

Lending Money or Investing Money

Author : admin

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Lending Money or Investing Money - Deducting Losses When Funds Become Unrecoverable

Meilleur v The Queen, [2016 TCC 287](#)

At issue was whether the taxpayer was in the business of lending money and suffered losses or whether the taxpayer was an investor.

The taxpayer failed to prove the existence of business as opposed to a mere investment. The taxpayer's position was harmed by their inconsistent reporting and filing history during the first two years, highlighting the importance of obtaining tax planning advice before any venture.

FACTS

The advances were made to real-estate ventures and the structure and documentation consisted of:

- A trust agreement was entered into with a mortgage company with the company acting as bare trustee and identified the taxpayers as investors and gave the trustee the right to purchase the investor's advance;
- the taxpayers executed irrevocable commitments to advance the funds on "mortgage investments";
- a commercial term sheet describing the aggregate capital required for each project was provided and the advance was a proportion of the total;

The advances when into default and losses were sustained.

ANALYSIS

There are a number of ways in which losses can be deducted, including:

- **Bad Debt Deduction** - ITA s 20(1)(p)(ii)(a) - where the taxpayer is an insurer or whose ordinary business incomes the lending of money, and a loan or lending asset was made or acquired in the ordinary course of the taxpayer's business or insurance of lending money, the loss can be deducted from income;
- **Doubtful or Impaired Debt Reserve** - ITA s 20(1)(l) - a reasonable reserve may be

taken against income in respect of doubtful debts for amounts previously reported as income but not received, or impaired loans or lending assets of a money lending business made in the ordinary course of that business - *Heron Bay Investment Ltd. v. R.*, [2009 TCC 337](#) at paragraph 26;

- **Allowable Business Investment Loss** - ITA s 39(1)(c) - loans to a qualified small business corporation may be deductible against all sources of income if the conditions are satisfied - *Rich v. Canada* [2003 FCA 38](#), .

The Court dismissed the possibility of a deduction as doubtful or impaired debts reserves and as ABIL summarily as the pre-conditions were not met on the evidence presented. The only matter remaining was the bad debt deduction. There the court had to determine whether:

- **there was a loan or lending asset;**
 - An advance is a loan where there is an agreement that the obligation to repay is on demand or at some predetermined date, and the payment of interest - *Loman Warehousing Ltd. v. HMQ*, [\[1999\] 4 CTC 2049](#), paras 21-22 (paras 37-38);
- **there was a business and this was the business of lending money;**
 - this requires the court to consider the intention of the taxpayer during the possession of the asset (*Happy Valley Farms Ltd. v. Minister of National Revenue*, [1986] CTC 259 at paragraph 15; *Canadian Marconi Co. v. R.*, [\[1986\] 2 SCR, 522](#) at pages 6529-6530; *Cragg v. Minister of National Revenue*, [1952] Ex CR 40 at paragraph 46; *Langhammer v. R.*, [2000 CanLII 473](#) at paragraph 34);
 - it is likely that the activities are a business where funds are actively sought out or obtained through borrowing, there is security for the loans, the loans are complex, there is advertising or promotion, there is an adequate accounting system in place, investigation of new borrowers is undertaken, and there is activity during the loan period (para 47);
 - the court asked "is there a sufficient level of commerciality achieved throughout which transforms the holding of real property mortgages in order to acquire interest income to that of an undertaking and activity in the nature of trade for profit concerned with a business of lending money?" (para 53) but held that it was not in this case providing detailed factors (para 54);
- **the loans were made in the ordinary course of that business of lending money;**
and
- **the taxpayer has established that the loan has become uncollectible or impaired in the year deducted.**

The taxpayers failed at the level of proving that there was deliberate and an overall sufficient level of commerciality to their activities needed to constitute a business (paras 55-56).

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