Docket: 2009-3346(IT)G

BETWEEN:

INDUSTRIES PERRON INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on April 21, 2011, at Montréal, Quebec.

Before: The Honourable Justice François Angers

Appearances:

Counsel for the appellant:	Ryan Rabinovitch
Counsel for the respondent:	Natalie Goulard

JUDGMENT

The appeal from the reassessment made pursuant to the *Income Tax Act* for the 2001 taxation year is dismissed, with costs, in accordance with the attached Reasons for Judgment.

Signed this 11th day of October 2011.

"François Angers"

Angers J.

Translation certified true
on this 12th day of January 2012.

François Brunet, Revisor

Citation: 2011 TCC 433
Date: 20111011
Docket: 2009-3346(IT)G

BETWEEN:

INDUSTRIES PERRON INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

REASONS FOR JUDGMENT

Angers J.

[1] This is an appeal from a reassessment of the appellant on February 3, 2005, in which the Minister of National Revenue (the "Minister") disallowed the $3,576,088 deduction in the calculation of its income for the 2011 taxation year. After receiving the Notice of Objection, the Minister amended the reassessment in question on May 2, 2005.

[2] At the beginning of the hearing, the parties submitted a partial agreed statement of facts and documents or exhibits deemed relevant to the resolution of this case. The relevant facts are as follows, with reference to exhibits attached to the agreement.

> [TRANSLATION]
> 1. The appellant is a Canadian-controlled private corporation.
>
> 2. The appellant's fiscal year ends on December 31 of each year.
>
> 3. The appellant exports Canadian lumber to the US.
>
> 4. On March 31, 2001, the Canada-US Softwood Lumber Agreement expired. Two days later, the US lumber industry filed a petition with the US Department of Commerce (DOC), for the introduction of

countervailing and antidumping duties.[1] The Canadian industry is accused of benefiting from a subsidy for its lumber production and selling it to the US at a price less than its cost of production.

5. Through its fiscal year ending December 31, 2001, the appellant accumulated an allowance (called an "allowance for countervailing and antidumping duties" on its financial records) of $3,578,088 in regard to the US softwood lumber industry petition.[2] When calculating its accrued and tax revenues for the 2001 taxation year, the appellant deducted $3,576,088.

US investigation into countervailing and antidumping duties

6. In the US, two authorities share responsibility of investigations into countervailing and antidumping duties, the DOC and the International Trade Commission (ITC).

7. The relevant US legislation can be found in the *Tariff Act of 1930*, 19 U.S.C. § 1671[3] and § 1673[4].

8. The DOC must determine whether the manufacture, production or export of merchandise imported or sold for import to the US is subsidized by a country's government, and whether the foreign merchandise is sold, or is likely to be sold, in the US at a price less than its fair value (dumping).

9. The ITC is responsible for determining whether there is a significant injury or threat of significant injury to an industry in the US because of subsidized imports or dumping.

10. The investigation process has two stages: the preliminary determination and the final determination. During the preliminary determination, the ITC and the DOC establish whether there is a "reasonable indication"/"reasonable basis to believe" in the existence of facts necessary to impose countervailing and antidumping duties (19 U.S.C. § 1671b(a) and (b); § 1671b(a) and (b)). During the final determination, the ITC and the DOC establish the existence of these facts (19 U.S.C. § 1671d(a) and (b); § 1673d(a) and (b)).

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1 US DOC, ITA, *Softwood Lumber From Canada*; 66 Fed. Reg. 18508 (2001) and US DOC, ITA, *Notice of Initiation of Countervailing Duty Investigation: Certain Softwood Lumber Products From Canada*; 66 Fed. Reg. 21332 (2001), **Exhibit A-1**.

2 Appellant's financial records for the fiscal year ending December 31, 2001, **Exhibit A-2**.

3 **Exhibit A-10**.

4 **Exhibit A-11**.

Preliminary determinations

11. On May 23, 2001, the ITC rendered a preliminary determination that there was a reasonable indication that the Canadian exports of softwood lumber to the US constituted a threat of serious injury to the US industry.[5] This determination applies to both the countervailing and dumping duties.

12. On August 17, 2001, the DOC rendered a preliminary determination that there was a reasonable basis to believe that subsidies were granted to Canadian lumber producers and exporters.[6] Because of this preliminary determination, the DOC set an estimated subsidy rate of 19.31% and asked customs to require, in accordance with 19 U.S.C. § 1671b(d)(1)(B),[7] a cash deposit or bond based on this rate.

13. On November 6, 2001, the DOC rendered a preliminary determination that there was a reasonable basis to believe that certain Canadian lumber products were sold, or were likely to be sold, in the US at a price less than their fair value.[8] Considering this preliminary determination, the DOC set an estimated weighted average dumping margin of 12.58% and asked customs to require, in accordance with 19 U.S.C. § 1673b(d)(1)(B),[9] a cash deposit or bond based on this margin.

14. In the months following the preliminary determinations, the appellant purchased term deposits and placed them as a guarantee with the Royal Bank of Canada.[10] These term deposits were to guarantee letters of credit

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5 US ITC, *Softwood Lumber from Canada*, Pub. No. 3426, May 2001, **Exhibit A-9**.

6 US DOC. ITA. *Notice of Preliminary Affirmative Countervailing Duty Determination, Preliminary Affirmative Critical Circumstances Determination, and Alignment of Final Countervailing Duty Determination With Final Antidumping Duty Determination: Certain Softwood Lumber Products From Canada*; 66 Fed. Reg. 43186 (2001), **Exhibit A-12**.

7 **Exhibit A-10**.

8 US DOC, ITA, Notice of Preliminary Determination of Sales at Less Than Fair Value and Postponement of Final Determination: Certain Softwood Lumber Poducts [*sic*] From Canada, 66 Fed. Reg. 56062 (2001), **Exhibit A-13**.

9 **Exhibit A-11**.

10 Deed of immovable hypothec guaranteeing the appellant's commitment to the Royal Bank of Canada, pursuant to the Bank's issuing a letter of credit dated September 20, 2011, in the amount of US$510M (CAN$790,500), **Exhibit A-3**; Letter of credit dated September 20, 2001, **Exhibit A-4**; Deed of immovable hypothec guaranteeing the appellant's commitment to the Royal Bank of Canada pursuant to the Bank's issuing a letter of credit dated October 17, 2001, in the amount of US$510M (CAN$790,500), **Exhibit A-5**; Letter of credit dated October 17, 2001, **Exhibit A-6**; Deed of immovable hypothec guaranteeing the appellant's commitment to the Royal Bank of Canada pursuant to the Bank's issuing a letter of credit

issued by the Royal Bank of Canada in favour of the Washington International Insurance Company (WIIC), which agreed to guarantee the payment of part of the countervailing and antidumping duties sought by the US lumber industry.

15. The term deposit rates of return varied between 1.35% and 2.05%.

16. The total amount of the term deposits was $2,371,500.

17. The total amount of the letters of credit issued by the Royal Bank of Canada was also $2,371,500.

18. The total amount guaranteed by WIIC during the appellant's fiscal year ending December 31, 2001, was US$1,530,000 (the equivalent of CAN$2,371,500).

Final determinations

19. On April 2, 2002, the DOC rendered a final determination that subsidies were granted by the Canadian government for certain Canadian lumber products exported to the US.[11] The DOC also rendered a final determination stating that merchandise was sold or likely to be sold in the US at prices less than their fair value.[12]

20. On May 22, 2002, the ITC rendered a final determination that a US industry was threatened with significant injury because of the importation of Canadian lumber, subsidized and sold at a price less than its fair market value.[13]

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dated December 12, 2001, in the amount of US$510M (CAN$790,500), **Exhibit A-7**; Letter of credit dated December 12, 2001, **Exhibit A-8**.

11 US DOC, ITA, *Notice of Final Affirmative Countervailing Duty Determination and Final Negative Critical Circumstances Determination: Certain Softwood Lumber Products From Canada*; 67 Fed. Reg. 15545 (2002), **Exhibit A-14**, amended by *Notice of Amended Final Affirmative Countervailing Duty Determination and Notice of Countervailing Duty Order: Certain Softwood Lumber Products From Canada*; 67 Fed. Reg. 36070 (2002), **Exhibit A-15**.

12 US DOC, ITA, *Notice of Final Determination of Sales at Less Than Fair Value: Certain Softwood Lumber Products from Canada*, 67 Fed. Reg. 15539 (2002), **Exhibit A-16**; amended by *Notice of Amended Final Determination of Sales at Less Than Fair Value and Antidumping Duty Order: Certain Softwood Lumber Products from Canada*, 67 Fed. Reg. 36068 (2002), **Exhibit A-17**.

13 US ITC, Softwood Lumber from Canada, Pub. No. 3509, May 2002, Exhibit A-18.

The orders

21. On May 22, 2002, the DOC published notices of its orders regarding the countervailing[14] and antidumping duties.[15]

22. Moreover, the DOC determined that imposing countervailing and antidumping duties for the period covered in its preliminary determinations was not warranted in this case. Therefore, the countervailing and antidumping duties are imposed only as of May 22, 2002, the publication date of the DOC orders, and the DOC directs customs to repay the cash deposits and release the bonds required as provisional measures following the preliminary determinations of August 17 and November 6, 2001.

23. All the bonds provided by WIIC on behalf of the appellant in 2001 and the term deposits placed as guarantee by the appellant with the Royal Bank of Canada were released in 2002.

24. The appellant and one of its successors included, for accounting and taxation purposes, $3,578,088 in their 2002 income.

25. On February 3, 2005, the Canada Revenue Agency issued reassessments disallowing the $3,576,088 deduction claimed by the appellant in 2001 and deducting the same amount from the 2002 income of the taxpayer and its successor.

26. Ultimately, the DOC orders were revoked pursuant to the *Canada-US Softwood Lumber Agreement*, signed on September 12, 2006.

[3] The issue is therefore whether the Minister was warranted in disallowing the $3,576,088 deduction in the appellant's income calculation for the 2001 taxation year. Was it an expense made or incurred by the appellant for the purpose of gaining income from its business in accordance with paragraph 18(1)(*a*) of the *Income Tax Act* (the Act)? Did this expense incurred by the appellant constitute a reserve, a contingent amount or sinking fund pursuant to paragraph 18(1)(*e*) of the Act or was the expense an amount paid by the appellant for an existing or proposed countervailing or antidumping duty in respect of property pursuant to paragraph 20(1)(*vv*) of the Act?

[4] Here are the relevant legislative provisions:

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[14] **Exhibit A-15**, *supra*, note 11.

[15] **Exhibit A-17**, *supra*, note 13.

Section 18: **General limitations**

(1) In computing the income of a taxpayer from a business or property no deduction shall be made in respect of

(a) **General limitation** — an outlay or expense except to the extent that it was made or incurred by the taxpayer for the purpose of gaining or producing income from the business or property;

…

(e) **Reserves, etc**. **—** an amount as, or on account of, a reserve, a contingent liability or amount or a sinking fund except as expressly permitted by this Part;

…

(*vv)* **Countervailing or antidumping duty —** an amount paid in the year by the taxpayer as or on account of an existing or proposed countervailing or antidumping duty in respect of property (other than depreciable property)

…

[5] The parties agree that paragraphs 18(1)(*a*) and 18(1)(*e*) of the Act should be interpreted together since the issues I am called to decide are whether the appellant had an obligation to pay an amount and whether the obligation was a result of a contingent liability or amount. This goes without saying. Under paragraph 18(1)(*a*), the expense must be incurred before it can be deductible, which generally implies that the taxpayer must have a legal obligation to pay this expense to a third party. According to the case law and paragraph 18(1)(*e*) of the Act, this obligation cannot be a contingency.

[6] That being said, the issue is whether, in view of the facts of this case, the appellant had a legal obligation to pay the amount in question and, if so, whether the obligation was a contingent liability.

18(1)(*a*) and 18(1)(*e*)

[7] The appellant submits that it had the right to deduct the total amount of the estimated subsidy rate of 19.31% and the estimated dumping margin of 12.58% since, once the preliminary determinations were rendered, it had to conform. To this end, the appellant had to conform to the requirements of the Washington International Insurance Company, a US company that issues bonds and required a

letter of credit from the Royal Bank of Canada, supported by term deposits the appellant purchased for a total of CAN$2.4 million. (See paragraphs 14, 16, 17, and 18 of the Facts.)

[8] The appellant submits that, in view of this obligation to purchase term deposits, it was responsible for paying this amount to the Royal Bank of Canada, to mortgage them to the Bank in return for the Bank's issuing the letters of credit. The appellant notes that this money was practically frozen in the sense that the appellant could not do what it wanted as long as the term deposits were mortgaged. The appellant submits that this obligation was not subject to a contingency because it had to pay the $2.4 million to purchase the term deposits.

[9] The respondent's theory is based on the fact that the appellant's only obligation for the 2001 taxation year was one that depended solely on a tax determination by the US authorities regarding the existence of a subsidy or threat to a US industry of significant injury, namely the imposition of countervailing and antidumping duties. As long as the final determination was not made, the obligation to pay the countervailing and antidumping duties did not exist; they would only come into existence if certain events occurred, which, in this case, did not happen.

[10] The respondent submits that this is in fact what paragraphs 18(1)(*a*) and 18(1)(*e*) of the Act prevent. They prevent the deduction of an expense that is not certain because it is only a preliminary determination that is subject to a contingency, namely the final determination and order being issued regarding the countervailing and antidumping duties. According to the respondent, an expense is generally incurred by a taxpayer at the time an obligation to pay an amount of money comes into existence.

[11] The parties respectively cited the same excerpts from the case law on what constitutes a certain legal obligation. I will stand by *McLarty v. R.* 2008 D.T.C. 6366, a Supreme Court decision, in which Rothstein J. summarized the issue at paragraph 18:

> **18** What constitutes a contingent liability was further clarified by Sharlow J.A. in *Wawang,* at para. 15. By themselves, three uncertainties will not determine whether a liability is contingent. I paraphrase her reasons as follows:
>
> - (a) Uncertainty as to whether the payment will be made. For example, a liability may be incurred when the taxpayer is in financial difficulty and there is a significant risk of non-payment. That does not mean the obligation was never incurred;

- (b) Uncertainty as to the amount payable. There is always uncertainty as to the amount that may be payable. There is never certainty that the borrower will be able to pay the amount owing when the note comes due. That type of uncertainty does not make a liability contingent;

- (c) Uncertainty as to the time by which payment shall be made. An obligation is not contingent because payment may be postponed if certain events occur.

The test is simply whether a legal obligation comes into existence at a point in time or whether it will not come into existence until the occurrence of an event which may never occur.

[Emphasis added]

[12] First and foremost, in this case, my view is that the appellant's obligation to pay a sum of money during the 2001 taxation year must be identified. According to the appellant, this obligation was to purchase certificates of deposit to meet the Bank's requirements, whereas the respondent claims that the appellant's only obligation in 2001 was to provide a cash deposit or bond based on the margins established in the preliminary determination. The right to impose countervailing and antidumping duties would be the subject of a final determination later, such that the countervailing duties, if any, would be established after the determination was made.

[13] The purchase of term deposits cannot, in my opinion, be considered a deductible expense in this case, under paragraph 18(1)(*a*) of the Act, even if these term deposits were mortgaged in favour of the Bank and the appellant temporarily lost enjoyment. The appellant's financial records show, in its assets, the term deposits in question with an explanatory note stating they were to be used to guarantee letters of credit. The appellant acknowledges that it is a contingency in explanatory note 18 of its financial records.

[14] Pursuant to section 1671b of the US law on countervailing duties (tab 10), the preliminary determination is based solely on information available at the time of the determination that show a reasonable indication that a US company might be injured or is threatened, and the effect of this determination means the US authorities have the duty to establish an estimated rate for the countervailing duties and order a deposit of money, bond or other guarantees for all entries of merchandise. The same is true for antidumping duties. Until the final determination is made, the appellant is under no obligation to pay the countervailing duties. There was only an estimate of

the countervailing rate and a requirement to pay or produce bond to guarantee payment, which the appellant did in the circumstances.

[15] The appellant's financial records indicate this state of affairs as I have already noted and a provision of $3.6 million was accounted for accordingly. I therefore agree with the respondent that in 2001, there was no obligation to pay the countervailing and antidumping duties. I also feel that in this case, the fact the appellant chose to guarantee its potential liabilities by purchasing term deposits is not relevant to the determination of its legal obligations to the US authorities.

[16] Therefore, in 2001, there was no legal obligation regarding the appellant's countervailing and antidumping duties. This legal obligation would only have existed upon the final determination by the US authorities. There were therefore no expenses incurred within the meaning of paragraphs 18(1)(*a*) and 18(1)(*e*) of the Act. Even if the appellant claims it paid the amount of the term deposits to the Royal Bank, the fact is, it only mortgaged them. Even if the appellant agreed to not use them without the Bank's consent, which is not clear according to the documents submitted to evidence, this would not be the equivalent of a transfer of property rights. The amounts of money in question are subject to a contingency, where the appellant defaults on the advances granted by the Royal Bank.

20(1)(*vv*)

[17] The appellant submits that under paragraph 20(1)(*vv*) the appellant may at least deduct the $2.4 million it paid to the Royal Bank for the term deposits, in the same manner as a taxpayer who paid cash for the rate estimated by the US authorities. In both cases, it would be a disbursement, no matter what. The appellant submits that it is an amount paid by the taxpayer during the year for existing or proposed countervailing or antidumping duties on property. It is a different concept than the one at paragraph 18(1)(*a*) of the Act that covers expenses incurred or made. According to the appellant, it is possible to find that the payments made to the Royal Bank to purchase the term deposits were actually paid as proposed countervailing and antidumping duties. The appellant focuses on the English version of the provision that mentions an amount paid as duty "or on account of an existing or proposed countervailing or antidumping duty." In the French version, there is no such advance account for countervailing or antidumping duties. According to the appellant, it would be difficult to not find that in this case, the payment made to the Royal Bank was a payment for the proposed countervailing and antidumping duties.

[18] The appellant also raised the issue of the interpretation of the word "paid" as found at paragraph 20(1)(*vv*) of the Act. It notes that the *Civil Code of Québec* applies in this case, considering the provisions of articles 8.1 and 8.2 of the federal *Interpretation Act* and the fact the concept of "paid" is rather broad. Article 1553 of the *Civil Code* defines the word "payment" as follows:

> Payment means not only the turning over of a sum of money in satisfaction of an obligation, but also the actual performance of whatever forms the object of the obligation.

[19] The respondent acknowledges that, contrary to paragraphs 18(1)(*a*) and 18(1)(*e*), paragraph 20(1)(*vv*) of the Act clearly provides for existing or proposed countervailing and antidumping duties such that, if the other conditions are met and the obligation is uncertain as is the case with a preliminary determination, the deduction may be allowed. However, she insists that under paragraph 20(1)(*vv*) of the Act, it must be an amount paid in cash for these duties, and therefore an amount actually paid to meet the obligation to pay the duties in question. The respondent claims that the usual and ordinary meaning of the verb "to pay" means giving an amount of money and that paragraph 12(1)(*z.6*) of the Act, which requires the amount received by a taxpayer during the year as repayment for an amount deducted under paragraph 20(1)(*vv*) to be included in the taxpayer's income, supports her interpretation that an amount of money must be paid before it can be reimbursed. It is clear that we are not talking about a guarantee or bond that would eventually be set aside, which is what happened in this case.

[20] It is true that article 1553 of the Civil Code defines payment to include not only the turning over of a sum of money in satisfaction of an obligation, but also the actual performance of whatever forms the object of the obligation. Many Quebec court decisions have confirmed this principle, see *Dufresne v. Paul Léger Ltd.* (1980) EYB 137591 and *Pisapia Construction Inc. v. St-Fabien Industriel Inc*. [1977] CA 528.

[21] Didier Lluelles and Benoit Moore, in *Droit des obligations*, make the following comments on the meaning of the word “payment”:

> [TRANSLATION]
> Through the payment, the debtor completes his duty to meet the obligation and is released from it. This duality of the payment makes it an extinguishing method that differs from other methods such as debt release or limitation. The payment relates to all services indiscriminately and not only those involving a monetary debt (art. 1553). Of course, the tenant who pays monthly rent meets his obligation. But the

> building painter who applies paint to the walls of his client's cottage or the diva who sings at the Opéra de Québec also "pay" their obligation. Similarly, the concept of payment also includes obligations to not act: by refraining from operating a similar business, in accordance with a non-competition clause, the cedant of a business "pays" his obligation. The Civil Code uses the word "payment" in a broader sense than that in common language.

[22] Article 1554 of the Civil Code also provides that a payment can exist when no prior obligation exists. This article reads as follows:

> 1554. Every payment presupposes an obligation; what has been paid where there is no obligation may be recovered.
>
> Recovery is not admitted, however, in the case of natural obligations that have been voluntarily paid.

[23] The above-noted authors comment on the scope of article 1554 as follows:

> [TRANSLATION]
> "Every payment presupposes an obligation", article 1554 states, in its first paragraph. The payment can therefore, to a certain extent, be subject to a "cancellation" at the request of the payor or the payor's heirs, if there is no prior obligation. A payment made in error is subject to recovery. The payment made before the existence of a suspensive condition is also subject to recovery since the debt did not yet exist. However, as we have seen, the voluntary payment of a natural obligation is irretrievable. As for a payment made before a deadline arrives, it is, in principle, valid because the debt was then in existence, although not yet due. We must remember that the creditor may, in certain cases, object to a pre-term payment.

[24] It is therefore necessary for an obligation to exist before a valid payment can be made. Beaudoin and Jobin, in the 6th edition of *Les obligations* (Yvon Blais, 2005), explain what constitutes an obligation.

> [TRANSLATION]
> In civilian terminology, the word "obligation" has a much more specific meaning. It is a legal relationship between two or more persons by which one person, called the debtor, is bound to render a prestation to another person, called the creditor, and which consists in doing or not doing something, subject to a legal compulsion.

[25] Does this broad interpretation of the word "payment" mean it is possible to find that the appellant paid an amount for existing or proposed countervailing or antidumping duties or as a deposit, as the English version implies?

[26] In this case, the appellant did not pay the US authorities any amount as existing or proposed countervailing or antidumping duties. The appellant chose to provide bail and, to do so, it had to pay the Royal Bank of Canada a sum of money to acquire term deposits that the appellant then mortgaged in favour of the Bank so it would issue letters of credit to the Washington International Insurance Company for it to guarantee the payment of part of the duties in question.

[27] Although the funds used for the acquisition of the term deposits were mortgaged and the use of the funds was restricted by the Royal Bank, they were still the appellant's property. Even if the appellant claims it paid the amount of the term deposits to the Royal Bank, in fact, it only mortgaged them and even if it committed to only dispose of them with the Bank's consent, this does not amount to a transfer of property.

[28] The only obligation the appellant had was to meet the Royal Bank's requirements in its relationship as debtor and creditor, which was created by the purchase of the term deposits. Moreover, at no relevant time during the 2001 taxation year were there existing or proposed countervailing or antidumping duties since these duties would only have been established in the final determination.

[29] The respondent is therefore warranted in disallowing the deduction in the calculation of the appellant's income for the 2001 taxation year. The appeal is dismissed with costs.

Signed, this 11th day of October 2011.

"François Angers"

Angers J.

Translation certified true
on this 12th day of January 2012.

François Brunet, Revisor

CITATION:	2011 TCC 433
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