2001] 3 C.T.C. 2001, 2001 DTC 496 (Tax Court of Canada [General Procedure]) – referred to.

Akhtar v. R., 1998 CarswellNat 896, [1998] 3 C.T.C. 2888 (Tax Court of Canada) – considered.

Anderton and Halstead, Ltd. v. Birrell, (1931) 16 T.C. 200 – considered.

Associated Investors of Canada Ltd. v. Minister of National Revenue, 1967 CarswellNat 274, [1967] C.T.C. 138, [1967] 2 Ex. C.R. 96, 67 DTC 5096 (Exchequer Court of Canada) – considered.

British Columbia Telephone Co. v. Minister of National Revenue, 1986 CarswellNat 306, [1986] 1 C.T.C. 2410, 86 DTC 1286 (Tax Court of Canada) – referred to.

Burkes v. R., 2000 CarswellNat 2001, [2000] 4 C.T.C. 2511, 2000 DTC 2576 (Tax Court of Canada [General Procedure]) – considered.

Canada Trustco Mortgage Co. v. R., 2005 CarswellNat 3212, 2005 SCC 54, 2005 DTC 5523 (Eng.), 2005 DTC 5547 (Fr.), [2005] 5 C.T.C. 215, 340 N.R. 1, 259 D.L.R. (4th) 193, [2005] 2 S.C.R. 601 (Supreme Court of Canada) – referred to.

Canadian Commercial Bank v. Prudential Steel Ltd., [1986] A.J. No. 1142, 49 Alta. L.R. (2d) 58, 75 A.R. 121, 66 C.B.R. (N.S.) 172, 3 A.C.W.S. (3d) 10 (AB.C.Q.B.) – referred to.

Cloverdale Paint Inc. v. R., 2006 CarswellNat 4230, 2006 TCC 628, [2007] 2 C.T.C. 2024, 2007 DTC 243 (Eng.) (Tax Court of Canada [Informal Procedure]) – referred to.

Coppley Noyes & Randall Ltd. v. R., 1991 CarswellNat 411, [1991] 1 C.T.C. 541, 43 F.T.R. 291, 91 DTC 5291 (Federal Court -- Trial Division), varied 93 DTC 5508 (FCA) – referred to.

Discovery Research Systems Inc. v. R., 1994 CarswellNat 896, [1994] 1 C.T.C. 2473, 94 DTC 1510 (Tax Court of Canada) – considered.

Dutch-More Corp. v. Minister of National Revenue, 1980 CarswellNat 535, [1981] C.T.C. 2023, 81 DTC 34 (Tax Review Board) – considered.

Flexi-Coil Ltd. v. R., 1995 CarswellNat 1380, [1996] 1 C.T.C. 2941 (Tax Court of Canada) – referred to.

Flexi-Coil Ltd. v. R., 1996 CarswellNat 1459, [1996] 3 C.T.C. 57, 96 DTC 6350, (*sub nom.* Flexi-Coil Ltd. v. Minister of National Revenue) 199 N.R. 120 (Federal Court of Appeal) – referred to.

Highfield Corp. v. Minister of National Revenue, 1982 CarswellNat 368, [1982] C.T.C. 2812, 82 DTC 1835 (Tax Review Board) – referred to.

Hogan v. Minister of National Revenue, 1956 CarswellNat 72, 15 Tax A.B.C. 1 (Income Tax Appeal Board) – referred to.

Industrial Investments Ltd. v. Minister of National Revenue, 1973 CarswellNat 248, [1973] C.T.C. 2161, 73 DTC 118 (Tax Review Board) – referred to.

Langhammer v. R., 2000 CarswellNat 2833, [2001] 1 C.T.C. 2372, 2001 DTC 45 (Tax Court of Canada [General Procedure]) – considered.

Loman Warehousing Ltd. v. R., 1999 CarswellNat 1092, [1999] 4 C.T.C. 2049, 99 DTC 1113 (Tax Court of Canada [General Procedure]) – considered.

Loman Warehousing Ltd. v. R., 2000 CarswellNat 2339, 2000 DTC 6610, [2001] 1 C.T.C. 50, 262 N.R. 282 (Federal Court of Appeal) – referred to.

Minister of National Revenue v. Kelvingrove Investments Ltd., 1974 CarswellNat 185, [1974] C.T.C. 450, 74 DTC 6357 (Federal Court -- Trial Division) – referred to.

Newton v. Pyke, (1908) T.L.R. 127 – considered.

Nourse v. Canadian Canners Ltd., (1935) 3 D.L.R. 168 (Ont. C.A.) – considered.

No. 81 v. Minister of National Revenue, 1953 CarswellNat 36, 8 Tax A.B.C. 82 (Income Tax Appeal Board) – considered.

Orban v. Minister of National Revenue, 1954 CarswellNat 44, 10 Tax A.B.C. 178, 54 DTC 148 (Income Tax Appeal Board) – referred to.

Re Pacific Mobile Corp., (1982) 141 D.L.R. (3d) 696 (QC. C.A.) – referred to.

Pacific Mobile Corp. (Trustee of) v. American Biltrite (Canada) Ltd., [1985] S.C.J. No. 15 [1985] 1 S.C.R. 290 (1985), 16 D.L.R. (4th) 319 (1985), 55 C.B.R. (2d) 32 (Supreme Court of Canada) – referred to.

R. v. E.V. Keith Enterprises Ltd., 1975 CarswellNat 332, [1976] C.T.C. 21 (Federal Court – Trial Division) – considered.

R. v. Pollock Sokoloff Holdings Corp., 1974 CarswellNat 177, [1974] C.T.C. 391, 74 DTC 6321 (Federal Court – Trial Division) – considered.

Rich v. R., 2003 CarswellNat 123, 2003 FCA 38, 2003 DTC 5115, 300 N.R. 29, [2003] 3 F.C. 493, [2004] 1 C.T.C. 308 (Federal Court of Appeal) – referred to.

Royal Bank of Canada v. Tower Aircraft Hardware Inc., [1991] A.J. No. 121, 78 Alta. L.R. (2d) 271, 118 A.R. 86, 3 C.B.R. (3d) 655 (AB.C.Q.B.) – referred to.

R.S. Jackson Promotions Ltd. v. Minister of National Revenue, 1985 CarswellNat 238, [1985] 1 C.T.C. 2151, 85 DTC 145 (Tax Court of Canada) – referred to.

Saltzman v. Minister of National Revenue, 1964 CarswellNat 117, 35 Tax A.B.C. 93, 64 DTC 259 (Tax Appeal Board) – referred to.

Société d'investissement Desjardins v. M.N.R., 1990 CarswellNat 556, [1991] 1 C.T.C. 2214, 91 DTC 393 (en.), 91 DTC 373 (fr.) (Tax Court of Canada) – referred to.

Swystun Management Ltd. v. Minister of National Revenue, 1979 CarswellNat 374, [1979] C.T.C. 2476, 79 DTC 417 (Tax Review Board) – referred to.

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Zaenker v. R., 2007 CarswellNat 2261, 2007 TCC 440, 2007 DTC 1365 (en.), [2008] 1 C.T.C. 2128 (Tax Court of Canada [General Procedure]) – considered.

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APPEARANCES:

Counsel for the Appellant:	William I. Innes Douglas Stewart Brendan Bissell
Counsel for the Respondent:	John Shipley Perry Derksen

COUNSEL OF RECORD:

For the Appellant:

Name:	William I. Innes
Firm:	Fraser, Milner, Casgrain LLP Toronto, Ontario
For the Respondent:	John H. Sims, Q.C. Deputy Attorney General of Canada Ottawa, Canada