Docket: 2009-2919(IT)I

BETWEEN:

GEORGE LEISSER,

appellant,

and

HER MAJESTY THE QUEEN,

respondent.

Appeal heard on March 30, 2010, at Montréal, Québec.

Before: The Honourable Justice Gaston Jorré

Appearances:

For the appellant:	The appellant himself
Counsel for the respondent:	Marjolaine Breton

JUDGMENT

In accordance with the attached reasons for judgment, the appeal from the assessments made under the *Income Tax Act* for the 2004 and 2005 taxation years is allowed, without costs, and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that:

(a) in the 2004 taxation year,
    (i) the appellant's income should be reduced by the $2,555.30 amount of the German pension,
    (ii) the rental loss of $8,924 should be increased to $19,563.14;
(b) in the 2005 taxation year, the appellant's net rental income should be decreased from $7,223 to $4,757.35.

Signed at Ottawa, Ontario, this 6th day of October 2011.

"Gaston Jorré"

Jorré J.

Citation: 2011 TCC 472
Date: 20111006
Docket: 2009-2919(IT)I

BETWEEN:

GEORGE LEISSER,

appellant,

and

HER MAJESTY THE QUEEN,

respondent.

REASONS FOR JUDGMENT

Jorré J.

Introduction

[1] The appellant appeals from assessments for the 2004 and 2005 taxation years. The appellant is in his late 80s. He has elected the informal procedure.

[2] In assessing, the Minister of National Revenue (Minister) substantially reduced net rental losses claimed by the appellant. I shall return to these changes in a moment.

[3] The appellant raised a number of other issues in his appeal.

Pensions

[4] The first relates to the taxability of foreign pensions.

[5] In 2005 the appellant claimed and received a deduction of $1,621.69 with respect to a German pension pursuant to the Canada-Germany tax treaty.[1]

[6] In appealing, the appellant claimed a deduction with respect to the same pension in 2004. After the hearing, the respondent wrote to the Court and the appellant and conceded that an amount of $2,555.30 was deductible pursuant to the treaty.[2]

[7] Accordingly, the appeal will be allowed to the extent of this concession.

Issues Relating to Years Prior to 2004

[8] The appellant also raised a number of other issues relating to earlier taxation years.

[9] While I cannot make changes to the assessment of taxation years not before me, I can of course consider whether something occurring in the prior year may have an effect that would have an incidence on the amount of tax that should be assessed in the two years before me.

[10] First, there was an issue relating to an RRSP amount of $18,000 from his wife's estate which he wished to roll over. This issue related to the 2003 taxation year.

[11] I was unable to understand how it would affect either 2004 or 2005; in any event, from the evidence before me, it appears that the amount was rolled over and that rollover was not challenged by the Canada Revenue Agency.[3]

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[1] Agreement between Canada and the Federal Republic of Germany for the avoidance of double taxation with respect to taxes on income and certain other taxes, the prevention of fiscal evasion and the assistance in tax matters, enacted by the *Income Tax Conventions Implementation Act*, 2001 (S.C. 2001, c. 30), Part 8.

[2] The Court appreciates that the respondent examined the documentation in support of this, which was not submitted at trial, but was provided by the appellant after the hearing. After examining the documentation, the respondent wrote on April 28, 2010 to advise that it would concede the amount. The appellant also received a pension from Austria. I did not understand the appellant to be taking the position that the pension from Austria was exempt under the Canada-Austria income tax convention. If one looks at the second page of Exhibit R-2, one finds a memo from the appellant's representative asking that the deduction be allowed for the German pension; one also finds in the last sentence of the first paragraph of that page a statement that the Austrian payments are taxable. In any event, nothing in the evidence before me demonstrates that the Austrian payments are of a nature such that they come within paragraph 2 of Article 18 of the Convention between Canada and the Republic of Austria for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income and on capital.

[3] See page 1 of the January 4, 2005 letter which is at the beginning of Exhibit A-3.

[12] Similarly there were issues relating to capital gains deductions prior to 2004, an allowable business investment loss calculation relating to 2003, the amount of unused net capital loss available in 2007 and a duplicate T5 issued to the appellant's wife relating to 2001 that was added to her income.[4]

[13] Among other things relating to these events, there was the bankruptcy of what I understand to have previously been the appellant's company.

[14] Much of what happened was very unfortunate and I commend the appellant's efforts to help his son.

[15] However, I was not, based on the evidence before me, able to discern what errors in assessing might have occurred relating to these matters, nor was I able to discern that they would have any effect on the two taxation years before me.

Rental Income and Losses

[16] The main issue in the appeal relates to rental income reported and rental losses claimed by the appellant. The property in question is located in the City of Westmount, Québec.

[17] In 2004, the appellant claimed a rental loss of $40,567.94; the Minister assessed on the basis that the 2004 rental loss was only $8,924.

[18] In 2005, the appellant reported rental income of $1,396.98; the Minister assessed on the basis that the rental income was $7,223.

[19] Excluding the basement, the property in question has three floors. The appellant lives on the second floor which measures 1,708 sq. ft.[5]

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[4] See Exhibits A-6, A-7, A-8, A-9 and A-10. There was also an issue of a GST determination that was not before me (see Exhibit A-5).

[5] The appellant's square footage figures are slightly different from those used by the Minister. The difference between the two appears to be the result of counting or not counting space such as hallways. I have used the Minister's figures rather than those of the appellant in Exhibit A-12 because the appellant shows a smaller square footage on the first floor than on the second floor; this is inconsistent with the diagram in Exhibit A-12 and the photo in Exhibit A-11.

[20] The third floor is rented to the appellant's daughter and measures 1,316 sq. ft.

[21] The first floor has three units and totals 1,708 sq. ft.

[22] In the two years under appeal, two of the first floor units were rented and one was vacant.

[23] The appellant attributed one third of the expenses related to the building to his personal apartment. For the purposes of computing his rental income or loss, he deducted two thirds of the expenses related to the building.

[24] In reassessing, the Minister:

(a) disallowed a small amount of expenses on the basis that they were not incurred at all; this amount was small: a net refusal of $1,864 out of $88,215 in the 2004 taxation year, and of $5,909 out of $26,102 in the 2005 taxation year;[6]
(b) accepted the rental of the two occupied units on the first floor as being of a commercial nature with the consequence that the appellant could claim all the expenses related to those units; and
(c) treated the third floor occupied by the daughter and the vacant unit on the first floor as not being of a commercial nature with the consequence that the Minister excluded from the property revenues the rent paid by the daughter and denied the deduction of the portion of the expenses related to the daughter's unit and the vacant unit.

[25] The Minister was of the view that, because no reasonable efforts were made to rent the vacant unit on the first floor, the empty first floor unit was no longer a source of income.

[26] With respect to the unit occupied by the daughter, the daughter moved into the unit in approximately 1998.[7]

[27] The Minister proceeded on the assumption that the daughter paid $570 a month for a five-room apartment while on the first floor arm's length tenants were paying $530 and $500 a month, respectively, for one-and-a-half-room apartments.

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[6] Exhibit R-1, Tab 2, letter of March 17, 2008 from the Canada Revenue Agency to the appellant, last columns of the attached schedules.
[7] At the hearing of this matter in 2010, the appellant stated that the daughter had moved in approximately 12 years earlier (transcript, page 51).

[28] Because of that, the respondent argued that the daughter was not paying a fair market value rent and that the unit was not a source of income.

[29] The appellant brought nothing forward in his evidence which would lead me to conclude that the daughter was paying a fair market rent. Indeed, considering the size relative to the other units and the absolute size, the rent is clearly well below market value.

[30] The appellant also testified that the daughter suffered from serious health problems.

[31] As to the vacant unit, the appellant described how he and his wife had had difficulties with a tenant who left in, approximately, 2001. After the difficulties he and his wife decided to take a break from renting the unit.

[32] The appellant’s wife died in 2002. After his wife died, because of the troubles that they had had, the appellant was still scared to rent the unit to just anyone and was only prepared to rent the unit by word of mouth. While the appellant did not explain what he meant by that, I take it to mean that he only wanted a tenant recommended to him by someone he knew.

[33] There was no evidence and no assumption by the Minister that the vacant unit had been reallocated to the use of the appellant or of his daughter.

[34] Apart from the $263.40 cost of the stove, at the hearing the appellant did not really contest the amounts disallowed as not incurred. As for the cost of the stove, it was disallowed on the basis that the appellant did not have leases showing that he provided appliances.

[35] Given that the appellant’s testimony, as I understood it, is that there were no leases, and given his testimony that over the years one tenant had damaged the unit’s stove, I am satisfied that he did indeed provide stoves and that the $263.40 expense should be allowed.

Analysis

[36] I shall start with the unit occupied by the daughter. Given the large difference in size between the daughter's unit and the two units rented on the first floor, I am satisfied that the unit was rented to the daughter for less than a fair market rent.

[37] I am satisfied that, applying the tests set out by the Supreme Court of Canada in *Stewart v. Canada*,[8] there is, applying the first test in *Stewart*, a personal element involved in leasing the third floor apartment. This personal element is the fact that the appellant, out of a very understandable wish to assist his daughter, gave the daughter a much lower rent than if he were renting out the unit to an unrelated person.

[38] Further, applying the second test in *Stewart*, there is nothing in the evidence to suggest that this is being operated in a sufficiently commercial manner to constitute a source of income.[9]

[39] Although the daughter has her own dwelling unit, the situation is more akin to the daughter contributing to household expenses than that of a commercial lease.[10]

[40] Accordingly, the Minister was correct in excluding from the property income the rent payments by the daughter and in excluding from the property expenses the pro rata share of the expenses related to the daughter's unit.

[41] I now turn to the vacant unit.

[42] It is worth repeating the particular facts relating to this unit: the appellant, while making little effort to rent the unit (no advertising), was prepared, if he could find a suitable tenant through word of mouth, to rent the unit; the unit was not converted to personal use and, rather importantly, the unit is part of the building the appellant owns and could not be sold separately from it.[11]

[43] Given these particular circumstances, in the two years in issue, I do not see how one could consider the unit to not form part of the first floor rental property. As

[8] 2002 SCC 46, paragraphs 48 to 60.

[9] Nothing in the appellant's evidence suggested that there was a plan or an intent to raise the rent to something close to a market rent that would not only cover current costs and depreciation, but would also produce some reasonable return on capital.

[10] In substance, this situation has similarities to that in *Rapuano v. The Queen*, 2009 TCC 150.

[11] It is also not irrelevant to consider that the appellant's age and the death of his wife in 2002 would slow down efforts to reconsider and reorient the use of the vacant unit and the rest of the rental property.

such, for the 2004 and 2005 taxation years, I am satisfied that the unit is still part of the first floor rental property and is still part of a source of income.[12]

[44] As a result, the appellant is entitled to deduct the expenses related to the vacant unit on the first floor.

[45] The result of these conclusions is that the total expenses incurred in 2004 should be revised upwards to $86,614.40.[13]

[46] The first floor represents 36.09% of the square footage of the three floors.[14] Accordingly, in the 2004 taxation year, 36.09% of the expenses incurred for the building, an amount of $31,259.14,[15] are deductible from the $11,696 revenue relating to the first floor. This produces a net loss of $19,563.14 in respect of the first floor.

[47] The Minister was correct in excluding the revenue from the daughter's unit and in denying the deduction of the unit's pro rata share of the expenses. This is true for both taxation years.

[48] In 2005, the net income must be recomputed on the basis that the revenues for the first floor are $12,045 and the expenses related to the first floor are $7,287.65.[16] This results in a net rental income of $4,757.35.

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[12] When a business ceases operation, the assets do not immediately become personal use assets making costs incurred in relation to them non-deductible. Consider, for example, *Génier v. The Queen*, 2010 TCC 641. Obviously, at some point, what were income earning assets may become personal assets; that has not happened in these circumstances and it is not necessary to consider, for the purposes of these taxation years, what circumstances might trigger a change in use.

[13] This is $88,215 (the amount claimed) minus $1,864 (the amount disallowed by the Minister as not being incurred) plus $263.40 (for the stove that I have concluded should be allowed).

[14] The first, second and third floors are 1,708 sq. ft., 1,708 sq. ft. and 1,316 sq. ft. respectively for a total of 4,732 sq. ft. Mathematically this means that the first floor represents 36.09% of the square footage.

[15] 36.09% of $86,614.40 equals $31,259.14.

[16] The Minister accepted that a total of $20,193 in expenses for the building had been incurred. This amount is the $26,102 claimed minus the $5,909 which the Minister did not accept as incurred. Of the $20,193 in expenses, 36.09%, or $7,287.65, relate to the first floor.

Conclusion

[49] For these reasons, the appeal is allowed, without costs, and the matter is referred back to the Minister for reconsideration and reassessment on the basis that:

- (a) in the 2004 taxation year,
  - (i) the appellant's income should be reduced by the $2,555.30 amount of the German pension,
  - (ii) the rental loss of $8,924 should be increased to $19,563.14;
- (b) in the 2005 taxation year, the appellant's net rental income should be decreased from $7,223 to $4,757.35.

Signed at Ottawa, Ontario, this 6th day of October 2011.

"Gaston Jorré"

Jorré J.

CITATION:	2011 TCC 472
COURT FILE NO.:	2009-2919(IT)I
STYLE OF CAUSE:	GEORGE LEISSER v. HER MAJESTY THE QUEEN
PLACE OF HEARING:	Montréal, Québec
DATE OF HEARING:	March 30, 2010
REASONS FOR JUDGMENT BY:	The Honourable Justice Gaston Jorré
DATE OF JUDGMENT:	October 6, 2011

APPEARANCES:

For the appellant:	The appellant himself
Counsel for the respondent:	Marjolaine Breton

COUNSEL OF RECORD:

For the appellant:

Name:

Firm:

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