Docket: 2015-533(IT)I

BETWEEN:

FARZAD PAKZAD,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on November 30, 2015, at Toronto, Ontario.

Before: The Honourable Rommel G. Masse, Deputy Judge

Appearances:

Counsel for the Appellant:	**Bryan A. Rowe**
Counsel for the Respondent:	Annie Paré

AMENDED JUDGMENT

Upon counsel for the Appellant informing the Court in writing that a typographical error was found in the spelling of his name in the appearances portion of the judgment;

The typographical error is hereby corrected and counsel name's is properly spelled.

The appeal from the reassessments made pursuant to the *Income Tax Act* for the 2010 and 2011 taxation years is dismissed, in accordance with the attached Reasons for Judgment.

This amended judgment is issued in substitution to the reasons for judgment issued on June 10, 2016.

Signed at Toronto, Ontario, this 24th day of June 2016.

"Rommel G. Masse"

Masse D.J.

Citation: 2016 TCC 144
Date: 20160610
Docket: 2015-533(IT)I

BETWEEN:

FARZAD PAKZAD,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Masse D.J.

[1] The issue to be decided in this matter is whether the Appellant had a source of business income during the 2010 and 2011 taxation years. If he did, then a secondary issue is whether he was entitled to deduct expenses that he claimed to be business losses in the amount of $79,856 for the 2010 taxation year and in the amount of $29,603 for the 2011 taxation year.

[2] In view of the decision I have reached on the first issue, it is not necessary to decide the secondary issue.

Factual Context

[3] The Appellant is an educated man having obtained a Science and Technology degree from the University of Calgary. He took courses in life sciences such as Chemistry, Biology, Biochemistry and Kinesiology. He began working with Bell Canada in 2003, part-time for the first three years, but then he began working at Bell on a full-time basis. During the 2010 and 2011 taxation years he was working with Bell full-time in the IT department.

[4] In 2010, he lived in a rental condominium unit at 2121 Lakeshore West, Etobicoke. In 2011, he lived in a home at 39 Daphnia, Thornhill. He testified that he maintained home offices at these residences and a home gym in his residence in Thornhill.

[5] The Appellant testified that during the 2010 and 2011 taxation years, in addition to his full-time employment, he was operating two separate businesses. The one business was that of a real estate consultant called "Real Estate Business Developments" ("REBD"). The other business was that of a personal health and fitness trainer under the name of "Personal Training and Coaching" ("PTC"). Both of these alleged businesses never generated any profits and so they failed. REBD ceased operations at the end of 2010 and PTC stopped operations at the end of 2012 or beginning of 2013.

[6] The Appellant started REBD in early 2008. He testified that this business involved advising clients who wished to sell real property on how to best renovate and prepare their properties for sale, how to market their property and how to get the best price for their property, all without the services of a real estate agent and without contracting expensive general contractors for renovations. The Appellant would search for properties and clients who might be interested in investments and developments in various geographic areas. Services included locating real estate properties in Canada, USA and Asia.

[7] He claims he was using his knowledge, skill set and experience to help clients make the best use of their properties, or the proceeds of sale of their properties. He believed that he could help people buy and sell property for just a fraction of the cost of what the client would pay to use the traditional services of contractors and real estate agents. The Appellant also offered to assist clients to relocate to a new community, province or country, to purchase a house in a new location and to get the best deal possible for the money they had available. He also marketed himself as a property manager for those clients who wished to rent out their properties. He really viewed himself as a real estate guru who could guide his clients through the entire renovating, selling, buying, financing, relocating and investing process.

[8] His fee for his services was half a percent of the full value of the transaction – much less than a real estate broker's commission. If the client did not want his full range of services but only wanted his advice on specific aspects of the process, then his fee was $50 per hour for consultations. The Appellant claims that he had a lot of knowledge and experience in this area, although it is not obvious to me, based on the evidence, where he obtained his knowledge and experience. He claims that he studied real estate a lot over the years and he thought that he could do what everybody else in the industry was doing. He expressed the desire to eventually become a real estate agent. However, he was of the view that one had to spend a lot of money to get into the game and to look successful as a real estate

agent. He was not prepared to spend the kind of money that was necessary to obtain the trappings of a successful real estate agent, such as a new car every couple of years, expensive clothing and costly advertising. He wanted to offer a comprehensive service at a modest cost to his clients. The hope was that if he could engage a client in an initial consultation, then the client could be persuaded to retain his services for the entire process.

[9] He admits that he has no formal training in real estate and he is not licensed as a real estate agent here or anywhere else. He has no certification or training in construction or renovations, in property management, in financing or real estate investment. He has no credentials in any of those disciplines here in Canada, the USA or in Asia. However, he claims that he has the knowledge and skills that allow him to guide a client through the entire process. He states that he was offering a much broader service than a real estate agent would offer. He contends that a license or certification is not required for the type of services he was providing. He was not buying and selling properties on behalf of his clients but was providing them with advice and guidance. This included providing leads, contact information, financing advice and guidance with respect to renovations, buying and selling, relocating, property management and investment. Because he was not affiliated with a real estate brokerage firm, which would have required him to pay fees, he was also able to offer his services cheaper than he could have as a registered realtor.

[10] The Appellant testified that he recruited clients for REBD by means of direct marketing. He would go door-to-door and hand out flyers and business cards. He did not advertise. Mass media advertising was not effective or cost efficient for him, so he says. He did not want to spend the money required to buy advertising. He testified that he would do his direct marketing from 5:00 to 9:00 pm after his regular work hours on weekdays and also on weekends or during his vacation time or statutory holidays. He says that he would knock on hundreds of doors. Whenever he met a potential client who showed any interest in what he had to offer, he would take the potential client out for a coffee or a meal in order to make his sales pitch. He did his direct marketing mostly in the Greater Toronto Area. He says that he also did some door knocking in Eastern and Western Ontario and in so doing he claims that he familiarized himself with the local real estate markets in those areas.

[11] The Appellant did take trips out of province and out of country where he thought there might be a market for his clients who might be thinking of relocating. Of particular note are trips that he took to Florida and Hawaii to assess the real

estate market in those areas and to look for properties for himself and his clients. However, what is astounding is that he incurred a great deal of expenses on these trips when he never had any clients whatsoever who were interested in relocating there. It does not elude me that Hawaii and Florida are prime vacation spots.

[12] His second business, PTC, was that of personal training and coaching. He started this business at the beginning of 2010. Just as in his real estate business, he claims that he had a lot of knowledge and experience in physical fitness, personal training and nutrition although he did not elaborate where this knowledge and experience came from other than a course in anatomy at university. This business involved recruiting customers and offering them a variety of indoor and outdoor exercises. His niche market was gym dropouts -- those individuals who would join a gym, workout for a few weeks or months and then quit. He also targeted those individuals who would not usually consider joining a gym or who did not have time to join a gym.

[13] When he lived in his apartment condominium, he used the gym that was available to all the residents of the building in order to carry out his physical fitness training. His condo would allow guests but he never had any agreement with the condominium corporation allowing him to use the gym for commercial purposes. He never did get liability insurance since he figured that he was covered by the condominium's insurance for any of his clients. It is clear that he did not verify if his business enterprise was in fact covered by the condominium corporation's general policy of insurance. It would have been prudent for him to do so from a business point of view, but he did not. In 2011, he had a gym set up in his home using new and used equipment. He did not verify if his homeowner's insurance policy covered any risks to his clients. Again, it would have been prudent from a business point of view to do so but he did not. It was his long-term plan to find an investment partner who shared his vision and who had the financial resources to invest in a fully equipped gymnasium. He really does not explain how he was to find this investor other than by knocking door-to-door and by word of mouth. He had no success in finding a financial backer.

[14] He was willing to engage and to facilitate clients who wanted to get involved in out of the ordinary physical experiences like mountain biking, snowboarding, fishing and hunting. He has a snowboarding instructor certificate (Exhibit A-1, Tab 29). He testified that this provided him with liability insurance as a snowboard instructor; however, this claim was not substantiated. He testified that he offered a complete package. He was willing to transport clients up to Blue Mountain for snowboarding lessons in his own personal vehicle. He was willing to take clients

hunting or fishing to Arizona or B.C. or anywhere else for that matter. However, there is no evidence that he had any clients willing to do that.

[15] He testified that he also offered nutrition and dieting advice to his clients. He offered to his clients a fitness and dietary regime that he claimed was attainable, sustainable and realistic and that would keep them healthy over a long time.

[16] The Appellant did not have any accreditation or certification in physical training, nutrition, weight training, hunting or fishing. He did not have any training in firearms safety nor did he have any firearms acquisition certificate. This obviously limits the scope of his hunting expeditions. He makes the dubious claim that he had more to offer his clients than the ordinary personal fitness trainer by virtue of his university education and his experience. He claims that his qualifications far exceed those obtained in any certification programme offered in these disciplines. However, he really does not detail his experience in any of these disciplines other than snowboarding.

[17] The Appellant admits that he did not have any kind of a written questionnaire or other instrument to establish the baseline physical condition of his clients prior to engaging in a physical fitness regime. He did not have his clients sign any contract or otherwise commit to a term for a fitness programme. PTC did not have any return business.

[18] The Appellant testified that he used door-to-door direct marketing in order to recruit clients for PTC just as he did for REBD. Like REBD, direct marketing did not prove to be a viable marketing strategy since it did not bring in many clients.

[19] The Appellant did not negotiate any small business bank loans in order to capitalize his businesses. He testified that he decided to self-finance by using money that he obtained from making withdrawals from his RRSP plan. This would result in the imposition of income taxes on the amount of his RRSP withdrawals. Since he did not maintain any books of account or any bank accounts for his businesses, there is no evidence other than his assertions that the withdrawals from his RRSP plan were in fact used for business purposes rather than personal purposes or living expenses. We do not know where the money was spent. He did not register his businesses pursuant to any provincial legislation. He did not obtain any business numbers for purposes of HST. There is no evidence that he obtained any municipal business licenses or permits. There is no evidence that he maintained any ledgers or books of account or that he produced any financial statements. He did not have a business plan for either of these businesses and in

fact he seemed not to understand what a business plan was. He simply stated that his long-range goal was to grow his business – that is a wish, not a plan. He did not establish any kind of budget and he did not prepare any income or expense projections or forecasts. He did not do any income and expenses analysis.

[20] The Appellant did introduce into evidence two binders containing copies of a large number of cash register receipts, vouchers, credit card slips and other documents that purport to establish his business expenses. Exhibit A-1 is in relation to business expenses for 2010 and Exhibit A-2 is in relation to 2011. Many of these documents indicate the purchase of coffee and meals for just one person from fast food restaurants that were consumed by the Appellant himself while on the road doing his direct marketing, so he says. Exhibits A-1 and A-2 also contain documents that relate to expenses incurred for fuel, repairs, and insurance for the Appellant's personal vehicle. He says that he travelled extensively using his vehicle while doing his door-to-door direct marketing. However, the Appellant did not keep a vehicle log of distances travelled, destinations or places or people visited. He did not seem to know what a vehicle logbook was or the purpose of it. These binders also contained hotel bills for travel to places such as Florida and Hawaii.

[21] Even though the Appellant did not want to spend any money on advertising, he spent much money on promotional schemes. As already indicated, he would take clients out for a coffee or buy them lunch or dinner. He would buy them alcohol. He would buy groceries so that he could entertain prospective clients in his home. Yet, we do not know how many of these clients he entertained in restaurants or in his home or who they were – he did not keep a record of that. He would give his clients expensive gifts such as clothing or gift certificates in an effort to build up business. This was very costly -- indeed, it was extravagant in all the circumstances. In 2010, he gave gifts amounting to $2,827.42 to his REBD clients and $2,628 to his PTC clients. The value of these gifts alone exceeded his gross revenue from both businesses. His gifts in 2010 averaged more than $200 per client. In 2011, he gave gifts to his PTC clients amounting to $1,836.24, more than half the amount of his revenue and more than $100 for each client that he had during that year. He has no record of what client received what gift item from what store. It is interesting to note that many of these gifts were from men's clothing stores. One cannot help but wonder if the Appellant was in fact buying clothing for himself.

[22] The Appellant ostensibly was very concerned about keeping costs down and yet he threw caution to the wind and he exercised no control at all over his

expenses. He admits that he let his expenses get away from him -- that is a gross understatement. Even though he meticulously collected every cash register slip for every little expense, it is clear that he exercised absolutely no control over how much he spent.

[23] As already indicated, the Appellant was very scrupulous in gathering together every cash register slip, every debit and credit card slip and any and all documents relating to every purchase or expense that he claimed was related to his business activities, no matter how minor. This is to be contrasted with the almost total absence of any documentation in relation to his client base and his revenue. In fact, there are no source documents at all in relation to his gross revenue. The Appellant did not keep any contact information for any of his clients. He does not know any of their addresses. This makes it impossible to contact any clients in order to verify revenue. The Appellant conducted his activities on a strictly cash basis. He did not accept payment by cheque, credit card or debit card. He never issued any invoices to his clients and there is no evidence that he issued any receipts to his clients for cash paid to him. There is no evidence that he deposited any of his gross receipts into any bank account. This makes it impossible to track funds.

[24] The Appellant's supposed business activities produced very little income during the taxation years. In computing income for his 2010 taxation year, the Appellant reported income from employment in the amount of $98,315. REBD had gross business revenue of $2,150 from only 14 clients and PTC had gross revenue of $1,800 from only 13 clients. Gross total business expenses for both enterprises were claimed in the amount of $83,805 for a net business loss in the amount of $79,855. In computing income for his 2011 taxation year, the Appellant reported income from employment in the amount of $85,160. PTC had gross revenues of $3,600 from only 18 clients. Gross business expenses were claimed in the amount of $33,253 for a net business loss in the amount of $29,603. The net business losses for these taxation years greatly exceeded the gross revenues.

[25] The Appellant has claimed business losses every year since 1999. He has tried a variety of activities none of which generated any profits. His losses in 1999 were $4,793 and his business losses steadily increased in practically every year since up to a maximum of $79,855 in 2010. All of these business losses generated significant tax refunds to the benefit of the Appellant.

[26] In a Notice of Reassessment dated March 24, 2014, the Canada Revenue Agency (the "CRA"), disallowed the business losses for 2010 and 2011 in their

entirety on the ground that the Appellant's activities were not sufficiently commercial in nature as to constitute a source of business income for the purpose of Section 9 of the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.) (the "*Act*"), and that the losses could therefore not be deducted against other income.

[27] The Appellant filed a Notice of Objection to the reassessment but the CRA confirmed the reassessment on January 26, 2015. Hence the appeal to this Court.

[28] The Appellant takes the position that REBD and PTC were carrying on business activities during the 2010 and 2011 taxation years. He contends that the activities of REBD and PTC constituted sources of business income. All expenses incurred by the Appellant were for the purpose of generating profits and such expenses were valid and reasonable in all of the circumstances, and not in any way related to personal or living expenses. The Appellant therefore urges this Court to allow the appeal and refer the matter back to the Minister of National Revenue for reassessment on the basis that the expenses claimed were valid business expenses.

[29] The Respondent takes the position that the Appellant's activities were not carried out with a sufficient enough degree of commerciality to constitute a source of business income pursuant to subsection 9(2) of the *Act*. Consequently, his so-called business losses were not deductible against employment income. Alternatively, if the Appellant's activities constituted a business, the expenses claimed were not made or incurred for the purpose of gaining or producing income. They were personal or living expenses or they were unreasonable in all the circumstances. The Respondent therefore urges this Court to dismiss the appeal.

Analysis

[30] The *Act* divides a taxpayer's income into various sources: office, employment, business and property. Section 9 of the *Act* provides that the taxpayer's income from business is the taxpayer's profit while his loss from business is such amount as computed in accordance with the *Act*; namely, income less permitted deductions.

[31] Section 18 of the *Act* provides that certain expenses may not be deducted from revenue in computing income. It provides:

> **18.**(1) In computing the income of a taxpayer from a business or property no deduction shall be made in respect of

> (*a*) an outlay or expense except to the extent that it was made or incurred by the taxpayer for the purpose of gaining or producing income from the business or property;
>
> …
>
> (*h*) personal or living expenses of the taxpayer, other than travelling expenses incurred by the taxpayer while away from home in the course of carrying on his business;

[32] Section 67 of the *Act* further provides that:

> **67.** In computing income, no deduction shall be made in respect of an outlay or expense in respect of which any amount is otherwise deductible under this Act, except to the extent that the outlay or expense was reasonable in the circumstances

[33] Section 248 of the *Act* defines "personal or living expenses" as follows:

> **248.**(1) In this Act
>
> ...
>
> "personal or living expenses" includes
>
> > (*a*) the expenses of properties maintained by any person for the use or benefit of the taxpayer or any person connected with the taxpayer by blood relationship, marriage or common-law partnership or adoption, and not maintained in connection with a business carried on for profit or with a reasonable expectation of profit,

[34] Subsection 248(1) of the *Act* gives a very broad definition of "business". A "business" includes "a profession, calling, trade, manufacture or undertaking of any kind" and generally includes "an adventure or concern in the nature of trade."

[35] The test for determining whether a taxpayer's activities constitute a source of business or property income was set out by the Supreme Court of Canada in *Stewart v. Canada*, [2002] 2. S.C.R. 645; [2002] S.C.J. No (QL). 46. In *Stewart*, the Court held that the "reasonable expectation of profit" test ("REOP") for determining if a taxpayer had a source of income from a business could no longer be maintained as a stand-alone independent source test. The REOP test should not be blindly accepted as the correct approach to the "source of income"

determination. The Court established a new test. Justices Iacobucci and Bastarache set out the broad principle in paragraph 5:

> [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 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 endeavor 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.
>
> [Emphasis added]

[36] The Court set out a two-step test for determining whether or not a taxpayer has a source of income from a business or property. The Court stated:

> 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.

[37] The purpose of the first stage of the test is simply to distinguish between commercial and personal activities. Where the nature of a taxpayer's activities contains elements that suggest that the activities could be considered a hobby or

other personal pursuit, but the activities are undertaken in a sufficiently commercial manner, the venture will be considered a source of income for the purposes of the *Act* (*Stewart*, paragraph 52).

[38] The "pursuit of profit" source test will only require analysis in situations where there is some personal or hobby element to the activity in question. 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 (*Stewart*, paragraph 53).

[39] The Court went on to note at paragraph 54:

> [54] . . . in order for an activity to be classified commercial in nature, the taxpayer must have the subjective intention to profit, in addition, . . . this determination should be made by looking at a variety of objective factors. . . . 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.
>
> [Emphasis added]

[40] In paragraph 55, the Court went to on to adopt, the objective standards of businesslike behaviour listed by Dickson J., in *Moldowan v. Canada*, [1978] 1 S.C.R. 480, at page 486 to determine the subjective intention to profit. These are:

(1) the profit and loss experience in past years;

(2) the taxpayer's training;

(3) the taxpayer's intended course of action; and

(4) the capability of the venture to show a profit.

[41] These factors are not intended to be exhaustive and the factors will differ with the nature and extent of the undertaking. For instance, Justice Pizzitelli in the case of *Cohen v. R.*, 2011 TCC 262, considered that risk minimization is also a factor to be considered. He adopted the dicta of Bonner J. in paragraph 10 of *Balanko v. The Minister of National Revenue*, 81 DTC 887, where that learned jurist stated:

> . . . While risk-taking is necessary in a business, it is management or minimization of risk which is the characteristic of business activity. . . .

[42] The Supreme Court also cautioned in paragraph 55 of *Stewart* that:

> [55] . . . although the reasonable expectation of profit is a factor to be considered at this stage, it is not the only factor, nor is it conclusive. The overall assessment to be made is whether or not the taxpayer is carrying on the activity in a commercial manner. However, this assessment should not be used to second‑guess the business judgment of the taxpayer. It is the commercial nature of the taxpayer's activity which must be evaluated, not his or her business acumen.

[43] In paragraph 56 of *Stewart*, the Court observed that in addition to restricting the source test to activities that contain a personal element, the activity which the taxpayer claims constitutes a source of income must be distinguished from particular deductions that the taxpayer associates with that source. An attempt by the taxpayer to deduct what is essentially a personal expense does not influence the characterization of the source to which that deduction relates; it only affects the deductibility of that particular expense. In addition, the profitability to which the expense relates does not affect the deductibility of the expense (see paragraph 58, *Stewart*).

[44] With respect to financing a business enterprise, the Court observed at paragraph 59 of *Stewart*:

> [59] . . . Clearly the existence of financing does not indicate that the underlying activity should not be characterized as a source of income. On the contrary, the fact that an activity has been financed externally is an indication that the taxpayer is operating his or her activity in a businesslike manner. As such, the existence of financing is an element which adds to the commerciality of a venture, and thus operates in favour of characterizing the activity as a source of income.

[45] The Court summarized in paragraphs 60 and 61 of *Stewart*:

> [60] In summary, the issue of whether or not a taxpayer has a source of income is to be determined by looking at the commerciality of the activity in question. Where the activity contains no personal element and is clearly commercial, no further inquiry is necessary. Where the activity could be classified as a personal pursuit, then it must be determined whether or not the activity is being carried on in a sufficiently commercial manner to constitute a source of income. . . .

> [61] As stated above, whether or not a taxpayer has a source of income from a particular activity is determined by considering whether the taxpayer intends to carry on the activity for profit, and whether there is evidence to support that intention. As well, where an activity is clearly commercial and lacks any personal element, there is no need to search further. Such activities are sources of income.

[46] In the case at bar, the Appellant testified that he intended to earn income from his after hours activities. If I accept that, then this would satisfy the subjective intent element of the *Stewart* test. However, I conclude that there existed some strong personal elements or benefits to the Appellant arising from his activities. The Appellant had a full-time job. Therefore, these activities were carried on during the Appellant's spare time; after hours, on weekends and on holidays. It could be said that the Appellant was dabbling in activities related to real estate and physical fitnesss during his spare time. PTC offered activities such as snowboarding, mountain biking, nutritional advice, dietary plans, customized exercise programmes, weight training, hunting and fishing – most of these are recreational activities conducted after hours and on weekends. He indicated that some of these activities would involve the use of the gym where he resided in 2010 and the setting up of a home gym in his home in 2011. Involving his home in these activities certainly imports a personal element. REBD offered assistance and advice to homeowners interested in renovating their homes, selling their homes or relocating to foreign properties in Asia, Florida, Montreal and Hawaii. The Appellant travelled to these locations and spent a fair bit of time there supposedly looking for properties for his clients and for himself but at no time did he actually have any clients who expressed an interest in relocating to these locations. There certainly was an element of personal vacation time relating to these travels. In addition, the Appellant generated significant expenses (which he refused or neglected to keep under control) resulting in substantial tax refunds that benefitted him personally. Many of his expenses related to goods and services that were subject to personal consumption by himself. Therefore, there is enough of a personal element to the Appellant's activities that it warrants taking a look at the objective factors identified in *Stewart* and *Moldowan*, as well as other relevant factors, in the context of the evidence to determine the commerciality of the activities in question.

Profit and Loss Experience in Past Years

[47] The Appellant is a very bad businessman. He certainly has known this for quite some time now. He has failed at every supposed business activity that he has ever undertaken. He has engaged in activities which he described as business

endeavours in past years where he has claimed significant business losses compared to gross business revenue since 1999. None of his activities resulted in any profit. In fact, the business losses steadily increased every year from net losses of $4,793 in 1999 to $47,140 in 2008 and $42,057 in 2009. His business losses peaked at $79,856 in 2010, and this after more than a decade of various supposedly entrepreneurial endeavours. If he learned anything from his so-called business ventures, he learned how to increase expenses to be deducted from his employment income but he has not learned how to increase revenues. The Appellant argues that these prior business activities were in relation to activities different than the ones here under consideration and thus an examination of previous years is only capable of showing that he was unsuccessful in running different, unrelated businesses prior to making his attempt to run REBD and PTC. As such, it is argued that the question regarding profit and loss in previous years does not properly apply to the situation at hand. The Appellant's business activities in the years under consideration were not operating during the prior years and so there can be no evaluation of whether the activities of REBD and PTC are properly considered businesses.

[48] I caution myself not to second-guess, in hindsight, the poor business decisions made by the Appellant. However, the fact that the Appellant has claimed increasingly larger business losses since 1999 is an indicator that the businesses in the past were not being operated in a businesslike manner and permits the inference that the businesses being operated in 2010 and 2011 were likely also not being operated in a businesslike manner. It should be noted that the activities of REBD started at the beginning of January 2008, according to the material placed before the Court, and so any start-up difficulties should have been ironed out by 2010. Based on his track record, the Appellant could not reasonably have expected these latest part-time adventures to generate any income. This factor shows a lack of commerciality on the part of the Appellant.

Limited education and knowledge of real estate and fitness training

[49] The Appellant did not have any training, degree, diploma, certification, license or accreditation in real estate, home renovation, financing, property management or property investment.

[50] The Appellant contends that he had specialized knowledge and experience of the necessary steps required to ready a home for the market place, how to effectively market the real estate and the necessary steps to complete a real estate transaction. As an example, he states that he can use internet websites to aid clients

to self-market their own homes without the high cost associated with retaining the services of a licensed real estate agent. He professes to have considerable knowledge about which areas in the Toronto area, and elsewhere, have potential as rental properties, the costs and benefits of renovations, and the places outside Toronto where one might chose to retire and buy a residence for themselves as well as an income property from the proceeds of sale of their Toronto property.

[51] I found the Appellant's evidence concerning his education, knowledge and training in the real estate industry to be unconvincing. His knowledge of real estate, marketing, home renovation, financing and property management was no greater than that of any interested individual homeowner who chose to make use of readily available tools such as the Internet to inform himself and explore his options.

[52] With respect to PTC, the Appellant did not have any degree, diploma, certification, training or coaching experience in personal or group fitness, weight training, hunting, fishing or mountain biking. He has no education or training as a dietician or nutritionist. The Appellant did obtain a level 1 snowboarding instructor's certificate in 2010, but had no other teaching or coaching experience. There is no evidence that he had any university degree, college diploma or other certificate in physical education.

[53] On the other hand, the Appellant contends that he displayed considerable knowledge about nutrition and human anatomy having gained such knowledge from his anatomy classes in university. It is argued that such an understanding gained as part of a university education in the sciences extends far beyond what one would expect of a personal trainer.

[54] Other than university courses in human anatomy and a snowboarders teaching certificate, he has no other accreditation or special knowledge that would qualify him to operate the business of a physical fitness trainer/coach, nutritionist, fishing guide or hunting guide. Again, I find the Appellant's evidence to the effect that he has special knowledge and experience in these fields to be unconvincing.

[55] A consideration of this factor militates against a finding in favour of the Appellant.

Taxpayer's intended course of action

[56] When the Appellant was asked if he had a business plan, he initially indicated that he did not know what that was. On further prompting, he admits that he did not draft a specific business plan with income and expense projections. The Appellant did not assess the feasibility or profitability of the proposed businesses. He believed that he would require professional help to draft such a plan at considerable cost. There were no short term or long-term marketing or advertising strategies. He eschewed media advertising due to its higher costs. He was prospecting for potential investors who would sponsor his activities. He does not indicate how much of an investment he was looking for. Yet, the only way he planned on attracting such investors was by word of mouth and by canvassing door-to-door – a very ineffectual and haphazard method of finding wealthy investors. Going door-to-door and relying on word of mouth is not the way to raise capital or find investors. If he had a business plan, it was simply to "build a good business". That is not a business plan; it is simply the expression of his wish to be successful.

[57] A business plan need not be sophisticated or very detailed but it should provide a business strategy with projections of revenue and expenses and include defined and realistic goals with a timetable within which to attain those goals. These goals can certainly change over the course of time. A business plan is a roadmap to establishing a sustainable business; it is not simply the wish to "build a good business".

[58] The absence of even a rudimentary business plan indicates a lack of commerciality. No reasonably prudent entrepreneur would enter into a business venture without at least some plan on how to establish and maintain a viable business. This factor is indicative of a lack of commerciality.

Capability to show a profit

[59] The Appellant's activities never did generate any profits but instead resulted in huge and disproportionate expenses for part-time activities – just like all of his past endeavours. Door-to-door direct marketing yielded very few clients. The Appellant produced no evidence that his part-time after-hours activities had any realistic capability to generate profits. This should have been quickly obvious to him and should have become more and more obvious as time went on. The success of PTC hinged on finding an investor who was willing to inject significant funds into the project – this was not forthcoming. The Appellant had no special attributes that would allow him to wrest business away from professionals or established businesses that were engaged in a very competitive market. He really had nothing

to offer other than an extremely low fee of ½ % for his real estate business – even at this low fee he had no takers. These part-time after-hours activities had no or limited capacity of generating any profits.

Risk management or risk minimization

[60] The Appellant took unnecessary financial risks. He avoided media advertising due to costs but yet he expended considerable sums of money travelling to Hawaii, Florida and other locations to scope out the real estate market even though he had no clients whatsoever who were interested in relocating there. He was lavish in gift giving and did not put into place any process to monitor his expenses or manage his risks. The absence of risk management and complete lack of control over run-away expenses contra-indicates commerciality.

Liability insurance

[61] The Appellant had no liability insurance for REBD or PTC. He claims that the level 1 snowboarding instructor certificate that he obtained in 2010 included liability insurance but he did not produce any documentary evidence to that effect when it would have been a simple matter to do so. He did not have any liability insurance in relation to his hunting (which is an inherently dangerous sport) or any other outdoor activities that he claims he carried on with PTC. He also admits that he did not have a firearms acquisition certificate or a hunting license. He claims that was not necessary since he hunted with a bow or crossbow – but what about clients who wished to hunt with firearms? The Appellant claimed that his fitness business was covered under the condominium's general insurance policy or his homeowner's policy but he is only supposing that and it is clear that he did not make any inquiries to find out if the condominium policy or his homeowner's policy extended coverage to any commercial activity conducted on the premises. No prudent businessman would undertake any enterprise as a sole-proprietorship without confirming that the commercial activities being undertaken were covered against all risks. To do so does not amount to commercial-like behaviour and indicates a lack of commerciality.

Banking and commercial transactions

[62] This is a very important factor. The Appellant did not set up any bank accounts for his alleged business activities. He did not keep any records of money going in or out of his account in relation to his businesses. He had few clients and when he did have any clients, he did not have them sign any contracts, he did not

invoice them, he did not make a record of their home addresses or maintain any record of their contact information. He did not issue any invoices to any of his clients, either REBD or PTC clients. In addition, he did not accept any form of traceable payments such as cheques, debit cards or credit cards. What businessperson does this? He only accepted cash and there is no evidence that he issued any receipts for the cash taken in. He did not produce any ledgers showing that the cash was deposited in a bank account. The absence of bank accounts, invoicing, deposit information, revenue and expense ledgers all point to lack of commerciality.

Capital investment

[63] The Appellant did not negotiate a business loan or any kind of a loan from any financial institution in order to finance his enterprises. Instead, he says he chose to finance his business by withdrawing money from his RRSP plan. This obviously resulted in unfavourable tax treatment. This is quite surprising for someone who states that part of his services is to give financing advice and guidance to his REBD clients. We have no idea what happened to the money withdrawn from his RRSP. We only have the Appellant's assertion that the money was used for business purposes. Had there been business bank accounts, it would have been a simple matter to establish that the RRSP moneys had in fact been dedicated to his business activities. It is up to the Appellant to affirmatively show that the RRSP money was used for business purposes. Using funds from one's RRSP plan to finance a business enterprise is not consistent with businesslike behaviour.

Record keeping

[64] The Appellant maintains that he kept meticulous records relating to his business activities – this is not true. The fact is that he preserved every scrap of paper that showed any possible expense such as cash register slips and credit card receipts. However, as already indicated, there is a conspicuous lack of documentation in relation to the revenue side of his record keeping. He had no information at all about his supposed clients except for their names. He had no record of their addresses or other contact information. He did not invoice them or issue receipts for cash received. Everything on the revenue side was done on a cash basis with no supporting documentation while everything done on the expenditure side was supported by a source document. There are no ledgers, no financial statements, no books of account, and no bank statements showing expense money

going out and revenues coming in. The failure to keep or to produce ledgers and books of account militate against a finding of commerciality.

Other factors

[65] One would think that a business enterprise would register its business name under relevant provincial legislation; this was not done. One would think that a business enterprise would obtain a business number for purposes of HST; this was not done. One would think that a business enterprise would obtain all required municipal licenses and permits; there is no evidence of this being done. All of this militates against a finding of commerciality.

Conclusion

[66] Having regard to all of the above, I find that the Appellant has not demonstrated that he conducted his activities in such a manner as to constitute a profession, calling, trade, undertaking, or adventure or concern in the nature of trade so as to fall within the definition of a business. Therefore, the Appellant has not satisfied me on the balance of probabilities that he had a source of business income.

[67] In addition, I observe that the Appellant was very remiss in documenting his supposed revenues but so very diligent in gathering together any and all source documents claimed to be business expenses. The Appellant's alleged business expenses are all of a nature that he could use them to offset personal or living expenses. The Appellant has known since 1999 that claimed business losses could be deducted against employment income and thus result in significant tax refunds. I conclude that the Appellant was probably only interested in generating tax-deductible expenses rather than run a commercial enterprise. He was not carrying on any business with any degree of commerciality.

[68] Accordingly, the Appellant's appeal is dismissed on this basis alone.

Deductibility of Expenses

[69] As I have already indicated, in view of my conclusion that the Appellant did not have a business source of income, it is not necessary to decide the deductibility of claimed expenses. However, I do have some comments to offer.

[70] It is for the Appellant to satisfy the Court on the balance of probabilities that the expenses he incurred were properly deductible from income. In order for a business expense to be deductible, the Court must be satisfied that the expense claimed was incurred for the purpose of earning income from a business within the meaning of subsection 18(1) of the *Act*. Pursuant to section 67 of the *Act*, the expense must also be reasonable in all of the circumstances.

[71] The business expenses claimed by the Appellant in respect of the 2010 and 2011 taxation years are as follows:

	Real Estate 2010	**Fitness 2010**	**Fitness 2011**
Advertising	--	--	--
Meals and Entertainment	$ 5,809.33	$ 4,736.98	$ 4,947.28
Bad debts	$ 7,427.00	--	--
Memberships, subscriptions		$ 97.97	$ 97.08
Insurance	--	--	$ 947.16
Office Expenses	$ 5,379.63	$ 3,379.69	$ 4,987.98
Supplies	$ 1,672.34	$ 1,044.18	$ 3,673.65
Professional fees	$ 341.09	--	$ 480.81
Rent	$ 4,800.00	$ 7,200.00	--
Maintenance & repairs	$ 1,053.61	$ 838.06	$ 315.86
Property taxes	--	--	$ 2,197.25
Travel	$ 5,822.08	$ 3,519.53	--
Telephone & utilities	$ 1,895.31	$ 1,662.48	$ 2,403.24
Delivery, freight & expenses	$ 280.21	$ 184.19	$ 125.46
Motor vehicle expenses	$ 12,585.43	$ 4,203.03	$ 9,712.63
CCA	$ 2,480.18	$ 1,937.16	$ 1,528.66
Gifts & networking	$ 2,827.42	$ 2,628.34	$ 1,836.24
Total	$ 52,373.63	$ 31,431.61	$ 33,253.30

[72] I observe that these are very large expenses for someone who is carrying on business after hours on a part-time basis. The magnitude of these expenses in relation to the gross revenue gives great cause for concern. I conclude that the

Appellant is overreaching when it comes to his claimed expenses. I will not engage in an item-by-item analysis of all of these expenses. Suffice it to say that most of these expenses relate to personal or living expenses or are patently unreasonable in all of the circumstances. The Appellant has not satisfied me on the balance of probabilities that the claimed expenses were expended for the purposes of generating business income.

Meals and entertainment

[73] These types of expenses are personal and living expenses and are not deductible unless the expenses were incurred by the taxpayer while away from home in the course of carrying on the taxpayer's business in accordance with paragraph 18(1)(*h*) of the *Act*.

[74] The Appellant provided copies of a large number of cash register receipts and credit card receipts regarding the cost of meals and entertainment. There were receipts from a variety of restaurants, receipts for alcohol and for groceries which he claimed was brought home for those clients that he received in his home. These documents take the form of invoices/cash register slips or credit card slips. Some of these documents are illegible. The invoices/cash register slips only show what was purchased and the place and time of the purchase. The credit card slips show how much was paid and when but do not show what was purchased. None of these documents show for whom the expenses were incurred or the purpose of the purchase. There is no evidence other than the assertions of the Appellant to show that the groceries, restaurant expenses and alcohol were business related and were incurred to earn income from a business. It would have been a simple matter for the Appellant to endorse the name of the potential client, contact information and purpose of the meeting on the back of the source document. This, he did not do.

[75] The Appellant claims that he consumed meals while on the road away from home on business. Most of the invoices were issued by restaurants all within the GTA, a short driving distance of the Appellant's residence or place of work. The total expenses for meals and entertainment also greatly exceed the amount of revenue generated. Expenses for meals and entertainment in 2010 were a total of $10,546 and $4,947 for 2011. Expenditures of this amount are not reasonable in the circumstances. As well, the Appellant contends that he brought groceries home in order to entertain clients. He did not produce any record of the names of the clients he entertained at home nor how many he so entertained, if any. Therefore he has not shown that the amount of money expended on meals and entertainment was for the purpose of earning income from his business. I conclude that these

groceries were for personal consumption and the Appellant has not convinced me that they are not. Those invoices issued by restaurants and businesses located out of town have not been shown by the Appellant to be related to his business endeavours.

Bad debts

[76] The Appellant sought to write off bad debts in the amount of $7,427. I have no idea what this bad debt was all about. This bad debt has not been shown to be in any way related to the Appellant's business activities and so is not deductible under the *Act*.

Memberships & subscriptions

[77] Membership fees of about $98 for 2010 and 2011 to maintain his snowboarding instructor certification would be allowable deductions if the Appellant were in fact in the physical fitness business.

Insurance

[78] The Appellant claims homeowners insurance in the amount of $947.16 for 2011. This represents 100% of the cost of his home insurance. Only that portion of the insurance that is referable to PTC would be allowed. That would be only 50% if I accept the calculation of the Appellant that 50% of the floor area of his home was dedicated to the business. Even then, 50% seems to be an exaggerated claim. This would mean that half of his living space was entirely dedicated to his part-time after-hours business for just a few clients – a specious claim at best.

Office expenses and supplies

[79] The Appellant claimed a total of $11,475.84 for office expenses and supplies in 2010 and $8,661.63 in 2011. These are ridiculously high office expenses for part-time businesses and are simply not reasonable in all of the circumstances. No reasonably prudent businessperson would expend that kind of money in order to earn so little income. The items purchased include toothpaste, Kleenex, magazines, chocolates, valentine cards, flowers, vitamins, Metamucil and other unexplained items. The Appellant did not explain or provide any credible evidence other than his assertions to show how he incurred these expenses for the purpose of earning income from a business. I have no difficulty concluding that these expenses are in the nature of personal or living expenses and thus are not deductible.

[80] In addition, $1,876,64 of these expenses was for computer hardware and furniture. These items are capital expenditures and as such are not current expenses and not deductible pursuant to subparagraph 18(1)(*b*) of the *Act*.

Professional fees

[81] Accounting fees would be justified if he were carrying on a business - $341.09 for 2010 and $480.81 for 2011.

Home office expenses

[82] The Appellant claimed a total of $12,000 for rent and a total of $3,557.79 for telephone and utilities in respect of his residence in unit 1801, 2121 Lakeshore Blvd West, Toronto (see Forms T2125 at Exhibit A-1, Tabs 7 and 27). It should be noted that his total rent payments for the year were $16,800. Thus the rental cost attributable to his alleged business activities amounted to 71% of the total rent that he paid for his residence in 2010. It is simply inconceivable that 71% of the living space in his rental unit was dedicated exclusively to his part-time after-hours businesses.

[83] The Appellant also claimed $2,197.25 for property taxes on his home in 2011 and the sum of $2,403.24 for telephone and utilities for that same year (see Exhibit A-2, Tab 4) for a total of $5,600.49 in relation to his fitness business.

[84] In order to claim expenses in respect of work space in a home, pursuant to subsection 18(12) of the *Act*, the work space must satisfy the following criteria:

a) The workspace is the individual's principal place of business; or

b) The work space is used exclusively for the purpose of earning income from business and used on a regular and continuous basis for meeting clients of the individual in respect of the business; and

c) Where the conditions in (a) or (b) are met, the amount that is deductible for the workspace for the year from the business shall not exceed the individual's income for the year from that business.

[85] With respect to REBD, there is no evidence to show that any of his 14 clients attended his home. In fact, it was the Appellant's evidence that he visited potential real estate clients in their homes or met with them in restaurants such as Tim Horton's. With respect to PTC, the Appellant testified that he used the gym and a meeting room located in the common areas of his condominium building to meet clients. These common areas were not and could not have been designated by the Appellant as a principal place of business or a space used exclusively for his business as they were common areas used in common by all condominium residents. These expenses cannot be allowed.

[86] Finally, any expenses claimed in respect of work space in home in excess of the reported income for each business is not deductible in the 2010 year. In this case, the Appellant reported an aggregate of $3,950 in 2010 and $2,403.24 in 2011. He is not entitled to deduct work space and home expenses in excess of those amounts pursuant to subsection 18(12) of the *Act*.

Maintenance and repairs

[87] The Appellant claimed expenses for maintenance and repair in the amount of $1,053.61 for REBD and $838.06 for PTC in 2010. He also claimed $315.86 for maintenance and repair for PTC in 2011. These expenses relate to computer repairs, property inspection agreement, various items purchased from Shopper's Drug Mart, moving services and other unidentified items (see Exhibit A-1, Tab 14 re. REBD and Tab 32 re. PTC).

[88] Exhibit A-2, Tab 13 relates to PTC for 2011 and includes invoices for clothing repairs and other unidentified items.

[89] The Appellant has not shown to my satisfaction how these items relate to the alleged businesses. They appear to be personal expenses in nature and it is up to him to convince me that they are not.

Travel

[90] The Appellant claimed expenses in the amount of $9,341.61 for 2010 – $5,822.08 for REBD and $3,519.53 for PTC. He travelled to Montreal (March 25-28), Miami (October 5 to 12) and Hawaii (August 26 to 30) with respect to REBD in order to look for investment properties for himself and

potential clients, so he says. However, he never had any clients at any time who were looking to relocate or invest in those locations. It is completely unreasonable for a small-time businessperson who is in business only part-time after-hours to spend that kind of money on travel to such far away places when he had no clients who were interested in investing or relocating to those places. These expenses were not incurred for the purposes of generating profit. The only conclusion I can arrive at is that these trips were for personal vacation purposes and were not business related.

[91] Exhibit A-1, Tab 33 catalogues his travel expenses relating to PTC. These expenses are for a banquet in Montreal, U-Haul equipment, vehicle reservation, hotel accommodations in Huntsville for 1 adult for 10 days, a hand written receipt for a three-day stay in a motel on June 6, 2010 and a car rental reservation in Toronto in the amount of $1,040.56 for September 18-25 – there appears to be some confusion as to the year, whether it was 2010 or 2013; I will assume 2010. There is also an invoice from the Hilton Garden Inn in Vaughan for two nights. The Appellant stated in evidence that this was likely when he was on his way up north for snowboarding but the date of the invoice is August 2010 – highly unlikely that he was snowboarding at that time.

[92] All of these expenditures have not been explained. It has not been shown to my satisfaction how these expenditures relate to the PTC or how they were expended for the purpose of generating income – especially the 10-day stay in Huntsville -- no explanation at all.

Gifts and networking

[93] The Appellant claimed a total of $5,455.76 for gifts and networking expenses in 2010 – this item alone is more than he earned in gross revenue. These gifts were for clothing and gift cards from Holt Renfrew, Zellers, Harry Rosen for $892.69, Moores, The Bay, and Tip Top Tailors (see Exhibit A-1, Tab 18 for REBD). Similar expenses are indicated at Exhibit A-1, Tab 36 for PTC such as $882.68 from Harry Rosen dated May 28, 2010. Expenditures in 2011 for PTC are collected together at Exhibit A-2, Tab 16 which includes expenditures for shoes, clothing etc.

[94] There is no evidence other than the Appellant's assertions that any of these gifts were in fact given to any clients and if so to whom and why. If these expenditures were in fact spent on gifts for prospective clients, they were

completely unreasonable when considered in the light of his revenue. Why would any reasonably prudent businessperson give a gift card in the amount of $100 to a prospective client unless the client actually signed up for a long-term contract? The Appellant admitted he did not sign up any clients to contracts. I conclude that these expenditures for men's apparel are personal items and have not been shown to be related to business activities.

Motor vehicle expenses and CAA

[95] The Appellant claimed expenses for his personal motor vehicle totaling $16,788.46 in 2010 and $9,712.63 in 2011. These expenses are for fuel & oil, insurance, license and registration, maintenance and repairs, CAA membership and car washes. He also claimed an additional $2,480.18 for capital cost allowance in 2010 and $1,528.66 in 2011.

[96] The Appellant did not maintain any kind of log-book to establish what proportion of the distance driven in his personal motor vehicle were for personal use and what was for business use. He did not keep a record of the distance he travelled in order to do his door-to-door direct marketing. In the absence of such a log or other proof showing what proportion of these expenses are attributable to his alleged business activities. These expenses ought not to be allowed.

Disposition

[97] As already indicated this appeal is dismissed on the basis that the Appellant did not have a source of business income for the 2010 and 2011 taxation years and his activities were not carried on in a sufficiently businesslike or commercial-like manner. His activities were not sufficiently commercial in nature as to constitute a source of business income for the purpose of Section 9 of the *Act* and the losses could therefore not be deducted against other income.

Signed at Kingston, Canada, this 10th day of June 2016.

"Rommel G. Masse"

Masse D.J.

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