Docket: 2010-285(IT)I

BETWEEN:

JEAN-MICHEL EMOND,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeals heard on November 26, 2010, at Montréal, Quebec

Before: The Honourable Justice Brent Paris

Appearances:

For the appellant:	The appellant himself
Counsel for the respondent:	Gregoire Cadieux

JUDGMENT

The appeal from the reassessment made under the *Income Tax Act* (the Act) for the 2004 taxation year is allowed, and the reassessment is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that $6,342 must be added in computing the deduction claimed by the appellant for travel expenses related to employment for the 2004 taxation year.

The appeal from the reassessment made under the Act for the 2005 taxation year is dismissed without costs.

Signed at Ottawa, Canada, this 10th day of March 2011.

"B.Paris"

Paris J.

Translation certified true
on this 31st day of October 2012
Margarita Gorbounova, Translator

Citation: 2011 TCC 142
Date: 20110310
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REASONS FOR JUDGMENT

Paris J.

[1] These appeals were filed in respect of the appellant's 2004 and 2005 taxation years. The Minister of National Revenue (the Minister) disallowed the deduction of employment expenses in the amount of $19,445 for 2004 and $4,260 for 2005 as well as the deduction of $23,596 in rental losses, which the appellant claimed for the 2005 taxation year.

Employment expenses

[2] The appellant worked as a commissioned employee-salesman. He sold videos to video rental stores in Quebec and Ontario. As part of his job, he had to travel a great deal, and his employer paid him an allowance of $5,371 in 2004 and $4,260 in 2005, to help pay for his travel expenses. He did not include that allowance in computing his income for either year at issue.

[3] In his tax returns, the appellant claimed travel expense deductions of $26,242 for 2004 and $11,232 for 2005 relative to his employment. The table below shows the amounts claimed by the appellant and the amounts the deduction of which was disallowed by the Minister:

	2004		2005	
	Claimed	Disallowed	Claimed	Disallowed
Motor vehicle expenses	12,249	6,853		
Legal and accounting fees	100			
Meal and drink expenses	1,205		1,402	
Parking expenses	235			
Loan payment	4,516	4,516		
Hotel	437			
Flight	757			
Vehicle rental	285			
Cell phone	1,410			
Telephone	631			
Passport, visa and insurance	1,800	1,800		
Interest fees	1,407	1,406		
Miscellaneous	273			
Office expenses			2,000	
Travel expenses			7,830	
Home office expenses	934			
Non-taxable allowances received		5,370		4,260
TOTAL	26,242	19,445	11,232	4,260

[4] The Minister disallowed the deduction of $6,853 in motor vehicle expenses for 2004 on the basis that the appellant used his vehicle for business purposes only

45% of the total time he used his vehicle, not 90% of the time as the appellant claimed. The deduction of the payment of $4,516 in respect of a loan was disallowed on the basis that the payment was actually a payment on account of capital relative to the purchase of the appellant's vehicle. In addition, the deduction of $1,800, described as expenses relative to "passport, visa and insurance", as well as the deduction of $1,406 in interest fees were disallowed given that the amounts in question were not expenses incurred to earn income from employment.

[5] The Minister also deducted from the total expenses claimed for each of the years at issue the amount of the allowance received by the appellant from his employer, which he had not included in his income.

[6] The statutory provision that applies in this case is paragraph 8(1)(*f*) of the *Income Tax Act* (the Act), which provides for the deduction of some expenses by commissioned salespeople. The provision reads as follows:

> 8(1)(*f*) where the taxpayer was employed in the year in connection with the selling of property or negotiating of contracts for the taxpayer's employer, and
>
> (i) under the contract of employment was required to pay the taxpayer's own expenses,
>
> (ii) was ordinarily required to carry on the duties of the employment away from the employer's place of business,
>
> (iii) was remunerated in whole or part by commissions or other similar amounts fixed by reference to the volume of the sales made or the contracts negotiated, and
>
> (iv) was not in receipt of an allowance for travel expenses in respect of the taxation year that was, by virtue of subparagraph 6(1)(*b*)(v), not included in computing the taxpayer's income,
>
> amounts expended by the taxpayer in the year for the purpose of earning the income from the employment (not exceeding the commissions or other similar amounts referred to in subparagraph 8(1)(*f*)(iii) and received by the taxpayer in the year) to the extent that those amounts were not
>
> (v) outlays, losses or replacements of capital or payments on account of capital, except as described in paragraph 8(1)(*j*),

> (vi) outlays or expenses that would, by virtue of paragraph 18(1)(*l*), not be deductible in computing the taxpayer's income for the year if the employment were a business carried on by the taxpayer, or
>
> (vii) amounts the payment of which reduced the amount that would otherwise be included in computing the taxpayer's income for the year because of paragraph 6(1)(*e*);

. . .

[7] In his testimony, the appellant confirmed that, in 2004, he had used his car almost exclusively for activities related to his job. He did not keep a logbook for the use of his vehicle, but he provided a reconstruction of his travel (Exhibit A-1) where it was indicated that he had travelled 50,833.7 kilometres in total and that 5,194.8 of them (10%) constituted travel from his home to his employer's place of business, which he had described as personal travel. The appellant stated that he went directly from his employer's place of business to see his clients before returning home. He therefore treated all the kilometres travelled, except for his travel from home to his employer's place of business, as being related to his job.

[8] At the hearing, counsel for the respondent agreed that the appellant had successfully proven that, in 2004, 80% of his car travel was attributable to activities related to his job in 2004. Counsel for the respondent argues, however, that, in addition to the travel from his home to his employer's place of business, the travel from his last appointment of the day to his home should be treated as personal.

[9] The appellant argues that, because he also worked from home, the travel from his last appointment of the day to his home should also be considered to be related to his job. For her part, the respondent argues that the total amount of motor vehicle expenses should be reduced by $568, that is, the difference between the amount claimed as car insurance stated in the list of vehicle costs attached to the appellant's 2004 tax return and the amount paid by the appellant for car insurance according to the Assurance Desjardins statement provided by the appellant.

<u>Analysis: travel expenses</u>

[10] It has been held that, when a taxpayer has to work from home, which therefore becomes a regular place of work, travel from and to the home constitutes travel done as part of the job. See *Toutov v. The Queen*[1] and *Campbell v. The*

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[1] 2006 DTC 2928.

Queen.[2] Consequently, the expenses related to that travel may be deducted under paragraph 8(1)(*f*) of the Act. The appellant's testimony, according to which he regularly worked at his home office, was not disputed by the respondent. I note also that the Minister allowed the deduction of his home office expenses. For that reason, I find that the appellant was able to prove that the travel at issue that he had done with his vehicle was related to the duties of his job and that he is entitled to deduct 90% of the expenses related to his vehicle in computing his income for 2004.

[11] As stated by the respondent, the amount should be reduced so that it represents the amount actually paid for car insurance based on the numbers on the Desjardins statement. The total amount of the deduction claimed as motor vehicle expenses for 2004 is $12,249. This amount should be reduced by 90% of $568 (that is, $511), which leaves $11,738. Given that the Minister has already allowed a deduction of $5,396, the appellant is entitled to an additional deduction of $6,342 as motor vehicle expenses.

[12] I cannot allow the appellant's claim to deduct the amount of $4,516 as the repayment of the balance of his car loan. This payment clearly represented a payment on account of capital, and subparagraph 8(1)(*f*)(v) prevents the deduction of that type of payment.

[13] The evidence presented by the appellant regarding the deduction he claimed under "passport, visa and insurance" was confusing, deficient and not sufficient to establish the nature or the purpose of the expenses in question. The appellant has therefore not discharged his burden of proving that those expenses had been incurred in order to earn income.

[14] The amounts deducted as interest included interest on an unpaid balance of at least one of the appellant's credit cards as well as on annual fees, fees for exceeding the credit limit and life insurance for that same card. In support of his deduction claim, the appellant filed in evidence a handwritten calculation sheet and part of a credit card bill. Unfortunately, it is impossible to establish what proportion of the items on the handwritten list of expenses were related to the appellant's job. Consequently, no part of the deduction claimed may be allowed.

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[2] 2003 DTC 420.

[15] I also find that the Minister correctly treated the travel expense allowance that the employer paid the appellant. Under subparagraph 8(1)(*f*)(iv) of the Act, in order for a taxpayer to be entitled to deduct travel expenses, he or she should not be receiving a reasonable allowance for travel expenses from his or her employer. If he or she receives an allowance that is not considered reasonable the taxpayer must include it in computing his or her income under paragraph 6(1)(*b*) of the Act. The respondent acknowledged that the allowance received by the appellant was not reasonable and that the appellant was therefore entitled to deduct the travel expenses related to his employment. We would obtain the same net result if we reduce the amount of the deduction claimed by the appellant as travel expenses by the allowance amount. This method was endorsed by the Court in *Vienot v. The Queen*.[3]

Rental losses

[16] The next issue deals with the deduction of rental losses of $23,596 claimed by the appellant for 2005. The Minister disallowed the deduction on the basis that the property to which the loss was related was not a source of income for the appellant.

[17] In July 2005, the appellant bought a 10-room inn in Saint-Zénon, Quebec, for $550,000. At around the same time, he started a company called Le Zénon Inc. in order to operate the inn, which had a bar and a restaurant.

[18] The evidence reveals that the appellant lives at the inn and has operated it on behalf of the company since he purchased it. It seems that the business venture has not been financially successful for the company despite all of the appellant's efforts. The appellant's partner, Lise Hamel, has also spent a great deal of time at the inn with her daughter and has helped the appellant operate the business. For a time, her daughter's horse was on the property. According to Ms. Hamel, the business was planning to establish an equestrian centre as part of the inn's activities. According to the witnesses, the appellant lives in the inn's basement, and Ms. Hamel and her daughter stay in a room on the first floor when they are at the inn.

[19] The company did not pay rent to the appellant in 2005. The appellant stated that it had not made enough money to pay rent during that year. Nothing in the

[3] 2010 TCC 112, at paragraphs 19 to 25.

evidence suggests that the company paid rent to the appellant in the course of the following years. No rental expenses are entered for the period at issue in the financial statements of the company for its fiscal year ending May 31, 2006. No other financial statements were filed in evidence. Based on what is stated at paragraph 7(n) of the Reply to the Notice of Appeal, the appellant reported a gross rental income of $20,160 in his personal tax return for the 2006 taxation year, but it had not been established whether it was the amount received as rent from the company. That income tax return was not filed in evidence at the hearing, and the evidence showed that in 2006 the appellant rented out the house he owned in Terrebonne. It is therefore impossible to establish whether part of the rental income reported represented rent received for the property in Saint-Zénon.

[20] The agreements concluded between the appellant and his company regarding the use of the property are unclear. In their testimony, the appellant and Ms. Hamel stated that a lease had been established between the appellant and the company, but they could not provide a copy of it to the Court given that the document was with counsel representing the appellant in another matter. The appellant did not say what the rent amount was, but Ms. Hamel said that it was $4,000 per month. However, at the audit stage, the appellant's representative told the auditor that the rent was $2,000 per month and that no lease had been signed. In addition, at the audit stage, the appellant was asked to answer a number of questions concerning the claim for a deduction of rental losses including the amount of rent that he was asking for. He did not respond. In response to the question of how the rent amount had been established, the appellant wrote [TRANSLATION] "through the amount of the hypothec." In addition, as previously mentioned, no amount of rent paid or to be paid was entered for the period at issue in the financial statements for the fiscal year ending on May 31, 2006.

Submissions: rental losses

[21] The respondent argues that the property was not a source of income for the appellant in 2005 and that, as a result, he cannot take his losses into account in computing his income under the Act. Counsel for the respondent stated that the ownership and use of the property by the appellant had at least two personal aspects: he lived there and let his company operate it without paying rent. Accordingly, following the Supreme Court's decision in *Stewart v. The Queen*,[4] it is necessary to take into account the commercial nature of the use the appellant made of the property. Counsel for the respondent argues that, because the appellant

4 [2002] 2 S.C.R. 645.

chose to allow the company to use the property without paying rent, he did not use the property in a commercial manner. Accordingly, the property cannot be considered as a source of income for the appellant.

[22] Alternatively, the respondent argues that, if the property really was a source of income, the losses were less significant than the appellant reported. The respondent questions the amount of the deduction claimed as interest.

[23] In his submissions, the appellant seemed to see the distinction between himself and his company, Le Zenon Inc., somewhat unclearly maintaining that he intended to operate the inn as a business and was therefore entitled to deduct the rental losses. His submissions focused mostly on the efforts that Ms. Hamel and he had deployed in order to make the inn a success as well as the difficulties that they had had to overcome. He maintains that, even though he had worked hard, he lost money in the business and that it would be fair to let him deduct the rental losses at issue.

Analysis: rental loss

[24] In *Stewart*, the Supreme Court of Canada ruled that, to establish that a taxpayer's activities are a source of income within the meaning of the Act, whether they consist of a business or a property, they must be undertaken in pursuit of profit. The Supreme Court's analysis of the criterion to apply in order to determine whether a business or property exists as a source of income is found at paragraphs 48 to 51 of that decision:

> 48 In our view, the determination of whether a taxpayer has a source of income, must be grounded in the words and scheme of the Act.
>
> 49 The Act divides a taxpayer's income into various sources. Under the basic rules for computing income in s. 3, the Act states:
>
>> 3. The income of a taxpayer for a taxation year for the purposes of this Part is his income for the year determined by the following rules:
>>
>> (*a*) determine the aggregate of amounts each of which is the taxpayer's income for the year ... from a source inside or outside Canada, including, without restricting the generality of the foregoing, his income for the year from each office, employment, business and property; [Emphasis added.]

With respect to business and property sources, the basic computation rule is found in s. 9:

> 9. (1) Subject to this Part, a taxpayer's income for a taxation year from a business or property is his profit therefrom for the year.
>
> (2) Subject to section 31, a taxpayer's loss for a taxation year from a business or property is the amount of his loss, if any, for the taxation year from that source computed by applying the provisions of this Act respecting computation of income from that source mutatis mutandis.

50 It is clear that in order to apply s. 9, the taxpayer must first determine whether he or she has a source of either business or property income. As has been pointed out, a commercial activity which falls short of being a business, may nevertheless be a source of property income. As well, it is clear that some taxpayer endeavours are neither businesses, nor sources of property income, but are mere personal activities. As such, the following two-stage approach with respect to the source question can be employed:

> (i) Is the activity of the taxpayer undertaken in pursuit of profit, or is it a personal endeavour?
>
> (ii) If it is not a personal endeavour, is the source of the income a business or property?

The first stage of the test assesses the general question of whether or not a source of income exists; the second stage categorizes the source as either business or property.

51 Equating "source of income" with an activity undertaken "in pursuit of profit" accords with the traditional common law definition of "business", i.e., "anything which occupies the time and attention and labour of a man for the purpose of profit": *Smith*, *supra*, at p. 258; *Terminal Dock*, *supra*. As well, business income is generally distinguished from property income on the basis that a business requires an additional level of taxpayer activity: see *Krishna*, *supra*, at p. 240. As such, it is logical to conclude that an activity undertaken in pursuit of profit, regardless of the level of taxpayer activity, will be either a business or property source of income.

[25] The Supreme Court also stated the following at paragraph 54:

54 It should also be noted that the source of income assessment is not a purely subjective inquiry. Although in order for an activity to be classified as commercial in nature, the taxpayer must have the subjective intention to profit, in addition, as stated in *Moldowan*, this determination should be made by looking at a variety of

> objective factors. Thus, in expanded form, the first stage of the above test can be restated as follows: "Does the taxpayer intend to carry on an activity for profit and is there evidence to support that intention?" This requires the taxpayer to establish that his or her predominant intention is to make a profit from the activity and that the activity has been carried out in accordance with objective standards of businesslike behaviour.

[26] In this case, as noted by counsel for the respondent, it must be established how the appellant, not the company, used the property. The appellant chose to purchase it in his own name rather than going through the company; he cannot ignore that choice when it does not suit his interests. The Court cannot ignore the existence of the company. In law, the business that it operated was separate from the rental activity carried out by the appellant. This point was established as follows by the Supreme Court of Canada in *Appleby v. The Minister of National Revenue*, [1975] 2 S.C.R. 805, [1974] C.T.C. 693, 74 D.T.C. 6514 to 813 (C.T.C. 698, D.T.C. 6517):

> Ever since *Salomon v. Salomon & Co.*, it has been accepted that although the shares of a limited company may be beneficially owned by the same person who also manages it, its business is nevertheless in law that of a distinct entity, a legal person having its own rights and obligations. The *Income Tax Act* unmistakably implies that this rule holds good for tax purposes.

[27] Thus, the rental activity carried out by the appellant must in itself be carried out with a view to making a profit or in a commercial manner in order to be a source of income within the meaning of the Act.

[28] In my view, the appellant did not satisfy the first requirement established by the Supreme Court in *Stewart*; that is, he did not prove that he had the subjective intention to make a profit when he provided his company's property so that it could use it to operate its business. The evidence seems to show that the appellant intended to rent out the property to the company in exchange for rent that was roughly equal to the hypothec payments, namely, a little over $2,000 per month. This is consistent with the statements of the appellant's representative to the auditor regarding the rent amount as well as the answer provided by the appellant to the question he was asked in writing regarding how the rent amount had been established. This amount was insufficient, however, to cover all the appellant's other expenses, such as insurance, taxes and maintenance. For 2005, the appellant claimed the deduction of expenses related to the property, including hypothecary interest of $4,000 per month. There is no reason to believe that the appellant did not know that the rent amount would not be sufficient to cover expenses and that it

would result in losses. The only conclusion that can be drawn is that the appellant did not intend to make a profit from renting the property to his company.

[29] I am not satisfied of the existence of an agreement specifying that the company had to pay rent of $4,000 per month. At least, it did not exist during the 2005 taxation year. This amount was not mentioned to the auditor, and the appellant did not mention it in the questionnaire he had filled out for the auditor. In addition, this amount does not seem to be included in the amount reported by the appellant as rental income and was not recognized as an expense in the company's financial statements.

[30] Even if an agreement stating that the company had to pay rent of $4,000 per month did exist, it was not proven that it could be expected that the agreement would result in a profit for the appellant. The loss of $24,838 for 2005 was recorded by the appellant between July 15 and December 31 of that year, that is, for a period of five and a half months, which means that it cost the appellant over $4,000 per month to maintain the property.

[31] The behaviour adapted by the appellant afterwards also leads to the conclusion that he was not carrying out rental activities in a commercial manner. He does not seem to acknowledge that the company owed him unpaid rent or that he had not tried to find a new tenant when his company was unable to generate enough revenue to pay rent.

[32] For these reasons, I unfortunately find that the appellant is not entitled to the deduction that he had claimed for rental losses for 2005.

[33] If I had found in favour of the appellant on this issue, I would not have reduced the amount of the deduction claimed by the loss amounts. I accept the appellant's evidence that the interest the deduction of which he claimed was made up of two parts: interest from the first hypothec for the inn as such and interest from the second hypothec that the appellant took out for his house in Terrebonne in order to recover the balance of the purchase price of the inn.

[34] The appeal is allowed to the extent that the deduction claimed by the appellant for travel expenses related to his employment must be increased by $6,342 for the 2004 taxation year.

[35] After the hearing ended, the appellant sent other documents to the registry of the Court asking that they be taken into account. The respondent objected to the hearing being reopened in order to allow new documents to be added to the record.

[36] Only one of these documents seemed as if it could be helpful in making findings on the issues before me in this case. It was a copy of a motion filed on behalf of the appellant in another matter. The motion contained a statement according to which there had indeed been an agreement stating that the appellant's company had to pay rent of $4,000 per month. However, as counsel for the respondent stated, it was not irrefutable evidence that the agreement had existed. In addition, it contradicted other evidence before me on the issue.

[37] Moreover, nothing implies that the appellant did not have access to the documents before the hearing.

[38] For these reasons, I find that it would not be in the best interests of justice to re-open the hearing to allow these documents to be filed. Therefore, I decline to do so.

Signed at Ottawa, Canada, this 10th day of March 2011.

"B.Paris"

Paris J.

Translation certified true
on this 31st day of October 2012
Margarita Gorbounova, Translator

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APPEARANCES:

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COUNSEL OF RECORD:

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