Citation: 2007TCC257
Date: 20070509
Docket: 2006-917(IT)I

BETWEEN:

STEVEN DEAN,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT
(Delivered Orally in Vancouver, B.C. on March 2, 2007)

Paris, J.

[1] The Appellant is appealing the disallowance of rental losses claimed for the 2001, 2002 and 2003 taxation years. The losses relate to a luxury condominium property at Whistler, B.C. acquired by the Appellant in August 2001. The amounts of the losses were $16,247.75 in 2001, $37,156 in 2002, and $27,177 in 2003.

[2] The issues in this appeal are whether the rental of the Whistler condominium constituted a source of income to the Appellant within the meaning of the *Income Tax Act*, and if so, whether the expenses related to the condominium were incurred to earn income from business or property, or were personal or living expenses of the Appellant.

[3] The determination of whether a taxpayer has a source of income is made on the basis of whether or not the activity is carried on predominantly for profit rather than as a personal endeavour. I refer in this regard to the Supreme Court of Canada case of *Stewart v. The Queen*, 2002 SCC 46, as cited by counsel. In this case, the Appellant's counsel concedes that there is a personal element to the Appellant's ownership of the Whistler property. This arises from the use of that property made by the Appellant and his family during the years in issue. It is clear that the personal use of the property was significant each year, and therefore the counsel's concession is appropriate. Given the existence of this personal element, I am required to analyze the rental activity to determine whether it was undertaken in a sufficiently commercial manner to be considered a source of income.

[4] The objective factors that have been referred to by the courts in assessing the commerciality of a taxpayer's undertaking include the profit and loss experience of the venture in past years, the taxpayer's training or experience, the taxpayer's intended course of action, and the capability of the venture to show a profit. This list is not exhaustive.

[5] The evidence shows that the rental activity in question resulted in substantial losses in the years under appeal and that it has continued to result in losses up to the present time. Although no figures for the later year's losses were provided, the appellant testified that the financial results of the operation in those later years was similar to the financial performance from 2001 to 2003. The Appellant stated the property was used as a rental property by the person from whom he bought it, but there was no evidence to show the financial result of the vendor's rental operation in the years prior to 2001.

[6] The Appellant testified that he had previously owned two other rental properties in Australia prior to coming to Canada in 2001. He did not describe those properties other than to say that they were not the same as the Whistler condo because they were not vacation rentals. The Appellant did not say how long he owned those other properties or when he owned them. The Appellant's training and experience in business and finance was noted, but it was not explained how this might have related to the operation of a vacation rental property.

[7] The Appellant's intended course of action was to obtain rentals both by means of a website on which Whistler vacation properties were advertised for rent, and through word of mouth. He or his spouse reviewed other Whistler rental listings on the internet or made inquiries of agents or other people in order to set the rental rates, which were $1500 a night for peak season, $1200 a night for mid-season, and $800 a night for off-season. They chose not to use the services of an agent because of the high commissions that agents charged. The Appellant required a minimum stay of seven nights in peak season and five nights in other seasons to ensure maximum rental income and to lower cleaning costs.

[8] The Appellant also testified that he charged himself or his spouse rent at the full market rate for any use he or his family made of the unit. However, the evidence presented falls short of satisfying me that the rent was in fact paid by the appellant or paid to the Appellant by his spouse. No documentation was produced to corroborate this allegation, and the Appellant admitted that his spouse did not pay him the particular or specific amounts of rent attributed to her in certain schedules and documents prepared by her or the Appellant. The Appellant stated that a separate bank account was maintained for the Whistler property and that he and his spouse would deposit the money into the account as required to pay the expenses related to the property. The Appellant believed that deposits made to the account by a spouse were at least equal to the amounts of rent notionally attributed to her, and that they likely exceeded the notional rent amounts. However, no proof of the deposits was put before the court, and no accounting appears to ever have been done of the amounts paid into the account by the appellant's wife. I also note that the Appellant said that for the 2001 year, the deposits to the Whistler account would have been made by him or out of his funds. The Appellant's spouse was not called to corroborate the alleged payment of rent by her to the Appellant.

[9] Another observation that I would make regarding the Appellant's personal use of the property is that that use appears to have been more extensive than reported. The Appellant said he relied on his wife to keep track of its use, but, again, she was not called to testify. The telephone bills for the condominium were included in the Appellant's book of documents and show that the condominium was likely occupied at certain periods other than those indicated in Exhibit A-1, tab 37. Which lists the periods the condominium was occupied either by the Appellant and his family or by arm's-length parties. I refer to the telephone bills dated April 7th, 2002, February 7th, 2002, January 7th, 2002, August 7th, 2003, September 7th, 2003, and January 7th, 2004, which showed numerous long-distance calls made from the condominium on

days it was supposedly vacant. The Appellant's explanation that his spouse may have been at the cabin to oversee repairs or take delivery of furniture on those days appeared to me to be, at best, speculation on his part.

[10] I also refer to Exhibit A-1, tab 9, a letter from the cleaner to the Appellant's spouse, which includes the statement, "We didn't dust anything other than your bedroom because you're having a lot of children visit this weekend." I note that that letter is dated November 6, 2001, and Exhibit A-1, tab 37, the list of occupancy dates, does not show that the condo was occupied at any time during the month of November 2001 by the Appellant or his family.

[11] There was little evidence produced respecting the ability of the rental activity to show a profit. The purchase price of the property was $1.3 million and the Appellant financed the purchase with a $900,000 mortgage. The Appellant said that he would have had to reduce his interest expense on his mortgage in order to make a profit, but said that he had been unable to do so. He did not say what efforts he had made in this regard. I note, though, that the Appellant reported income in his 2001 to 2003 taxation years of between approximately 300,000 and 1.8 million dollars each year.

[12] The only analysis done by the Appellant of the property's potential to earn a profit from rentals was, in his own words, a “back-of-the-envelope kind of thing”, and particulars of that analysis were not provided at the hearing. No projections of income and expenses were presented. The Appellant referred to his expectation that rental rates would increase over time and that his major costs would remain fixed. But he also said that there had been increases in property taxes and utility bills since 2001. It also seems reasonable to expect that, as the condominium aged, repair bills and condo fees might increase. The Appellant also said that he was counting on the 2010 Olympic Games at Whistler to bring the rental operation into profitability.

[13] The Respondent contends that the Appellant placed too many restrictions or conditions on the rental of the condos, such as requiring a lengthy minimum stay, not taking credit cards and not confirming reservations within a reasonable time. The Appellant gave evidence that these conditions were similar to other properties in the area and were imposed to maximize revenue, reduce costs, and allow time for proper reference checks of potential renters rather than to discourage rentals.

[14] These conditions appear to me reasonable in the circumstances, subject to the observation that the Appellant might have considered modifying these and other requirements in order to stimulate rentals. The Appellant's “fussiness”, as he put it, in choosing to whom the condo was made available, is understandable but it was also quite apparent that the manner in which the operation was carried out was not producing acceptable commercial results. I refer to the fact the condo was rented to arm's-length parties five days over five months in 2001, nineteen days in 2002, and only eight days in 2003.

[15] The Appellant's failure to make changes to the operation to attempt to increase rentals is not reflective of a commercial operation. Possible changes might have included advertising the property more widely, making rental rates more competitive, or working with agents to find clients. The Appellant's assertion that the agents' commissions were too high seemed to ignore the possible increase in occupancy rate that could have been achieved and additional revenue that could have been earned if an agent were used. Similarly, the Commission of 5 of 6 percent payable on credit card sales may have been offset by increased rentals.

[16] The Appellant testified that the skiing conditions at Whistler were not good between 2001 and 2006, which may have led to lower rentals. Once again, no details of variations in snowfall were given, nor was any evidence led to demonstrate a general downturn in the tourism industry in Whistler over those years.

[17] Reference was made to possible effect of the SARS epidemic or the downturn in stock markets during the period. However, no dates were given by the Appellant for the outbreak of SARS, which appears to have occurred during in the spring of 2003. With respect to the downturn in the economy or the drop in the stock markets, the drop in the stock markets would have started in 2000, and therefore would have been something known to the Appellant prior to his purchase of the property.

[18] Overall I am not convinced that the rental losses were the result of unforeseen circumstances or unexpected adverse conditions.

[19] A further factor to be taken into account in assessing the commercial nature of the Appellant's operation is the Appellant's expectation of making a gain on the

eventual disposition of the property. The Supreme Court of Canada in Stewart said that this motive would not detract from the commerciality of a rental venture and might be a factor in assessing the overall course of a taxpayer's conduct. I take this to mean that the Appellant's intention to make a capital gain on the sale of the property must be balanced against all the other factors in assessing whether the Appellant's predominant intention in acquiring a property and renting it out was to earn a profit. In my view, the appellant has not succeeded in proving that this was his predominant intention. The Appellant did not show that he or anyone on his behalf undertook any serious evaluation of the profit potential of the property as a rental unit at the time he acquired it, despite his lack of experience in the particular market of vacation rentals, which he acknowledged to be a specialized market. Furthermore, the Appellant has not modified the way in which the rental operation has been carried out, despite ongoing losses, but instead has chosen simply to accept those losses as inherent in the operation.

[20] Finally I am left with the impression that the property as operated in the years under appeal and it continues to be operated, is unable to make a profit and will not be able to make a profit for many years to come.

[21] All of these factors, in combination with the significant personal use made of the property each year, convinces me that the Appellant's predominant intention with respect to the property was not to earn a profit. I find that the Appellant's intention to use the property for family recreation was at least equal to, if not greater than, any intention to make a profit from it. A reflection of this state of affairs may, perhaps, be found in Exhibit A-35, on the last page of the information relating to the property which was given to renters, which reads:

> "Although this list seems long and pedantic, it will help you to make the most of our home during your Whistler retreat. We sincerely hope you will enjoy your holiday in Whistler as much as we enjoy spending family time here throughout the year."

[22] Given my conclusions above, it is not necessary to deal with the Respondent's alternative arguments.

[23] For all these reasons the appeal is dismissed.

Signed at Ottawa, Canada, this 9th day of May 2007.

"Brent Paris"

Paris J.

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APPEARANCES:

Agent for the Appellant:	A.N. Nanji
Counsel for the Respondent:	J. Gibb-Carsley

COUNSEL OF RECORD:

For the Appellant:	
Name:	
Firm:	
For the Respondent:	John H. Sims, Q.C. Deputy Attorney General of Canada Ottawa, Canada