Docket: 2017-230(IT)G

BETWEEN:

1717398 ONTARIO INC. O/A LOST FOREST PARK,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on June 14, 2019, at Toronto, Ontario

Before: The Honourable Justice Guy R. Smith

Appearances:

Counsel for the Appellant:	Christine Ashton
Counsel for the Respondent:	Devon E. Peavoy

JUDGMENT

In accordance with the attached reasons for judgment, the appeal from a reassessment made under the *Income Tax Act* in respect of the Appellant's 2012, 2013 and 2014 taxation years is hereby dismissed with costs to the Respondent in accordance with Tariff B.

Signed at Ottawa, Canada, this 29 day of August 2019.

"Guy R. Smith"

Smith J.

Citation: 2019 TCC 183
Date: August 29, 2019
Docket: 2017-230(IT)G

BETWEEN:

1717398 ONTARIO INC. O/A LOST FOREST PARK,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Smith J.

I. **Introduction**

[1] The Appellant appeals from a Notice of Reassessment made by the Minister of National Revenue (the "Minister") on November 18, 2015 disallowing the Appellant's claim for the small business deduction (the "SBD") for the 2012, 2013 and 2014 taxation years.

[2] The SBD described in section 125 of the *Income Tax Act* (the "Act") provides for a reduced corporate tax rate on a private corporation's active business income but excludes income from, *inter alia*, a "specified investment business" ("SIB") defined as "a business…the principal purpose of which is to derive income from property…" unless it employs, directly or indirectly, more than five full-time employees.

[3] In this instance, the Minister denied the SBD on the basis that the Appellant earned its income primarily from the rental of seasonal and extended seasonal campsites and the storage of recreational vehicles ("RV's") and that it did not employ at least five full-time employees.

[4] The Appellant concedes that it did not employ more than five full-time employees but argues that it carried on an active business providing a significant

bundle of services that "were integral to the success of its business operations" and that its principal business was not simply to earn income from property.

II. **Issue**

[5] The sole issue in this appeal is whether the Appellant falls within the definition of a SIB. If so, the Appellant is not entitled to the SBD.

III. **Evidence**

[6] Mr. Alan Nacinovic was the Appellant's only salaried employee as well as the only witness. His parents were the principal shareholders of the corporate Appellant. He testified that the Appellant earned income from three general activities: the rental of campsites, RV storage and mobile RV sales.

A. The Mobile Home / RV Park

[7] The RV campground was purchased in 2007 and Mr. Nacinovic described it as "run-down." He researched competing campsites in the geographic area and, as a result, entered a period of expansion, renovation and capital improvements that included the following:

i. Installation of new water systems;
ii. The addition of 50 new extended season campsites with new water and sewage systems, new hydro connections and newly paved roads;
iii. Addition of picnic tables and fire pits at each campsite;
iv. Replacement of outdated playground with a modern structure;
v. Installation of new security gates and cameras;
vi. Institution of weekly private garbage collection from the sites;
vii. Improved swimming pool, pool house, and pool area – including indoor showers and washrooms;
viii. Renovation of the picnic pavilion/recreational hall;
ix. Installation of a coin-operated laundry room; and

x. Installation of outdoor athletic courts (beach volleyball, basketball, bocce ball, and horseshoe pits).

[8] The Appellant then began to actively market the improved "Lost Forest Park" through its own website and other forms of media.

[9] The campground had two types of fully serviced sites: seasonal and extended seasonal both used almost exclusively by mobile home / RV's (i.e. on wheels). Exceptionally, if a seasonal site was unoccupied, daily campers were allowed to pitch a tent and use the facilities in exchange for an "overnight" fee.

[10] The seasonal sites were open for occupation from April to October. If a camper paid a storage fee (not included in the seasonal site fee) the trailer could remain on site during the off-season. Seasonal campers could, at their own expense, erect decks, build small structures and landscape their site, provided that a plan was submitted and approved by the Appellant. While improvements or customizations varied, Mr. Nacinovic testified that plans had to be pre-approved to maintain aesthetic standards.

[11] The extended seasonal sites were open annually with the exception of a two month period at the beginning of each calendar year due to a municipal by-law. The fees paid by the extended seasonal campers included storage of the RVs as they remained on the lot for the entire year, assuming the camper had renewed its agreement for the following year. Subject to approval, extended seasonal campers were allowed to add decks, related structures and landscaping to their site.

[12] Over time, the Appellant significantly increased the number of extended seasonal sites such that during the relevant years, the park contained approximately 58 extended seasonal sites and 91 seasonal sites.

B. RV Storage Services

[13] As previously mentioned, the Appellant provided RV storage services to both seasonal and extended seasonal campers but the seasonal campers had to pay a storage fee in addition to the seasonal site fee. For extended seasonal campers, the storage services were rolled into the fees for year.

[14] Campers were responsible for winterizing their structures and trailers that remained on the Appellant's lots during the respective off-season.

C. Mobile Home / RV sales

[15] Originally, the Appellant earned referral fees from the sale of an RV mobile home. These referral fees were paid by dealers or manufacturers. Mr. Nacinovic explained that having a site to use and store an RV was an important part of the purchase decision such that dealers would form relationships with RV campgrounds to facilitate sales. In other words, dealers needed appropriate sites such as Lost Forest Park to sell mobile RV homes.

[16] In 2011, the Appellant purchased a model home RV and began to operate as a registered dealer. Net sales increased significantly over time but actual sales were only made to purchasers who agreed to enter into an agreement as a seasonal or extended seasonal occupant of Lost Forest Park.

IV. **Analysis**

[17] Subsection 125(7) of the Act contains a definition of a SIB as follows:

> ***specified investment business***, carried on by a corporation in a taxation year, means a business (other than a business carried on by a credit union or a business of leasing property other than real or immovable property) the principal purpose of which is to derive income (including interest, dividends, rents and royalties) from property but, except where the corporation was a prescribed labour-sponsored venture capital corporation at any time in the year, does not include a business carried on by the corporation in the year where
>
> **(a)** the corporation employs in the business throughout the year more than 5 full-time employees, or
>
> **(b)** any other corporation associated with the corporation provides, in the course of carrying on an active business, managerial, administrative, financial, maintenance or other similar services to the corporation in the year and the corporation could reasonably be expected to require more than 5 full-time employees if those services had not been provided.

[18] Subsection 125(7) also contains a definition of an "active business carried on by a corporation" and indicates that it "means any business carried on by the corporation other than a specified investment business (…)". This is analogous to the definition of "active business" in subsection 248(1) of the Act.

[19] While the use of the word "active" might suggest a minimum level of activity, the Federal Court of Appeal has indicated that a business need not actually

be "active": *Ollenberger v. Canada*, 2013 FCA 74, (para. 28). As a result, Parliament sought to exclude certain businesses. The Court explained that:

> [29] This is what brought the legislator to change course in 1984. At that time the definition of "active business" was first introduced (1984, c. 45, ss. 92(1) and 40(1)), and has since remained unaltered. The definition effectively recognizes that any business being carried on is an active business, but rather carves out of this definition particular businesses such as those which derive their income from property and do so without the need to employ a certain number of employees (see the definition of "specified investment business" in subsection 125(7)).
>
> (My emphasis)

[20] The notion that subsection 125(7) "carves out" businesses that "derive their income from property" (unless they have a minimum number of employees) was reviewed in *Weaver v. Canada*, 208 FCA 238 ("Weaver") where the taxpayer had developed land for use "as a retirement community consisting of manufactured homes on leased lots" (para. 2). The Court explained that:

> [25] The definition of "specified investment business" does not ask about the general nature of the business of a corporation, or the degree of activity or passivity actually required by that business. Rather, it asks about the legal character of the income that the business is intended principally to earn. If on the relevant date the legal character of that income is rent, for example, then the business meets the definition unless once of the statutory exceptions applies (none of those exceptions is relevant in this case).
>
> (My emphasis)

[21] The Court must therefore consider the "legal character of the income" rather than the degree or level of activity. As noted in Weaver (para. 26), "[T]he key question is whether the principal purpose of that business…was to derive income from property (such as rent)".

[22] The earlier decision of the Tax Court of Canada in *Lee v. Canada*, [1999] 3 CTC 2200 ("Lee") reached a similar conclusion where the taxpayer operated a mobile home park. The Court rejected arguments that focused on the level of activity including "the high level of service and superior maintenance standards", finding that the exclusive purpose of the business was to "derive income from property in the form of rent (…)" and therefore was a SIB. (para. 10).

[23] In *0742443 B.C. Ltd.* v Canada, 2014 TCC 301 (confirmed by the Federal Court of Appeal at 2015 FCA 231), relied upon by the Appellant, the taxpayer

operated a storage facility and provided additional services. The Court considered the appellant's advertising and invoicing documents to determine the legal character of the income. Once it concluded that income earned from storage had the legal character of rental income, it then examined whether the additional services changed the nature of that income into something other than rent.

[24] Justice Miller concluded that all customers were basically "buying storage space" and that:

> [29] There is a tipping point where the provision of services overcomes the provision of property. The CRA have administratively determined that hotel/motel accommodation steps over that tipping point. I conclude that R-Xtra Co. does not: a few services to a few customers does not change the inherent nature of income from property.
>
> (My emphasis)

[25] In this instance, the Appellant's advertisements, financial statements, and site fee agreements for the seasonal campers were entered into evidence. I have considered each below in addition to the testimony provided by Mr. Nacinovic on the Appellant's three general activities.

A. The Advertisements

[26] The Appellant advertised in various types of media but the most detailed advertisement discussed was a full-page flyer with a half page devoted to each type of campsite. The flyer referred to the extended seasonal sites as a "quiet, gated and private resort community ideal for adults seeking affordable living, set to retire or escape to the country" and to the seasonal sites as "fully serviced" in a "clean and well maintained park" with many amenities (pool, athletic courts, playground, laundry facilities, etc.). The flyer indicated that the park is a short drive from grocery stores, shopping malls, restaurants and highways.

[27] The focus of the ad for the "extended season snowbird sites" was not the provision of a bundle of services but that the Appellant's park was conducive to a snowbird lifestyle with luxurious "living space" in "park model homes." The ad stated that there is "access to all park amenities."

[28] The ad for "seasonal family camping" also focused on the amenities and services offered by the Appellant by listing them and referring to the sites as "fully serviced."

B. Financial Statements and Site Fee Agreements

[29] According to its income statements for the relevant years, the Appellant earned the majority of its revenues from "seasonal site fee[s]", "rent income", "storage income", and "hydro income" – all of which relate to fees charged to the seasonal and extended seasonal campers.

[30] Mr. Nacinovic testified that the line item "rent income" referred to the fees charged for extended seasonal sites while "seasonal site fees" referred to the seasonal campers. The "storage fees" applied only to seasonal campers and "hydro fees" were charged to both types of campsites based on usage. A hydro deposit was charged in the seasonal site agreement and campers would be refunded or receive additional charges depending on their usage.

[31] While no agreement for the extended seasonal campers was produced in evidence, Mr. Nacinovic testified that these campers paid a monthly fee by agreement for 12 months of the year. It included a line item for a "Seasonal Site Fee" which matches the term used in the Income Statements.

[32] Although the Appellant's promotional material referred to "seasonal family camping" or "seasonal campground", it was apparent from the testimonial evidence that the Appellant operated a park dedicated to mobile homes and other types of "RV's", most of which, were installed on a semi-permanent basis, despite being on wheels. It is difficult to distinguish this case from the findings in the decisions of Weaver and Lee, cited above.

[33] On that basis, I have no difficulty finding that the legal character of the income earned from the extended seasonal sites was rental income. Regarding the seasonal sites, it was possible for the RV to remain on site for the entire year, subject to the payment of a "storage fee" and these agreements could be renewed for consecutive years. The ability to customize the site to personal preferences with structures and landscaping in addition to the ability to remain on site for consecutive years leads me to believe that the legal character of the income earned from both the seasonal sites and extended seasonal sites was rental income. The campers were effectively paying to occupy a particular site for either 5 or 10 months of the year and the mobile home RV was stored (i.e. unoccupied) on site for the remainder of the year in many cases.

[34] To address an argument raised by the Appellant, I will now consider whether providing certain services changed the nature of the income principally earned by the Appellant from rental income to something else.

[35] This requires an analysis of the principal purpose of a business.

[36] To determine the principal purpose of a business, the Appellant referred to the statement made by Justice Bowman (as he then was), as quoted in *Barrette v. Canada*, 2004 TCC 437 (para 28) where he indicated that:

> In determining the "principal purpose" of a business carried on by a corporation the stated object of the person who carries it on is not necessarily the only, or even the most important, criterion. Of critical importance is what the corporation in fact does and what its sources of income are.

[37] A principal purpose determination was also made by the Tax Court of Canada in the decision of Lee, noted above. In determining that "the exclusive purpose thereof was to derive income from property in the form of rent", the Court indicated that:

> There can be no doubt… that the tenants were attracted and retained by the high level of service and superior maintenance standards which were offered by the Cassidy Park. Nevertheless, so far as Cassidy's income earning activity is concerned, the clear purpose was to derive rental income from the tenants who occupied the pads under leases of the sort entered in evidence. What was paid by the tenants and received by Cassidy was described in the leases, and fairly so, as "rent". Cassidy had no other significant source of revenue.
>
> (My emphasis)

[38] On the basis of the testimonial and documentary evidence, I similarly find that the Appellant's campers were attracted by high-quality services, superior maintenance standards as well as the common amenities offered by Lost Forest Park, all of which were part of the "camping experience" referred to by Mr. Nacinovic. These features were used to entice mobile home owners and RV campers to occupy the various seasonal and extended seasonal campsites so that the business could accomplish its principal purpose – to earn rental income.

[39] The Court accepts that the Appellant made substantial capital improvements and installed various amenities, as described above. It also arranged or organized for certain events such as fireworks or magic shows (which would only occur if there was sufficient interest), but the campers were responsible for everything else.

[40] The evidence establishes that some campers took care and maintenance of their site to an extreme (based on the photographs provided) with landscaping, manicured lawns, decks, sheds, etc.. When winter arrived, they were responsible for winterizing their mobile homes or RV's. The campers did their own laundry, cleaned their personal RVs, and maintained the customized items added to their sites. Mr. Nacinovic testified that he was consulted regarding the customizations, but this was because the park wished to maintain certain "aesthetic" standards.

V. **Conclusion**

[41] In the end, I find that the services and amenities offered by the Appellant were not sufficient to reach the "tipping point where the provision of services overcomes the provision of property" (See 0742443 B.C. Ltd, *supra*).

[42] I am not satisfied that the services provided by the Appellant, including limited event planning, garbage pick-up, office hours and "on-call" availability, changed the legal character of the income to something other than that of rental income contemplated by the definition of a SIB in subsection 125(7).

[43] The duration of the occupancy agreements in particular (seasonal and extended seasonal vs. daily or weekly) suggest quite clearly that the principal purpose of the business was to derive rental income. As noted above, it is difficult to distinguish these facts from the decisions of Weaver and Lee.

[44] Having concluded that the Appellant's principal purpose was to earn income from property in the form of rental income, its business activities fall under the definition of a SIB and it is not entitled to the SBD.

[45] The appeal is therefore dismissed with costs to the Respondent.

Signed at Ottawa, Canada, this 29 day of August 2019.

"Guy R. Smith"

Smith J.

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APPEARANCES:

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