Docket: 2010-2215(IT)I

BETWEEN:

CHRIS SKALING,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on February 3, 2011, at Victoria, British Columbia

Before: The Honourable Justice L.M. Little

Appearances:

Agent for the Appellant:	Jim Mitchell
Counsel for the Respondent:	Rob Whittaker

JUDGMENT

The appeals from the assessments made under the *Income Tax Act* for the 2006 and 2007 taxation years are dismissed, without costs.

Signed at Vancouver, British Columbia, this 23rd day of March 2011.

"L.M. Little"

Little J.

Citation: 2011 TCC 180
Date: 20110323
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BETWEEN:

CHRIS SKALING,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Little J.

A. FACTS

[1] The appeals deal with the Appellant's 2006 and 2007 taxation years.

[2] During the years under appeal, the Appellant was employed as an automobile mechanic by Alpine Transmission & Auto Repairs Ltd. ("Alpine").

[3] The Appellant worked four days per week for Alpine.

[4] Prior to 2006, the Appellant's hobby was working on high performance automobiles which were used in drag races.

[5] The Appellant explained that "drag races" were races where "muscle cars" competed in straight-line racing usually over a distance of one-quarter mile. (Transcript, page 5, lines 19 to 25 and page 6, lines 14 to 25)

[6] The Appellant stated that in the 2006 year, he started a business which consisted of rebuilding automobile engines plus entering his 1970 Buick GS (the "Race Car") in drag races at various race tracks in British Columbia (the "Business"). (Transcript, page 34, lines 5 to 8)

(Note: The Appellant testified that he actually started the Business in 2002, but because he was very busy at Alpine, he was forced to discontinue his Business until 2006.) (Transcript, page 24, lines 15 to 20).

[7] The Business operated by the Appellant was a sole proprietorship.

[8] The Appellant operated the Business from a garage at his home.

[9] The Appellant said that he had the following income from the Business of rebuilding automobile engines:

a) 2006 - $19,223;
b) 2007 - $20,795.

[10] When the Appellant commenced operating the Business, he owned a number of tools (the "Tools") which he claims that he had acquired over a number of years.

[11] The Appellant also owned a Truck and Trailer used to haul the Race Car to and from the race tracks.

[12] The Tools, the Race Car and the Truck and Trailer were all acquired by the Business in 2006 and recorded by the Appellant's accountant, Mr. Jim Mitchell, in the Capital Cost Allowance Schedules ("CCA") of the Business.

[13] The Tools were recorded in the Appellant's CCA Schedule at a value of $27,140.

[14] The Minister of National Revenue (the "Minister") maintained that the fair market value ("FMV") of the Tools at the beginning of 2006 was not more than $13,750.

[15] The value of the Race Car was recorded on the books of the Appellant at a value of $35,546. The Minister maintained the FMV of the Race Car was $4,455.

[16] The Truck and Trailer were recorded on the Appellant's books at a value of $40,000.

[17] In the 2007 taxation year, the Appellant claimed Supplies of $13,432. (Note: This amount was the operating expense of the Race Car for that year.)

[18] When the Appellant filed his 2006 and 2007 income tax returns, he claimed CCA on the Tools, Race Car and Truck and Trailer.

2006 Taxation Year	
CCA	Allowed by Canada Revenue Agency ("CRA")
Tools at 20 per cent ½ year rule: $2,714	$1,357
Race Car at 30 per cent ½ year rule: $5,332	$0.00
Truck and Trailer at 30 per cent – ½ year rule: $6,000	$0.00

2007 Taxation Year	
CCA	Allowed by CRA
Tools at 20 per cent: $4,885	$2,443
Race Car at 30 per cent: $9,000	$0.00
Truck and Trailer at 30 per cent: $10,030	$0.00

(Exhibit R-1, Tab 4)

[19] The CCA Schedules of the Appellant and the Minister show the following:

2006 Taxation Year	
Additions to 2006 CCA Schedule	Allowed by CRA
Tools: $27,140	$13,570
Race Car: $35,546	$0.00
Truck and Trailer: $40,000	$0.00
UCC End of the Year	Allowed by CRA
Tools: $24,426	$12,213
Race Car: $30,214	$0.00
Truck and Trailer: $34,000	$0.00
Net amount of capital assets disallowed: $89,116	
Net amount of CCA disallowed for the period: $12,689	
Ending UCC: $12,213	

2007 Taxation Year	
Beginning UCC on 2007 CCA Schedule	Allowed by CRA
Tools: $24,426	$12,213
Race Car: $30,314	$0.00
Truck and Trailer: $34,000	$0.00
UCC End of the Year	Allowed by CRA
Tools: $19,541	$9,770
Race Car: $21,214	$0.00
Truck and Trailer: $23,910	$0.00
Net amount of CCA disallowed: $21,473	
Ending UCC: $9,770	

(Exhibit R-1, Tab 4)

(Note: The Appellant testified that he discontinued the Business at the end of 2008 because he is unable to work and receives a disability payment).

B. ISSUE

[20] The issue is whether the Appellant is allowed to deduct amounts in excess of the amounts that were allowed by the Minister.

C. ANALYSIS AND DECISION

[21] In cross-examination, Counsel for the Respondent asked the Appellant the following questions:

> Q … Approximately how many races in '06 and in '07 [did] Steve Braithwaite participated in? If you recall.
>
> (Note: Steve Braithwaite was the driver of the Race Car).
>
> A Not too many. We kind of slowed down. Probably half a dozen perhaps. We didn't go to Bremerton either one of those years.
>
> (Note: Bremerton is the location of a race track in the State of Washington.)
>
> Q So that's half a dozen in total for both years?

A No no, each year.

(Transcript, page 46, lines 9 to 17)

[22] Counsel for the Respondent also asked the Appellant the following question:

Q And you were not provided money by some wealthy person to assist you in your auto racing, is that correct?

A No, I was provided by actually -- yeah, Peter Wille at Victoria Automatic. Transmission stuff and whatnot, the parts like I discussed earlier. $1,000 from Lordco.

(Transcript, page 46, line 25 to page 47, lines 1 to 6)

[23] At page 35 of the transcript, the Appellant said:

A Lordco used to give me $1,000 every year for sponsorship that I could -- it was on an account. Account number 474 at Lordco. I go in there and I get parts not at wholesale but at cost, and I could buy up to $1,000 worth of parts.

(Transcript, page 35, lines 21 to 25).

[24] Counsel for the Respondent also asked the Appellant:

Q …what prize money was won in '06 first and what prize money was won in '07?

A I know in Port Alberni, I think we got -- I think it was like 4 or 500 bucks for one race and then just trophies other than that.

Q Okay. So is it fair to state that over two years you got some trophies but the only prize money you generated was 4 to $500?

A I think we got a few first prizes at Western Speedway, but the pay isn't that great, right? You'd be like 150 bucks or whatever.

(Transcript, page 48, lines 1 to 11)

[25] Counsel for the Respondent then said:

> Q … Can you tell the court, in terms of '06, what sort of expenses would you be incurring for the auto racing activity?

(Transcript, page 48, lines 13 to 15).

[26] The Appellant responded with the following information:

Item	2006	2007
A pair of slicks at $750 per year times 2 (Note: "slicks" are specialized rear tires designed for racing)	$1,500	$1,500
Race fuel (approximate cost)	$500	$500
Valve springs	$150	$150
Coil springs ($150 x 2)	$300	$300
Fuel for the Truck to get the Race Car to the track and back to the Appellant's home	$300 to $500	$300 to $500
TOTAL:	$2,750 to $2,950	$2,750 to $2,950

(Transcript, pages 48 to 54)

[27] At page 56 of the transcript, Counsel for the Respondent said:

> Q … This is a passion. Racing is a passion of yours, correct? …
>
> A Yes. It's a passion, it's what I know. My dad taught me…

(Transcript, page 56, lines 18 to 22).

[28] Counsel for the Respondent called Dalyce Levesque as a witness. Ms. Levesque is an auditor with the CRA. She was the auditor on this file. Counsel for the Respondent said:

> Q … And can you tell the court what were the issues that were the subject of this audit?
>
> A …through the course of the audit I determined that Mr. Skaling was in the business of building custom engines, so I determined that the race car, the truck and trailer were not related to those. I also determined that the -- he had tools, but that they were valued inaccurately and reduced the valuation of those tools.

(Transcript, page 69, lines 14 to 15 and lines 21 to 25 to page 70, lines 1 to 2)

[29] Counsel for the Respondent asked the auditor at page 75:

> Q Now, your evidence indicates you didn't allow any amounts for the car, the truck/trailer. Can you tell the court why you didn't allow any amounts in respect of those items for capital cost allowance?
>
> A The race car and the truck and trailer were related to, of course, racing and my interview and discussion with Mr. Skaling indicated that he was in the business of building Buick engines and not -- there was no -- the business of racing wasn't there.

(Transcript, page 75, lines 5 to 13)

Advertising

[30] Counsel for the Respondent noted that the auditor had allowed an advertising expense. Counsel for the Respondent said:

> Q Can you tell the court why you decided to allow that?

> A Given that he was in the business of building engines, it was discussions with my team leader and we decided that it was reasonable that he may use his hobby of racing to advertise that building [sic "business"] since it is, you know, it is a similar industry.
> …

(Transcript, page 76, lines 23 to 25 to page 77, lines 1 to 4)

(Note: Ms. Levesque stated at page 77 of the transcript that to be reasonable and fair, a percentage of his operating costs of his Race Car be allowed as an advertising expense. According to Exhibit R-1, Tab 3, the following expenses were allowed: advertising in 2006 at $445 and 2007 at $1,343. This is 10 per cent of the amount claimed by the Appellant.)

[31] In his argument, Mr. Mitchell, the Appellant's accountant, said that the Appellant has not gone overboard in any expenses. He said that the Race Car and the engine rebuilding business is one Business, all designed to promote Mr. Skaling's endeavours to establish a Business on his own and be self-employed.

[32] Counsel for the Respondent noted that the CRA determined that the capital cost of the UCC for the Tools was one-half of what was claimed.

[33] Counsel for the Respondent stated that the CRA determined that the capital cost that was allowed was restricted to the Tools and that any capital cost claimed re the Race Car, the Truck and the Trailer were disallowed because they were not part of the Business. It was noted by Counsel for the Respondent that 10 per cent of the operating expenses claimed for 2007 were allowed, i.e. 10 per cent of $13,432 or $1,343 (see paragraph [17] above).

[34] Counsel for the Respondent said:

> MR. WHITTAKER: I think that the basic premise for that was simply auto racing was not a business. While the taxpayer may have described it as a business, there was no reasonable expectation of profit. So that's the basic reason why that was disallowed. Plus, CRA took the view that the race car, the trailer and the truck, while there could be an argument that there was some business purpose to rolling it into the engine

> rebuilding part of the business, there was also a large personal element. And because there's a person element as well, the capital cost allowance would not be available. That's really the nub of the CRA position.
>
> (Emphasis added)

(Transcript, page 104, lines 13 to 24)

[35] Counsel for the Respondent then stated:

> MR. WHITTAKER: Our basic position is this, and the appellant has testified that auto racing was his passion and that's clearly understandable. So we say there's a large personal element to the race car, the purchase of the truck, the trailer, and because of that large personal element, we submit based on the law that the capital cost allowance is not available for those assets.

(Transcript, page 105, lines 11 to 17)

[36] As noted above, Counsel for the Respondent said that the basic reason the expenses related to the Race Car were disallowed is that there was no reasonable expectation of profit.

[37] In *Stewart v Canada (Her Majesty The Queen)*, [2002] 2 S.C.R. 645, 2002 SCC 46, [*Stewart*], the Supreme Court of Canada dealt with the question of whether the reasonable expectation of profit test is an acceptable test to determine whether a taxpayer was carrying on a commercial venture. Justices Iacobucci and Bastarache said:

> 5 It is undisputed that the concept of a "source of income" is fundamental to the Canadian tax system; however, any test which assesses the existence of a source must be firmly based on the words and scheme of the Act. As such, in order to determine whether a particular activity constitutes a source of income, the taxpayer must show that he or she intends to carry on that activity in pursuit of profit and support that intention with evidence. The purpose of this test is to distinguish between commercial and personal activities, and where there is no personal or hobby element to a venture undertaken with a view to a profit, the activity is commercial, and the taxpayer's pursuit of profit is established. However,

where there is a suspicion that the taxpayer's activity is a hobby or personal endeavour rather than a business, the taxpayer's so-called reasonable expectation of profit is a factor, among others, which can be examined to ascertain whether the taxpayer has a commercial intent.

…

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?

…

52 … Thus, where the nature of a taxpayer's venture contains elements which suggest that it could be considered a hobby or other personal pursuit, but the venture is undertaken in a sufficiently commercial manner, the venture will be considered a source of income for the purposes of the Act.

53 We emphasize that this "pursuit of profit" source test will only require analysis in situations where there is some personal or hobby element to the activity in question. With respect, in our view, courts have erred in the past in applying the REOP test to activities such as law practices and restaurants where there exists no such personal element: see, for example, *Landry*, *supra*; *Sirois*, *supra*; *Engler v The Queen*, 94 D.T.C. 6280 (F.C.T.D.). Where the nature of an activity is clearly commercial, there is no need to analyze the taxpayer's business decisions. Such endeavours necessarily involve the pursuit of profit. As such, a source of income by definition exists, and there is no need to take the inquiry any further.

(Emphasis added)

[38] In other words, the Supreme Court of Canada in *Stewart* introduced a new test for determining whether an activity was a business, especially when there was some "personal or hobby" element to the activity in question.

[39] In my opinion, Mr. Skaling was pursuing a personal activity or a hobby when he was engaged in auto racing AND the auto racing activity was not undertaken in a sufficient commercial manner to be considered a source of income.

[40] I have reached this conclusion because the Appellant stated that when he entered races he only earned $400 to $500 in one year, plus $150 for a total of $550 or $650 in cash prizes and a number of trophies. However, he owned the following assets which were related to racing:

a) Race Car - $35,546;
b) Truck and Trailer - $40,000.

In addition, the Appellant claimed that he had Tools with a value of $27,140. In other words, the FMV of the assets used by the Appellant were in excess of $100,000 whereas the income for 2006 and 2007 was $550 to $650 for both years.

[41] It should also be noted that the Appellant had the following operating expenses for the Race Car and Truck and Trailer:

a) 2006 - $2,750 to $2,950;
b) 2007 - $2.750 to $2,950.

(See paragraph [26] above.)

[42] In his argument, Counsel for the Respondent referred to the decision of the Supreme Court of Canada in *Hickman Motors Ltd. v Canada (Her Majesty the Queen)*, [1997] 2 S.C.R. 336, 51 D.T.C. 5363, to support the Minister's decision that CCA should not be allowed on the Race Car and on the Truck and Trailer. I agree with the Minister's position on this issue.

D. CONCLUSION

[43] After carefully examining the evidence and reviewing the relevant Court decisions, I have concluded that the Minister was correct when he concluded that the Appellant's "hobby" of drag racing did not constitute a commercial venture or a business.

[44] The appeals are dismissed, without costs.

Signed at Vancouver, British Columbia, this 23rd day of March 2011.

"L.M. Little"

Little J.

CITATION:	2011 TCC 180
COURT FILE NO.:	2010-2215(IT)I
STYLE OF CAUSE:	CHRIS SKALING AND THE QUEEN
PLACE OF HEARING:	Victoria, British Columbia
DATE OF HEARING:	February 3, 2011
REASONS FOR JUDGMENT BY:	The Honourable Justice L.M. Little
DATE OF JUDGMENT:	March 23, 2011

APPEARANCES:

Agent for the Appellant:	Jim Mitchell
Counsel for the Respondent:	Rob Whittaker

COUNSEL OF RECORD:

For the Appellant:	
Name:	
Firm:	
For the Respondent:	Myles J. Kirvan Deputy Attorney General of Canada Ottawa, Canada