

Docket: 2008-1964(IT)I

BETWEEN:

ROGER S. LEWIN,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on October 24, 2008, at Edmonton, Alberta
Before: The Honourable Justice Wyman W. Webb

Appearances:

Agent for the Appellant: Forrest J.R. Wright
Counsel for the Respondent: Robert Neilson

JUDGMENT

The appeal from the assessment made under the *Income Tax Act* for the Appellant's 2004 taxation year is allowed, with costs, and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that the Appellant is entitled to deduct the \$8,146 that he incurred in replacing the deck as an expense in computing his income for 2004.

Signed at Ottawa, Ontario, this 13th day of November 2008.

“Wyman W. Webb”

Webb J.

Citation: 2008TCC618
Date: 20081113
Docket: 2008-1964(IT)I

BETWEEN:

ROGER S. LEWIN,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Webb J.

[1] The issue in this appeal is whether the amount incurred by the Appellant to replace a deck attached to his rental property was deductible in computing his income for 2004 or whether this amount was a capital expenditure and should be added to the capital cost of the rental property.

[2] The Appellant is a medical doctor who was practicing in Alberta. In 2003 he purchased a house in British Columbia as a rental property with a view to eventually retiring and moving to this property. After 2004 and prior to this hearing the Appellant did relocate to this property.

[3] Prior to purchasing the property he arranged to have the property inspected. The inspection report stated that parts of the deck that was attached to the house were rotting and that work would have to be done to repair the deck. The estimated cost of the repairs was \$1,200.

[4] Following the purchase of the property, the tenants raised concerns about the condition of the deck and the Appellant arranged to have a contractor provide an estimate of the cost of replacing the deck. The estimated cost to replace the deck, including GST, was \$8,627. When the work was actually completed, the Appellant

received credit for some items that did not need to be replaced and additional charges for changes that were made. The total cost of replacing the deck was \$8,146.30. The Appellant claimed this amount as an expense in computing his income for 2004. The position of the Respondent is that this amount should be added to the capital cost of the building and not deducted as a current expense.

[5] Justice Lamarre Proulx of this Court in *Bergeron v. Minister of National Revenue*, [1990] 2 C.T.C. 2220, 90 DTC 1505 reviewed several cases that dealt with the issue of whether amounts incurred for repairs / renovations would be deductible as a current expense or should be added to the capital cost of the asset. In paragraph 20 of this case she listed the cases that she had reviewed and these were as follows:

- *Minister of National Revenue v. Vancouver Tug Boat Company Ltd.*, [1957] Ex. C.R. 160, [1957] C.T.C. 178, 57 D.T.C. 1126;
- *Thompson Construction (Chemong) Ltd. v. Minister of National Revenue*, [1957] Ex. C.R. 96, [1957] C.T.C. 155, 57 D.T.C. 1114;
- *Minister of National Revenue v. Haddon Hall Realty Inc.*, [1962] S.C.R. 109, [1961] C.T.C. 509, 62 D.T.C. 1001;
- *Canada Steamship Lines Ltd. v. Minister of National Revenue*, [1966] Ex. C.R. 972, [1966] C.T.C. 255, 66 D.T.C. 5205;
- *Minister of National Revenue v. Algoma Central Railway*, [1968] S.C.R. 447, [1968] C.T.C. 161, 68 D.T.C. 5096;
- *Dubé et al. v. Minister of National Revenue*, [1979] C.T.C. 2241, 79 D.T.C. 10;
- *Shabro Investments Ltd. v. The Queen*, [1979] C.T.C. 125, 79 D.T.C. 5104;
- *Healey v. Minister of National Revenue*, [1984] C.T.C. 2004, 84 D.T.C. 1017;
- *S. Coleman v. Minister of National Revenue*, [1984] C.T.C. 2725, 84 D.T.C. 1637;
- *Johns-Manville Canada Inc. v. The Queen*, [1985] 2 S.C.R. 46, [1985] 2 C.T.C. 111, 85 D.T.C. 5373;
- *A.B. Wager v. Minister of National Revenue*, [1985] 1 C.T.C. 2208, 85 D.T.C. 222;
- *J. Méthé v. Minister of National Revenue*, [1986] 1 C.T.C. 2493, 86 D.T.C. 1360;
- *Québec (Sous-ministre du revenu) v. Goyer*, [1987] R.D.F.Q. 159;
- *Gold Bar Developments Ltd. v. The Queen* (1987), 9 F.C. 303, [1987] 1 C.T.C. 262, 87 D.T.C. 5152;
- *Damon Developments Ltd. v. Minister of National Revenue*, [1988] 1 C.T.C. 2266; 88 D.T.C. 1128.

[6] After reviewing these cases, Justice Lamarre Proulx stated as follows:

33 The principles I draw from these cases are the following:

income-related expenses include repairs the purpose of which is to make the part or the property repaired suitable for normal use again;

capital expenses include work the purpose of which is to replace an asset by a new one and work which involves such a degree of improvement to an asset that it becomes a new one. This asset must have significant value compared to the rest of the property or be an asset in itself; work to change the use of premises or a room or to add new premises or a new room is usually capital in nature; the same is true of a change in the heating system;

although the factor of recent purchase is not significant when there is no change of use, the increase in value of the real property over the purchase price, as a result of the repairs, is an indication that the cost or part of the cost of the expenses is in the nature of the purchase price of property;

expenses must also be reasonable in the circumstances (section 67 of the Act): the question is whether they were reasonably incurred to derive income or to increase the value of the property, and in what proportion; future profits can be taken into account if the expenses in question reduce subsequent expenses and also I suppose the unforeseen scale of the costs.

[7] Justice Brulé of this Court in *Marklib Investments II-A Ltd. v. The Queen*, [2000] C.T.C. 2513, 2000 DTC 1413, reviewed the following cases in relation to whether expenditures incurred for repairs were operating expenses:

- *B.P. Australia Ltd. v. Commissioner of Taxation of Australia* (1965), [1966] A.C. 224, [1965] 3 All E.R. 209 (Australia P.C.)
- *British Insulated & Helsby Cables Ltd. v. Atherton* (1925), [1926] A.C. 205, 10 T.C. 155, [1925] All E.R. 623 (U.K. H.L.)
- *Canada Steamship Lines Ltd. v. Minister of National Revenue*, [1966] Ex. C.R. 972, [1966] C.T.C. 255, 66 D.T.C. 5205 (Can. Ex. Ct.)
- *Canaport Ltd. v. R.*, (*sub nom. Canaport Ltd. v. Canada*) [1993] 2 C.T.C. 2830, 93 D.T.C. 1226 (T.C.C.)
- *Chambers v. R.* (1997), [1998] 1 C.T.C. 3273 (T.C.C.)
- *Earl v. R.* (1992), (*sub nom. Earl v. Canada*) [1993] 1 C.T.C. 2081, 93 D.T.C. 65 (T.C.C.)
- *Gold Bar Developments Ltd. v. R.*, 87 D.T.C. 5152, [1987] 1 C.T.C. 262, (*sub nom. Gold Bar Devs. Ltd. v. M.N.R.*) 9 F.T.R. 303 (Fed. T.D.)
- *Healey v. Minister of National Revenue* (1983), [1984] C.T.C. 2004, 84 D.T.C. 1017 (T.C.C.)

- *Johns-Manville Canada Inc. v. R.*, [1985] 2 S.C.R. 46, 85 D.T.C. 5373, [1985] 2 C.T.C. 111, 21 D.L.R. (4th) 210, 60 N.R. 244 (S.C.C.)
- *Méthé v. Minister of National Revenue*, 86 D.T.C. 1360 (Eng.), 86 D.T.C. 1364 (Fr.), [1986] 1 C.T.C. 2493 (T.C.C.)
- *Minister of National Revenue v. Haddon Hall Realty Inc.* (1961), [1962] S.C.R. 109, [1961] C.T.C. 508, 62 D.T.C. 1001, 31 D.L.R. (2d) 201 (S.C.C.)
- *Morel v. Minister of National Revenue* (1951), 51 D.T.C. 431, 5 Tax A.B.C. 213, 1951 CarswellNat 190 (Can. Tax App. Bd.)
- *Québec (Sous-ministre du Revenu) c. Goyer*, [1987] R.J.Q. 988, 10 Q.A.C. 70, [1987] R.D.F.Q. 159 (Que. C.A.)
- *Shabro Investment Ltd. v. R.*, [1979] C.T.C. 125, 79 D.T.C. 5104, 28 N.R. 327 (Fed. C.A.)
- *Wager v. Minister of National Revenue*, 85 D.T.C. 222, [1985] 1 C.T.C. 2208 (T.C.C.)

[8] It is interesting to note that while several of the cases that were reviewed by Justice Lamarre Proulx were also reviewed by Justice Brulé, there is no reference to *Bergeron* in the decision of Justice Brulé. After reviewing the cases, Justice Brulé stated as follows:

34 This Court is unable to find the relevance of a number of cases the respondent relied on in his argument. The respondent relied on cases involving newly-acquired buildings in poor condition, the need of repairs to get the building operational, and payment of a decreased purchase price because of the building's poor condition. All of the above cases are distinguishable from the case at bar as all involved the taxpayer acquiring or purchasing a deteriorated property. The taxpayers knew the state and condition of the property upon acquisition. I have to wonder whether the respondent is extracting the reasoning out of the cases and erecting it into general principles without taking into consideration the specific facts of the cases. If there is one thing that is established through the case law, I think it is that, to determine the question of current or capital, the facts specific to the particular situation must be examined and given some weight.

35 It is the purpose, rather than the result, of an expenditure that determines whether it is characterized as a capital outlay or a current expense; and the focus of the test is on whether or not the expenditure brings into existence an asset of enduring value, rather than on the determination of the frequency or recurrence of the expenditure. The cases seem to promote the idea that as long as the repairs were done to preserve or conserve the asset and not to create a new asset then the repairs will be considered current expenses.

36 An expenditure that merely maintains an asset or restores it to its original condition is a deductible current expense. As already seen from the cases above, this is easier said than done. There is a lot of grey area in between the capital outlay and current expense distinction. Furthermore, the magnitude of the expense must be examined in the context of the value of the building. However, simply because the amount of money expended is significant does not in itself render the expenditure capital in nature.

37 There is no one test for determining whether the expenditure is of a capital nature or a current nature. A number of factors and circumstances are to be examined and weighed.

[9] Justice Brulé also referred to *Interpretation Bulletin - IT128R - Capital Cost Allowance - Depreciable Property*. Paragraph 4 of this Interpretation Bulletin provides as follows:

Capital Expenditures on Depreciable Property versus current Expenditures on Repairs and Maintenance

4. The following guidelines may be used in determining whether an expenditure is capital in nature because depreciable property was acquired or improved, or whether it is currently deductible because it is in respect of the maintenance or repair of a property:

(a) Enduring Benefit — Decisions of the courts indicate that when an expenditure on a tangible depreciable property is made “with a view to bringing into existence an asset or advantage for the enduring benefit of a trade”, then that expenditure normally is looked upon as being of a capital nature. Where, however, it is likely that there will be recurring expenditures for replacement or renewal of a specific item because its useful life will not exceed a relatively short time, this fact is one indication that the expenditures are of a current nature.

(b) Maintenance or Betterment — Where an expenditure made in respect of a property serves only to restore it to its original condition, that fact is one indication that the expenditure is of a current nature. This is often the case where a floor or a roof is replaced. Where, however, the result of the expenditure is to materially improve the property beyond its original condition, such as when a new floor or a new roof clearly is of better quality and greater durability than the replaced one, then the expenditure is regarded as capital in nature. Whether or not the market value of the property is increased as a result of the expenditure is not a major factor in reaching a decision. In the event that the expenditure includes both current and capital elements and these can be identified, an appropriate allocation of the expenditure is necessary. Where only a minor part of the expenditure is of a capital nature, the Department is prepared to treat the whole as being of a current nature.

(c) Integral Part or Separate Asset — Another point that may have to be considered is whether the expenditure is to repair a part of a property or whether it is to acquire a property that is itself a separate asset. In the former case the expenditure is likely to be a current expense and in the latter case it is likely to be a capital outlay. For example, the cost of replacing the rudder or propeller of a ship is regarded as a current expense because it is an integral part of the ship and there is no betterment; but the cost of replacing a lathe in a factory is regarded as a capital expenditure, because the lathe is not an integral part of the factory but is a separate marketable asset. Between such clear-cut cases there are others where a replaced item may be an

essential part of a whole property yet not an integral part of it. Where this is so, other factors such as relative values must be taken into account.

(d) Relative Value — The amount of the expenditure in relation to the value of the whole property or in relation to previous average maintenance and repair costs often may have to be weighed. This is particularly so when the replacement itself could be regarded as a separate, marketable asset. While a spark plug in an engine may be such an asset, one would never regard the cost of replacing it as anything but an expense; but where the engine itself is replaced, the expenditure not only is for a separate marketable asset but also is apt to be very substantial in relation to the total value of the property of which the engine forms a part, and if so, the expenditure likely would be regarded as capital in nature. On the other hand, the relationship of the amount of the expenditure to the value of the whole property is not, in itself, necessarily decisive in other circumstances, particularly where a major repair job is done which is an accumulation of lesser jobs that would have been classified as current expense if each had been done at the time the need for it first arose; the fact that they were not done earlier does not change the nature of the work when it is done, regardless of its total cost.

[10] In this particular case, the Appellant was simply replacing a deck that was 20 years old and that needed to be replaced. The deck was restored to its original condition with some changes. The previous deck had a fiberglass covering to protect the surface of the deck from the elements and the new deck had a vinyl covering to protect the surface from the elements. As well vinyl lattice instead of wood lattice was used in the area below the deck, a concrete step was installed instead of a wooden step, aluminum railings were used instead of wood railings and a vented soffit was installed under the walkway.

[11] As noted by Justice Brulé when he was referring to the decision of Justice Jerome in *Gold Bar Developments Ltd.*:

22 Mr. Justice Jerome found that it was the intention of the taxpayer to repair a condition which had become dangerous rather than to improve the asset. Because the plaintiffs in the case went beyond answering the defects, and made the building not only fully resistant to the problem of falling bricks, but also substantially improved the building's appearance does not necessarily make the expenditure capital in nature. Once the decision to repair is forced upon the taxpayer, he does not have to ignore advancements in building techniques and technology in carrying out the work. However, Mr. Justice Jerome examined the building's value at the material time compared to the sum expended on repairs and it was found that the sum in issue represented less than 3% of the value of the asset. Therefore there was no issue of the expenditure being so substantial as to constitute a replacement of the asset. Not to mention that Mr. Justice Jerome found that the structure of the building remained unchanged.

[12] There was no indication in this case whether the fiberglass covering that was used when the original deck was built was still available in 2004. The Appellant stated that the material that was generally being used to cover the floor surface area of decks in 2004 was a vinyl material. Therefore the vinyl covering would simply be the equivalent material that was available in 2004.

[13] The other changes are, in my opinion, not significant changes to the deck and should not affect the determination of whether the amount spent on replacing the deck should be considered to be a capital expenditure or a current expense.

[14] The Appellant stated that the cost of the aluminum railings was approximately the same as the wooden railings. The cost of the vinyl lattice and the vented soffit were less than \$370 (including GST). The deck, based on the pictures that were submitted into evidence, appears to be less than 2 feet above the ground along the back and the vinyl lattice simply covers the opening from the deck to the ground. The cost of the concrete step was not provided. It was only a single step made from concrete poured into a wooden frame. It does not seem reasonable that the cost of the concrete step would be a significant part of the \$8,146 cost.

[15] The Appellant paid \$259,000 to acquire the rental property in 2003. The amount spent on replacing the deck was \$8,146 which is approximately 3.1% of the total cost of the property. The deck is not a separate asset but attached to and part of the rental building. Although the Appellant knew that the deck would have to be repaired before he bought the property and the price paid may have reflected this estimated cost, at that time the estimate was only \$1,200 to repair the deck which is less than 1% of the purchase price of \$259,000 and therefore would not have resulted in a significant reduction in the purchase price.

[16] As a result, in my opinion, the amount incurred by the Appellant to replace the deck in 2004 was a current expense that was deductible by the Appellant in computing his income for 2004.

[17] The appeal is allowed, with costs, and the matter is referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that the Appellant is entitled to deduct the \$8,146 that he incurred in replacing the deck as an expense in computing his income for 2004.

Signed at Ottawa, Ontario, this 13th day of November 2008.

“Wyman W. Webb”

Webb J.

CITATION: 2008TCC618

COURT FILE NO.: 2008-1964(IT)I

STYLE OF CAUSE: ROGER S. LEWIN AND HER MAJESTY
THE QUEEN

PLACE OF HEARING: Edmonton, Alberta

DATE OF HEARING: October 24, 2008

REASONS FOR JUDGMENT BY: The Honourable Justice Wyman W. Webb

DATE OF JUDGMENT: November 13, 2008

APPEARANCES:

Agent for the Appellant: Forrest J.R. Wright
Counsel for the Respondent: Robert Neilson

COUNSEL OF RECORD:

For the Appellant:

Name:

Firm:

For the Respondent:

John H. Sims, Q.C.
Deputy Attorney General of Canada
Ottawa, Canada