

Docket: 2005-3149(GST)I

BETWEEN:

173122 CANADA INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on June 12, 2006, at Sherbrooke, Quebec

Before: The Honourable Justice Alain Tardif

Appearances:

Agent for the Appellant: Danièle Léger

Counsel for the Respondent: Mario Laprise

JUDGMENT

The appeal from the assessment of goods and services tax under Part IX of the *Excise Tax Act*, notice of which is dated June 3, 2005, and bears No. PACT-0240 LO, for the period from April 1, 2001 to April 30, 2004, is dismissed, without costs, in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Canada, this 7th day of February 2007.

"Alain Tardif"

Tardif J.

Translation certified true
on this 20th day of August 2007

Mavis Cavanaugh, Reviser

Citation: 2007TCC17
Date: 20070207
Docket: 2005-3149(GST)I

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173122 CANADA INC.,

Appellant,

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REASONS FOR JUDGMENT

Tardif J.

[1] This is an appeal from an assessment, notice of which is dated June 3, 2005, and bears No. PACT-0240 LO, and pertains to the period from April 1, 2001, to April 30, 2004.

[2] The issue to be determined is whether the Appellant was engaged in a commercial activity during the period covered by the assessment, and, if so, whether it was entitled to input tax credits (“ITCs”) in the amount of \$5,096.12.

[3] The Appellant was represented by Danièle Léger. A major player in the management of the Appellant's affairs and an erudite person who was clearly on top of all the information in the file, Ms. Léger explained the circumstances that led the business, founded in the mid-1990s, to its undoing.

[4] Initially, the business owned a single truck. In 2001, the business was growing fast and it seemed as though the sky was limit; the business owned roughly 10 trucks and the future looked promising.

[5] In early 2001, the insurance broker in charge of renewing the civil liability insurance policies on the trucks apparently neglected to keep track of the matter,

and, as a result, the company had to cease operations in March 2001, because it was unable to comply with the numerous statutory and regulatory requirements, including the requirement to have appropriate insurance coverage.

[6] Since it was no longer able to do any transportation, the company quickly lost its income source and the lenders subsequently recalled their lines of credit and realized their guarantees.

[7] After the events of March 2001, the Appellant fought for its survival. It sued the insurance broker. Having lost almost all of its assets, it was able to retain only a small pickup truck, which it used in an attempt to rebuild the business through various initiatives. However, it did not keep a log of the distances driven.

[8] The Appellant's agent and her spouse were very determined and refused to throw in the towel. They devoted themselves entirely to searching for new activities that would draw on their expertise in the transportation field. But hope was the only fruit that these various attempts bore.

[9] Throughout this lengthy period, the Appellant made a whole series of requests; it considered various investment projects and had several meetings, including meetings with lawyers aimed at obtaining compensation for the loss caused by the carelessness and negligence of the broker responsible for renewing the insurance policies.

[10] The Appellant argued that it is entitled to the ITCs that it claimed for the period from April 1, 2001 to April 30, 2004. The Respondent, for her part, maintained that commercial activities were no longer being engaged in at that time.

[11] In order to make and confirm the assessment under appeal, the Respondent relied on certain facts listed in paragraph 13 of the Reply to the Notice of Appeal, which reads as follows:

[TRANSLATION]

- (b) The Appellant operated a business that transported goods by truck ("trucking business").
- (c) The Appellant ceased operating its business on or about March 31, 2001.
- (d) Following an audit, the Minister disallowed ITCs claimed by the Appellant and assessed the Appellant accordingly on June 7, 2004.

- (e) During the objection process, the Appellant provided the Minister with additional information and documents.
- (f) After analyzing this additional information and documentation, the Minister noted that, based on the Appellant's accounting books, the Appellant, until August 2002, entered supplies that had been purchased while the trucking business was still being operated (that is to say, before March 31, 2001), and that the supplies were related to the business.
- (g) Thus, the Minister granted the Appellant the ITCs for the period from April 1, 2001 to August 31, 2002, for all supplies related to the periods during which its trucking business was operating, provided they were related to the said business, hence the assessment of June 3, 2005, which constitutes the decision concerning the objection.
- (h) Aside from the supplies made in the course of its trucking business, the Appellant reported no taxable supplies during the period at issue.
- (i) Aside from the trucking, the Minister determined that the Appellant carried on no other commercial activity during the period at issue.
- (j) Consequently, the Minister disallowed all the ITCs claimed by the Appellant in respect of supplies other than those acquired in the course of its trucking business.
- (k) The Appellant did not show that the supplies for which it is claiming ITCs were purchased for consumption, use or supply in a commercial activity.
- (l) Moreover, based on an analysis of the ITCs claimed, the Minister noted that certain ITCs were claimed on purchases of purely personal supplies.
- (m) Consequently, the Appellant owes the Minister the amount of the adjustments to its net reported tax for the period at issue.

[12] The facts set out in subparagraphs (b), (d), (e), (f), (h) and (j) were admitted, and the other facts were denied.

[13] At the Court's request, the parties produced notes in support of their respective positions.

[14] The Appellant is claiming ITCs even though, during the period from April 1, 2001 to April 30, 2004, it made no supplies, except to receive and report

\$1,091.96 as income during the period ending December 31, 2002, income which does not appear to have anything to do with supplies related to the transportation of goods.

[15] Following an audit, the Minister of National Revenue ("the Minister") disallowed the ITCs on the grounds that he determined that the Appellant had ceased all commercial activity on April 1, 2001. The disputed ITCs amounted to \$12,269.90 at the time of this determination.

[16] Further to a challenge raised following a notice of objection, the file was reviewed. The Respondent then changed the date on which commercial activity ceased to August 30, 2002, and consequently, allowed \$7,252.06 worth of additional ITCs. Thus, this appeal is about the difference, that is to say, \$5,017.84 in ITCs that were disallowed for the period from September 1, 2002 to April 30, 2004.

[17] I must state from the outset that, even if I come to the conclusion that the Appellant continued to carry on business during the period under appeal, its claim will not automatically succeed.

[18] Entitlement to ITCs requires more than a commercial activity within the meaning of sections 169 and 123 of the *Excise Tax Act* (the "Act"). All claimants must retain documentation supporting their claims within the meaning of subsection 169(4) and section 286 of the Act, and must be able to provide it.

[19] In the case at bar, Ms. Léger submitted essentially oral explanations in support of her ITC claim. She did not submit any supporting documentation, and she primarily insisted that she and her spouse did everything they could to stay in the trucking business.

[20] It is not easy to determine when a commercial enterprise begins and when it ends. The beginning does not always coincide with the date of creation of the legal entity that forms the business, and the end is not always when the commercial activities cease. Certain activities may extend the true end of a business that has ceased to carry on the activities related to its vocation; for example, a business might collect debts or sell accumulated inventory after its manufacturing has ceased.

[21] In this regard, the Honourable Justice Rip, in *Two Carlton Financing Ltd. v. Her Majesty the Queen*, [1998] T.C.J. No. 447, docket 96-523(GST)G, 2000 G.T.C. 4020, wrote as follows:

- 29 Since Carlton did not report any taxable supplies until February 1995 and did not collect any GST during the period, respondent's counsel concluded Carlton was not engaged in any commercial activity during the period.
30. Appellant suggests that during the period Carlton was starting up a business. Its counsel referred to Revenue Canada Interpretation Bulletin No. IT-364 for the proposition that a business commences whenever some significant activity is undertaken that is a regular part of the income earning process in that type of business or is an essential preliminary to normal operations. Counsel also referred to Bowman, T.C.C.J. who stated that:

In determining when a business has commenced, it is not realistic to fix the time either at the moment when money starts being earned from the trading or manufacturing operation of the provision of services or, at the other extreme, when the intention to start the business is first formed. Each case turns on its own facts, but where a taxpayer has taken significant and essential steps that are necessary to the carrying on of the business it is fair to conclude that the business has started.

[22] Further on in the same judgment, our colleague, in a discussion of considerations that are of great relevance to the case at bar, stated as follows:

35. . . . The definition of "commercial activity" in subsection 123(1) of the Act does not expressly require that taxable supplies be made. Nonetheless, it is difficult to imagine the carrying on of a business without its activity falling within the scope of a supply.
36. . . . Since the appellant reported no sales or revenues during the period, one may reasonably infer that the appellant was not engaged in commercial activities during the period and, if so, the appellant cannot be considered eligible for ITCs in the period.
37. . . . ITCs are generally unavailable unless the inputs for which the ITCs are claimed were used in the production of other taxable supplies. Carlton did not report any taxable supplies during the period in issue which, if it were in fact carrying on the business it purported to acquire immediately on acquisition, supplies would have been made.

[23] It is not easy to determine a precise moment or date because there can be grey or transitional areas.

[24] In the case at bar, the Respondent interpreted the facts in a very broad and even advantageous way, both with respect to eligibility for the ITCs and with respect to the period.

[25] In support of her submissions, the Respondent cited some very relevant decisions. In *Strachan v. The Queen*, [1993] G.S.T.C. 72, No. 98-1914(GST)I, the Court set out certain principles that are very much on point:

[23] Immediate profit is not required, however, certain things must happen in the start-up period. Although every business is entitled to a grace period for start-up costs, it still must be shown that the business is "structured, organized, manned, financed and planned in such a way as to be found to be reasonably capable at that time of yielding a profit in due course." When the business criteria are present the length of time to lead to profitability is a direct function of the endeavour in question.

...

[24] There is a strong personal element in that the site of the activity is also the personal residence of the Appellant.

[25] . . . [T]he Appellant in this case was still in her training and development stage. I conclude there was insufficient supportive criteria to justify a conclusion of commercial activity within the meaning of the Act.

...

[28] . . . in relation to the dog biscuit endeavours, the project was in its embryo development stage and did not have a reasonable expectation of profit or the indicia of commercial viability.

[29] I conclude for the assessment period there was no commercial activity conducted on the premises.

[26] In *Janitsch v. The Queen*, 2004 GTC 326, No. 202-3892(GST)I, the Appellant was a visual artist. Before analyzing the facts, the Court stated in

passing, at paragraph 7, that "because of the statutory definition, the *Stewart* decision does not affect GST appeals."

[27] Although the Appellant made a sale (albeit its only sale), the Court determined that its work could not be considered a commercial activity.

[28] In *Haberdan Construction Inc. v. The Queen*, 1999 GTC 3249, No. 98-85(GST)I, the appellant had not reported any sales or collected any GST, and the Appellant attributed this to the bankruptcy of its customers and its inability to collect from them. The Court held:

[7] The Appellant has the burden of proof of establishing his case and regrettably the Appellant has been unable to do so. This may have resulted from the bankruptcy of the Appellant's customers and his inability to collect but it would appear that since there were no sales there was no commercial activity carried on.

[29] Lastly, in *Hegerat v. The Queen*, 2000 GTC 629, No. 98-2863(GST)I, the Appellant designed and promoted products. In its analysis, the Court stated, *inter alia*, as follows:

[15] It seems to me that he has gone to these lengths to establish the fact that everything about his apartment is deductible for either income tax purposes or can be used for input tax credits for goods and services tax because it is just as much a place of business as if he owned a factory and it were the factory. . . .

[17] On the main issue, the disallowance of the input tax credits in the amount of \$713.97 as shown in Exhibit R-2, I find that the Appellant's case is hopeless. He cannot possibly succeed against the Minister's disallowance of those tax credits for the following reasons. In the goods and services tax legislation, the definition of commercial activity in section 123 contains the following words:

123(1) Commercial activity of a person means

(a) a business carried on by the person (other than a business carried on by an individual ... without a reasonable expectation of profit) except to the extent that ...

As I read that definition, a commercial activity of a person means a business carried on by the person other than a business carried on by an individual without a reasonable expectation of profit. If there is no reasonable expectation of profit from an activity which purports to be a business, then it is not a business for purposes of commercial activity and, therefore, not a business in respect of which input tax credits can be claimed.

[18] That raises the question whether this activity of invention, design and product development is an activity with a reasonable expectation of profit. I find that it is not. It is an activity in respect of which there is no revenue. There is no question that the Appellant has an intense interest in it, and he is imaginative, to say the least, and dedicated to the idea of bringing better mouse traps to the market but, without any revenue at all, without any sales, I find it hard to visualize this activity as a business. If I could compare it to a mine, the Appellant is like a person who has discovered an ore body and is working at it before producing an ounce of ore. The Appellant is working at the development of ideas without an idea which he can yet take to market.

[30] That decision was affirmed by the Federal Court of Appeal on the issue of the ITCs disallowed by reason of the absence of commercial activity: 2000 GTC 4117, No. A-477-98.

[31] In the case at bar, the Appellant had to bear the disastrous consequences of certain people's negligence and carelessness to the point of losing, according to its explanations, the vast majority of the assets that enabled it to engage in commercial activities related to the transportation of goods.

[32] Very courageously, several initiatives were taken in order to revive the business. Hope, optimism and determination are remarkable qualities, but they are not, in and of themselves, sufficient to constitute the foundation of commercial activity within the meaning of the Act.

[33] In its written submissions, the Appellant seeks the following relief:

[TRANSLATION]

- That the seizure of our bank account be revoked.
- That our GST/QST registration be reactivated.
- That your decision be made to apply to the QST as well . . .
- That I be reimbursed the taxes to which I consider myself entitled, plus interest.

[34] In an appeal under section 306 of the Act, the Court can only vacate or vary the assessment. Consequently, the Court cannot grant any of the relief sought by the Appellant.

[35] As for the QST, our Court has no jurisdiction, because such jurisdiction is vested exclusively in the Court of Quebec under sections 93.1.10 and 93.2 of the *Act respecting the Ministère du Revenu*, R.S.Q., c. M-31.

[36] After disallowing the ITCs for the period from April 1, 2001 to April 30, 2004, the Respondent revised the file and allowed the ITCs up to August 31, 2002.

[37] For the remainder of the period—that is, from September 1, 2002 to April 30, 2004—the ITC must be disallowed by reason of the absence of commercial activity.

[38] In addition, even if the Appellant had succeeded in showing the existence of genuine commercial activities, I would still have had to dismiss the appeal, because the evidence submitted, evidence that was based on essentially oral explanations, is insufficient to justify the reimbursement of the ITCs.

[39] Although this matter elicits sympathy and although Ms. Léger devoted a great deal of energy to her preparation, I cannot dispose of this appeal based on sympathy.

[40] Essentially, I must apply the law pertaining to the assessment that gave rise to this appeal. Based on the evidence submitted by each of the parties, that assessment was correctly made.

[41] Having reviewed all the documents submitted by the Appellant, I find that the Appellant was no longer engaged in a commercial activity within the meaning of the Act; consequently, the appeal must be dismissed.

Signed at Ottawa, Canada, this 7th day of February 2007.

"Alain Tardif"

Tardif J.

Translation certified true
on this 20th day of August 2007

Mavis Cavanaugh, Reviser

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PLACE OF HEARING: Sherbrooke, Quebec

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Respondent's reply: October 20, 2006
Appellant's reply: November 2, 2006

REASONS FOR JUDGMENT BY: The Honourable Justice Alain Tardif

DATE OF JUDGMENT: February 7, 2007

APPEARANCES:

Agent for the Appellant: Danièle Léger

Counsel for the Respondent: Mario Laprise

COUNSEL OF RECORD:

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Name:

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