Vol. 18 No. 5 September 2015

2 Bloor Street West, Suite 2603, Toronto, Ontario M4W 3E2
Telephone: (416) 961-5612 Fax: (416) 961-6158
E-mail: valuators@marmerpenner.com

Marmer Penner Inc. Newsletter

Written by Steve Z. Ranot, CPA, CA•IFA/CBV
Edited by James A. DeBresser, CPA, CA•IFA, CBV

Legal Fees Incurred to Dispute Estate's Use of Funds Non-Deductible

Stop me if you've heard this one before: Father remarries and his children incur legal fees fighting the step-mother over her use of the estate's funds.

In a recent court decision, we noted a tax twist to this age-old battle. Father died leaving an estate to which the step-mother was the income beneficiary and to which the children of his first marriage were the capital beneficiaries. In other words, this was a typical spousal trust. The children contested the type of retirement fund the step-mother caused the estate to purchase. If the estate purchased a GIC, the children would be pleased because the principal would remain intact for them. If, instead, she purchased a life annuity, there would be no principal left for them with such an investment. The children contested her choice of investments in Quebec Superior Court and the Quebec Court of Appeal and lost in both. Then, one of the children tried to deduct the legal fees as a fee incurred to earn investment income, albeit in the future only. Their position was that if they could limit how much the step-mother was permitted to withdraw from the estate, that would increase their expected future investment income therefrom. Canada Revenue Agency denied the deduction and the taxpayer appealed that assessment to the Tax Court of Canada.

The Tax Court of Canada dismissed the appeal on the following grounds:

a) The legal fees were incurred by the taxpayer to establish alleged rights to the father's estate, rights which the court determined he did not have; and

b) Fees relating to the establishment of rights are capital in nature and not directly incurred to gain or produce income.

This is our second newsletter in 2015 focused on Tax Court of Canada decisions that denied the deductibility of legal fees. Our January 2015 newsletter related to deducting legal fees incurred by the father to collect support. Practitioners should be wary when assuring clients that fees may be deductible. "May" may be too strong a word.

shareholders' loans in subsidiary corporations (the "Loans") on which it realized losses. The Minister determined that the taxpayer's non-capital losses for 2001 did not include the losses on the disposition of the Loans (the "Losses"). The taxpayer appealed to the Tax Court of Canada.

The taxpayer's appeal was allowed. The Court needed to determine the fair market value of the Loans at the time of their non-arm's length disposition and whether the Losses were on income or capital account. The fair market value of the Loans was no higher than what the taxpayer had claimed and the Minister was unable to prove otherwise, so the Losses amounted to $411,830. Although the taxpayer was in the business of lending money, the Loans were not part of that business. However, the Loans were made for the purpose of earning income from the taxpayer's home manufacturing business, so its non-capital losses for 2001 should be increased by the amount of the Losses. The Minister was ordered to reassess accordingly.

¶48,888, *SRI Homes Inc.*, 2014 DTC 1185

Taxpayer not entitled to deduct legal expenses incurred in litigation involving his father's estate

GD was the taxpayer's father. The taxpayer and his siblings incurred legal expenses associated with litigation concerning the interpretation of GD's will. The issue concerned the type of retirement fund GD's surviving wife, GG, was entitled to purchase using estate funds, since the taxpayer and his siblings were entitled under the will to what remained of that retirement fund upon GG's death. Those siblings were therefore interested in restricting the type and amount of investment chosen by GG, to ensure that a larger amount would be available to them out of GD's estate on her death. They therefore instituted proceedings in two separate actions in the Quebec Superior Court, alleging that GG was restricted in the range of retirement fund investments available to her under the provisions of GD's will. In both actions this allegation was rejected, and the conclusion reached by the Quebec Superior Court and the Quebec Court of Appeal in both cases was that GG was not limited in the range of retirement fund investments available to her under GD's will. In assessing the taxpayer for 2011, the Minister disallowed the deduction of $21,609, which represented the taxpayer's share of the legal expenses incurred in the second of the two unsuccessful actions (the "Disputed Expenses"). The taxpayer appealed to the Tax Court of Canada.

The taxpayer's appeal was dismissed. The purpose of the taxpayer's second action was to establish his entitlement to benefits from GD's estate, and to support the estate's claim for the reimbursement of excess amounts allegedly paid to a liquidator. In essence, therefore, the Disputed Expenses were incurred by the taxpayer to establish alleged rights to GD's estate, which the courts determined that he did not have. Hence, it was difficult to see how the $21,609 in issue could be deducted under paragraph 18(1)(*a*) of the *Income Tax Act* (the "Act") as a legal expense incurred to earn income, inasmuch an increased entitlement to a portion of GD's estate on GG's death did not constitute income from property. Nor did the reimbursement payment to GD's estate being sought by the taxpayer constitute income to him in respect of which he had incurred the Disputed Expenses. Finally, even if the Disputed Expenses were laid out to earn income from property, they were capital in nature and, hence, non-deductible under paragraph 18(1)(*b*) of the Act. The Minister's assessment was affirmed accordingly.

¶48,890, *Deschenes*, 2014 DTC 1187

Director liability assessments dismissed as directors had validly resigned from company

The taxpayers, D and S, were reassessed for $500,000 of unremitted tax withholdings including penalties and interest of 1056922 Ontario Limited, a corporation whose affairs and business were managed and operated by their husbands. The amounts were for the 2000 to 2005 tax years. The taxpayers argued that they had resigned more than two years before the director liability assessments and, alternatively, they were directors in name only and relieved of liability by the due diligence defence.

The taxpayers' appeals were allowed. While the taxpayers' husbands could have been pursued as directors or as *de facto* directors, the Minister instead chose to pursue the taxpayers, who were the *de jure* directors. The taxpayers had validly resigned from the corporation more than two years before the assessments. Even if the resignations were not

forward either a doctor's note or a medical certificate. The Appellant did not forward a doctor's note; he did not even respond to the Court's letter and his request for an adjournment was denied.

[22] Sometime between May 14, 2014 and July 7, 2014, the Appellant engaged counsel for the sole purpose of requesting an adjournment of this appeal. On July 7, 2014, a Notice of Application for an Order adjourning the hearing date was filed with the Court. On July 8, 2014, the Appellant and George Alatopulos, counsel on the application, were notified that Associate Chief Justice Rossiter had denied the adjournment request. Mr. Alatopulos appeared in Court on July 9, 2014 and he made it clear that he was engaged by the Appellant for the sole purpose of making the adjournment request. I confirmed that an adjournment would not be granted.

[23] The documents which accompanied the application for an adjournment disclosed that the Appellant had been living in the United Kingdom since at least September 14, 2010. According to his Marriage Certificate, he married Ping Wang, a British citizen, in Oxford, England on that date. His profession was listed as a car dealer. Also included with the attachments to the application for an adjournment was a letter from Visa & Immigration UK which indicated that on June 15, 2014, the Appellant had submitted an application for naturalisation in the United Kingdom.

[24] At no time prior to the application for an adjournment, did the Appellant inform this Court that he was no longer living in China and had moved to the United Kingdom.

[25] On a review of this file, it appears to me that the Appellant was more interested in obtaining a Visa to enter Canada than he was in prosecuting his appeal. The Appellant was given numerous opportunities to proceed with his appeal and he chose instead to insist that the Court should assist him with obtaining a Visa to enter Canada. The appeal is dismissed for want of prosecution.

COSTS

[26] The Respondent has asked for costs of $11,693.43. It is my view that she is entitled to costs as the Appellant's delay in proceeding with this appeal has been inordinate and has caused the Respondent to incur costs. He has failed to prosecute his appeal in spite of the many accommodations given to him over a period of nine years. The Respondent is entitled to her disbursements of $4,218.43 and costs for the services of counsel in the amount of $5,725 for a total cost of $9,943.43.

Michel Deschenes (Appellant) v. Her Majesty the Queen (Respondent)

2014 DTC 1187

2014 CCI 261

Tax Court of Canada, August 29, 2014, Dossier No. 2013-4861(IT)I

Deductions — Deductible expense or non-deductible capital outlay — Taxpayer incurred legal expenses in attempt to determine his ultimate entitlement to a portion of a retirement fund provided in his father's estate for his father's surviving wife — Whether such legal expenses deductible — *Income Tax Act*, RSC 1985, c. 1 (5th Supp.), s. 18(1)(*a*), (*b*).

GD was the taxpayer's father. The taxpayer and his siblings incurred legal expenses associated with litigation concerning the interpretation of GD's will. The issue concerned the type of retirement fund GD's surviving wife, GG, was entitled to purchase using estate funds, since the taxpayer and his siblings were entitled under the will to what remained of that retirement fund upon GG's death. Those siblings were therefore interested in restricting the type and amount of investment chosen by GG, to ensure that a larger amount would be available to them out of GD's estate on her death. They therefore instituted proceedings in two separate actions in the Quebec Superior Court, alleging that GG was restricted in the range of retirement fund investments available to her under the provisions of GD's will. In both actions this allegation was rejected, and the conclusion reached by the Quebec Superior Court and the Quebec Court of Appeal in both cases was that GG was not limited in the range of retirement fund investments available to her under GD's will. In assessing the taxpayer for 2011, the Minister disallowed the deduction of $21,609, which represented the taxpayer's share of the legal expenses incurred in the second of the two unsuccessful actions (the "Disputed Expenses"). The taxpayer appealed to the Tax Court of Canada.

Held: The taxpayer's appeal was dismissed. The purpose of the taxpayer's second action was to establish his entitlement to benefits from GD's estate, and to support the estate's claim for the

reimbursement of excess amounts allegedly paid to a liquidator. In essence, therefore, the Disputed Expenses were incurred by the taxpayer to establish alleged rights to GD's estate, which the courts determined that he did not have. Hence it was difficult to see how the $21,609 in issue could be deducted under paragraph 18(1)(*a*), of the *Income Tax Act* (the "Act") as a legal expense incurred to earn income, inasmuch an increased entitlement to a portion of GD's estate on GG's death did not constitute income from property. Nor did the reimbursement payment to GD's estate being sought by the taxpayer constitute income to him in respect of which he had incurred the Disputed Expenses. Finally, even if the Disputed Expenses were laid out to earn income from property, they were capital in nature and hence non-deductible under paragraph 18(1)(*b*) of the Act. The Minister's assessment was affirmed accordingly.

Counsel: The appellant on his own behalf; A.-M. Boutin for the respondent

Before: Jorré J

JORRÉ J :

[1] Dans sa déclaration de revenu pour l'année fiscale 2011, l'appelant a déduit 21 609 $ à titre de frais juridiques.

[2] En cotisant, le ministre du Revenu National a refusé la déduction et l'appelant appelle de la cotisation.

[3] Il s'agit d'une très longue histoire avec beaucoup de faits, mais les faits essentiels ne sont pas compliqués.

[4] Le père de l'appelant, Guy Deschenes, est décédé en 1997. Parmi les dispositions dans le testament de M. Deschenes, il y a le paragraphe suivant :

> Je donne et lègue à titre de legs particulier à ma conjointe Dame Ghislaine Gagné mon Régime Enregistré Épargne Retraite (REER) en pleine et absolue propriété dès l'instant de mon décès. Cependant madite conjointe devra à mon décès acheter un Fonds [*sic*] Enregistré de Régime Retraite (FERR) dont les bénéficiaires seront madite conjointe Dame Ghislaine Gagné et à son décès mes enfants ci-après.

[5] L'appelant croit qu'en vertu de cette disposition, Ghislaine Gagné était obligée d'acheter un fonds enregistré de revenu de retraite avec certaines caractéristiques d'une compagnie d'assurance.

[6] Mme Gagné était d'avis qu'elle pouvait choisir n'importe quel fonds enregistré de revenu de retraite.

[7] La conséquence pratique de ce désaccord est que, si l'appelant avait eu raison, Mme Gagné aurait été restreinte dans les montants qu'elle pouvait recevoir et, potentiellement, au décès de Mme Gagné, l'appelant et les autres enfants de M. Deschenes recevraient un montant d'argent plus élevé.

[8] Ce litige a été très longuement débattu devant les tribunaux. Les tribunaux, y compris la Cour d'appel du Québec en 2007, sont d'accord avec Mme Gagné; elle peut choisir librement le fonds enregistré de revenu de retraite qu'elle veut. En 2008, le fonds choisi par Mme Gagné a reçu l'argent provenant du régime enregistré d'épargne retraite de M. Deschenes.

[9] Toutefois, ceci n'est pas la fin de l'histoire, car, en 2010, l'appelant et ses deux frères ont intenté une autre demande en justice en Cour Supérieure. Cette demande mène à la décision dans *Deschênes c. Services financiers Dundee ltée*, 2011 QCCS 5954. Les motifs ont été rendus le 31 octobre 2011.

[10] Les détails de cette saga sont énumérés dans les motifs de la décision *Deschênes*.

[11] Les frais juridiques encourus en 2011 et dont il est question sont engagés dans le cadre de cette demande. Le montant de 21 609 $ représente un tiers des frais juridiques encourus. Les deux frères de l'appelant ont payé le reste des frais.

[12] Quand on lit le jugement, on constate qu'il s'agit d'un effort de la part de l'appelant de poursuivre, d'une autre façon, la même question d'interprétation du testament qui avait déjà été décidée. En plus, la succession a fait une demande en dommages-intérêts.

[13] L'appelant n'a mis en preuve que la première page de la requête introductive d'instance,[1] mais, la Cour Supérieure, au paragraphe 56 du jugement *Deschênes*, reproduit :

> ... Les deux principales conclusions de la requête introductive d'instance amendée sont reproduites ci-dessous :
>
> > ORDONNER à Dundee de retourner à Ghislaine la somme de 1 040 090,00$ (UN MILLION QUARANTE MILLE QUATRE-VINGT-DIX DOLLARS) somme initialement reçue afin que Ghislaine Gagné puisse stipuler pour autrui à un contrat FERR d'assurance qui créera, dès la conclusion du contrat, une créance irrévocable entre le promettant Dundee et les bénéficiaires Deschênes qui n'entrera à aucun moment dans le patrimoine du stipulant le tout selon les instructions du document d'adhésion P-12 ayant par contrat judiciaire force de chose jugée;

[1] Pièce A-4 (pour identification) à l'onglet 4, qui est en preuve.

> CONDAMNER Dundee à payer la Succession de feu Guy Deschênes la somme de 122 000,00$ (CENT VINGT-DEUX MILLE DOLLARS) en remboursement du travail excédentaire du liquidateur suite au Jugement Hallée somme à parfaire du 1er juin 2008 jusqu'au terme de la présente procédure;

[14] L'appelant n'a pas eu plus de succès en 2011 qu'auparavant. Je note aussi que sa tentative d'appel à la Cour d'appel du Québec a été rejetée suite à des requêtes de la part des parties défenderesses.[2]

[15] Il est clair que le but des dépenses encourues en 2011 par l'appelant est d'établir qu'il a certains droits dans la succession. Il y avait aussi un deuxième but; la succession cherchait à obtenir des dommages-intérêts.

[16] Je ne vois pas comment, dans ses circonstances, il peut s'agir de dépenses déductibles.

[17] Pour qu'une dépense soit déductible il y a, entre autres, deux conditions générales prévues aux sous paragraphes 18(1)*a)* et *b)* de la *Loi de l'impôt sur le revenu* :

> 18 (1) Dans le calcul du revenu du contribuable tiré d'une entreprise ou d'un bien, les éléments suivants ne sont pas déductibles :
>
> *a)* les dépenses, sauf dans la mesure où elles ont été engagées ou effectuées par le contribuable en vue de tirer un revenu de l'entreprise ou du bien;
>
> *b)* une dépense en capital, une perte en capital ou un remplacement de capital, un paiement à titre de capital ou une provision pour amortissement, désuétude ou épuisement, sauf ce qui est expressément permis par la présente partie;

[18] Il ne s'agit certainement pas de dépenses d'entreprise.

[19] Un droit de quelque nature est un bien au sens de la Loi.[3]

[20] L'appelant prétend que son but été de préservé un bien, certains droits, parce que, selon l'appelant, ces droits existaient des le décès de son père. Mais les tribunaux ont clairement décidé que ce n'était pas le cas; l'appelant n'a pas les droits qu'il prétendait avoir. Une personne ne peut préserver un bien qu'il n'a jamais eu.

[21] En conséquence, les dépenses juridiques faites en 2011 ont été engagées dans un nouvel effort d'établir les droits que l'appelant prétend avoir.

[22] Ce n'est pas différent que s'il s'agissait d'un litige ou Mme Gagné aurait prétendu qu'un legs testamentaire comprend le lot A et l'appelant aurait prétendu que le legs en question comprenait des droits additionnels, le lot B en plus du lot A.

[23] Même en supposant qu'il s'agit d'une dépense en vue de tirer un revenu de bien, ces dépenses sont des dépenses de nature capitale, établir ses droits, et ils ne sont pas déductibles selon le paragraphe 18(1)*b)*.

[24] De plus, je ne vois pas comment dans ces circonstances il peut s'agir de dépenses effectuées par le contribuable en vue de tirer un revenu de bien au sens du paragraphe 18(1)*a)*. Le but est d'obtenir des droits qui vont peut-être avoir comme conséquence qu'au décès de Mme Gagné, l'appelant recevrait un montant d'argent plus élevé. Hériter d'un montant plus élevé au décès de Mme Gagné ne constitue pas un revenu de bien.[4]

[25] Dans la mesure où il s'agit de dépenses pour obtenir des dommages-intérêts payables à la succession de Guy Deschênes en remboursement du travail excédentaire du liquidateur, il ne s'agit pas de dépenses engagées en vue de tirer un revenu de bien. De plus, ce qui était recherché est un paiement à la succession et non au contribuable.

[26] L'appelant attache beaucoup d'importance à l'arrêt *65302 British Columbia Ltd. c. Canada*[5], une cause ou la question était la déductibilité pour une entreprise avicole d'une taxe de dépassement de quota de production d'œufs. Les circonstances sont très différentes de celles ici et je ne vois pas comment l'arrêt *65302 British Columbia* peut aider l'appelant.

[27] L'appelant invoque également l'arrêt *Nadon c. Canada* [*sic, Nadeau*][6] notamment le paragraphe 17. Toutefois, ce paragraphe traite d'une dépense pour recouvrer un montant dû en vertu d'un droit déjà existant. Or, il n' y' a pas de tel montant ici.

[28] En conséquence, vu que les frais en question ne sont pas déductibles, l'appel est rejeté.

---

[2] *Deschênes c. Services financiers Dundee ltée*. 2012 QCCA 395.

[3] Voir la définition de « bien » à l'article 248 de la Loi.

[4] C'est recevoir le bien; de même, si l'hériter reçoit le lot B dans l'exemple ci-haut, la réception du lot B ne

[5] [99 DTC 5799] 1999 3 S.C.R. 804.

[6] [2003 DTC 5736] 2003 CAF 400.