

Docket: 2007-1145(IT)I

BETWEEN:

LENORA P. FAGAN,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeals heard on August 7 and 8, 2007
at St. John's, Newfoundland and Labrador

Before: The Honourable Justice G. A. Sheridan

Appearances:

Agent for the Appellant: David Randell

Counsel for the Respondent: Selena Sit

JUDGMENT

In accordance with the attached Reasons for Judgment, the appeals of the assessments of the 1999, 2000 and 2001 taxation years are allowed, with costs fixed at \$200, and the assessments are referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that the Appellant is entitled:

1. to motor vehicle recapture income for 1999 in the amount of \$128.71;
2. to a capital loss in respect of the land allocation for the Elizabeth Property of \$1,293.01;
3. to have vacated in their entirety the "repeat failure to file" penalties under subsection 162(1) of the *Income Tax Act*;

4. to motor vehicle expenses of \$729.30 in 1999 and of \$380.32 in each of 2000 and 2001;
5. to an increase of \$600 in the interest expense allowed by the Minister;
6. to capital additions to the buildings on the three properties of 95 per cent of the amounts originally claimed by the Appellant for 1999, 2000 and 2001;
7. to a capital loss (building) for the Allandale property of \$272 and of \$5,996 for the Byron property. For the Elizabeth property, the capital loss (building) shall be calculated by adding \$1,362 to amounts shown for that property in the column entitled "Minister's Revised Position" in the chart in the *Minister's Revised Position for the Purpose of the Tax Court Hearing on August 7 and 8, 2007 in St. John's, Newfoundland before Justice Sheridan*, reproduced in paragraph 7(d), "Furniture Additions to the Properties and Calculation of Capital Losses (Building)", of these Reasons for Judgment;
8. to computer expenses of 20 per cent of the amount originally claimed by the Appellant;
9. to a business expense claim of \$600 in 2000 and \$250 in 2001 in respect of the washer and dryer.

Signed at Ottawa, Canada, this 20th day of August, 2007.

"G. A. Sheridan"

Sheridan, J.

Citation: 2007TCC478
Date: 20070820
Docket: 2007-1145(IT)I

BETWEEN:

LENORA P. FAGAN,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Sheridan, J.

[1] The Appellant, Lenora Fagan, is appealing the assessment of the Minister of National Revenue of her 1999, 2000 and 2001 taxation years. During those years, the Appellant owned, operated and ultimately disposed of three rental properties in St. John's, Newfoundland and Labrador: the "Elizabeth property", the "Allandale property" and the "Byron property". The Minister disallowed certain claims related to these properties, each of which is dealt with under the headings set out below.

[2] The Appellant was represented by her agent, Mr. David Randell, a Chartered Accountant, with nearly 30 years of accounting experience. Both the Appellant and Mr. Randell testified at the hearing. The Appellant was quite distressed, apparently the effect of having gone through a lengthy illness, the forced sale (at a loss) of her rental properties and the audit process itself. Her agitated state had an adverse effect on the clarity and precision of her evidence but I found her to be nonetheless truthful.

[3] Mr. Randell, by contrast, was entirely clearheaded and precise in the presentation of his testimony. He had acted as the Appellant's accountant for several years and also represented her throughout the auditor's review and the objection process. I found his evidence entirely convincing. Further, in cross-examining the Respondent's witness, he effectively demonstrated the weaknesses in the auditor's report that had formed the basis for the Minister's assessment.

[4] This last point, however, ought not to be construed as a criticism of Judy Moores who, as Team Leader for the Office Examination Division, was called

upon to replace the auditor and another official who had worked on the Appellant's file who, notwithstanding that the Notice of Hearing had been sent some three months prior, were not available at the time of the hearing. Ms. Moores became Team Leader in January 2005. As such, her duties included being available to discuss files with the auditors and signing off on their final reports. Though Ms. Moores was straightforward and helpful in her testimony, the force of her evidence was weakened by the fact that she simply had not been directly involved with the audit or the objection process. Accordingly, she had to rely on her understanding of the auditor's actions and her interpretation of her [the auditor's] notes and reports.

[5] At the conclusion of his cross-examination, Mr. Randell wished aloud that he had had the benefit of her assistance during the audit. I can only echo his sentiments; given their mutual respect for each other's roles and their capacity for listening and compromise, I am convinced they could have resolved without much difficulty what began as a relatively simple matter. Instead, the Appellant's file seems to have taken on a life of its own, becoming unnecessarily complicated, ultimately requiring a day and a half of litigation to sift through the sort of minutiae that is more appropriately reviewed at a meeting between auditor and taxpayer.

[6] By the close of the Appellant's case, however, some progress had been made. Counsel for the Respondent, Ms. Moores and Mr. Randell were able to resolve some of the items in dispute, on the terms set out below:

1. motor vehicle recapture income for 1999 is \$128.71;
2. capital loss in respect of the land allocation for the Elizabeth Property is increased from \$936.45 to \$1,293.01 (following the discovery of a departmental calculation error); and
3. the "repeat failure to file" penalties under subsection 162(1) of the *Income Tax Act* are vacated in their entirety.

[7] Turning now to the items remaining in issue, I make the following findings:

(a) Motor Vehicle Expenses 1999, 2000 and 2001

While I accept the Appellant's statement that she used her personal motor vehicle to some extent in her property rental business, the difficulty is that she did not keep a log of any kind to document the percentage of usage in each year; accordingly, she was unable to provide sufficient evidence to rebut the assumed motor vehicle expenses of \$729.30 in 1999 or to establish the expenses claimed for 2000 and 2001.

At the close of the Appellant's case, however, the Respondent conceded a motor vehicle expense amount of \$380.32 in each of 2000 and 2001, being a proportion of the amount allowed in 1999. These amounts are reasonable and are fixed accordingly.

(b) Mortgage Expenses for 1999

The Minister allowed all but \$600 of the \$6,933.78 claimed for mortgage expenses in 1999. The auditor refused to allow the full amount on the basis that the Appellant lacked the documentary evidence to show the \$600 had been paid for business interest. I accept the Appellant's evidence, however, that in addition to the interest paid on the mortgage, she paid interest on certain smaller business loans and lines of credit totalling \$1,300¹. I also accept as Mr. Randell's evidence regarding his general practices and procedures, and methods employed in the preparation of the Appellant's returns for the years in question. Accordingly, I have no reason to doubt his testimony that the amounts shown in Exhibit A-4 accurately reflect information he had gleaned from the Appellant's business records. The 1999 mortgage interest expense claim is therefore increased by \$600.

(c) Capital Additions to the Buildings in 1999, 2000 and 2001

The Minister disallowed 50 per cent of the amount claimed for capital additions to the Elizabeth, Allandale and Byron properties in 1999, 2000 and 2001. At the close of the Appellant's case, counsel for the Respondent conceded that the allowable amounts ought to be increased from 50 per cent to not more than 75 per cent, arguing that the documents relied upon by the Appellant fell short of justifying the full amounts claimed. Given the relative insignificance of the alleged flaws in the documentation, the reasonableness of the explanations for such deficiencies, the large number of receipts provided, the questionable accuracy of the auditor's conclusions and her (apparent) unwillingness to accede to Mr. Randell's repeated requests to identify and address her concerns, I am not completely persuaded by the Respondent's submission. However, allowing a small percentage for error, I am satisfied that, on balance, there is sufficient evidence to support the Appellant's entitlement to 95 per cent of the capital addition amounts originally claimed in respect of the three properties.

¹ Exhibit A-4 – Copy of 1999 Interest Expense Working Papers for Mr. Randell.

(d) Furniture Additions to the Properties and Calculation of Capital Losses (Building)

At the close of the Appellant's case, counsel for the Respondent advised the Court that the Respondent had revised the amounts the Minister was prepared to allow in respect of furniture which had been acquired for use in the partially furnished rental properties and which was ultimately sold as part of each rental property. The revised figures were provided for the Court's reference in a document entitled *Minister's Revised Position for the Purpose of the Tax Court Hearing on August 7 and 8, 2007 in St. John's, Newfoundland before Justice Sheridan*, the relevant portion of which is set out below:

Allandale Property

Item	Claimed by Appellant as set out in Exhibit A1	Minister's Revised Position	Comments
Furniture in house at time of conversion	\$4,700	\$2,257	Based on depreciation at 20% for Class 8 assets
Capital additions - 1998	\$1,985	\$1,985	
Sears – washer	\$530	\$530	
TOTAL	\$7,215	\$4,772	
Allocation upon disposition based on FMV	(\$4,500)	(\$4,500)	
Loss	\$2,715	\$272	

Elizabeth Property

Item	Claimed by Appellant as set out in Exhibit A3	Minister's Revised Position	Comments
Fridge	\$1,362	\$0	Per Mr. Randall's testimony
Bowring furniture, curtains,bedspreads	\$1,182	\$236	Receipt at E7 shows only 1 final amount
Endtables/entertainment centre	\$297	\$297	
Used furniture	\$5,000	\$5,000	
TOTAL	\$7,841	\$5,533	
Allocation upon disposition based upon FMV	(\$4,000)	(\$4,000)	
Loss	\$3,841	\$1,533	

Byron Property

Item	Claimed by Appellant as set out in Exhibit A2	Minister's Revised Position	Comments
Furniture in house at time of conversion	\$9,950	\$7,650	Reduced by 50% the items for dining room and fridge/stove at B3
Capital expenditures in preparation for rental	\$1,086	\$1,086	
Capital additions – 1993	\$1,710	\$1,710	
Sears – dryer	\$469	\$469	
Bombay Co. – desk	\$598	\$0	Not reasonable
Bombay Co.	\$322	\$0	Not reasonable
Grand Warehouse	\$956	\$956	
Used washer	\$125	\$125	
Fridge	\$1,362	\$0	Per Mr. Randall's testimony
TOTAL	\$16,578	\$11,996	
Allocation upon disposition based upon FMV	(\$6,000)	(\$6,000)	
Loss	\$10,578	\$5,996	

In my view, for the Allandale and Byron properties, the Appellant has not presented sufficient evidence to challenge the figures shown in the column "Minister's Revised Position" in the chart above. Accordingly, the Appellant is entitled to a capital loss (building) of \$272 and \$5,996, respectively.

For the Elizabeth property, however, a further adjustment is required. In reviewing his papers during the course of the hearing, Mr. Randell realized that he had inadvertently shown an amount of \$1,362 (for the same fridge) in each of the Elizabeth and Byron properties² and conceded that it ought to be deleted from one of the properties. A review of the figures contained in the chart above for the Elizabeth and Byron properties in the "Minister's Revised Position" column reveals that this amount has been deleted from *both* properties, thereby disallowing any amount for the fridge. In my view, this is not correct. Accordingly, in the calculation of the capital loss (building) for the Elizabeth property, the amount of \$1,362 shall be added to the amounts shown in the "Minister's Revised Position" column for that property.

² Exhibits A-2 and A-3.

(e) Computer

The Appellant claimed certain expenses in respect of the purchase of a computer, printer and computer-related items. The auditor rejected her claim on the basis that there was no proof that the computer had been used in the Appellant's rental business. According to her own evidence, the Appellant relied on Mr. Randell for the preparation of her accounting books and records; what records she kept herself were more likely to have been handwritten. Further, there was no evidence of her having possessed or used any accounting software for the computer. Nonetheless, I am satisfied that the Appellant used the word processing function of the computer and the other equipment for such things as business correspondence, invoicing, drafting rental advertisements and so on. Accordingly, the computer expenses are allowed to the extent of 20 per cent of the amount claimed by the Appellant.

(f) Washer and Dryer

As the above heading illustrates, if ever there was a file that cried out for meetings between the auditor and the taxpayer, it was this one. In any event, having carefully reviewed the evidence of the Appellant's business transactions, I am satisfied on a balance of probabilities that the Appellant has successfully made her case for the washer and dryer expenses that were rejected by the auditor. I accept the Appellant's evidence that the dryer was bought second-hand and its repeated malfunction necessitated the rental of another dryer. Thus, the claim of both the purchase price and the rental cost during the same period was not a duplication of an expense as assumed by the auditor. The Appellant's claims of \$600 in 2000 and \$250 in 2001 are allowed.

Conclusion

[8] The Appellant asked for a range of other relief, including action against the alleged bad behaviour of certain officials, a guarantee of fair treatment from the Canada Revenue Agency in the future and the recovery of business income and interest lost during the audit review period. As explained to her at the hearing, none of this is within the Court's jurisdiction.³

[9] Another sore point for the Appellant was the collapse and seizure of her RRSP accounts by the Collections Division of the Canada Revenue Agency. Not only did

³ *Main Rehabilitation Co. Ltd. v. Her Majesty the Queen*, [2005] 1 C.T.C. 212 (F.C.A.).

this deplete entirely the Appellant's life savings, it triggered a fresh tax liability. Quite apart from these fiscal repercussions, it caused no small amount of anxiety to the Appellant who is in her 60's and a widow. According to the Appellant, she had been assured by the Collections officials that her RRSP's would not be touched during the objection stage. The Appellant testified that, had she been informed otherwise, she would have borrowed money to reduce her tax liability, thus avoiding the drastic consequences of having her RRSP's cashed in. She ended up having to borrow the funds needed when in 2004, the department ultimately allowed her to restore to some extent her RRSP account for that year. (According to the Appellant, similar administrative relief was denied in 2005.) It may be that there is another side to this story but there was no one from the CRA in a position to challenge the Appellant's allegations. In any event, it is beyond the power of this Court to provide any remedy in this regard to the Appellant. I include her version of events here only because it is consistent with the other evidence of the rather rough treatment accorded to the Appellant over the course of the review.

[10] Finally, the Appellant asked for costs to cover, among other things, her accountant's fees which, as of the date of this hearing, Mr. Randell estimated would be over \$10,000. These appeals were heard under the Informal Procedure and accordingly, an order for costs of that magnitude would not be appropriate. Quite apart from that, no matter how able an agent may be, costs for taxable fees are restricted to legal counsel⁴. In the circumstances of this case, however, I am satisfied that an award of costs is justified at least to help defray the cost of the preparation and production of documents in support of the same claims she ought reasonably to have been allowed to present to the auditor. Had she been given that opportunity, such costs (never mind the cost of having Mr. Randell prepare for and attend at a hearing of a day and a half's duration) might well have been avoided.

[11] The appeals are allowed, with costs fixed at \$200, and the assessments are referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that the Appellant is entitled:

1. to motor vehicle recapture income for 1999 in the amount of \$128.71;
2. to a capital loss in respect of the land allocation for the Elizabeth Property of \$1,293.01;

⁴ *Munro v. Her Majesty the Queen*, [1998] 4 C.T.C. 89 (F.C.A.).

3. to have vacated in their entirety the "repeat failure to file" penalties under subsection 162(1) of the *Income Tax Act*;
4. to motor vehicle expenses of \$729.30 in 1999 and of \$380.32 in each of 2000 and 2001;
5. to an increase of \$600 in the interest expense allowed by the Minister;
6. to capital additions to the buildings on the three properties of 95 per cent of the amounts originally claimed by the Appellant for 1999, 2000 and 2001;
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Signed at Ottawa, Canada, this 20th day of August, 2007.

"G. A. Sheridan"

Sheridan, J.

CITATION: 2007TCC478
COURT FILE NO.: 2007-1145(IT)I
STYLE OF CAUSE: LENORA P. FAGAN AND HER MAJESTY
THE QUEEN
PLACE OF HEARING: St. John's, Newfoundland and Labrador
DATE OF HEARING: August 7 and 8, 2007
REASONS FOR JUDGMENT BY: Justice G. A. Sheridan
DATE OF JUDGMENT: August 20, 2007

APPEARANCES:

Agent for the Appellant: David Randell

Counsel for the Respondent: Selena Sit

COUNSEL OF RECORD:

For the Appellant:

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