Docket: 2007-4950(IT)G

BETWEEN:

MICHEL TREMBLAY,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

Appeal heard on November 3, 2009, at Chicoutimi, Quebec.

Before: The Honourable Justice Paul Bédard

Appearances:

Counsel for the Appellant :	Éric Le Bel
Counsel for the Respondent:	Sylvain Ouimet

JUDGMENT

The appeal from the reassessment made under the *Income Tax Act* for the 1999 taxation year is dismissed, with costs, in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Canada, this 9th day of February 2010.

"Paul Bédard"

Bédard J.

Translation certified true
on this 28th day of May 2010.

Erich Klein, Revisor

Citation: 2010 TCC 79
Date: 20100209
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BETWEEN:

MICHEL TREMBLAY,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

[OFFICIAL ENGLISH TRANSLATION]

REASONS FOR JUDGMENT

Bédard J.

[1] This is an appeal from a reassessment made on April 19, 2004, under the *Income Tax Act* ("the Act") by the Minister of National Revenue ("the Minister") against the Appellant for his 1999 taxation year. By this reassessment, the Minister added, among other things, a taxable capital gain of $200,901 to the Appellant's income.

Background

[2] In 1986, the Appellant built two contiguous buildings located at 940 and 950 Thérèse-Casgrain Street, in the city of Saguenay ("the Property"). At the time, the cost of the land was $46,874 and the cost of the buildings was $785,258. Each building had 16 rental units on three floors and a half basement. On March 31, 1999, by notarized contract (see Exhibit I-1, Tab 6), the Appellant transferred the Property by voluntary surrender to 9060-8027 Québec Inc., whose majority shareholder at the time was Jean-Eudes Tremblay, the Appellant's brother. The Minister contends that the fair market value (FMV) of the Property as at March 31, 1999, was $1,100,000, whereas the Appellant maintains that it was $912,000.

Issue

[3] The only issue to be decided is whether the Minister properly determined that the Property's FMV as at March 31, 1999, was $1,100,000.

Testimony

[4] The Appellant testified. Ghislain Ruest, the Appellant's expert witness on real estate appraisal, testified in support of the Appellant's position. The Respondent's only witness was Yvon Bergeron, the Respondent's real estate appraisal expert.

Preliminary remarks

[5] I would immediately note that Mr. Ruest's appraisal report (Exhibit A-1) states that the Property's FMV in February 2001 was $912,000, based on the direct comparison method rather than the income or cost methods of valuation. I would also note that this appraisal report was prepared by Mr. Ruest at the request of Jean-Eudes Tremblay (the Appellant's brother) and was used by Jean-Eudes Tremblay during his dispute with the Canada Customs and Revenue Agency ("the Agency") concerning the FMV of the Property at the time it was transferred in February 2001 by 9060-8027 Québec Inc. to Jean-Eudes Tremblay. The Appellant claims that, in its dispute with Jean-Eudes Tremblay, the Agency admitted that the FMV of the Property in February 2001 was $912,000. Therefore, the Appellant argues, the Court should accept the conclusions in Mr. Ruest's appraisal report (Exhibit A-1) because the market conditions in 2001 were the same as they were in 1999.

[6] In the case at bar, Mr. Ruest used 11 real estate transactions for the purposes of his analysis. The transactions had the following characteristics, among others:

	Location	Number of dwelling units	Date of transaction
Subject property	940-950 Thérèse-Casgrain Street, Chicoutimi	Multi-family	
Building 1	2288 des Roitelets Street, Chicoutimi	4 units (4½ rooms each)	18/11/2002
Building 2	457 Bécard Street, Chicoutimi	8 units (2½ rooms to 4½ rooms)	27/12/2002
Building 3	1420-26 Alphonse-Desjardins St., Chicoutimi	4 units (4½ rooms each)	28/11/2002
Building 4	1291-1293 Renaud Street, Chicoutimi	11 units (3½ rooms each)	05/04/2002
Building 5	64 Paquet Street, Chicoutimi	8 units (3½ rooms to 5¼ rooms)	22/10/2002
Building 6	733 des Hospitalières Street, Chicoutimi	6 units (4½ rooms each)	27/12/2002
Building 7	980 St-Judes Street, Alma	16 units (4½ rooms each)	01/11/2002
Building 8	2260 St-Jérôme Street, Jonquière	10 units (3½ rooms and 5½ rooms)	05/04/2004
Building 9	763 des Hospitalières Street, Chicoutimi	13 units	16/05/2002
Building 10	708 Dequen Street, Alma	24 units (4½ rooms each)	11/12/2002
Building 11	2530-2532 du Perche Street, Jonquière	12 units (3½ rooms and 4½ rooms)	12/04/2002

[7] The Appellant submits that Mr. Bergeron's determination of the FMV of the Property as being $1,100,000 does not take the condition of the Property into account, and should be reduced by at least $200,000 in view of how badly rundown the Property was in 1999.

[8] Mr. Bergeron's appraisal report (Exhibit I-2) puts the FMV of the Property as at March 31, 1999 at $1,100,000. This value was determined using the direct comparison method. I note that Mr. Bergeron excluded the income method in determining the Property's FMV because there was very little reliable information regarding the income and expenses associated with the rental activities involving the Property. Lastly, I note that Mr. Bergeron ruled out the cost method because the Chicoutimi area real estate market was relatively active during the appraisal period.

[9] For the purposes of his analysis, Mr. Bergeron used 11 transactions involving buildings which had the following characteristics, among others:

	Location	Number of dwelling units	Date of transaction
Building 1	Place des Écorceurs, Saguenay	6 buildings of 16 units each (48 units with 4½ rooms and 48 units with 5½ rooms)	02/08/1995
Building 2	750A-750B Georges-Vanier Street, Saguenay	32 units	19/04/1996
Building 3	130 Des Écorceurs St., Saguenay	16 units, of which 8 have 4½ rooms and 8 have 5½ rooms	01/03/1996
Building 4	70 Des Écorceurs St., Saguenay	16 units, of which 8 have 4½ rooms and 8 have 5½ rooms	01/05/1996
Building 5	120 Des Écorceurs St., Saguenay	16 units, of which 8 have 4½ rooms and 8 have 5½ rooms	01/10/1997
Building 6	731 Alma Street, Saguenay	30 units, of which 6 have 2½ rooms and 24 have 3½ rooms	26/09/1997
Building 7	1775-1825 Tadoussac Street, Saguenay	6 buildings of 4 units each (16 units with 4½ rooms and 16 units with 5½ rooms)	27/03/1998
Building 8	1675-1715 Tadoussac Street, Saguenay	4 buildings of 4 units each (8 units with 4½ rooms and 8 units with 5½ rooms)	27/03/1998
Building 9	291 Rimbaud Street, Saguenay	12 units (4½ rooms each)	16/07/1999
Building 10	1246-1256 Roitelet St., Saguenay	36 units, of which 9 have 3½ rooms and 27 have 4½ rooms	08/10/1999
Building 11	1240 Lorenzo-Genest Street, Saguenay	16 units, of which 9 have 4½ rooms and 7 have 5½ rooms	08/10/1999

The Appellant's testimony

[10] The Appellant testified as follows:

(i) During the two years preceding its sale, the Property was managed by the holder of the hypothec thereon (the Laurentian Bank of Canada), which it did from Quebec City. The Appellant explained that the Laurentian Bank ("the Bank") just collected the rent during that period. The Appellant pointed out that the Property was very rundown on March 31, 1999, since the Bank had done no repairs or maintenance during the two-year period in question. The Appellant added that, owing to the Bank's neglect, the Property's vacancy rate was 45% on March 31, 1999, and the only new tenants during that two-year period were social assistance recipients. I immediately note that a rental income and expense forecast for the year 1998 (Exhibit I-1, Tab 4) prepared by the Appellant's accountants suggests that the anticipated vacancy rate for 1998 was roughly 5%.

(ii) 9060-8027 Québec Inc. had to invest roughly $200,000 in the Property [TRANSLATION] "to fix it up and make it rentable again, and just about the whole lot of tenants was changed" (see paragraph 79 of the transcript, at page 30.) I note that the Appellant did not specify the nature of the work done by the company controlled by his brother, that he did not specify the period in which the work was done, and, lastly, that he provided no supporting documents in this regard.

(iii) The condition of the Property on February 1, 2001 (the date on which Property was transferred by 9060-8027 Québec Inc. to Jean-Eudes Tremblay at a price of $912,000) was the same as it was on March 31, 1999, and this is why the Appellant decided to use the appraisal report (Exhibit A-1) that Mr. Ruest had prepared (at his brother Jean-Eudes's request) for the purpose of determining the FMV of the Property on February 1, 2001, when it was transferred by 9060-8027 Québec Inc. to his brother Jean-Eudes.

Analysis and conclusion

[11] When sufficient market data exist, the FMV of real estate is estimated using three conventional methods: the cost method, the direct comparison method and the income method. The cost method is based primarily on the principle of substitution,

which posits that an informed purchaser will not pay more for a building than the cost of building a similar one, provided there are no costly delays at the time of the substitution. The direct comparison method is also based on the principle of substitution, which holds that an informed purchaser would pay no more for a property than it would cost to purchase a comparable property. In other words, the direct comparison approach essentially consists in using as a reference point the selling prices of properties that have similar characteristics, are located as close as possible to the property to be appraised, and are sold as close as possible to the relevant appraisal date. The income method is based essentially on the principle of present value capitalization, and is the most appropriate method for valuing income-producing property. The basis of this method is the relationship between the net income generated, its future value, and the value of the property.

[12] In my opinion, the two experts used the right valuation method to determine the Property's FMV given the circumstances. Moreover, I note immediately that, for the reasons set out below, I do not find Mr. Ruest's analysis and conclusions credible:

(i) First of all, as we have seen, Mr. Ruest's report (Exhibit A-1) determines the FMV of the Property as at February 1, 2001, not March 31, 1999. Mr. Ruest explained that this fact is not relevant in the case at bar because the market conditions in 2001 were the same as they were in 1999. Even as an expert, Mr. Ruest could not hope to convince me of this fact simply by stating it. Indeed, it would have been very interesting to know the basis for his assertion in that regard.

(ii) The Appellant must understand that, in applying the direct comparison method, the greater the difference between the characteristics of the property to be appraised and the similar property, and the farther removed one gets from the appraised property or from the appraisal date, the more open to doubt the appraisal becomes. Conversely, the more similar the characteristics, and the closer together the properties and the closer the dates, the easier it is to estimate the value of the subject property. In the case at bar, I am of the opinion that the characteristics of the properties that Mr. Ruest selected for his analysis were too different from those of the Property. Indeed, buildings 1, 2, 3, 4, 5, 6, 8, 9 and 11 (see paragraph 6), which have four units, eight units, four units, 11 units, eight units, six units, 10 units, 13 units and 12 units respectively, are not, in my opinion, similar to the Property, which, as we have seen, has 32 units. The market for those buildings is not the same market as for the Property. The number of buyers for 32-unit

> buildings is more limited than the number of buyers for four-, six- or eight-unit buildings. In addition, buyers of 32-unit buildings are usually better informed and are therefore harder negotiators than buyers of buildings with a small number of units. Lastly, buildings 7, 8, 10 and 11 are too far from the Property to be valid comparables: they are located in cities other than Saguenay, where the Property is situated. In my opinion, properties in a city neighbouring the city in which the Property is located can also be valid comparables, provided satisfactory proof is provided of the market conditions in each city. Here, the Appellant's evidence in this regard was based solely on the testimony of Mr. Ruest, who claims that the market conditions in Chicoutimi were the same as those in Alma and Jonquière. Once again, even as an expert, Mr. Ruest could not hope to convince me of this merely by making an assertion that it was so. Lastly, all of the 11 real estate transactions that Mr. Ruest selected for his analysis took place after March 31, 1999, and on dates that were considerably later than that date. A transaction subsequent to the appraisal date, and even relatively distant in time from the appraisal date, can be taken into account when using the direct comparison method, if the extent to which the market evolved between the appraisal and transaction dates can be satisfactorily shown, in which case one will usually need to make adjustments to take any market changes into account. Here, the Appellant's evidence in this regard rested solely on the testimony of Mr. Ruest, who claims that the market conditions in 2002, 2004 and even 2005 were the same as in 1999. Once again, even as an expert, he could not hope to convince me of this merely by making an assertion that it was so. Indeed, it would have been very interesting to know the basis for his assertion in that regard.

[13] I have accepted Mr. Bergeron's conclusion regarding the FMV of the Property because I find that the characteristics of the properties that he chose for the purposes of his analysis are quite similar to the Property's characteristics. Indeed, all the transactions selected by Mr. Bergeron involved buildings with 16 units or more. Furthermore, all of the buildings were located in the same city as the Property. I would add that most of them were located in the same neighbourhood as the Property. Lastly, not only did all the transactions used by Mr. Bergeron take place prior to March 31, 1999, many of them took place on dates that were rather close to that date. In sum, although Mr. Bergeron's analysis is imperfect in several respects, his conclusions regarding the FMV of the Property appeared to me to be more credible than Mr. Ruest's conclusions in that regard.

[14] As I have stated, the Appellant submits that the Respondent should have taken the condition of the Property into account in determining its FMV, and therefore reduced by $200,000 the value assigned to the Property using the direct comparison method. In my opinion, adjustments must be made to take the particular state of a property into account when using the direct comparison method, but this still requires satisfactory evidence of the property's condition and of the adjustments that should be made. Here, the Appellant's evidence consisted solely of his own testimony and that of Mr. Ruest, who had supposedly visited a few of the Property's units in 1999. As we have seen, the Appellant testified that the Property was in a very rundown state on March 31, 1999, because the Bank (which was managing the Property from afar) performed no maintenance or repairs on the Property for two years. As we have also seen, the Appellant testified that the vacancy rate of the Property on March 31, 1999, was 45%, owing to the Property's general condition at the time. Lastly, I would point out that the Appellant stated that 9060-8027 Québec Inc. (controlled by his brother Jean-Eudes) had to invest about $200,000 in the Property after it was acquired, in order [TRANSLATION] "to fix it up and make it rentable again, and just about the whole lot of tenants was changed." Furthermore, Mr. Ruest went no further than saying that he had visited a few units in the Property in 1999 when looking for an apartment for a close relative, and that he had noticed the poor condition of those units at that time. The Appellant could have satisfied me that the Property was in a rundown state on March 31, 1999, and, above all, he could have convinced me of the cost of making it rentable again, if his brother, or an officer of the Bank, had testified regarding the Property’s general condition, and if he had tendered serious supporting documents related to the $200,000 that his brother allegedly spent to restore the building to a rentable condition. The Appellant could have adduced such evidence, but did not do so. The inference I draw from this is that such evidence would have been unfavourable to him. I would add that the fact that the Appellant did not raise this important point at the objection stage or and in his Notice of Appeal only increased my doubts as to the veracity of the Appellant's allegations in that regard.

[15] As for to the Appellant's argument that I should accept the conclusions of the appraisal report prepared by Mr. Ruest in light of the fact that the Agency accepted them in the case involving Jean-Eudes Tremblay, I am of the opinion that it has no weight in the case at bar, notably because no evidence was adduced regarding the circumstances under which the Agency purportedly accepted those conclusions.

[16] To sum up, the Appellant, who bore the burden of proof, has not satisfied me that the FMV of the Property as at March 31, 1999, was not $1,100,000.

[17] For all these reasons, the appeal is dismissed, with costs.

Signed at Ottawa, Canada, this 9th day of February 2010.

"Paul Bédard"

Bédard J.

Translation certified true
on this 28th day of May 2010.

Erich Klein, Revisor

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APPEARANCES:

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