Docket: 2022-1463(IT)I

BETWEEN:

JEAN-LUC GAUTHIER,

Appellant,

and

HIS MAJESTY THE KING,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on May 23, 2023, at Montreal, Quebec

Before: The Honourable Justice Gaston Jorré, Deputy Judge

Appearances:

Agent for the appellant:	Yves Chartrand
Counsel for the respondent:	Anne Elizabeth Morin

JUDGMENT

In accordance with the attached reasons, the appeal under the *Income Tax Act* for the 2017 taxation year is allowed, without costs, and the matter is referred back to the Minister for reconsideration and reassessment on the basis that the appellant was entitled to elect to defer the capital gain under subsection 45(3) of the *Income Tax Act.*

Signed at Ottawa, Canada, this 20th day of February 2024.

"G. Jorré"

Jorré D.J.

Citation: 2024 TCC 22
Date: 20240220
Docket: 2022-1463(IT)I

BETWEEN:

JEAN-LUC GAUTHIER,

Appellant,

and

HIS MAJESTY THE KING,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

REASONS FOR JUDGMENT

Jorré D.J.

I. **Introduction**

[1] There is no disagreement concerning the facts. There is no disagreement concerning the figures.

[2] In 2008, the appellant purchased a duplex in Montreal.

[3] He occupied the lower unit as his principal residence and he rented out the upper unit to other people.

[4] In 2017, the appellant stopped renting out the upper unit. He did some renovations in order to transform the duplex into a single-family residence.

[5] After the changes were made, the appellant used the single-family residence as his principal residence. There was therefore a change of use in 2017.

[6] The transformation in 2017 triggered a deemed disposition resulting from the change of partial use, and therefore a capital gain and a taxable capital gain.

[7] In June 2018, the appellant filed his tax return for the 2017 taxation year, in which he declared a capital gain in connection with the change of use and did not ask that the capital gain be deferred under subsection 45(3) of the *Income Tax Act*.

[8] The Minister's initial assessment accepted the appellant's tax return as filed.

[9] On November 13, 2018, the appellant served a notice of objection in order to make his election under subsection 45(3) of the *Income Tax Act*.

[10] The Minister confirmed the initial assessment.

[11] The appellant argued that under subsection 45(3) of the *Income Tax Act*, he was entitled to elect to defer the capital gain.

[12] The respondent made the opposite argument. In the respondent's submission, the election was available only if there was a change of use of the entire property, the duplex.

[13] Amendments were made to subsection 45(3) of the *Income Tax Act* that came into force after March 18, 2019.

[14] At the end of 2017, subsection 45(3) read as follows:

> **(3)** Where at any time a property that was acquired by a taxpayer for the purpose of gaining or producing income ceases to be used for that purpose and becomes the principal residence of the taxpayer, subsection 45(1) shall not apply to deem the taxpayer to have disposed of the property at that time and to have reacquired it immediately thereafter if the taxpayer so elects by notifying the Minister in writing on or before the earlier of
>
> > **(a)** the day that is 90 days after a demand by the Minister for an election under this subsection is sent to the taxpayer, and
> >
> > **(b)** the taxpayer's filing-due date for the taxation year in which the property is actually disposed of by the taxpayer.
>
> (Emphasis added.)

[15] At present, paragraph 45(3) reads as follows:

> **(3)** If at any time a property that was acquired by a taxpayer for the purpose of gaining or producing income, or that was acquired in part for that purpose, ceases in whole or in part to be used for that purpose and becomes, or becomes part of, the principal residence of the taxpayer, paragraphs (1)(a) and (c) shall not apply to

> deem the taxpayer to have disposed of the property at that time and to have reacquired it immediately thereafter if the taxpayer so elects by notifying the Minister in writing on or before the earlier of
>
> > **(a)** the day that is 90 days after a demand by the Minister for an election under this subsection is sent to the taxpayer, and
> >
> > **(b)** the taxpayer's filing-due date for the taxation year in which the property is actually disposed of by the taxpayer.
>
> (Emphasis added.)

[16] If the change of use had taken place after March 18, 2019, there would be no doubt that the appellant could have deferred the capital gain.

[17] One consequence of the interpretation by the Canada Revenue Agency is that the taxpayer must pay the tax despite the fact that he did not sell the property, and in his financial circumstances, this could cause him cash flow problems. While that may be so, a cash flow problem can arise in various situations in which the Act creates a deemed disposition.

[18] This is a somewhat surprising outcome, given that an individual who rents out a house that he owns and changes the use of the house to make it his principal residence may make the election and avoid it triggering a deemed disposition.[1]

II. Analysis[2]

[19] No conclusions may be drawn regarding the prior rights from the fact that the Act was amended with effect as of March 18, 2019.[3]

---

[1] I note that if the CRA's interpretation is the correct one, the owner of a duplex who was renting out two units and decided to move into one of the units and use it as their principal residence could not have avoided the deemed disposition.

[2] Various documents were brought to my attention relating to the administrative positions taken by the Canada Revenue Agency and the Agence de Revenu du Québec. The courts may consider those administrative positions.
The respondent's representative produced various documents in the course of his submissions; while these are not evidence, to facilitate identification of the documents they were identified as A-1 to A-14.
At one time, the CRA took the administrative position that the election could be made in circumstances such as those in issue here. However, the CRA changed its position well before 2017. The ARQ seems to be of the contrary opinion; however, the ARQ seems to have followed the CRA under the provisions relating to "related elections". See the last page of Exhibit A-5.

[3] See section 45 of the *Interpretation Act* and paragraph 86 of *Canada v. Oxford Properties Group* 2018 FCA 30 (CanLII).

[20] It is agreed that provisions must be interpreted using a textual, contextual and purposive analysis to find a meaning that is harmonious with the Act as a whole.[4]

[21] In interpreting subsection 45(3), it is important to consider the text of section 45 of the *Income Tax Act*, as it read at the end of 2017, as a whole:

> Property with more than one use
>
> **45 (1)** For the purposes of this subdivision the following rules apply:
>
> **(a)** where a taxpayer,
>
> **(i)** having acquired property for some other purpose, has commenced at a later time to use it for the purpose of gaining or producing income, or
>
> **(ii)** having acquired property for the purpose of gaining or producing income, has commenced at a later time to use it for some other purpose,
>
> the taxpayer shall be deemed to have
>
> **(iii)** disposed of it at that later time for proceeds equal to its fair market value at that later time, and
>
> **(iv)** immediately thereafter reacquired it at a cost equal to that fair market value;
>
> **(b)** where property has, since it was acquired by a taxpayer, been regularly used in part for the purpose of gaining or producing income and in part for some other purpose, the taxpayer shall be deemed to have acquired, for that other purpose, the proportion of the property that the use regularly made of the property for that other purpose is of the whole use regularly made of the property at a cost to the taxpayer equal to the same proportion of the cost to the taxpayer of the whole property, and, if the property has, in such a case, been disposed of, the proceeds of disposition of the proportion of the property deemed to have been acquired for that other purpose shall be

[4] See, for example, *Minister of National Revenue v. Al Saunders Contracting & Consulting Inc*. 2020 FCA 89 at paragraph 20 or *Canada v. BCS Group Business Services Inc*., 2020 FCA (CanLII) at paragraph 21, in which the Federal Court of Appeal summarizes the principles of interpretation as follows:

> The modern approach to statutory interpretation is well established. The words of the Act are to be read in their entire context and in their grammatical and ordinary sense, harmoniously with the scheme of the Act, the object and the intention of Parliament. This means that one must read the text, taking into account the purpose of the Act and of the provision at issue and all relevant context, including established common law and civil law concepts unless these are clearly ousted by legislation.

deemed to be the same proportion of the proceeds of disposition of the whole property;

(c) where, at any time after a taxpayer has acquired property, there has been a change in the relation between the use regularly made by the taxpayer of the property for gaining or producing income and the use regularly made of the property for other purposes,

(i) if the use regularly made of the property for those other purposes has increased, the taxpayer shall be deemed to have

(A) disposed of the property at that time for proceeds equal to the proportion of the fair market value of the property at that time that the amount of the increase in the use regularly made by the taxpayer of the property for those other purposes is of the whole use regularly made of the property, and

(B) immediately thereafter reacquired the property so disposed of at a cost equal to the proceeds referred to in clause 45(1)(c)(i)(A), and

(ii) if the use regularly made of the property for those other purposes has decreased, the taxpayer shall be deemed to have

(A) disposed of the property at that time for proceeds equal to the proportion of the fair market value of the property at that time that the amount of the decrease in use regularly made by the taxpayer of the property for those other purposes is of the whole use regularly made of the property, and

(B) immediately thereafter reacquired the property so disposed of at a cost equal to the proceeds referred to in clause 45(1)(c)(ii)(A); and

(d) in applying this subsection in respect of a non-resident taxpayer, a reference to "gaining or producing income" shall be read as a reference to "gaining or producing income from a source in Canada".

Election where change of use

(2) Where at any time a property that was acquired by a taxpayer for the purpose of gaining or producing income ceases to be used for that purpose and becomes the principal residence of the taxpayer, subsection 45(1) shall not apply to deem the taxpayer to have disposed of the property at that time and to have reacquired it immediately thereafter if the taxpayer so elects by notifying the Minister in writing on or before the earlier of

> **(a)** the day that is 90 days after a demand by the Minister for an election under this subsection is sent to the taxpayer, and
>
> **(b)** the taxpayer's filing-due date for the taxation year in which the property is actually disposed of by the taxpayer.
>
> Election concerning principal residence
>
> **(3)** Where at any time a property that was acquired by a taxpayer for the purpose of gaining or producing income ceases to be used for that purpose and becomes the principal residence of the taxpayer, subsection 45(1) shall not apply to deem the taxpayer to have disposed of the property at that time and to have reacquired it immediately thereafter if the taxpayer so elects by notifying the Minister in writing on or before the earlier of
>
> **(a)** the day that is 90 days after a demand by the Minister for an election under this subsection is sent to the taxpayer, and
>
> **(b)** the taxpayer's filing-due date for the taxation year in which the property is actually disposed of by the taxpayer.
>
> Where election cannot be made
>
> **(4)** Notwithstanding subsection 45(3), an election described in that subsection shall be deemed not to have been made in respect of a change in use of property if any deduction in respect of the property has been allowed for any taxation year ending after 1984 and on or before the change in use under regulations made under paragraph 20(1)(a) to the taxpayer, the taxpayer's spouse or common-law partner or a trust under which the taxpayer or the taxpayer's spouse or common-law partner is a beneficiary.

[22] Subsection 45(1) contains general rules that apply to changes in the use of a property, from use for the purpose of gaining or producing income to use for some other purpose, and vice versa.

[23] Paragraph 45(1)(a) applies when a property that is acquired for a single purpose is subsequently used solely for the other purpose. The paragraph deems a disposition.

[24] Paragraph 45(1)(b) applies when the property is to be used for both purposes at the time of the acquisition. This paragraph operates to divide the cost of acquisition between the two purposes.

[25] Paragraph 45(1)(c) deems a disposition when there is a change in the percentage of the use of the property for each purpose.[5]

[26] Subsections 45(2) and (3) allow a taxpayer to defer deemed dispositions in certain circumstances. Subsection 45(2) is not relevant in this case.

[27] The key question could be summarized as follows. Must the phrase:

> a property that was acquired by a taxpayer for the purpose of gaining or producing income ceases to be used for that purpose

be understood as if it read:

> a property that was acquired by a taxpayer **exclusively** for the purpose of gaining or producing income ceases to be used for that purpose?

[28] I can understand how the phrase "a property that was acquired by a taxpayer for the purpose of gaining or producing income ceases to be used for that purpose" could be read, at first glance, as applying only in circumstances in which the property was acquired exclusively for the purpose of gaining or producing income, that is, the situation described in subparagraph 45(1)(a)(ii).

[29] For one thing, the fact that paragraphs 45(1)(a) and (c) deal separately with changes from one single purpose to the other single purpose and with changes in the proportion of use for each purpose, respectively, could suggest that Parliament had planned to address these two situations separately within subsection 45(3) if its intention was to allow the election in subsection 45(3) in both situations.

[30] Having regard to the general scheme of section 45, I am satisfied, for the following reasons, that subsection 45(3) of the Act also applies in the fact situation in this appeal.

[31] First, while it was necessary to separate subsections 45(1)(a) and (c) since the consequences of the two types of deemed dispositions, in terms of their effects, are different, no such separation was necessary in drafting subsection 45(3), because the consequence is simply to defer the disposition in both cases.

[32] I note that subsection 45(3) is not limited to paragraph 45(1)(a); that subsection contains the phrase "subsection 45(1) shall not apply...".

---

[5] Paragraph 45(1)(d) is of no relevance in this case.

[33] Second, the objective of subsection 45(3) when it was added in 1985 was to allow deemed dispositions of a residential property to be deferred when the property became a principal residence and subsection 45(4) did not apply.[6]

[34] Although the technical notes talk about a residential property, there is nothing to suggest that the amendments were intended to exclude conversion of part of the property, for example half of a duplex.

[35] An interpretation that excludes a partial change of use is contrary to the objective intended when subsection 45(3) was added.[7]

[36] Third, I do not see how it could be said that once the taxpayer ceased to rent out the upper part of the property he did not cease to use the property for the purpose of gaining or producing income. The taxpayer is no longer receiving a penny of income.

[37] The appeal is therefore allowed, without costs, and the matter is referred back to the Minister for reconsideration and reassessment on the basis that the appellant was entitled to make the election and defer the capital gain under subsection 45(3) of the *Income Tax Act*.

Signed at Ottawa, Canada, this 20th day of February 2024.

"G. Jorré"

Deputy Judge

[6] See the technical notes dated September 9, 1985, provided by the Minister of Finance. It is agreed that the Court may consider technical notes: *Silicon Graphics Ltd v. R.*, 2002 FCA 260.

[7] As well, in the context of section 45, the ordinary meaning of property acquired "for the purpose of gaining or producing income" does not exclude property acquired in part for the purpose of gaining or producing income.

CITATION:	2024 TCC 22
COURT FILE NO.:	2022-1463(IT)I
STYLE OF CAUSE:	JEAN-LUC GAUTHIER AND HIS MAJESTY THE KING
PLACE OF HEARING:	Montreal, Quebec
DATE OF HEARING:	May 23, 2023
REASONS FOR JUDGMENT BY:	The Honourable Justice Gaston Jorré, Deputy Judge
DATE OF JUDGMENT:	February 20, 2024

APPEARANCES:

Agent for the appellant:	Yves Chartrand
Counsel for the respondent:	Anne Elizabeth Morin

COUNSEL OF RECORD:

For the appellant:

Name:

Firm:

For the respondent: Shalene Curtis-Micallef
Deputy Attorney General of Canada
Ottawa, Canada