Docket: 2008-1019(IT)I

BETWEEN:

LOUISE C. NORTON,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeals heard together on common evidence with the appeals of
Gregory W. Norton (2008-1020(IT)I)
on May 27 and 29, June 1, and December 1 and 2, 2009
at Halifax, Nova Scotia

Before: The Honourable Justice Wyman W. Webb

Appearances:

Counsel for the Appellant:	Joseph M. J. Cooper
Counsel for the Respondent:	Toks C. Omisade

JUDGMENT

The appeals from the reassessments made under the *Income Tax Act* (the "*Act*") in relation to the Appellant's 2001, 2002, 2003 and 2004 taxation years are allowed, with costs, and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that:

(a) the income, for the years under appeal, of the partnership between the Appellant and Gregory Norton is to be reduced by the following amounts:

Description	**2001**	**2002**	**2003**	**2004**
Amount allowed by agreement:	$2,434	$1,588	$6,006	$1,888
Nets, traps and related material:	$2,768	$5,521	$12,082	$11,376
Reels and related materials:	$3,600	$7,578	$4,386	$3,855
Appraisal and water test:	$8	$8	$8	$8
Interest for 2003 re 2000 Ford Explorer debt (25% of $1,354):			$338	
All Terrain Vehicles – repairs and new tires			$267	
Tolls:	$302	$231	$38	$39
Rental of Stone Roller:		$80		
Total:	$9,112	$15,006	$23,125	$17,166

and

(b) the $215.04 spent by the Appellant and Gregory Norton to acquire a police scanner in 2002 is to be added to the undepreciated capital cost of the Class 8 assets of the partnership.

It is further ordered that the filing fee of $100 be refunded to the Appellant.

Signed at Ottawa, Canada, this 2nd day of February, 2010.

"Wyman W. Webb"

Webb J.

Docket: 2008-1020(IT)I

BETWEEN:

GREGORY W. NORTON,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

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Louise C. Norton (2008-1019(IT)I)
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Before: The Honourable Justice Wyman W. Webb

Appearances:

Counsel for the Appellant:	Joseph M. J. Cooper
Counsel for the Respondent:	Toks C. Omisade

JUDGMENT

The appeals from the reassessments made under the *Income Tax Act* (the "*Act*") in relation to the Appellant's 2001, 2002, 2003 and 2004 taxation years are allowed, with costs, and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that:

(a) the income, for the years under appeal, of the partnership between the Appellant and Louise Norton is to be reduced by the following amounts:

Description	**2001**	**2002**	**2003**	**2004**
Amount allowed by agreement:	$2,434	$1,588	$6,006	$1,888
Nets, traps and related material:	$2,768	$5,521	$12,082	$11,376
Reels and related materials:	$3,600	$7,578	$4,386	$3,855
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Tolls:	$302	$231	$38	$39
Rental of Stone Roller:		$80		
Total:	$9,112	$15,006	$23,125	$17,166

(b) the $215.04 spent by the Appellant and Louise Norton to acquire a police scanner in 2002 is to be added to the undepreciated capital cost of the Class 8 assets of the partnership; and

(c) the proceeds of disposition related to the sale by the Appellant of his lobster licence in 2002 were $75,000 and not $100,000.

It is further ordered that the filing fee of $100 be refunded to the Appellant.

Signed at Ottawa, Canada, this 2nd day of February, 2010.

"Wyman W. Webb"

Webb J.

Citation: 2010TCC62
Date: 20100202
Docket: 2008-1019(IT)I

BETWEEN:

LOUISE C. NORTON,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

Docket: 2008-1020(IT)I

AND BETWEEN:

GREGORY W. NORTON,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Webb J.

[1] The Appellants, who are married to each other, were carrying on a fishing business as a partnership throughout 2001, 2002, 2003 and 2004. It was agreed by the parties that 50.5% of the profits (or losses) of the partnership should be allocated to Gregory Norton and 49.5% of such profits (or losses) should be allocated to Louise Norton. As a result of a very thorough audit by the Canada Revenue Agency ("CRA"), the Appellants were reassessed:

(a) to deny some of the amounts claimed as expenses on the basis that such expenditures had not been incurred or were personal expenditures;

(b) to reclassify other amounts claimed as expenses as capital expenditures;

(c) to reduce the percentage of business use of the automobiles (which resulted in a reduction in the amount allowed as automobile expenses); and

(d) to reduce the percentage that the home was used for business purposes (which resulted in a reduction in the amount allowed as business use of the home expenses).

There were also some acquisitions of capital assets and disposition of capital assets that had not been taken into account when the tax returns for the Appellants were prepared and filed.

[2] The assumptions made by the Minister in determining the Appellants' tax liability for 2001, 2002, 2003 and 2004 are set out in paragraph 9 of the thirty-four page Reply (which included six pages of Schedules). There are 81 subparagraphs of paragraph 9 designated by letters (from (a) to (cccc)) with several subparagraphs being further divided into separate clauses. Several subparagraphs or clauses include tables with several different amounts. Needless to say the hearing took longer than the one day that was originally scheduled for the hearing.

[3] There was a significant gap in time between the conclusion of the Appellants' case on June 1, 2009 and the opening of the Crown's case on December 1, 2009. During that time the parties were able to complete and execute a Partial Agreed Statement of Facts which consolidated a list of the matters that the Appellants were no longer pursuing and a list of the items that were being allowed by the Respondent. Since the matters that the Appellants are no longer pursuing will not change the reassessments, there is no need to list those matters.

[4] The following table lists the amounts that the Respondent has agreed to allow as a deduction in computing the income of the partnership:

Paragraph in the Reply:	**Description:**	**Amount Allowed**:			
		2001	**2002**	**2003**	**2004**

Paragraph in the Reply:	Description:	Amount Allowed:			
		2001	2002	2003	2004
9(h)	Crew shares			$1,570.63	
9(j)	Boat Fuel	$442.06			
9(k)	Line	$674.28			
9(k)	Rope	$754.11			
9(l)	Line		$440.54		
9(m)	Line			$523.65	
9(m)	Rope			$1,133.80	
9(m)	Bait bags			$265.00	
9(o)	Line				$928.40
9(o)	Rope				$702.00
9(y)(i)	Lamp etc.		$65.98		
9(y)(iii)	Line		$325.15		
9(hh)(i)	Insurance			$535.50	
9(oo)(ii)	Line		$284.85		
9(pp)(iii)	Line			$679.14	
9(tt)	Outboard motor			$408.46	
9(ggg)(iii)	Property taxes	$493.42			
9(ggg)(iii)	Barbeque	$69.99			
9(iii)	Property taxes		$471.12		
9(kkk)	Property taxes			$519.74	
9(kkk)	Hunting ammo, fan			$230.53	
9(kkk)	Hotel in Yarmouth			$139.32	
9(lll)	Meal				$16.35
9(lll)	Cape Cod Colony Motel				$50.00
9(lll)	Property taxes				$131.30
9(lll)	Credit Notes				$60.00
Total:		$2,433.86	$1,587.64	$6,005.77	$1,888.05

[5] The Respondent also agreed that the $215.04 spent by the Appellants to acquire a police scanner in 2002 should be added to the undepreciated capital cost of the Class 8 assets of the partnership.

[6] As part of the reassessment of Gregory Norton, the Minister had assumed that he sold his lobster licence for $100,000 in 2002. The Respondent has agreed that the proceeds of disposition for this licence were $75,000 not $100,000, which will affect the balance of the cumulative eligible capital of Gregory Norton as of the end of 2002.

[7] There are a number of matters that were not resolved between the parties. Counsel for the Appellants in his closing arguments identified the items that the Appellants were still disputing and these will be dealt with in these reasons. The number and letter references are to the subparagraphs of the Reply.

9(h) – Crew Shares

[8] The assumption made by the Minister was that $8,071 claimed by the Appellants as crew shares in 2003 had not been incurred. As part of the Partial Agreed Statement of Facts the Respondent agreed that $1,571 of this amount should be allowed as a deduction leaving a balance that was denied of $6,500. During closing arguments counsel for the Appellants stated that the Appellants should be allowed to deduct $1,060 of this $6,500 amount (and therefore the Appellants were no longer claiming that they were entitled to deduct $5,440[1]).

[9] The Appellants called three witnesses – the two Appellants and their bookkeeper. The only witness for the Appellants who had any knowledge of this claim was the bookkeeper. The total amount claimed as crew shares in 2003 was $13,571. Since the Minister had denied a claim for $8,071, the amount that had been allowed (at the time of the reassessment) was $5,500. The bookkeeper stated during her testimony that the $5,500 (that had been allowed) related to the tuna wages or share paid to Chance Norton (who is the Appellants' son). The additional claim now being made by the Appellants is that Chance Norton was paid an additional amount of $1,060 in 2003 by two cheques – one for $660 dated July 3, 2003 and the other for $400 dated December 19, 2003. As a result the total amount paid to Chance Norton, as alleged by the Appellants, in 2003 would be $6,560.

[10] The auditor for the CRA also testified during the hearing. She stated that she had reviewed the tax return that Chance Norton had filed for 2003 and that he had only reported $5,500 as his income from crew shares in 2003. Chance Norton did not testify at the hearing. In the *Law of Evidence in Canada*, second edition, by Sopinka, Lederman and Bryant, it is stated at p. 297 that:

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[1] $6,500 - $1,060.

> In civil cases, an unfavourable inference can be drawn when, in the absence of an explanation, a party litigant does not testify, or fails to provide affidavit evidence on an application, or fails to call a witness who would have knowledge of the facts and would be assumed to be willing to assist that party.

[11] Chance Norton would have knowledge of the amount that he was paid in 2003 and, since he is the Appellants' son, would presumably be willing to assist the Appellants, if his testimony would have assisted them[2]. Without hearing from Chance Norton to confirm the amount that he was paid in 2003 and to explain why, if he had been paid $6,560 as crew shares in 2003, he only reported $5,500 in his tax return, the Appellants cannot succeed on this issue. The additional amount of $1,060 that the Appellants claim was paid to Chance Norton in 2003 (in addition to the $5,500) is not allowed as a deduction in computing the income of the Appellants.

9(k),(l),(m) and (o) – Anchors, nets, traps, reels and related materials

[12] The following amounts had been claimed as expenses by the Appellants but were reclassified by the auditor for the CRA as capital expenditures (and added to the Class 8 assets of the partnership as additions):

	2001	2002	2003	2004
Anchors, nets, traps and related materials	$2,767.72			
Nets, traps and related materials		$5,520.83	$12,081.78	$11,376.10
Reels and related materials	$3,600.20	$7,577.69	$4,386.38	$3,854.90
Total:	$6,367.92	$13,098.52	$16,468.16	$15,231.00

[13] The bookkeeper testified that these amounts had been included in the amount claimed as "gear" and were claimed as expenses in computing the income of the Appellants for these years. The amounts that were claimed as "gear" in determining the income of the partnership for 2001 to 2004 were the following amounts:

	2001	2002	2003	2004
Gear:	$13,204.57	$16,119.60	$25,665.51	$24,054.66

[2] While there was an indication that Chance Norton was fishing in December, there was nothing to indicate why he could not have testified in late May.

[14] It also appears that in some of the years prior to the years under appeal, the amount spent on traps was treated as a capital expenditure. It appears that Gregory Norton was claiming an investment tax credit in relation to the traps. Investment tax credits are determined by multiplying the capital cost of qualifying property, which pursuant to the provisions of section 4600 of the *Income Tax Regulations*, are restricted to depreciable property of the classes as set out in that section of the *Regulations*, by the applicable percentage. Therefore in order to claim an investment tax credit in relation to the traps, the traps would have to be capital property.

[15] The issue in this case is whether the amount spent on traps and nets during 2001 to 2004 should be treated as a deductible expense or as a capital expenditure. Not only was this not an easy matter for the Appellants to resolve (who, in some years, treated the amounts spent on traps as capital expenditures and for the years under appeal, as an expense), it also appears that the CRA is not taking a definitive position that the amounts spent must be treated as capital expenditures.

[16] In the fishing income guide published by the CRA (T4004), it is stated in relation to Line 9137 -- Nets and traps in part as follows:

> Nets and traps include lines, hooks, buoys, anchors, and radar reflectors.
>
> Generally, you cannot deduct the entire cost of nets and traps you bought in the year. Instead, there are two methods you can use to deduct these costs.
>
> **Method 1** – Capital cost allowance (CCA) method
> Capitalize the cost of nets and traps and claim CCA.
> See Chapter 3 for details on CCA.
>
> **Method 2** – Inventory method
> Include in inventory the cost of nets and traps and deduct the loss in value, as shown in the following example:
>
> **Example**
> Value of nets, traps, twine, etc., on hand at the
> end of your 2007 fiscal period ..... $ 750
>
> **Add:** Cost of nets and traps you bought
> in your 2008 fiscal period..... $200

Cost of twine and other net and trap materials you bought in your 2008 fiscal period (do not include the value of your own labour)....…….	125	325*
Subtotal.....		$1,075
Minus: Value of nets, traps, twine, etc., on hand at the end of your 2008 fiscal period..... ……..…….....$700**		
Proceeds from the sale of nets, traps, twine, etc..... .. ..……	150	850
Loss on nets and traps		$ 225

* If you use the inventory method, do not deduct this amount as an expense.

** The value of nets and traps on hand is the amount you would receive if you sold them to another fisher who was not related to you.

If you just started fishing, choose one of the two methods. If you have been fishing for several years and each year you claim the cost of replacing nets and traps, you can keep on doing so. However, you can choose to change to either the CCA or the inventory method. If you choose to do this in 2008, the value of nets and traps on hand at the end of 2007 will be zero since you have deducted their value in previous years.

You can change from the inventory method to the CCA method. However, you cannot change from the CCA method to the inventory method

[17] In the report of the auditor for the CRA, a copy of which was introduced as an exhibit, the auditor stated as follows:

Capitalization of assets: One of the most offensive practices of this REP is her accounting for capital purchases. Because she considers nets, traps, lines, buoys, fishing equipment to be “gear” (it is common among fishermen to refer to their equipment as gear) she expenses all such capital acquisitions as “gear”. Our fishing guide defines gear as clothing and small tools and explains that these items can be expensed.

Nets and Traps are defined in the guide as: nets, traps, lines, hooks, buoys, anchors, radar reflectors. Nets and traps are afforded a special treatment, although it is by

> policy, not by virtue of the act. Basically, for those fishermen who have used cost replacement method (that is they expense 100% of the cost) prior to 1988, and have always continued to do so, for their nets and traps, they may continue with this practice. In 1988, section 28 of the ITA was added and from that point on, new fisherpersons, or those who had never used cost replacement method, could no longer elect this method. Nets and traps were, from that point onwards, considered class 8 capital assets; however, as a matter of policy, we do allow fishermen to use an inventory method to expense nets and traps. The inventory and capital methods are the only 2 methods available, and once a fisherman elects the capital method, he cannot change to inventory method.

[18] Inventory is defined in section 248 of the *Income Tax Act* (the "*Act*") as follows:

> "inventory" means a description of property the cost or value of which is relevant in computing a taxpayer's income from a business for a taxation year or would have been so relevant if the income from the business had not been computed in accordance with the cash method and, with respect to a farming business, includes all of the livestock held in the course of carrying on the business;

[19] The definition of inventory is very broad and refers to a description of property the cost or value of which is relevant in computing income. If the word "inventory" is given a literal interpretation, what property of a business would not be included as property the cost of which is *relevant* in computing income? It does not state that the cost must be deductible, only that the cost is relevant.

[20] The Supreme Court of Canada in *The Queen v. Canada Trustco Mortgage Company*, 2005 SCC 54, 2005 DTC 5523 (Eng.), [2005] 5 C.T.C. 215, 340 N.R. 1, 259 D.L.R. (4th) 193, [2005] 2 S.C.R. 601, stated that:

> 10 It has been long established as a matter of statutory interpretation that "the words of an 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 of the Act, and the intention of Parliament": see *65302 British Columbia Ltd. v. R.*, [1999] 3 S.C.R. 804 (S.C.C.), at para. 50. The interpretation of a statutory provision must be made according to a textual, contextual and purposive analysis to find a meaning that is harmonious with the Act as a whole. When the words of a provision are precise and unequivocal, the ordinary meaning of the words play a dominant role in the interpretive process. On the other hand, where the words can support more than one reasonable meaning, the ordinary meaning of the words plays a lesser role. The relative effects of ordinary meaning, context and purpose on the interpretive process may vary, but in all cases the court must seek to read the provisions of an Act as a harmonious whole.

[21] It seems to me that the words used in defining inventory are not precise and unequivocal. Edwin C. Harris, Q.C. in his text *Canadian Income Taxation*, fourth edition, stated at pages 443 – 445 as follows:

> Any business that, in the usual course, sells goods (whether or not manufactured by it) or land will normally maintain an inventory, i.e., a stock of things held for sale. This inventory may be in finished form, or in progress as part of a manufacturing or processing operation, or in the form of raw materials awaiting manufacturing or processing. Many such businesses will also maintain an inventory of supplies that will be consumed during the production process….
>
> …
>
> The Act defines "inventory" as "a description of property the cost or value of which is relevant in computing a taxpayer's income from a business for a taxation year. *This definition is too broad and too vague to be of much help.* It is interesting, however, that the definition refers to the description or list of property, rather than to the property itself – which is the more usual meaning of "inventory". Subject it to this difference, which does not appear to have any important consequences, *"inventory" for tax purposes generally has the same meaning as it does in accounting practice*. It includes not merely any assets in which the taxpayer deals but also any asset that he acquires and subsequently disposes of, even in an isolated transaction, through an "adventure in nature of trade" (see 7.02(3) (g)). As well, it includes most kinds of consumable supplies.
>
> (emphasis added)
>
> (The above text also included several footnote references that can be found at the bottom of pages 444 and 445 of the text.)

[22] Justice Major, writing on behalf of the majority of the Justices of the Supreme Court of Canada in *Friesen v. The Queen*, [1995] 2 C.T.C. 369, 95 DTC 5551, stated as follows:

> 31 In order to take advantage of the valuation method in subsection 10(1), a taxpayer must also establish that the property in question is inventory. A definition of "inventory" is contained in subsection 248(1) of the Act:
>
> > "inventory" means a description of property the cost or value of which is relevant in computing a taxpayer's income from a business for a taxation year;
>
> 32 The first point to note about this definition of inventory is that property is not required to contribute directly to income in a taxation year in order to qualify as inventory. Provided that the cost or value of an item of property is relevant in

computing business income in a year that property will qualify as inventory. Generally the cost or value of an item of property will appear as an expense (and the sale price as revenue) in the computation of income.

33 Reduced to its simplest terms, the income or profit from the sale of a single item of inventory by a sales business is the ordinary tracing formula calculated by subtracting the purchase cost of the item from the proceeds of sale. This is the basic formula which applies to the calculation of profit before the value of inventory is taken into account, as is made clear by Abbott J. in *Minister of National Revenue v. Irwin*, [1964] S.C.R. 662, [1964] C.T.C. 362, 64 D.T.C. 5227 at page 664-665 (C.T.C. 364, D.T.C. 5228):

> The law is clear therefore that for income tax purposes gross profit, in the case of a business which consists of acquiring property and reselling it, is the excess of sale price over cost, subject only to any modification effected by the "cost or market, whichever is lower" rule.

34 Thus, for any particular item:

> Income = Profit = Sale Price - Purchase Cost.

35 It is clear from the formula above that the cost of an item of property sold by a business is relevant in computing the income from the business in the taxation year in which it is sold. As discussed above, an adventure in the nature of trade constitutes a business under the Act. Therefore, an item of property sold as part of an adventure in the nature of trade is relevant to the computation of the taxpayer's income from a business in the taxation year of disposition and so is inventory according to the plain language of the definition in subsection 248(1).

36 … The plain meaning of the definition in subsection 248(1) is that an item of property need only be relevant to business income in a single year to qualify as inventory: "relevant in computing the taxpayer's income from a business for a taxation year". *In this respect the definition of inventory in the Income Tax Act is consistent with the ordinary meaning of the word. In the normal sense, inventory is property which a business holds for sale* and this term applies to that property both in the year of sale and in years where the property remains as yet unsold by a business.

(emphasis added)

[23] Therefore it seems to me that inventory for the purposes of the *Act* will mean property as described by the Supreme Court of Canada above and by Edwin C. Harris, Q.C. in his text, together with the specific items added by the *Act*. "Inventory" for the purposes of the *Act* will therefore mean property held for sale, raw materials that will be used to make property for sale, supplies consumed during the production

process, livestock held in relation to a farming business and any property described in subsection 10(5) of the *Act* (that would not otherwise be included as inventory)[3]. The lobsters caught by the Appellants would be part of their inventory until they were sold to the buyer. It does not appear to me, however, that the traps and nets would be part of their inventory. The nets and traps were not held by the Appellants for sale and although they were damaged or destroyed, would not be consumed during the production process. As a result I do not find that the inventory method as outlined in the Fishing Guide referred to above is in accordance with the provisions of the *Act*.

[24] Although the auditor clearly stated during her testimony that it was the policy of the CRA, as outlined in the Fishing Guide referred to above, that nets and traps had to be treated as either inventory or capital property, neither counsel for the Appellants nor counsel for the Respondent submitted any arguments that the Appellants had to choose either the inventory method as described above or the capital cost allowance (CCA) method as described above. The arguments were only based on whether the amounts spent in each year under appeal (2001, 2002, 2003 and 2004) in relation to the nets and traps should be treated a capital expenditure incurred in that year or should be allowed as a deduction in computing income for that year.

[25] The Supreme Court of Canada in *Johns-Manville Canada Inc. v. The Queen*, [1985] 85 DTC 5373, [1985] 2 S.C.R. 46 dealt with the issue of whether amounts spent on the acquisition of land to allow an open-pit mine to continue operating were on account of capital or were current expenditures. Justice Estey, writing on behalf of the Supreme Court of Canada stated as follows:

> 13 When one turns to the appropriate principles of law to apply to the determination of the classification of an expenditure as being either expense or capital, an unnerving starting place is the comment of the Master of the Rolls, Sir Wilfred Greene in *British Salmson Aero Engines Ltd* v. *CIR* (1938), 22 TC 29, at 43:
>
> > ... there have been ... many cases where this matter of capital or income has been debated. There have been many cases which fall upon the borderline: indeed, in many cases it is almost true to say that the spin of a coin would decide the matter almost as satisfactorily as an attempt to find reasons. ...
> >
> > …

[3] Section 34 provides that, if the appropriate election is made, work in progress is excluded in determining the income from the business of the professional practices designated in that section. Under subsection 10(14) of the *Act*, such property is included in inventory for the purposes of subsections 10(12) and (13) of the *Act*.

20 At one time, the test applied by the courts in discriminating as between revenue and capital was the "once and for all" test. This test was adopted by Viscount Cave, LC in *British Insulated and Helsby Cables v. Atherton*, [1926] A.C. 205 at 213. Viscount Cave observed that the finding of revenue or capital was a question of fact, but then concerned himself with the answer to the question because of an imprecise finding below. The test he adopted at 213 was "... to say that capital expenditure is a thing that is going to be spent once and for all, and income expenditure is a thing that is going to recur every year", although he recognized that this test was not "to be a decisive one in every case". Later on the same page the Lord Chancellor elaborated:

> ... [W]hen 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 is a very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital.

In this the Court relied upon the earlier decision of *Vallambrosa Rubber Co Ltd* v. *Farmer*, [1910] SC 519 at 525. A few years later in *Ounsworth* v. *Vickers Ltd*, [1915] 3 K.B. 267 at 273, Rowlatt, LJ interpreted this test as not requiring that expenditures be made on an annual basis in order to qualify them as a deduction from revenue but rather than the expenditures be "pursuant to a continuous demand".

21 This discussion of authorities takes one full circle to the words of Lord Reid in *Regent Oil* v. *CIR*, [1966] A.C. 295, at 313:

> So it is not surprising that no one test or principle or rule of thumb is paramount. The question is ultimately a question of law for the court, but it is a question which must be answered in the light of all the circumstances which it is reasonable to take into account and *the weight which must be given to a particular circumstance in a particular case must depend rather on common sense than on strict application of any single legal principle.* [Emphasis added by Justice Estey]

22 It is of little help, in my respectful opinion, to attempt to classify the character of the expenditure according to the subject of that expenditure.

…

40 In applying the law to the above stated observations, one is thrown back to the pronouncement by Lord Wilberforce in *Tucker v. Granada Motorway Services*, [1979] 2 All E.R. 801, where he said at 804:

> It is common in cases which raise the question whether a payment is to be treated as a revenue or as a capital payment for indicia to point different

> ways. *In the end the courts can do little better than form an opinion which way the balance lies*. There are a number of tests which have been stated in reported cases which it is useful to apply, but we have been warned more than once not to seek automatically to apply to one case words or formulae which have been found useful in another.... Nevertheless reported cases are the best tools that we have, even if they may sometimes be blunt instruments. [Emphasis added by Justice Estey.]

41 We must also remember the previously cited words of Lord Pearce in *BP Australia*, *supra*, at 264: "It is a commonsense appreciation of all the guiding features which must provide the ultimate answer."

42 If we were to apply the three-step test adopted by the Australian court in *Sun Newspapers, supra*, these expenditures would qualify as expenses rather than being capital in nature. The character of the advantage sought is that of an advantage in the current operations of the taxpayer. The practice was recurring and the manner in which the object of the expenditures was applied was directly incorporated into the mining operations of the taxpayer. Finally, the means adopted by the taxpayer to gain this advantage was the periodic outlay of its funds which would formerly have been classified, in the vocabulary of that day, as circulating capital. In the words of Dixon, J, as he then was, in *Sun Newspapers, supra*, at 362, we are here concerned with an expenditure of a revenue nature because:

> ... its purpose brings it within the very wide class of things which in the aggregate form the constant demand which must be answered out of the returns of a trade or its circulating capital and that actual recurrence of the specific thing need not take place or be expected as likely.

The same judge in *Hallstroms Pty Ltd*, *supra*, at 648, reminds us that the classification of such expenditures "... depends on what the expenditure is calculated to effect from a practical and business point of view rather than upon the juristic classification of legal rights ...", *supra*. The old rule of "once and for all" as well as the "common sense" test, *supra*, lead us to a result favourable to the taxpayer's contention.

43 The characterization in taxation law of an expenditure is, in the final analysis (unless the statute is explicit which this one is not), one of policy….

[26] *In ATCO Electric Limited v. The Queen*, 2007 TCC 243, 2007 DTC 974, [2007] 4 C.T.C. 2297, Justice Sheridan held that the costs of replacing transformers were deductible as a current expense. Justice Sheridan stated as follows:

> 60 The case law for determining whether an expense is current or capital in nature are well established.* In *Rainbow Pipe Line Co. v. R.**, Mogan, J. set out the relevant considerations:

1. whether the expense was recurring or non-recurring;

2. whether the expense was a major repair;

3. whether the expense brought into existence an asset for the enduring benefit of the appellant's business; and

4. whether the expense was substantial in relation to the book value of the property, other expenses and annual profits.

…

62 How do transformers fit into the Appellant's electricity manufacturing business? Electricity is generated at the Appellant's generating stations and makes its way to Alberta consumers through a series of substations, wires, poles and transformers. A transformer is a device that allows for the transfer of electricity from one circuit to another: the voltage can be either increased or decreased depending on what is required for the movement of electricity at any particular point in the network. There are approximately 83,000 transformers in the Appellant's system varying in capacity, size and price: from the “10kVA” (10,000 volts), about the size of a garbage can* at a unit price of $300 to $350 to the “3MVA” (3 million volts), the size of a mini-van and worth approximately $50,000 each.

63 Because the smaller transformers are sealed units, it is more economical to replace than to repair them. I accept Mr. DeChamplain's evidence detailing his calculation that in 2000, the Appellant replaced 709 transformers ranging from 10 to 75 kMV at an average unit cost of $943.16*. Only about 2,000 of the Appellant's 83,000 transformers were 3MVA transformers. Unlike smaller transformers, in the case of malfunction they can be opened up and repaired; in 2000, however, five of the 3MVA's had to be replaced rather than repaired. Because of their greater value and the infrequency of their replacement, the Appellant classified such expenses as capital; thus, their cost was not included in the $622,990 at issue in this appeal.

64 Turning, then, to the *Rainbow Pipe Line* factors, the Respondent contends that the transformer replacement costs were “non-recurring” since the average life span of a transformer is 33 years. This submission might be persuasive if all of the transformers always lived up to such projections. The fact is, however, that each year 500 to 1,000 of the 83,000 transformers in the Appellant's distribution system become non-functional thanks to lightning strikes, “shorting-out” and vandalism* all of which are, by their nature, quite likely to continue to occur. In these circumstances, it is probable that the Appellant will always be and in 2000 was obliged to replace a certain percentage of its transformers. Accordingly, the expense of regular transformer replacement is recurring in nature.

65 The next consideration is whether the replacement expense was “major”. This, like the Minister's assumption that transformers are “large”* and “expensive”*,

is a relative question. It is common ground that the Appellant's outlays were limited to the costs of replacing transformers which had been damaged; newly acquired transformers or upgraded models of existing transformers were not included in the Appellant's claim. The number of transformers and the cost per unit was small relative to the Appellant's overall distribution system, representing less than 1% of all of the transformers in the system and their replacement cost, less than 1% of the Appellant's revenues, expenses and profit for 2000.

66 In these circumstances, the replacement of a few transformers here and there in a multi-million dollar electrical system is akin to changing a few bulbs in an otherwise functioning string of Christmas tree lights*. Perhaps a better example is that of the spark plug, described in Interpretation Bulletin IT-128R:

> (d) Relative value - The amount of the expenditure in relation to the value of the whole property or in relation to previous average maintenance and repair costs often may have to be weighed. This is particularly so when the replacement itself could be regarded as a separate, marketable asset. While a spark plug in an engine may be such an asset, one would never regard the cost of replacing it as anything but an expense; but where the engine itself is replaced, the expenditure not only is for a separate marketable asset but also is apt to be very substantial in relation to the total value of the property of which the engine forms a part, and, if so, the expenditure likely would be regarded as capital in nature.

67 In the circumstances of this appeal, the small transformers are the sparkplugs, rather than the engine, in the automobile that is the Appellant's electricity distribution system. Relative to the quantum of the expense in relation to the book value of the assets, other expenses and annual profits, the transformer replacement expense was not “major” in the sense contemplated by *Rainbow Pipe Line*.

68 It remains to consider whether the transformers constituted an “enduring benefit” to the Appellant's business. In support of the Respondent's position that their replacement was an enduring benefit, counsel for the Respondent argued that the transformers are an integral part of the electrical distribution system. As each one was replaced, the overall asset was enhanced by 33 years of use; thus, their replacement was a “betterment” that materially improved the distribution system beyond its original condition.

69 I am not persuaded this is so. The issue of the transformers' life expectancy has already been considered above. I accept that the transformers were “integral” to the Appellant's system in the sense that electricity could not be transmitted without them. Their replacement, however, did not enhance the system; it merely restored it to the state required to keep it functioning as intended….

…

> 70 Thus, while any given transformer might remain useful for 33 years, at any given moment there will always be another, somewhere in the system, that needs to be replaced. In these circumstances, the benefit of replacing non-functional transformers is anything but enduring; rather, the effect of the replacement was simply to preserve the status quo of the original network.
>
> 71 For all of these reasons, I am persuaded by the Appellant's argument that the transformer replacement expenditures are analogous to the costs associated with the sort of on-going maintenance repairs which Mogan, J. concluded in *Rainbow Pipe Line* should be treated as current expenses. On the evidence before me, I am satisfied that the replacement of the transformers was a current expense.
>
> (The footnote references have not been included but can be found with the original text.)

[27] While the decision of Justice Sheridan in *ATCO Electric Limited* was appealed to the Federal Court of Appeal (who dismissed the appeal), that part of Justice Sheridan's decision that related to the deductibility of the amounts incurred in relation to the replacement of the transformers was not appealed.

[28] There was very little evidence in this case to assist in any determination of how long a lobster trap will last. Gregory Norton did not provide any evidence in relation to this issue on direct examination and was evasive when he was asked this question on cross examination:

> Q. And how long -- so you used the nets and traps and they last you for a few years?
>
> A. Oh, well if you have a storm you lose them all.
>
> Q. So how long are they typically lasting?
>
> A. There's no set time, sir. It could vary. Usually nets are repaired every year and the traps are repaired every year too but they're both built each year. There's new ones built each year.
>
> Q. So you built them and then you used them and then you repaired them and the -- you ---
>
> A. Throughout the year if you use them and they get damaged a bit you'll repair them and try to get -- finish the year. And then you'll build new ones in the winter.

[29] There was no indication of the number of traps that the Appellants held at the beginning or end of any year or how many traps were built each year. A copy of the agreement of purchase and sale between Gerald Norton (Gregory Norton's father) and the Appellants dated December 29, 1999 was introduced[4]. Under this agreement the Appellants purchased 400 lobster traps with lines and buoys for $25,000. This would mean that the amount paid for each lobster trap would be less than $62 (since some amount would presumably be allocated to the lines and buoys). Since these assets were acquired from Gregory Norton's father, the amount paid may not be the best indication of fair market value. There was no evidence to establish how the amount paid by the Appellants to Gregory Norton's father would compare to the fair market value of these assets.

[30] On March 7, 2002, in what appears to be an arm's length transaction, Gregory Norton[5] sold to Glen Tassell, Gary Tassell, and Delia Tassell a boat (the "Bound to Be"), a lobster licence, 300 lobster traps and rope, 120 buoys, a depth sounder, a Rayteon GPS, a radio, and some other licences for $200,000. As noted above, the parties have agreed that the proceeds of disposition for the lobster licence were $75,000. The auditor for the CRA allocated $75,000 of the $200,000 amount to the sale of the boat and this allocation was not challenged by the Appellants. As a result, the balance of $50,000 was received for the 300 lobster traps, rope, buoys, electronic equipment and the other licences. It appears that the auditor for the CRA allocated all of the remaining $50,000 to the disposition of Class 8 assets and therefore presumably, no amount was allocated to the other licences (mackerel handlining licence and gaspereaux, herring and mackerel bait fishery licences). The sale of assets in 2002 suggests that the fair market value of the lobster traps is less than $167 each since some portion of the $50,000 would be allocated to the rope, the buoys, and the electronic equipment.

[31] Since Gregory Norton's father had 400 lobster traps (which he sold together with his licence to catch lobsters) and the Tassells acquired 300 lobster traps (together with a licence to catch lobsters), it seems to me that a logical conclusion that can be drawn from these two agreements is that a person who is carrying on a business of catching lobsters would have a large number of lobster traps. It

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[4] A lobster licence was also acquired under this agreement and it appears that this licence was acquired by Gregory Norton. Since he already held a lobster licence, Gregory Norton held two lobster licences until he sold a licence to Glen Tassell, Gary Tassell, and Delia Tassell in 2002. Louise Norton also held her own lobster licence.

[5] There was no explanation of why only Gregory Norton signed this agreement of purchase and sale or whether the 300 lobster traps were part of the 400 lobster traps that had been acquired by the Appellants from Gregory Norton's father.

therefore seems logical that since Gregory Norton had another lobster licence (before he acquired a lobster licence from his father) that he would have had 300 to 400 lobster traps before the Appellants acquired the additional traps from his father. Louise Norton also held a lobster licence and there was no evidence of how many lobster traps she held. Both Appellants were setting traps and catching lobsters during the same two months (May and June) of each year. Since there were two of them (each with their own licence) it seems logical that they would have had a larger number of traps than one person (or a group with only one licence in the case of the Tassells). It does seem logical that they would have had 400 or more lobster traps after the sale of the assets to the Tassells since each of the Appellants held a lobster licence and were setting traps and catching lobsters after that sale.

[32] There was no evidence with respect to how the labour costs related to the construction of a lobster trap would compare to the material costs. The only evidence related to the construction of the lobster traps by the Appellants related to the material costs since Gregory Norton constructed the traps himself. There was no evidence with respect to the number of lobster traps that would be built each year. It would appear, based on the amounts claimed as material costs and based on the value of the lobster traps that they held[6], that not all of the lobster traps were being replaced each year. As a result it seems logical to conclude that lobster traps would normally last one year or more.

[33] It seems to me that a person carrying on a business of catching lobsters will have several traps and each year some will have to be repaired and others will have to be replaced. If the person is not increasing the number of traps that such person has but is simply maintaining the same number of lobster traps each year (or a smaller number), then it seems to me that the amount spent to repair or replace damaged, destroyed or lost traps is incurred to simply maintain the number of lobster traps and hence to maintain the *status quo*. These amounts are being spent to satisfy a continuous demand and to maintain or restore the number of lobster traps that the person has available for catching lobsters. As a result it seems to me that the commonsense approach would be that such amounts will be deductible as a current expense in computing that person's income from the fishing business. It does not seem to me that amounts spent to simply restore the number of lobster traps to the

[6] Although the evidence was not sufficient to determine a definitive value of the lobster traps held by the Appellants, it does appear that the material costs for each year are significantly less than the value of the traps that they held.

number that the person had at the beginning of the immediately preceding lobster fishing season[7] (as a result of traps being damaged, destroyed or lost) should be treated as a capital expenditure. If the person increases the number of traps that such person owns or replaces traps that have been sold, then it seems to me that the amount spent to acquire the additional traps or the replacement traps would be a capital expenditure. Maintaining the number of lobster traps by replacing traps that have been destroyed or lost is analogous to replacing the transformers in the *ATCO Electric Limited* case.

[34] The amount spent on nets and traps in each of the years was as follows:

	2001	**2002**	**2003**	**2004**
Anchors, nets, traps and related materials	$2,767.72			
Nets, traps and related materials		$5,520.83	$12,081.78	$11,376.10

[35] The anchors referred to above were anchors that were used to hold the nets in place. There was no evidence of any change in the fishing activity related to the nets. It seems to me that the amounts spent on anchors and nets each year would be amounts spent to repair or replace damaged, destroyed or lost nets and anchors, hence such amounts would be spent to simply restore the anchors and nets to the number and condition of such anchors and nets as of the beginning of the current fishing season (for nets replaced during the fishing season) or as of the beginning of the immediately preceding fishing season (for nets replaced after the end of the fishing season). As a result the amount spent on anchors and nets each year is allowed as a deduction in computing the income of the partnership.

[36] The amounts shown above include amounts for nets and anchors (for 2001) and for nets (for 2002 to 2004). The amount spent in 2001 is significantly less than the amounts spent in 2002, 2003 and 2004. Based on the information contained in the Gregory Norton's tax returns for 1996 to 1998[8], the following amounts were spent on trap materials in those years:

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[7] Gregory Norton would build the replacement traps during the winter, which was between lobster fishing seasons.

[8] Although the tax returns for 1999 and 2000 were also submitted, the amount spent on traps and nets was not indicated as a separate item. It would appear that the amount spent on traps and nets was included in 1999 and 2000 as "gear". The amount claimed for "gear" in 1999 was $6,567.13 and in 2000 was $7,836. The years 1999 and 2000 were not audited by the CRA and as noted above in the years that were reviewed there were more items included in "gear' than just the

	1996	1997	1998
Trap materials	$4,168.95	$3,494.72	$4,937.25

[37] This amount does not include the amount spent on nets during those years and therefore the amount that would have been spent on nets and trap materials during these years would have been greater and closer to the amount spent in 2002 on nets and traps. It seems to me that since the Appellants acquired 400 lobster traps from Gregory Norton's father in 1999 and sold 300 lobster traps to the Tassells in 2002, that the Appellants gained a net total of 100 lobster traps. These extra lobster traps could explain why a smaller amount was spent on repairing or replacing traps in 2001.

[38] As indicated above, amounts spent to repair or replace lobsters traps that have been damaged, destroyed or lost will be deductible as the person is simply restoring his or her traps to the number and condition of such traps before they were damaged, destroyed or lost. If the person sells his or her lobster traps, then the costs incurred to replace the lobster traps that were sold will be on account of capital. If the person increases the number of lobster traps that he or she holds, then the cost of the additional traps will be on account of capital. This would include the initial purchase of lobster traps by a person who is starting the business of catching lobsters.

[39] It seems to me that the Appellants were carrying on their business of catching lobsters on a consistent basis from one year to the next during the years under appeal. It seems to me that each year the Appellants were simply repairing or replacing lobster traps that had been damaged, destroyed or lost that year or during the immediately preceding lobster season. As a result the amounts spent on repairing or replacing the lobster traps in this case will be deductible in computing the income of the partnership.

[40] The amount claimed for "gear" also included amounts for reels and related materials. These were used in the tuna fishery. There was no indication that there was any change in the tuna fishery during the years under appeal or that any tuna fishing gear was sold during these years. It seems to me that, as with the lobster traps, these

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amounts spent on nets and traps. In 2001, the amount claimed as "gear" was $13,205 of which $2,768 related to nets and traps, in 2002, the amount claimed as "gear" was $16,120 of which $5,521 related to nets and traps, in 2003, the amount claimed as "gear" was $25,666 of which $12,082 related to nets and traps, and in 2004, the amount claimed as "gear" was $24,055 of which $11,376 related to nets and traps. It is therefore not possible to determine the amount spent on nets and traps in 1999 and 2000.

amounts must have been incurred to replace reels and related materials that were damaged, destroyed or lost. These expenditures were made to simply restore the reels and related materials to the number and condition of the reels and related materials that the Appellants had at the beginning of the current fishing season (for reels and related materials replaced during the fishing season) or at the beginning of the immediately preceding fishing season (for reels and related materials replaced after the end of the fishing season) so that the Appellants could continue to fish as they had been fishing. These expenditures would have been incurred "pursuant to a continuous demand" and commonsense would indicate that these recurring costs of replacing reels and related material to simply restore the reels and related materials of the Appellants should be deductible and not on account of capital. As a result it seems to me that these amounts incurred for the reels and related materials should be allowed as a deduction in computing the income from the fishing business.

[41] In 2003 an amount identified as the cost of wire mesh had been claimed as a current expense. The auditor for CRA had included this expenditure as a capital expenditure. In 2004 an unidentified amount had been claimed as a current expense. The auditor for CRA had included this amount as a capital expenditure. There was no evidence with respect to the use of the wire mesh nor was there any evidence with respect to the unidentified item. Therefore, no adjustment will be made in relation to these two items.

9(n) – Amount Claimed Twice for reel, drag washer assemblies and ball bearings

[42] The Appellants produced two invoices in relation to the acquisition of 20 reel drag washer assemblies and 5 reel ball bearings. The first invoice was dated February 18, 2003 and was from Vernon D'Eon Lobster Plugs Ltd. This invoice was for 20 reel, #6-130 drag washer assemblies, and 5 reel, #55-130 ball bearings. The second invoice was from Polar Foods International Inc. (who bought at least some of the lobsters or tuna caught by the Appellants) and was dated February 22, 2003. This invoice was for 20 reel #6-130 drag washer assemblies, and 5 reel #55-130 ball bearings and two other items that were not on the other invoice from Vernon D'Eon Lobster Plugs Ltd. It is the position of the Appellants that these were two separate purchases of 20 reel drag washer assemblies and 5 reel ball bearings (and hence a total of 40 reel drag washer assemblies and 10 reel ball bearings).

[43] However it seems obvious to me that these two invoices were for the same 20 reel drag washer assemblies, and 5 reel ball bearings. The invoice from Vernon D'Eon Lobster Plugs Ltd. indicates that the 20 reel drag washer assemblies, and 5

reel ball bearings were sold to Polar Foods International Inc. and shipped to Gregory Norton. The invoice from Polar Foods International Inc. indicates that the items were "picked up at Vernon D'Eon". The increase in price on the Polar Foods International Inc. invoice was the mark-up taken by Polar Foods International Inc. for processing the transaction. It seems obvious that, although these items were picked up by Gregory Norton at Vernon D'Eon Lobster Plugs Ltd., the 20 reel drag washer assemblies, and 5 reel ball bearings were sold by Vernon D'Eon Lobster Plugs Ltd. to Polar Foods International Inc. (to be charged to Gregory Norton's account) and then by Polar Foods International Inc. to Gregory Norton.

[44] As a result, the amount claimed by the Appellants for these 20 reel drag washer assemblies, and 5 reel ball bearings was claimed twice and no adjustment will be made in relation to this item.

9(r) – Insurance costs

[45] The issue related to the insurance costs is whether the Appellants are entitled to deduct insurance costs of $846.67 incurred in relation to a loan obtained from the Credit Union. Paragraph 20(1)(*e.2*) of the *Act* provides 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:
>
> (e.2) such portion of the lesser of
>
> (i) the premiums payable by the taxpayer under a life insurance policy (other than an annuity contract) in respect of the year, where
>
> (A) an interest in the policy is assigned to a restricted financial institution in the course of a borrowing from the institution,
>
> (B) the interest payable in respect of the borrowing is or would, but for subsections 18(2) and (3.1) and sections 21 and 28, be deductible in computing the taxpayer's income for the year, and
>
> (C) the assignment referred to in clause (A) is required by the institution as collateral for the borrowing
> and

> (ii) the net cost of pure insurance in respect of the year, as determined in accordance with the regulations, in respect of the interest in the policy referred to in clause (i)(A),
>
> as can reasonably be considered to relate to the amount owing from time to time during the year by the taxpayer to the institution under the borrowing;

[46] It is the position of the Appellants that this insurance was required by the lender and should be deductible. A copy of the Single Premium Credit Life and Credit Disability Member's Enrollment form related to the loan was introduced as an Exhibit. This is a form prepared by CUIS – Credit Union Insurance Services. PART 3 – STATEMENT BY MEMBER provides that:

> I ELECT TO BECOME INSURED UNDER THE POLICIES AS NOTED IN PART 2 AND AGREE TO PAY THE REQUIRED INSURANCE PREMIUM(S). I HAVE RECEIVED A COPY OF THE ENROLLMENT FORM AND CERTIFICATE OF INSURANCE HIGHLIGHTING THE MAIN FEATURES OF THE POLICIES.
> I understand that:
>
> 1. Election for insurance under the CUMIS Life Policies is voluntary and purchase of insurance from CUMIS is not a factor in the approval of my loan.

[47] Counsel for the Appellants argued that this form was prepared by the company providing the insurance, not by the lender, and therefore does not necessarily lead to a conclusion that the lender did not require insurance. However, it seems to me that there was a direct connection between the lender and the insurance company as the insurance was arranged by the credit union and this form was prepared by Credit Union Insurance Services. Therefore it seems to me that the statement that the member was not required to purchase the insurance must relate to the requirements of the lender.

[48] The Appellants, in their testimony, stated as follows:

> **Gregory Norton – During Cross-Examination**
>
> **Q.** And the first numbered item in there it says that:
>
> "Election for insurance under Cumis Life policy is voluntary and purchase of insurance from Cumis is not a factor in the approval of my loan."

A. That's what it says but actually the way Cumis works for insurance for any fisherman is if you have enough life insurance that covers off the loan that you're buying they waive the insurance that you don't have to have the insurance.

But I didn't have life insurance to cover it so it was always mandatory to buy insurance when you have a loan.

Q. But in this case though for this loan it was not a requirement?

A. That says that on every Cumis thing. It always says that so you can waive it if you have your insurance.

Q. Yes but just reading the words of what was -- what you signed and what you agreed to it said that's not a factor in providing the loan.

A. I'm not sure what that says but I know I had to have the insurance or I wasn't going to get the loan. It's required by the company.

Louise Norton – During Direct Examination

Q. Okay. And there it says:

> "Part III, statement by member. I elect to become insured under the policies as noted in Part II and agree to pay the required insurance..."

I don't need to read it. It's plain for what it say -- so it's setting up an election. What, if any, choice did you have in negotiating this loan as to whether or not or what option did you have in setting up this loan as to whether or not you would take life insurance on it?

A. Well, I didn't -- or we didn't feel it was an option but we wanted insurance on it in the event if something was to happen to myself.

Q. Who wanted insurance?

A. In the event that something was to happen.

Q. Who wanted insurance on it?

A. I did.

Q. Yeah. What about the Credit Union, what was their attitude?

A. They advise people to have insurance on loans.

Louise Norton – During Cross-Examination

Q. Are you there? That is in relation to -- the document in there is in relation to the loan you'd taken out to purchase your 2002 Ford Explorer, correct?

Now you'd said that the bank or the insurance company ---

A. The bank.

Q. --- or Credit Union -- the bank had told you about insurance options.

A. I never understood it to be an option. I always felt that we required insurance.

Q. You always thought that you required insurance?

A. We were -- I was made to believe yes, I required insurance.

[49] Since the *Act* provides that the assignment of the insurance must be required by the lender, it is significant whether the Credit Union advised the Appellants to obtain the insurance (as stated by Louise Norton during her direct examination) or required the Appellants to obtain the insurance (as stated by Gregory Norton and by Louise Norton during her cross-examination). In this particular case, given the clear language of the form prepared by Credit Union Insurance Services and the conflicting testimony of Louise Norton, in order for the Appellants to establish that the insurance was a requirement of the Credit Union, notwithstanding the wording of the form prepared by Credit Union Insurance Services, it would have been necessary for the Appellants to call evidence directly from a representative of the Credit Union to confirm that it was a requirement to obtain the loan. Absent such evidence from a representative of the Credit Union, the Appellants cannot succeed in establishing that the insurance was required by the Credit Union and cannot succeed in relation to their claim for a deduction for these insurance costs.

9(t) – Appraisal and Water Test

[50] The Appellants claimed $225 in relation to the cost of an appraisal of their house and $100 in relation to a water test at their home. These costs were incurred so that the Appellants could obtain a mortgage on their house. I accept the Appellants testimony that these costs were necessary to obtain the mortgage. The revised position of the Appellants is that these costs should be included as part of the business use of their home expenses (which would be subject to the applicable percentage that their home is used in their business).

[51] It seems to me that these costs are related to obtaining a mortgage on their house that will be in place for several years, and would not, but for the provisions of paragraph 20(1)(*e*) of the *Act* be deductible in computing their income. Since these costs were incurred in the course of borrowing money that was used by the Appellants in carrying on their business, a portion of these costs will be deductible as provided in paragraph 20(1)(*e*) of the *Act*. The portion of these costs that will be deductible will be equal to the percentage of their house that is used in carrying on their business. Since, as noted below, I have concluded that no adjustment should be made for the percentage use of their home for business purposes, 12.5% of 20% of these costs (12.5% x 20% x $325) will be deductible in each year. Therefore the amount that will be allowed for these costs will be as follows:

	2001	**2002**	**2003**	**2004**
Amount Allowed:	$8	$8	$8	$8

9(u) & 9(bb)(i) – Use of the 2000 Ford Explorer in 2003

[52] Gregory Norton would purchase vehicles that were damaged (and in some cases written off), repair the vehicles and then use them. Generally the vehicles could not be operated on the road until they were repaired. Once the vehicles were ready to be used on the road, the vehicle would be registered with the Province of Prince Edward Island and the provincial sales tax would be paid. One of the vehicles in question was the 2000 Ford Explorer and one of the issues in relation to this vehicle is what portion, if any, of the interest paid in 2003 in relation to the amount borrowed to purchase or repair this vehicle should be allowed as a deduction in computing income in 2003.

[53] The 2000 Ford Explorer was Louise Norton's vehicle. Based on the information from the Province of Prince Edward Island it appears that the provincial sales tax was paid on this vehicle on January 3, 2001 and therefore this appears to be the date that this vehicle was ready for the road. In the fall of 2002, another Ford Explorer (the 2002 Ford Explorer) was acquired. The testimony of the Appellants in relation to the date that this newer vehicle was available for use and the date that they stopped using the 2000 Ford Explorer was vague.

[54] Louise Norton testified as follows:

> **Q.** Then it shows you owned the 2000 Explorer, starting in January, '01 up until October of 2003. But it shows an overlap of the 2002 Explorer starting in October

of 2003 going again to October of -- I'm sorry, October of 2002 going to October of 2003. Okay?

A. Um-hmm.

Q. Can you explain to us why that overlap there?

A. Well, the 2002 was bought damaged.

Q. Yes.

A. It wasn't on the road until some time later. So that's why the two vehicles were together. That's why we had the two vehicles and then we hung onto the '02 just basically till we got the price that we wanted before we sold it.

Q. You held on to the ---

A. The 2000 ---

Q. --- 2000.

A. --- until October.

Q. Okay. Until October until you what?

A. Until we sold it.

Q. Okay. When do you recall the -- or do you recall -- when did the 2002 -- when did you start using the 2002 full time if you like, as your vehicle?

A. I'm not 100 percent sure on the exact date.

Q. Okay. All right. And so the 2002 was purchased in October and some repair work was done on it.

A. Yes.

[55] According to the records obtained from the Province of Prince Edward Island, the 2000 Ford Explorer was sold on November 4, 2003 and the provincial sales tax was paid on the 2002 Ford Explorer on October 22, 2002. Therefore there appears to be approximately a one year period when both the 2000 Ford Explorer and the 2002 Ford Explorer were both available for use. It also appears that, as soon as the 2002 Ford Explorer was available, Louise Norton started using this vehicle. She also indicated that the 2002 Ford Explorer had been damaged during hurricane Juan in September 2003 and that while it was being repaired she again used the 2000 Ford

Explorer but there was no indication of the length of time that she again used the 2000 Ford Explorer. Presumably since the 2002 Ford Explorer would not have been operable until it was repaired, the 2000 Ford Explorer would have been used for the same percentage business and personal use as the 2002 Ford Explorer during this time.

[56] It seems to me that once the 2002 Ford Explorer was ready for the road on October 22, 2002, the 2000 Ford Explorer was only being held for sale or as a back-up vehicle that was used when the 2002 Ford Explorer was damaged by hurricane Juan. The percentage use for business purposes of the 2000 Ford Explorer would not change for the period of time that it was being held for sale. If the Respondent is correct, then the interest incurred in relation to an amount borrowed to buy any vehicle or any other asset used in a business would not be deductible for the period of time while that asset was being held for sale after it had been replaced. It seems to me that the percentage of business use for the 2000 Explorer would remain the same for 2003 until it was sold. As a result, 25% of the interest incurred in relation to the amount borrowed to purchase or repair this vehicle will be deductible in 2003.

9 (y)(iii) – Kerosene Drum

[57] As part of the audit, the auditor for the CRA added $253.11 to the Class 8 assets of the partnership in relation to the acquisition of a kerosene drum. During closing arguments counsel for the Appellants stated that they were no longer contesting this issue. Therefore no adjustment will be made in relation to this item.

9 (bb), (ee), (hh), (ii) – Percentage of Business Use of the Vehicles

[58] Gregory Norton owned trucks and Louise Norton owned the Ford Explorers. They claimed that both the vehicles owned by Gregory Norton and the vehicles owned by Louise Norton were used 100% of the time in carrying on their business. However is seems obvious that Louise Norton used her vehicle personally on many occasions. She would take the children to their hockey games and practices and she was also taking university courses in Charlottetown. The Appellants would have to drive to do any personal errands. The Appellants live in Annandale, Prince Edward Island which is a small fishing community with no stores or other services.

[59] Neither one of the Appellants kept a mileage log. There were two journal entries that were made in which only 25% of the costs related to Louise Norton’s vehicle were treated as business expenses. Given the extensive use of the vehicles by Louise Norton for personal purposes and the effective admission in the two journal

entries that her vehicles were used 25% for business purposes, the Appellants have failed to demolish the Minister's assumption that Louise Norton's vehicles were only used 25% for business purposes.

[60] Gregory Norton insisted that his trucks were used 100% for business purposes. His testimony consisted of simply the general statement that the trucks were only used for business purposes. The auditor for CRA compared the odometer reading on the trucks from the time that the vehicles were ready for the road until they were sold and determined the average number of kilometers that the vehicles were driven each year. She also estimated the number of kilometers that Gregory Norton drove his trucks in carrying on the fishing business. Her analysis did not support a finding that the trucks were used 100% for business purposes. Her conclusion was that the trucks were used 75% of the time for business purposes. Counsel for the Appellant did not in cross-examination or otherwise successfully challenge the analysis completed by the auditor and therefore I find that the trucks were used 75% of the time for business purposes and no adjustment will be made in relation to the percentage use of the trucks.

9 (bb)(ii), (hh)(the second iv), (ii)(i) – All Terrain Vehicles

[61] The amounts in dispute in relation to all terrain vehicles are for two separate claims:

- in 2003 the amount of $533.77 was claimed as an expense for repairs and new tires for an ATV and

- in 2004 the amount of $1,077.99 was claimed as an expense for repairs to an ATV

[62] Both claims were denied by the auditor for the CRA. It appears that the Appellants had two all terrain vehicles from 2001 to 2003 and three all terrain vehicles in 2004. Gregory Norton's testimony in relation to the all terrain vehicles was as follows:

> **A.** Yes, I use a tractor that I have around the place there. And I use a four-wheeler.
>
> **Q.** Okay. And what's the four-wheeler?
>
> **A.** It's an all terrain vehicle. And I use it for ---

Q. No, I know what it is.

A. Oh.

Q. But what's it's make and model?

A. Oh, it's a 2001 Honda.

Q. Two thousand and one Honda. How many four-wheel vehicles did you have, all terrain vehicles did you have during this time?

A. I had three but there was only one that was entered in the business. The '04 that I had I didn't send it over for business use.

Q. So you had three, the family had three vehicles during this time? You say you acquired an '04?

A. Yes.

Q. And was that one of the three or was that an extra?

A. That's right. No, that was one of the three.

Q. Okay. But you only used one in the business?

A. There was two used in the business but I only sent one over to my accountant.

Q. Okay. When you say sent one over to your accountant, what do you mean by that?

A. Okay, I claimed it as a business expense.

Q. Now what kind of work would you do with the all terrain vehicle?

A. I used it for moving equipment around the yard, like from my boathouse to the work shop.

Q. Yes.

A. Whether it was buoys or rope or trap material. I had a small trailer for it that I hooked on behind. I used it to pull my nets, spread my nets out on the lawn. The nets are heavy so -- I mostly work alone.

So lots of times I have to use motor vehicles to help me. I use it for going up to the woods. That's pretty well it.

Q. Okay. What percentage of time were you using the all terrain vehicle in the business aspect of your fishing?

A. About 50 percent of the time.

Q. Who else used it?

A. My two boys.

Q. The other Honda or the other vehicle that you had I'm taking from this you said you had three all terrain vehicles all tolled during this time span? One was a 2004 which you purchased in 2004.

So you had another one in 2001?

A. Yes.

Q. And what was it?

A. It was an Arctic Cat.

Q. Yeah. And who used that?

A. It was used some but mostly by the kids. It was -- I used it very little.

Q. Okay. And you're clear that the only expense account you would have sent or expense statement you would have sent to your accountant would be the ones relating to that one that you used in the business?

A. Yes.

And on Cross Examination:

Q. Okay. Now one of these ATV's was used -- you said -- you testified in your Direct testimony that one of these ATV's was used for business use, is that correct?

A. Fifty percent of the time, yeah.

Q. So half of it, 50 percent of the time.

A. That's right.

Q. And the other two were used for personal uses?

A. No. The '04 was never sent over to be expensed out in my books.

Q. Oh, it was not expensed out to the expense?

A. No. The '01 Honda was used 50 percent of the time as personal and 50 percent for my business. And the other one, unless I'm mixing the names up, one of the 2001's was used 50 percent of the time and the other one was used mostly for personal.

[63] It appears that from 2001 to 2003 the Appellants had two all terrain vehicles – the 2001 Honda and the Arctic Cat. The third ATV (the 2004 Honda) was acquired in 2004. It also appears that the Arctic Cat vehicle was used mainly by the Appellants' two boys. The 50% business use for 2001 to 2003 as claimed by Gregory Norton was related to the 2001 Honda ATV. Gregory Norton stated that the amount claimed for repairs and new tires in 2003 was for repairs and tires for the 2001 Honda ATV. I accept that the business use of the 2001 Honda was 50% and therefore 50% of the amount claimed for repairs and new tires will be allowed, which will result in an additional deduction of $267[9].

[64] There was, however, no indication which ATV was repaired in 2004. Since one ATV (the Arctic Cat ATV) was used personally by the Appellants' sons, without anything to establish that the repairs were made to the 2001 Honda ATV that was being used in the business (or the 2004 Honda ATV after it was acquired), no amount will be allowed for repairs in 2004.

9(ee)(iii), (gg)(i),(hh)(v), and (ii)(ii) - Tolls

[65] The amounts claimed (and denied) for parking expenses and tolls were as follows:

	2001	**2002**	**2003**	**2004**
Amount	$302	$231	$38	$39

[66] The amounts claimed for 2003 and 2004 would represent one crossing of the Confederation Bridge. Gregory Norton stated that he was fishing for tuna off the

[9] It is not entirely clear whether the actual amount spent on the repairs and tires was $533.77 or 2 x $533.77 = $1,067.54. However since Gregory Norton stated that he "only sent one over to [their] accountant", it seems to me that he did not claim 50% of the amount incurred in determining the income of the partnership and that the actual cost of the repairs and new tires was $533.77. If this is not correct, the onus was on the Appellants to show the actual amount that was incurred and since there was no evidence of the actual amount, the Appellants failed to show that they had already only claimed 50% of the amount incurred.

south coast of Nova Scotia and would travel by truck to Shelburne, Nova Scotia. As well the accountant for the Appellants worked in Dartmouth, Nova Scotia. I accept that these amounts were incurred for the purpose of earning income and they will be allowed as a expense in computing the income of the partnership.

9(gg)(ii),(hh)(iii) – Costs incurred to Make Vehicles Roadworthy

[67] Gregory Norton, as noted above, purchased vehicles that had been damaged (including some vehicles that had been written off for insurance purposes). The vehicles that he purchased could not be driven on the road in the condition that they were in when he purchased them. He would repair the vehicles and then register them for road use once the vehicles were repaired. In *LeCaine v. The Queen*, 2009TCC382, 2009 DTC 1246, I stated that:

> [22] The capital cost of a depreciable property is included in determining the undepreciated capital cost of that property. "Capital cost" is not defined in the *Income Tax Act* (the "*Act*"). In the text "Principles of Financial Accounting a Conceptual Approach" by Finney and Miller, 1968 it is stated at page 245 that:
>
> > *Incidental costs*. The cost of an asset includes not only the basic, or purchase, price, but also related, incidental costs such as the following: costs of title searches and legal fees incurred in the acquisition of real estate; transportation, installation and breaking-in costs incident to the acquisition of machinery; storage, taxes and other costs incurred in aging certain kinds of inventories, such as wine; and expenditures made in the rehabilitation of a plant purchased in a run-down condition.
>
> And at page 198:
>
> > **Determination of cost.** As a general statement, it can be said that the cost of an asset is measured by, and is equal to, the cash value of the consideration parted with when acquiring the asset. As applied to fixed asset acquisitions, cost includes all expenditures made in acquiring the asset and putting it into a place and condition in which it can be used as intended in the operating activities of the business. Thus, the cost of machinery includes such items as freight and installation costs in addition to its invoice price.
>
> [23] In "Accounting Standards in Evolution", 2nd ed., by Milburn and Skinner, 2001, it is stated at page 188 – 189 that:
>
> > The majority of tangible capital assets are purchased from external sources. The chief element of cost, then, is the invoiced price less any applicable cash or trade discounts. The chief costing problem lies in ensuring that costs incidental to acquisition and costs of making the asset capable to serve are

> capitalized... With respect to equipment, costs include all customs duties and taxes, transportation inward, insurance in transit, foundations and installation costs, and other charges for testing and preparation.
>
> [24] The cost of a capital asset should be determined for the purposes of the *Income Tax Act* in the same manner as it is for accounting purposes. The purpose of determining the capital cost of an asset for the purposes of the *Income Tax Act* is to determine the amount that should be added to the undepreciated capital cost and then amortized over time by claiming capital cost allowance ("CCA") in accordance with the *Income Tax Regulations*. There is no reason why the incidental costs (such as freight) would be added to the cost of a capital asset for accounting purposes but not included for the purpose of determining the capital cost of the asset for the purposes of the *Act*. In each case the objective is to determine the total cost of the asset that should be capitalized.

[68] The costs incurred in repairing the vehicles were simply costs incurred to make the vehicles capable of being used. These costs are simply part of the capital cost to the Appellants of acquiring a roadworthy vehicle. These repair costs should be added to the capital cost of the vehicles and no adjustment will be made in relation to these expenditures.

9(kk) – Wages reduced by $2,946.62 for 2001

[69] The Appellants claimed $18,778.57 as crew shares and $22,992.83 as salaries or wages in computing the income of the partnership in 2001. The auditor for the CRA determined that the salaries or wages were comprised of the following:

	Amount
Robert Jamieson	$4,994.99
Roger Dingwall	$4,886.64
Glenda Livingston	$3,002.49
Source deductions	$5,486.59
Darren Victor	$1,675.50
Total:	$20,046.21

[70] The difference between the total above ($20,046.21) and the amount claimed as salaries or wages ($22,992.83) is $2,946.62 and it is the denial of this amount as a deduction that is in dispute. The amounts paid to Glenda Livingston (who was the babysitter for the Appellant's children) were also denied but the Appellants are not disputing the denial of the deduction for the amounts paid to Glenda Livingston.

[71] To support the claim for the additional amount of $2,946.62 as salary or wages the Appellants introduced statements from Polar Foods International that indicated the following:

	Amount
Share to Jeff Palmer	$995.50
Share to Jeff Palmer	$675.00
Share to Share Person	$1,475.80
Share to Jeff Palmer	$540.00
Share to Jeff Palmer	$633.94
Share to Jeff Palmer	$301.88
Total:	$4,622.12

[72] The total of these amounts is significantly less than the amount of $18,778.57 that was claimed as crew shares (and which was allowed as a deduction in addition to salary and wages). No combination of any of these amounts will add to $2,946.62. If the Appellants are correct, then a portion of the amount paid to Jeff Palmer would have been claimed as crew shares and a portion would have been claimed as salary and wages. There was no explanation of why the amount paid to him would have been split between these two categories nor did the Appellants establish that these amounts were not already included in the amounts claimed (and allowed) as crew shares. Therefore no adjustment will be made in relation to the amount allowed as salary and wages.

9(ss) – Upgrade to Boat Engine

[73] The only evidence related to this item was provided by the auditor for the CRA. Gregory Norton, although he was asked more than once, was unable to recall why this expenditure was incurred or to what it was related. As a result no adjustment will be made in relation to this item.

9(iii) – Rental of a Stone Roller

[74] Gregory Norton indicated that he rented the stone roller to push any rocks or other debris on the lawn into the ground before he spread out his nets. I accept his testimony and will allow the $79.70 incurred in relation to the rental of the stone roller as an expense in determining the income of the partnership in 2002.

9(www) – (cccc) - Business Use of the Home

[75] The Appellants claim that 60% of their home was used for the purpose of carrying on their fishing business in each year under appeal (2001, 2002, 2003, and 2004). The Respondent allowed expenses on the basis that 12.5% of the home was used for the purpose of carrying on the fishing business for each of these years.

[76] Gregory Norton stated that the house was approximately 34 feet by 36 feet in size. It is a two story house with a full basement. Using these measurements, the total square footage of all three floors would be 3,672 square feet. There was an office on the main level that is 100 square feet and which was accepted by the Respondent as being used in carrying on the business. There were also some areas of the basement that were used for storage or making bait bags. The basement was also used for personal purposes. There were other rooms on the main floor that were used for both business purposes and personal purposes.

[77] In order for the Appellants' percentage use of 60% to be accepted, 2,203 square feet of the house would have to be used for the purpose of earning income. Since there was no evidence that any part of the third floor was used for the purpose of earning income, this would mean that 2,203 square feet of the 2,448 square feet that comprised the first floor and the basement would have to be used for the purpose of earning income or 90% of these two floors. I do not accept that 90% of the first floor and the basement were used exclusively for business purposes.

[78] The Appellants also wanted to include the garage and the shed in the determination. While the garage may have been used to store traps, it appears that it was also used for personal purposes. The shed was not built until 2003.

[79] The Respondent's assumption that the percentage of business use for the home was 12.5% would mean that 459 square feet was used for business purposes. The Appellants did not lead sufficient evidence to demolish this assumption and therefore no adjustment will be made to the percentage of business use of the home.

Conclusion

[80] As a result the appeals are allowed, with costs, and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that:

(a) the income of the partnership for the years under appeal is to be reduced by the following amounts:

Description	**2001**	**2002**	**2003**	**2004**
Amount allowed by agreement:	$2,434	$1,588	$6,006	$1,888
Nets, traps and related material:	$2,768	$5,521	$12,082	$11,376
Reels and related materials:	$3,600	$7,578	$4,386	$3,855
Appraisal and water test:	$8	$8	$8	$8
Interest (2000 Ford Explorer) for 2003 – 25% of $1,354:			$338	
All Terrain Vehicles – repairs and new tires			$267	
Tolls:	$302	$231	$38	$39
Rental of Stone Roller:		$80		
Total:	$9,112	$15,006	$23,125	$17,166

(b) the $215.04 spent by the Appellants to acquire a police scanner in 2002 is to be added to the undepreciated capital cost of the class 8 assets of the partnership; and

(c) the proceeds of disposition related to the sale by Gregory Norton of his lobster licence in 2002 were $75,000 and not $100,000.

Signed at Ottawa, Canada, this 2nd day of February, 2010.

"Wyman W. Webb"

Webb J.

CITATION:	2010TCC62
COURT FILE NOS.:	2008-1019(IT)I, 2008-1020(IT)I
STYLE OF CAUSE:	LOUISE C. NORTON AND HER MAJESTY THE QUEEN AND BETWEEN GREGORY W. NORTON AND HER MAJESTY THE QUEEN
PLACE OF HEARING:	Halifax, Nova Scotia
DATES OF HEARING:	May 27 and 29, June 1, December 1 and 2, 2009
REASONS FOR JUDGEMENT BY:	The Honourable Justice Wyman W. Webb
DATE OF JUDGMENT:	February 2, 2010

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