Docket: 2007-2354(IT)G
2007-2356(GST)G

BETWEEN:

SLX MANAGEMENT INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeals heard on common evidence with the appeal of *Paul Miller* (2007-2357(IT)G) on October 1, 2 and 3, 2009 at Calgary, Alberta
By: The Honourable E. P. Rossiter, Associate Chief Justice

Appearances:

Counsel for the Appellant:	Curtis R. Stewart and Nandini Somayaji
Counsel for the Respondent:	Mark Heseltine

JUDGMENT

The appeals from the reassessments made under the *Income Tax Act* for the 2002, 2003, 2004 and 2005 taxation years and the appeal from the reassessment made under the *Excise Tax Act*, notice of which is dated July 31, 2006 in respect of the period of September 17, 2001 to September 16, 2003, are allowed, and the reassessments are referred back to the Minister of National Revenue for reconsideration and reassessment in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Canada, this 12th day of March, 2010.

"E.P. Rossiter"

Rossiter A.C.J.

2007-2357(IT)G

BETWEEN:

PAUL MILLER,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeals heard on common evidence with the appeals of *SLX Management Inc.* (2007-2347(IT)G and 2007-2356(GST)G) on October 1, 2 and 3, 2009 at Calgary, Alberta
By: The Honourable E. P. Rossiter, Associate Chief Justice

Appearances:

Counsel for the Appellant:	Curtis R. Stewart and Nandini Somayaji
Counsel for the Respondent:	Mark Heseltine

JUDGMENT

The appeals from the reassessments made under the *Income Tax Act* for the 2001, 2002 and 2003 taxation years are allowed, and the reassessments are referred back to the Minister of National Revenue for reconsideration and reassessment in accordance with the attached Reasons for Judgment.

Signed at Ottawa, Canada, this 12th day of March, 2010.

"E.P. Rossiter"

Rossiter A.C.J.

Citation: 2010TCC148
Date: 20100312
Docket: 2007-2354(IT)G
2007-2356(GST)G

BETWEEN:

SLX MANAGEMENT INC.,

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Respondent,

2007-2357(IT)G

AND BETWEEN:

PAUL MILLER,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

REASONS FOR JUDGMENT

Rossiter A.C.J.

Introduction

[1] The core issue in these appeals is categorization of expenses. The Minister reassessed the Appellants and denied the deduction of several expenses that were made against business income, alleging that they were personal in nature. The Appellants argue that all expenses were incurred for the purpose of gaining or producing income.

[2] SLX Canada Limited ("Canada") was incorporated to handle Canadian National Railway's ("CN") leased rolling stock for extended periods of time: to deal with lenders, primarily insurance companies and equipment suppliers, and to

deal with options to purchase by CN when the equipment came off lease [that intent being to keep the rolling stock off CN's balance sheet]. All operational expenses of Canada were to be the responsibility of SLX Management Inc. ("Management") pursuant to a Management Agreement between Management and Canada. Canada was owned 51 percent by CN, 16.66 percent by Management, 16.66 percent by a David Smith and 16.66 percent by DLG Consulting. The Appellant Paul Miller ("Miller") was the President, sole shareholder and director of Management. Smith was Vice-President of Management. During the period in question, Management's stream of revenue was 100 percent derived from Canada; Canada's stream of income was solely from CN. The stream of income for Canada and from CN and thereby for Management was time sensitive and set to expire in 2007.

[3] In 2000, Management started to look elsewhere for an alternative future revenue stream. Management had an aircraft for years and used the aircraft to troll North America for projects and in doing so claimed certain aircraft operating expenses plus travel. Management also claimed, as a business entertainment expense, a twelve day cruise by the principals and employees of Management plus their significant others and other persons, mostly former employees of CN who were familiar with Canada's operations with CN over the years. There were also claims by Management for: (a) a loss of investment in an automatic technology for underground transportation equipment, (b) expenses associated with Management renting a condominium in Montreal, (c) expenses of an office in a house in Florida owned by Miller, (d) expenses for an aircraft hangar where the Management aircraft was stored on occasion in Florida, and (e) some subscription magazine expenses.

[4] CRA disallowed the deduction of these expenses/losses from Management's income and attributed certain of them as shareholder's benefits to Miller. CRA also alleges that there was a change of use as of September 17, 2001 of Management's aircraft such that it triggered a deemed supply under the *Excise Act*. The Appellants appealed the reassessments.

Facts

[5] Miller was originally an employee of CN. Lease residuals on CN rolling stock turned out to be a problem for CN. Miller developed a method of dealing with this CN problem through Canada. Canada was a company without employees but with physical assets of up to $500 million. These assets included rail cars, locomotives and the leases for this type of equipment. All Canada did was hold assets, but it

was a fully operational lease company borrowing funds, acquiring equipment, refurbishing equipment, issuing debentures, and also dealing with residual risk and the remarketing of any equipment coming back to Canada. Management looked after all business operations of Canada pursuant to an agreement and got paid by:

1. A percentage of the total amount of transactions completed which were laddered;
2. By additional monies based upon Management showing that it borrowed monies at lower than the targeted rate set by CN on a present value basis;
3. By lease profit sharing with Management, if Management could generate a profit by taking a packaged lease with debt and selling it to, say, an insurance company.
4. By additional fees to Management if there was an exceptional deal that served CN's interests.

Article 2.01 of this Management/Canada agreement provides:

> The Company appoints Management and Management agrees to manage, supervise and conduct the business in accordance with this agreement.

Business was defined to mean the business of Canada according to its articles of incorporation.

[6] The duties and services undertaken by Management for Canada were extremely broad and all inclusive, basically to run all of the operations of Canada. The head offices of both Canada and Management were in Alberta because Alberta did not have a capital tax and the cost of operations from Calgary were significantly lower than those in Toronto or Montreal. Canada was restricted by terms of operations in doing business with CN and with only A-rated Canadian corporations in order to keep its credit rating as high as possible. Management was not limited to just doing business with CN. CN wanted Management to do business with other companies. Management attempted to do a variety of projects other than those associated with CN including acquisition of land in the United Kingdom, proposals with respect to the fast-ferry operations in British Columbia, and P3 projects in Nova Scotia.

[7] Management had four employees, the Appellant, Miller, David Smith and two administrative staff on a part-time basis. Vice-President Smith was the person responsible for Management's financial statements and tax returns plus did liaison work with the accountants and maintained the accounting records. Miller received

his designated shareholder's benefits annually on his T4 after discussions with Smith. The shareholder's benefits related to automobile usage, shareholder's loans and other ancillary matters.

[8] Management had a consulting and participation agreement with DLG Consulting Limited up until November 1, 1998 to provide consulting on the business of Management.

[9] One hundred percent of the revenue of Canada during the taxation years in question came from CN. Management's stream of income was almost exclusively from Canada. The agreement between Canada and CN in relation to CN's residuals of rolling stock, was to expire in 2007, and as a result, the stream of revenue for Canada and Management's stream of income had a sunset of April 1, 2007.

[10] Numerous attempts were made by Miller to broaden the business of Management including attempts to work with CN on a number of proposals. During the relevant period of time, the revenues of Management were roughly $2.5 million dollars annually.

Aircraft:

[11] In carrying out its operations, Management acquired a Cessna aircraft which was used extensively for travelling within Canada and the United States and which Miller states was only used on a personal basis about ten percent of the time. In 2000, Management acquired an additional aircraft, a TBM-700, and put the Cessna up for sale. The Cessna was eventually sold by Management in April, 2002 for a handsome capital gain. The TBM-700 was technologically advanced and higher end in terms of safety and reliability compared to the Cessna, and had lower operating costs. According to Miller the TBM-700 was used in the same fashion as the Cessna in the operations of Management.

[12] The operating expenses for the TBM-700 included fuel, hangar costs, insurance, maintenance, landing fees, charts and GPS. Management provided supporting invoices and claimed the appropriate capital cost allowance for the TBM-700 for the years in question.

[13] With respect to aircraft use, Miller maintained a log of flights and used this record to calculate any personal trips which would be attributable to him as a shareholder's benefit.

[14] The TBM-700 flight logs for the taxation years in question were maintained for the purpose of determining personal usage and maintenance. A summary of these logs for the 2002 taxation year show a total of nineteen trips, seventeen of which were attributable to business and two which were attributable to Miller personally. In the 2003 taxation year there were a total of fifteen trips, thirteen attributed to business and two attributed to personal; for the stub year of September 16, 2003 to December 31, 2003 there were five trips, one personal and four attributable to business.

[15] The usage of the TBM-700 by Management was attributed, to a large extent, to the pursuit of a distribution agreement with Socata, an aircraft manufacturing company from France. Socata did not have any distribution outlets for their aircrafts in the northwestern United States or western Canada. The pursuit for a distribution agreement involved negotiations of terms. A draft MOU was prepared by Management for Socata. In pursuing this distribution agreement, Management also sought information on the depth of pilot availability in their distributorship territory, as well as reviewed bookings of prospective purchasers for the TBM and had provided some demonstration flights on the TBM-700.

[16] In anticipation of a distribution agreement with Socata, Management attempted to solicit people familiar with the aviation industry and who might be of assistance to Management in acting as distributors in British Columbia and the northwestern United States. These persons would not take on any inventory of Socata aircraft but could be of assistance in distributing the Socata aircraft product.

[17] The TBM-700 was also used to attend a variety of aircraft conventions or TBM-700 Pilots' Associate meetings in places such as New Orleans, Oshkosh, Orlando, and Los Cabos, Mexico. On numerous occasions the TBM-700 was used to fly to locations where Miller was investigating business opportunities for Management. These business opportunities included two visits to Premiere Electric which was a fire damage company requiring some capital investment in or about Seattle; Dixon Networks which was a company to supply commercial equipment for installation of supernet in Alberta; an introduction to a Tyco official for the purpose of petroleum business with Tyco; numerous trips to meet a Mr. Frick in Florida for the purpose of scouting out coastal properties, in particular properties which were investment properties; an opportunity in North Bay, Ontario involving technology for automated underground mining vehicles; and potential acquisition of an FBO ("Fixed Base Operation") aircraft facility in Florida.

[18] During the periods in question, Management did not generate any revenue from its Socata ventures or any other business ventures it was investigating at the time for which the TBM-700 was used.

[19] Many trips on the TBM-700 were purportedly for business purposes, and were corroborated by witnesses other than Miller including flights to North Bay, Ontario for the automated underground vehicle technology, the FBO and prospective operations in Florida and the Premiere Electric possible investment in Seattle. Miller asserted that the TBM-700 was required to be on an on-call basis with Canada for the purpose of looking after Canada's business operations which were tied in with CN. Miller asserted they needed to be in the air within a one-half hour demand even though during the relevant time periods, not once were they ever called upon by CN or by Canada on such an urgent basis. A retired Chartered Accountant for CN confirmed that when Canada was established and the management agreement was entered between Canada and Management the potential for Management acquiring a corporate aircraft was discussed, but CN did not care whether or not Canada or Management had a corporate aircraft.

[20] Of all the trips in the TBM-700 claimed for business purposes during the taxation periods in question, the only trip that was related to CN was a trip to Toronto or a trip to Halifax to see DLG Consulting. For other trips to Montreal, of which there might have been two or three in the time period, commercial airlines were used. No real explanation was given as to why this trip to Halifax was taken with the TBM-700 as opposed to flying commercially.

[21] Miller asserted that he and Smith used commercial airlines when it made sense and they used points as well as trains and automobiles when required.

Cruise:

[22] Management incurred as an entertainment expense a cruise of $44,818. According to Management, this cruise was undertaken for two reasons; firstly, as a thank you to key persons who generated significant revenue for Canada and therefore generated revenue for Management; secondly, it was an attempt to get some persons together who were key business architects from Management's point of view to try to strategize where Management could go forward for additional business with CN, if any, given the sunset timelines (2007) of the management agreement between Management and Canada and Canada's stream of business

from CN. These key persons who Miller was referring to were a lawyer and accountant from Price Waterhouse, both of whom declined to attend, former personnel from CN, the Vice-President of Management and his spouse, as well as Miller and his spouse and a Mr. Gorveat and his companion from the DLG consulting. An original director of Management and architect of the documentation of Management did not attend. The cruise entertainment expense included the cost of the cruise, return airfare and other transportation costs.

[23] Spouses were invited especially for the three persons who worked for CN, as Management wanted face time with the former CN personnel and they could only give them a considerable length of face time if spouses attend. The three personnel from CN were then retired and they were not social friends of Miller, employees of Management or shareholders of Canada. It was explained that when in port, they would go on tours, and at night, Miller and Smith had dinner with the guests. They would have five or six hours face time with the guests each day and they also had two formal meetings while on the ship to discuss how Management had been developed and grown, what might happen post 2007 in terms of revenue stream and the issue of residuals of the CN rolling stock. A few proposals and ideas came out of this cruise but none related to CN business.

Montreal Condo:

[24] Miller owned a condo in Montreal where he resided before he terminated his employment with CN and developed Management. Management used this condo since its incorporation when Miller was doing transactions for Management with CN. Initially the condo was paid for on a daily basis, then a monthly basis. It sat vacant when not used by Management. When Management was dealing with CN, facilities of CN were not used as Miller felt that Management needed space to conduct its own analysis, whether it be in a hotel or a condo, and they used the condo occasionally. Miller acknowledged that he kept the Montreal condo partly because of its investment value and he was hesitant to part with the condo from a personal point of view (real estate was a building block for assets and he was hesitant to part with it). During the period of time under review, Miller only flew to Montreal on one occasion with the TBM-700 and only stayed in the Montreal condo overnight once.

Medical Expenses:

[25] Miller incurred medical expenses in 2002 of $4,277 for a visit to the Mayo Clinic and in 2003, $876 for dental treatment. These medical expenses were not for

a pilot's license check-up. His family had a history of use of the Mayo Clinic. Miller had no referral to the Mayo Clinic, nor did he have a family physician in Calgary at the time. He acknowledged that there was Alberta Health Care Insurance in existence at the time. Little explanation was given with respect to the medical expenses except that Miller thought he was important to Canada and Management and therefore his health was of concern to ensure the continued success of Management.

Automated Mining Underground Transportation Equipment (Mintronics):

[26] Glenn Brophy, a friend of the Appellant Miller, had been working for a North Bay, Ontario company involved in automated mining underground transportation vehicles. Brophy had left the company and acquired some automated underground transportation technology. Management investigated the opportunity presented by this technology and put up $38,135 to Brophy for the purpose of paying legal fees to acquire the intellectual property for the automated technology. Management was involved to the extent of acquiring the sub-surface rights for the technology. Brophy incorporated a company called 142924 Ontario Inc. when these rights were acquired. Miller made about three trips to North Bay to examine the opportunities presented by this technology. They looked at the consumer possibility of this technology with Canadian Tire as well as some other possibilities with Laidlaw, a school bus manufacturer, where the technology would be used for the purpose of transporting children; and Ford Motor Company with respect to forklift operations, and retailers generally on a "find-it" system. Miller, Brophy and a third shareholder did not have a shareholders' agreement, but according to Brophy and Miller, the $38,135 was put up by Miller while the other shareholder and Brophy carried out other efforts to advance the use of the technology. The money for the legals, $38,135, was transferred by Management and wired to the credit of Glenn Brophy, at Canada Trust. When the business venture was not going to be successful, financial statements were prepared for 142942 Ontario Inc.. Miller only then noted that he was a shareholder in 142942 Ontario Inc. and the investment was shown as a shareholder's loan for Miller. This was, according to Miller, an error and the investment had been made on behalf of Management.

Travel Expenses:

[27] There were numerous travel expenses also claimed by Management which were disallowed. These travel expenses were travel expenses which tied in almost

exclusively with the use of the TBM-700. These are the amounts of $7,089 for 2002 and $12,799 for 2003.

Subscription Costs of Association Dues:

[28] There were subscription costs claimed in 2002 of $1,531 and in 2003 of $2,085 which related mainly to aviation magazines or memberships in flying or aeronautical associations.

Florida Home Office and Hangar:

[29] Miller purchased a house in Spruce Creek, Florida, in 2003 near a community airport and a hangar for the TBM-700 came with the property. Management was charged $1,200 per month for the use of the hangar as well as $300 per month for the use of the home office. The charges were only made on per-use basis. Miller asserted that the usage of the aircraft was not to get to Florida but for access to clients. Miller asserted that he was able to work from this property in Florida with a dedicated office with the plane also dedicated. He could go anywhere and in fact could be off the ground in thirty minutes.

[30] Miller took many flights to Florida. He would spend only a few hours or maybe a day or two on business, and then stay in Florida for an extended period of time, with the airplane close by his side. Miller's spouse, Barbara, accompanied him on many of the flights.

Issues

[31] A: Management – Income Tax Appeal:

1. The deductibility of certain expenses from Management's income including:

a) operating expenses for the TBM-700 owned by Management as well as the CCA claimed for the aircraft;
b) entertainment cruise expenses;
c) miscellaneous travel expenses;
d) Montreal condo expenses;
e) medical expenses;
(f) Florida home office and hangar expenses;

(g) subscription expenses and association dues.

2. The deductibility of an investment in what was known as the North Bay Project.

[32] B: Management – GST Appeal:

1. The timeliness of the GST assessment,
2. Whether there was a change of use for the TBM-700 on September 17, 2002 such that there was triggered a deemed supply under the *Excise Tax Act.*

[33] C: Miller – Income Tax Appeal:

1. If any of the expenses claimed by Management as deductible are not properly deductible, were they shareholders' benefits under subsection 15(1) of the *Income Tax Act* or under section 56(2) of the *Income Tax Act* and therefore attributable to the Appellant Miller?
2. An issue of gross negligence penalties levied against the Appellant Miller was conceded by the Respondent – that is gross negligence penalties were not appropriate for 2001, 2002 or 2003.

Analysis

1. A: Management – Income Tax Appeal

[34] Section 9 – *Income Tax Act*

Business/Source of Income: The first issue is whether the expenses incurred by the Management in the years 2002, 2003 and a stub year ending December 31, 2003, are deductible from Management's income for those years. Counsel for the Respondent is of the opinion that these expenses are not deductible because in its view, Management was not operating as a business during those years to which the expenses related or there was no source of income. Management, however, submits that the expenses incurred for the years in question were for the purposes of operating the Appellant's business.

[35] Section 9 of the *Income Tax Act* states in part as follows:

> 9(1) Subject to this Part, a taxpayer's income for a taxation year from a business or property is the taxpayer's profit from that business or property for the year.

> (2) Subject to section 31, a taxpayer's loss for a taxation year from a business or property is the amount of the taxpayer's loss, if any, for the taxation year from that source computed by applying the provisions of this *Act* respecting computation of income from that source with such modifications as the circumstances require.

[36] In *Stewart v. R.*, 2002 SCC 46, the Supreme Court of Canada dealt extensively with a source of either business or property income. At paragraph [50], the Supreme Court of Canada stated as follows:

> [50] It is clear that in order to apply s. 9, the taxpayer must first determine whether he or she has a source of either business or property income. As has been pointed out, a commercial activity which falls short of being a business, may nevertheless be a source of property income. As well, it is clear that some taxpayer endeavours are neither businesses, nor sources of property income, but are mere personal activities. As such, the following two-stage approach with respect to the source question can be employed:
>
> (i) Is the activity of the taxpayer undertaken in pursuit of profit, or is it a personal endeavour?
> (ii) If it is not a personal endeavour, is the source of the income a business or property?
>
> The first stage of the test assesses the general question of whether or not a source of income exists; the second stage categorizes the source as either business or property.

[37] According to the Supreme Court of Canada, the purpose of the first stage of the test is to distinguish between the commercial and personal activities. In *Stewart*, *supra*, at paragraph [60], the Supreme Court of Canada further stated:

> [60] In summary, the issue of whether or not a taxpayer has a source of income is to be determined by looking at the commerciality of the activity in question. Where the activity contains no personal element and is clearly commercial, no further inquiry is necessary. Where the activity could be classified as a personal pursuit, then it must be determined whether or not the activity is being carried on in a sufficiently commercial manner to constitute a source of income. …

[There was a variety of indicia of commerciality or badges of trade referred to by former Chief Justice Bowman in *Graeme Nichol v. The Queen*, 93 D.T.C. 1216]

[38] In *Harquail v. The Queen*, 2001 FCA 320, the Federal Court of Appeal, at paragraph [62] stated in part as follows:

> It is not easy to delimit the content of the concept of carrying on business. One can see two outside parameters where the carrying on of business does not occur: on the one hand, when a company, which has been incorporated, has not actually commenced operation and, on the other hand, when a company has become dormant and is only holding annual meetings and filing its returns so as to avoid the forfeiture of its charter. There are, in between, some activities, however, which are signs that a company is operating and which should fall within the spectrum of the concept of carrying on business, even though, for example, the activities are carried on for the purpose of reaching an agreement which eventually is not reached or even though they do not result in the earning of income.

[39] In *Setchell v. R.*, 2006 TCC 37 a taxpayer who after being laid off from her employment, took a computer course expecting that the computer course would enable her to find employment or take related freelance work and she claimed the cost of the course as a tuition expense. Madame Justice Woods stated in part as follows:

> [16] … I agree with counsel that the fees are not deductible unless Mrs. Setchell was carrying on business at the time the course was taken. I do not agree, however, that it was necessary for Mrs. Setchell to have entered into business contracts in order to be considered to be carrying on a business. Judicial decisions make it clear that this is not necessary. If the capital structure of the business is in place and a taxpayer is actively pursuing business opportunities, then the business has commenced even if no business contracts have been entered into. …
>
> [17] I also note that this test appears to be accepted by the Canada Revenue Agency. Their administrative policy is of course not law but it is helpful to refer to when it reflects the judicial decisions. The Agency's administrative policy is set out in Interpretation Bulletin IT-364, at paragraph 2. According to the Bulletin, the Agency considers that a business has not commenced if activities are undertaken in the hope that the information obtained will justify going into a business and that a business will be considered to have commenced if there are serious or continuous efforts to begin normal operations.

[40] Also, consideration must be given to *Wacky Wheatley's TV & Stereo Ltd. v. Minister of National Revenue*, [1987] 2 C.T.C. 2311 (TCC). In that case, the taxpayer corporations were associated in the business of retail marketing of television, stereos and related electronic consumer products and were contemplating an expansion into the Australian market. In doing so, they incurred certain expenses which they sought to deduct as current business expenses. The Tax Court of Canada stated, in part, as follows:

> [26] … These expenses were anterior to any business decision to enter the Australian market and it is my opinion that they were clearly incurred as part of the current expenses of the appellants' operations.
>
> …
>
> [28] In the present case, the evidence shows that expansion into new markets was an on-going concern of the appellants. It is my opinion that the expenditures in question resulted from the current operations of each of the appellants "as part of the every day concern of its officers in conducting the operations of the company in a business-like way."
>
> [29] A major expenditure of many businesses today is monies expended to maintain or increase market share under increasingly competitive conditions. To this purpose, many corporations spend significant amounts each year in advertising, promotions and market surveys. The expenditures in issue in these appeals, in my view, related to such an endeavour. They were monies spent to determine the profit potential of the Australian market and were current expenses of the appellants. This characterization reflects the "business and commercial realities of the matter".

[41] I believe that the activities of Management can certainly be classified as commercial in nature given the commercial indicia of Management's operations. I conclude that Management was carrying on business during the period in question as follows:

1. Management had been in operation since the early 1990s with revenues on some occasions in excess of $2 million per year.
2. Management's operations surrounded the management of the operations of Canada but were not limited thereto and Management actively sought out other business ventures or activities.
3. The principal of Management, Miller, had professional training as an Engineer as well as Master's Degree in Business Administration and had been working in the business environment for years. He developed Canada and Management and successfully operated both at a profitable level for a number of years.
4. Management had set out an intended course of action to develop new sources of revenue other than Canada because of the sunset of its revenue stream in 2007 from Canada.
5. Management was trawling North America for business opportunities that would show a profit. There was a certain personal aspect to the commercial nature of Management, related to the Appellant Miller's personal interest in aircraft and aviation in general. The business prospects of Management in aviation were only part of its business pursuits being investigated.

[42] I am satisfied on the evidence and in applying the principles enunciated in *Stewart*, that, even though efforts of Management had not brought in revenue with respect to the ventures for which it was seeking a business deduction, Management was involved in commercial activity and searching out business opportunities. I refer to the *Harquail*, *Setchell* and *Wacky Wheatley* cases as support for finding the proposition that the business activities carried on by Management were for the purpose of earning income and deriving a profit. Although this purpose was not reached or attained, the activities were nevertheless commercial in nature.

[43] The Respondent's submission that although there was a desire and an effort by Management, there was no business is simply not an accurate reflection of the activities of Management. Management was looking for opportunities and projects while they were still conducting an ongoing business and this is really no different than the situation as described in *Harquail* and *Setchell* referred to above.

Section 18 – *Income Tax Act*

[44] Subsection 18(1) of the *Act* states in part as follows:

> 18.(1) In computing the income of a taxpayer from a business or property no deduction shall be made in respect of
>
> > (*a*) an outlay or expense except to the extent that it was made or incurred by the taxpayer for the purpose of gaining or producing income from the business or property;
> >
> > …
> >
> > (*h*) personal or living expenses of the taxpayer, other than travel expenses incurred by the taxpayer while away from home in the course of carrying on the taxpayer's business;

"Personal or living expenses" under subsection 248(1) are defined as follows:

> "Personal or living expenses" includes
>
> > (a) the expenses of properties maintained by any person for the use or benefit of the taxpayer or any person connected with the taxpayer by blood relationship, marriage or common-law partnership or adoption, and not maintained in connection with a business carried on for profit or with a reasonable expectation of profit,

> (b) the expenses, premiums or other costs of a policy of insurance, annuity contract or other like contract if the proceeds of the policy or contract are payable to or for the benefit of the taxpayer or a person connected with the taxpayer by blood relationship, marriage or common-law partnership or adoption, and
> (c) expenses of properties maintained by an estate or trust for the benefit of the taxpayer as one of the beneficiaries;

[45] In *Symes v. R.*, [1993] 4 S.C.R. 695 (S.C.C.) the issue was whether the taxpayer could deduct child care expenses from a business income. The SCC outlined several factors that may be taken into consideration in determining whether expenses are incurred for the purposes of producing or gaining income, which may be summarized as follows:

1. Whether the expense is deductible according to accounting principles;

2. Whether the expense is normally incurred by other taxpayers carrying on similar businesses;

3. Whether the expense would have been incurred were the taxpayer not engaged in pursuit of business or property income;

4. Whether the taxpayer could have avoided the expense without affecting gross income;

5. Whether the expense is of “the trader” of “the trade”. In the latter case, the expense might be considered an income earning expense.

6. Whether a particular expense was incurred in order to approach the income producing circle or was it incurred within the circle itself.

[46] Some expenses may be considered as dual purpose expenses. These expenses are particularly deductible pursuant to paragraph 18(1)(*a*) which prohibits the deduction of expenses to the extent that they were not income-earning expenses. The *Income Tax Act* contains several deeming provisions for expenses that are inevitably dual-purpose, such as entertainment or travel expenses.

[47] Some other factors that might be considered are the extent to which a taxpayer can make a lifestyle choice while maintaining the same capacity to gain or produce income - such choices tend to be seen as personal consumption decisions and result in expenses as personal expenses. Also, in terms of need-base, traditionally

expenses that simply make the taxpayer available to the business are not considered business expenses since the taxpayer is expected to be available to the businesses *quid pro quo* for the business income received. This translates into the fundamental distinction often drawn between the earning or a source of income on one hand and the receipt or use of income on the other hand.

I. Aircraft Expenses:

[48] There are numerous key assumptions in the Reply of the Respondent, which relate to aircraft expenses.

> 32. …
>
> x) the Aircraft was used primarily or substantially all of the time for the personal purposes of Mr. Miller;
> y) during the years in issue Mr. Miller devoted substantial time to Aircraft related activities that had no business purpose and no connection with the Appellant's management duties;
> z) Mr. Miller flew the Aircraft outside of Canada and North America, which trips were exclusively for his personal purposes;
> …
> ff) the Appellant did not acquire or use the Aircraft to gain or produce income from a business or property;
> gg) the cost of the purchasing and operating the Aircraft was a personal or living expense of Mr. Miller;
> hh) the cost of purchasing and operating the Aircraft was unreasonable;

[49] Paragraph 27 of the Reply reveals disallowed management aircraft expenses for 2002 of $151,408 and for 2003 of $103,377. By agreement, the 2002 figures have been adjusted downwards from $151,408 to $125,722. This reduction would necessarily lead to an equivalent reduction in the Income Tax appeal of Miller at paragraph 18(v) of the Reply for 2002 reduced from $151,408 to $145,233 and for 2003 reduced from $103,323 to $97,705.

[50] Management purchased the TBM-700 aircraft as a replacement for the older Cessna aircraft at the end of the 2000 fiscal year. Management alleges that the purpose of the aircraft was to gain and produce income for both its management agreement with Canada and other independent business ventures. Management deducted expenses related to the Cessna and the TBM-700 for 2002 and also incurred expenses with respect to 2003.

[51] The Respondent alleges that the expenses related to the TBM-700 are personal living expenses of Miller and pointed out that:

- The management agreement with Canada did not require Management to buy or maintain aircraft;
- Miller was an experienced pilot;
- The TBM-700 was insured for business and pleasure usage; and
- The Appellant Miller frequently used the aircraft to fly to Florida for personal use.

[52] The Respondent also alleges that the cost of purchasing and operating the aircraft was unreasonable. Management concedes that Miller took three personal flights in the year ending September 16, 2002 and two personal flights in the year ending September 16, 2003 and one personal flight for the stub year ending December 31, 2003.

[53] In *Stewart v. R., supra*, the SCC, in dealing with a personal element to certain activities, stated:

> [56] In addition to restricting the source test to activities which contain a personal element, the activity which the taxpayer claims constitutes a source of income must be distinguished from particular deductions that the taxpayer associates with that source. An attempt by the taxpayer to deduct what is essentially a personal expense does not influence the characterization of the source to which that deduction relates. This analytical separation is mandated by the structure of the *Act*. While, as discussed above, s. 9 is the provision of the *Act* where the basic distinction is drawn between personal and commercial activity, and then, within the commercial sphere, between business and property sources, the characterization of deductions occurs elsewhere. In particular, s. 18(1)(*a*) requires that deductions be attributed to a particular business or property source, and s. 18(1)(*h*) specifically disallows the deduction of personal or living expenses of the taxpayer: …
>
> [57] It is clear from these provisions that the deductibility of expenses presupposes the existence of a source of income, and thus should not be confused with the preliminary source inquiry. If the deductibility of a particular expense is in question, then it is not the existence of a source of income which ought to be questioned, but the relationship between that expense and the source to which it is purported to relate. The fact that an expense is found to be a personal or living expense does not affect the characterization of the source of income to which the taxpayer attempts to allocate the expense, it simply means that the expense cannot be attributed to the source of income in question. As well, if, in the circumstances, the expense is unreasonable in relation to the source of income, then s. 67 of the *Act* provides a mechanism to reduce or eliminate the amount of the expense. Again,

> however, excessive or unreasonable expenses have no bearing on the characterization of a particular activity as a source of income.

[54] I believe the expenses related to the aircraft may be deductible to the extent that they were incurred for the purposes of gaining or producing income for Management and are reasonable in that regard, but there are two limitations on these deductions that surfaced in the evidence. First, I believe that the aircraft had a dual purpose. I say the aircraft had a dual purpose because even by the Appellant's own admission, in the year ending September 16, 2002 the aircraft was used for at least three personal trips, in the year ending September 16, 2003 for two personal trips and for the stub year ending December 31, 2003 for one personal trip and in all likelihood there were more personal trips therein which I will discuss later.

[55] Second, the aircraft was used in relation to a business other than Management, SLX Aviation, which is a subsidiary of Management. A distribution agreement being negotiated with Socata by Miller anticipated that this other entity and not Management would be the distributor. Miller stated that Management itself would never be the owner of anything in terms of this venture with Socata. According to the principles enunciated in *Stewart*, *supra*, any aircraft expenses incurred for the purpose of gaining income for SLX Aviation are not deductible by Management.

[56] In analyzing the dual purpose, one must consider Miller's involvement in Management and the aircraft. Miller was basically Management. It was essentially a one-man show, albeit he had one other employee and two part-time staff. He was the brains behind the organization, he was the single shareholder, the President and sole director of the company. He had an interest in aviation since childhood, his father was an inventor and involved in the aviation business for most of his life. Miller watched movies on aviation; he built models of airplanes; he obtained his private flying license in Canada and two years later obtained his U.S. license; in 1978 he even obtained his U.S. commercial pilot's license; as a summer student, he worked part-time with Canadaair in a simulation vehicle monitoring the vibration of the vehicle. He was a founder of the TBM Owners & Pilots' Association in 2004 and went to numerous conventions of TBM Owners & Pilots' Association in July and August, 2002 and 2003, as well as the National Business Aircraft Association ("NBAA") in New Orleans in December, 2001 and the NBAA in Orlando in December, 2002, for a total of four flights for conventions or association meetings during the years in question.

[57] By any measure Miller had a significant and longstanding interest in aircraft and aviation on a personal level. I find this interest to some extent spilled over to these travels for Management in the TBM-700 which I address as follows.

(i) TBM-700 Usage 2002:

[58] On the usage of the TBM-700 for the year September 17, 2001 to September 16, 2002, I would note as follows:

1. Trip No. 1 - The NBAA New Orleans. This was a trip by Miller to the NBAA. This association was of a personal interest to Miller and not really of interest to Management. Miller asserted that the trip was primarily to introduce maintenance facility personnel to key players at the NBAA meetings in New Orleans. I believe from the tenure of evidence, that this was basically a personal trip by Miller because of his personal interest in aviation. I saw no business venture associated with this trip and the use of the TBM-700.

2. Trip No. 3 – Socata. This trip included a flight from Calgary to Wichita, Kansas with a stop-over at U.S. Customs and then on to Fort Lauderdale, Florida where Miller was in attendance for ten to eleven days. On this occasion the Appellant was accompanied by his significant other. During these eleven days, Miller probably had two or three meetings with Socata during which time he would look at Socata's maintenance facilities and meet with the Vice-President of marketing and the CEO of Socata's North American operations. They would go to lunch. Miller did not recall how long the meetings were, but there were to be two or three meetings at most. Miller asserted that there was a second meeting although he did not recall the duration or the location and he had no specific documentation with respect to that trip. At most, he had spent three to four hours with Socata. The balance of the trip was for vacation time that included a cruise from Fort Lauderdale which lasted for about ten days.

I believe that this trip was more for the personal convenience of Mr. Miller than for Socata meetings. Of the eleven days that the plane was actually situated in Florida, he had spent three to four hours, at most, with Socata representatives where there was "some discussion about the whole distribution concept of Socata" and the balance of the trip was on holiday with his significant other on a cruise.

Throughout Miller's evidence, he spoke many times about his trips to deal with Socata on a distribution agreement. Almost all of these trips involved a significant personal aspect such that it appears the Socata aspect was secondary, was an add-

on. [not the personal aspect] His evidence was vague, not particularized, filled with phrases of “I would have”, “I could have” “I likely had a meeting” and many times he did not know the duration or the specifics talked about: he spoke often in generalities. His presentation on the trips purportedly on business development with Socata was not generally particularly impressive.

3. Trip No. 4 – Hartzell. This trip involved a flight from Calgary to North Dakota for the purposes of obtaining a replacement propeller for the plane, and then to Florida where Miller left the aircraft and went under Simcom training for approximately one day. He ultimately returned to Calgary on or about February 27, 2002. During the time in Florida, Miller had met with a friend of his, a Mr. Frick, purportedly for the purpose of looking for properties in the area and apparently he and Mr. Frick looked at a business opportunity with respect to Socata moving part of the manufacturing operation to the United States. Even though Miller met with Socata officials, the prospect of a possible move to the United States was never discussed with them, although he did discuss with them some aspects with respect to their assembly plant in Stewart, Florida. There were no minutes of the meeting or documentation. Again, a portion of this trip was strictly business, but also a certain portion of the trip would appear to be personal in nature. The vagueness of the evidence of Miller on this particular point where he was using phrases such as “would have”, “could have” and “probably” was somewhat disconcerting. Of even more concern was that the business opportunity discussed between Mr. Frick and Miller was never discussed with Socata.

4. Trip No. 5 – Ed Radu. This was a test flight by Miller in the TBM-700 with an Ed Radu of Calgary to Red Deer and return. Apparently Radu was a prospective client for purchase of a TBM-700. No sales agreement was ever signed, nor was there any distributor agreement between Management and Radu.

5. Trip No. 6 - Ivan Klispell. This flight was to examine and tour possible maintenance facilities close to the U.S. border, which could be used should Management attain a distributorship for Socata for the northwestern United States and western Canada. Miller flew on to Ohio for warranty repair work on the TBM-700 propeller and then on to Toronto for a meeting with Management’s accountants and lawyers. The Ohio stop was for maintenance of the aircraft while the Toronto stop was clearly for Management business reasons. I believe this was a business use of TBM-700.

6. Trip No. 7 – Rochester. Miller flew to the Mayo Clinic for a Mayo Executive Check-up. I do not find there is any evidence to substantiate that this travel related

to business or the business development of Management or Canada. It was personal in nature. Miller attended the Mayo Clinic because he liked their Executive Check-up program, and he had favourable experiences with it in the past. The trip had nothing to do with a pilot license check-up: Miller's family had a long history of use of the Mayo Clinic. Miller had no referral to the Mayo Clinic and the Alberta Health Care Insurance plan was in existence at the time to deal with any medical issues he may have experienced. This trip was personal, and not commercial in nature.

7. Trip Nos. 8 and 12 - Everett-Washington and Paine, Washington. Management was looking into a business opportunity with respect to a fire damage company in Washington. This opportunity was brought to Miller's attention by Glen Toomey. These trips were commercial in nature with Miller looking at specific business opportunities for Management.

8. Trip Nos. 10, 13 and 15 - Hawker, Dalen and Charon. In 2002, Miller took several individuals on what he would classify as test flights on the TBM-700. He invoiced Hawker and Dalen for these flights but intimated that there was a possible sale or an opportunity for a possible sale of a Socata aircraft to these individuals; I did not take his evidence in that manner. I feel that these were basically plane rides, taken by Miller for the purpose of entertainment of friends and colleagues to show the TBM-700. I find these flights were personal and not commercial in nature.

9. Trip No. 11 – Mintronics. Management had advanced approximately $38,000 to cover legal fees to secure certain intellectual property rights on an IP security tag and it was an investment opportunity brought to his attention by his friend Ben Brophy for Management. I am of the view that this trip was business oriented and further reference is made herein on page 8 of this Judgment.

10. Trip No. 14 - OshKosh and Socata. Miller had picked up a gentleman named Emsland in B.C. Emsland who was going to be associated with Management if Management obtained a distribution agreement with Socata. According to Miller he wanted to introduce Emsland to Socata so flew him and his son to OshKosh, Wisconsin where there is the world's largest air show. Miller asserted that he had a variety of meetings with Socata; he wanted to see whether or not they were interested in making the distribution agreement. On cross-examination it became evident that although the OshKosh convention lasted seven days, the time spent with Socata by the Appellant Miller was very limited. There were a variety of aircraft vendors present, aircraft on display, aircraft manufacturers, and an air

show, all of which were of great personal interest to the Appellant Miller. He testified that “he probably met with Socata as they had a full set of facilities and aircraft outfitted and tents for marketing to the customers”. He said that he had the opportunity to meet the Vice-President of Marketing and met with him on at least two days and “probably” met them the day after they arrived. In total, it would appear that there may have been a total of four hours of meetings over the six or seven day period. In my view, although this trip was commercial in nature, it also had a significant personal element in it in that there were only four hours of meetings over the entire seven days with Socata, and the meetings all appeared to have occurred in the first two days after Miller arrived.

11. Trip No. 19 – NBAA – Orlando. This was a follow up with the NBAA trip to Florida in an attempt to forge a distributor relationship with Socata. Cross-examination revealed that this trip was for a period of six days and the purported primary purpose was the NBAA convention where Socata was announcing a new model of aircraft. According to Miller, of the six day trip, Miller may have gone to Socata operations and the convention for one or two days and the rest appeared to be vacation time. Again, part of this trip was commercial and part of it was personal and vacation time.

12. Trip No. 16 – Halifax and Montreal. This trip was to meet with Management’s consultants and was business in nature.

[59] For the year ending September 16, 2002, of the nineteen trips for which the TBM-700 was used, there were three which were indicated by Miller as being personal. Upon my review of the evidence, I find that nine trips were totally personal, that is Trip Nos. 1, 2, 7, 9, 10, 13, 15, 17 and 18. On the evidence, I find that four trips were partially personal in nature, that is, Trip Nos. 3, 4, 14 and 19. Based upon the evidence, I am of the view that these four trips should be apportioned forty/sixty, that is, forty percent commercial and sixty percent personal. The balance of the trips, based on the evidence, were commercial in nature – Trip Nos. 5, 6, 8, 11, 12 and 16. Based upon the foregoing apportionment of the nineteen trips in the TBM-700 trip summary for the year ending September 17, 2002, 11.4 of the nineteen trips would be personal and these expenses are not deductible.

(ii) TBM-700 Usage 2003:

[60] On the usage of the TBM-700 for the year ending September 16, 2003, I would note as follows:

1. Trip No. 2 - Dixon Networks – This trip was commercial in nature. This trip was an attempt by Management to promote its abilities to supply communications equipment for the installation of a super net in Alberta with a Mr. Glen Hawker.

2. Trip No. 4 – Tyco – This trip was for a meeting with Tyco officials to discuss business opportunities and, again was commercial in nature.

3. Trip No. No. 9 – Mintronics – This trip was commercial in nature being a follow up on Trip No. 11 for 2002 year as noted earlier.

4. Trip No. 11 – Premiere Electric – This trip related to a meeting with a Mr. Toomey over a business opportunity with Premiere Electric – much the same as Trip Nos. 8 and 12 for the year ending September 16, 2002.

5. Trip No. 3 - Los Cabos – Miller and his significant other attended a specific convention where Management was to be named as Socata's newest distributor, although there was no such announcement. This was to be a significant trip for Management because of the prospective announcement. On the whole, I believe it to be commercial in nature.

6. Trip No. 6 - Stewart, Florida - Miller described this trip as a property viewing trip to Florida with Mr. Frick. Mr. Frick was a personal friend of Miller and Miller stayed at Frick's residence for an extended period of time. Frick owned a TBM-700 so they had some interests in common, that is, their interest in TBM-700's and aviation. Miller's significant other traveled with him to Florida on this occasion and although they may have looked at some coastal properties this trip certainly appears to be vacation and personal in nature as opposed to commercial oriented. In fact, Mr. Miller took a tour of a property at Spruce Creek where he ultimately bought a personal residence that had a hangar for the TBM-700.

7. Trip No. 7 – Orlando – This trip was purportedly for the purpose of having a Simcom training for Miller. It appears that Miller stayed in Florida in total from February 5, 2003 until April 7, 2003. Miller was in Orlando for a total of five days, two of which were for Simcom training. Miller continued on to Spruce Creek, Florida where he closed his personal residence purchase. Aside from two days of Simcom training, the travel was a personal holiday.

[61] 8. Trip No. 13 – Florida - This trip was purportedly for the purpose of taking a flight from France to the United States with Socata, but a significant portion of the

time was spent by Miller at his new home in Spruce Creek, Florida; the trip was mainly personal in nature.

[62] 9. Trip No. 14 – OshKosh - This flight was for attendance at the OshKosh convention. There was no evidence given that the convention had anything to do with the Socata distributorship agreement. This trip was personal in nature as was the similar OshKosh convention the previous year.

[63] 10. Trip No. 15 – Boise, Idaho - This flight was associated with the exhaust system on the TBM-700 and can be considered as either maintenance for the aircraft or a business venture.

11. Trip No. 1 – Dalen – Miller asserted that this was a flight with Mr. Dalen whom he invoiced for the trip. No particulars were given for the trip. This flight was similar to Trip No. 15 in the year ending 2002 and for the same reasons, I find it personal in nature.

12. Trip No. 5 – Miller described this flight as a test flight for maintenance or checking for something. No particulars were given. Again, I am of the view that this was just a flight for Miller's enjoyment of flying. I find this trip was personal in nature.

13. Trip No. 10 – Toronto - This was a trip to Toronto by Miller to meet with Management company advisors and accountants and was commercial in nature.

[64] For the year ending September 16, 2003 based on the evidence I find that six trips were personal based on the evidence before the Court and Miller's acknowledgment that Trip Nos. 8 and 12 were personal: Trip Nos. 1, 5, 6, 8, 12 and 14. I found that Miller in his evidence attempted to play down the personal use of the TBM-700 but in essence used the aircraft as a personal taxi while either going on vacation or pursuing his lifelong love of aviation.

[65] I further find, on the evidence, that Trip Nos. 7 and 13 were partly personal and partly commercial in nature. I believe the evidence revealed that the commercial nature of these trips were significantly lower than the personal aspects of the trips. I apportion each of these trips as ninety percent personal and ten percent commercial.

[66] For the year ending September 16, 2003, of the fifteen trips for the TBM-700, six were personal, Nos. 1, 5, 6, 8, 12 and 14, seven were commercial, Nos. 2, 3, 4,

9, 10, 11 and 15 and two were partly personal, Nos. 7 and 13, and partly commercial. Based on the foregoing apportionment of the fifteen TBM-700 trips for this period, 7.8 are personal in nature and these expenses are not deductible.

(iii) TBM-700 Usage stub year 2003:

[67] On the usage of the TBM-700 in the stub year ended December 31, 2003, I note the following:

1. Trip No. 18 - Calgary-Daytona – This was acknowledged to be a personal trip.

2. Trip No. 16 - Calgary-Santa-Fe - This trip was commercial in nature as it was for a meeting with respect to the Socata distributorship.

3. Trip No. 17, Santa Fe-Daytona-Calgary – This trip was partially commercial and partially personal. Miller left Calgary to Montana, then flew to Santa Fe where for two days he assisted Socata in setting up their next convention. He then went from Santa Fe to Naples ferrying a Socata official, Bill Alberts, and Miller stayed in Florida for several days at his house. I would apportion this trip, on the evidence, at seventy percent commercial and thirty percent personal.

4. Trip No. 19 – Lacombe – This trip was an annual certification and inspection of the aircraft and therefore commercial.

5. Trip No. 20 – Daytona to Spruce Creek – This trip was primarily personal in nature with one meeting with respect to an FBO facility as a business opportunity. Based on the evidence I would apportion this trip at eighty-five percent personal and fifteen percent commercial.

[68] For the stub year ending December 31, 2003, of the five trips for the TBM-700, there were 2.55 personal in nature and 2.45 were commercial in nature and these expenses are not deductible.

[69] This is not the end of the matter of deductibility of the aircraft expenses. Although the intent appeared to be to obtain a distributorship to sell new and used Socata planes, it is not clear that Management was a party to this business arrangement either as an authorized sales representative for Socata or as a distributor. An agreement made on March 5, 1996, that subsequently lapsed, authorized a company called SLX Aviation Inc. to be the sales representative for Socata. Management was apparently the sole shareholder of SLX Aviation Inc. but

Management was not party to this agreement, and had no enforceable rights to it whatsoever. The agreement contained the following clause at paragraph 12(j):

> NO THIRD PARTY BENEFICIARIES:
>
> This agreement does not create, and shall not be construed as creating any right enforceable by any person not a party to this agreement.

[70] Management was not intended to be the distributor for Socata. Miller stated that this was the intention throughout the documentation stage. On cross-examination, Miller acknowledged that the distribution agreement which he negotiated with Socata, could not be between Management and Socata but had to be with another party. Miller acknowledged that it was anticipated that another entity would be the distributor and that he never said SLX Management would be the legal owner of anything and that draft discussion points regarding the buying and settling of aircrafts, show Paul J.D. Miller as the proposed new distributor. There was no reference whatsoever to Management.

[71] Given the foregoing, it appears that all the travel in the TBM-700 associated with the Socata distributorship was not in fact for Management, but was for the benefit of another entity to be incorporated or for the benefit of Miller. Having reached this conclusion, I believe the number of TBM-700 trips which are deductible as a business trip for Management is somewhat altered, as follows:

[72] For the year ending September 16, 2002 Trip Nos. 3, 4, part of 5, and 19 were incurred for some other entity other than Management and therefore the expenses associated with same are not attributable to Management, but those portions of those trips identified as personal are still for the personal benefit of Miller and shall be treated as such. Only 6 trips that were commercial in nature are deductible by Management.

[73] For the years ending September 16, 2003 Trip Nos. 3 and part of 13 were incurred for some other entity other than Management and therefore the expenses associated with same are not attributable to Management but the portion of those trips identified as personal are still for the personal benefit of Miller and shall be treated as such. Only 6.1 trips that were commercial in nature are deductible by Management.

[74] For the stub year ending December, 2003, Trip Nos. 16 and part of 17 were no longer commercial but were incurred for some other entity other than Management

and therefore the expense associated with same are not attributable to Management but the portion of those trips identified as personal are still for the personal benefit of Miller and shall be treated as such. One (1) trip is deductible by Management.

Section 67: - Income Tax Act

[75] A section 67 *Income Tax Act* analysis is not otherwise required on the expenses allowed as deductible as I am satisfied on the evidence the expenses presented were reasonable in quantum.

II. Capital Cost Allowance:

[76] In closing argument the Respondent moved to amend its Reply to include reference to section 13(7) of the *Income Tax Act* which would allow it to argue that there was a deemed disposition of the aircraft and a reacquisition, such that the new date of reacquisition would be September 17, 2001 and not the original date as suggested by the Appellant. The Appellant naturally objects to such a motion and I must agree with the Appellant. The trial for all real purposes had concluded except for closing argument of the Appellant. The timing of the motion could not have been worse – how could the Appellant not be severely prejudice by the granting of such a motion? The Appellant lead its case based on the Reply put forth by the Respondent. It would be totally unfair and highly prejudicial to the Appellant to allow this motion at such a late stage in the trial and the motion is therefore dismissed.

[77] The capital cost allowance is available to the Appellant, Management, under section 20(1).

[78] In *Hickman Motors Ltd.* [1997] 2 S.C.R. 336, the Supreme Court of Canada laid out the legal test to determine whether CCA deductions are permitted on an item of property :

> 57 Once the "income from a business source" is established, the next step is to determine what, if anything, can be deducted therefrom in order to arrive at the taxable income. Section 20(1) provides that,
>
> > 20.(1) ...there may be deducted ... such of the following amounts as are wholly applicable to that source ... or such part of the ... amounts ... as applicable thereto....

> 58 The "following amount" may be either "wholly applicable" or "partly applicable" to "that source", that is, the business source. So a specific amount could be "partly applicable" to income from a business source, and "partly applicable" to income from another source such as, for example, income from a property source. Or a specific amount could be "wholly applicable" to the business source only. Here, this distinction is not at issue: the amount sought to be deducted would be "wholly applicable" to income from the business source identified above.
>
> …
>
> 65 The second part of the test is: where the item of property does not produce income, was it acquired for the purpose of producing income? This is determined by an objective evaluation of the specific facts and circumstances of each case in relation to appropriate jurisprudence, having regard to whether the taxpayer acted in accordance with reasonably acceptable principles of commerce and business practices. In the affirmative, the deduction is allowable. In the negative, the deduction is not allowable.

[79] I believe that the aircraft was acquired for the primary purpose of gaining or producing income for Management and not for Miller's personal use. Nonetheless, Miller did often use the aircraft for personal use so the CCA deductions are not wholly allowed but are permitted only to the extent that they are attributable to Management's ventures. In 2002, this proportion is 6 of 19 flights. In 2003, this proportion is 6.1 of 15 flights. In the stub year of 2003, this proportion is 1 out of 5 flights. CCA deductions should be permitted accordingly

III. Entertainment Expenses:

[80] There are several key assumptions in the Respondent's Reply with respect to entertainment expenses:

> 32. …
>
> ss) the cost of the cruise was not incurred for the purposes of earning income from a business or property;
>
> tt) the cost of the Cruise was a personal or living expense;
>
> uu) the cost of the Cruise was unreasonable;

[81] I am of the view, that the costs of the cruise, as presented by Management, were incurred for the purpose of earning income for business and that the cost of the cruise was not a personal or living expense. One must look to the history of Management to clarify this finding. Management was an entity created by Miller to look after all the operational expenses of Canada. Canada was established for the purpose of handling all the rolling stock of CN. CN had this problem which they encountered on a regular basis of how to deal with the rolling stock. CN wanted

the rolling stock to be off balance sheet so the arrangement was for Canada to lease the rolling stock of CN and provide it to CN with a certain revenue stream up until the year 2007. Canada then offloaded its operational expenses to Management with Miller playing a key role in both these entities. His personal relationships with the personnel of CN, as well as his own educational experience and intricate knowledge of CN, were key to the success enjoyed by Canada and Management. This relationship obviously grew and there appeared to be a significant confidence placed by CN officials in the abilities of Miller and the operation of Canada and Management. Without these key relationships with Ken White, who was Assistant Treasurer for CN at the time, as well as a Treasurer and Accountant of Finance, it is fair to say that neither Canada nor Management would have been as successful as they were, even given the obvious business prowess of Miller. At the same time, these individuals would be of assistance to the Appellant in developing ideas and opportunities for business development. Ken White, the then Assistant Treasurer of CN, since retired, gave evidence as to his relationship with Miller, Management and Canada and the types of things which were discussed on this cruise. Miller said the reason for the cruise was that he and Smith wanted an opportunity to corral these individuals into one location, for an extended period of time, to get an extended period of face time with them in order to pick their brains with respect to expanded business opportunities for Management. Out of these particular discussions came the possibility of having a similar arrangement which Canada had with CN, with the Go-Train fleet in Toronto. Also, there was a proposal with respect to oil well supply in Sarnia on which a specific proposal had been presented, but was not successful. There was also detailed discussion about capital self insurance programs which was explained in detail by Miller and which he followed up on after the cruise. I believe that this expense was for the purpose of developing business and income for Management.

[82] It is to be noted that the expense put forward was as an entertainment expense and not as a business development expense. The cruise expense was for a total of $44,818. The evidence disclosed that a total of ten persons attended the cruise, that is, Mr. White and his spouse, the former Treasurer of CN and his spouse, the accountant from CN and his spouse, Mr. Miller and his significant other and Mr. Smith and his significant other for a total of ten. The cost of the cruise, which included the cruise itself, return airfare and transportation costs was certainly reasonable in the circumstances. I also agree with the suggestion that the spouses of the individuals had to attend, otherwise, the individuals likely would not have been able to attend given the time duration of the cruise, (as it may have been difficult to be away for such a cruise without their spouses in attendance) and this certainly would have affected the ability of Miller and Smith, on behalf of

Management, to have a significant block of face time with these persons to discuss the business opportunities.

IV. Montreal Condo Expenses:

[83] In the Reply, there were some significant assumptions relied upon by the Respondent with respect to the Montreal condo expenses:

> 32. …
>
> yy) the condominium was not used by the Appellant in 2001 or 2003 for any business purpose;
> zz) the rent expenses were not incurred for the purpose of earning income from a business or property;
> aaa) the rent expenses paid for personal or living expense of Mr. Miller;
> bbb) the rent for the Montreal condominium was unreasonable;

[84] I do not believe that the expenses associated with the Montreal condo were expenses incurred for the purposes of gaining or producing income; therefore, they are not deductible. As indicated, Miller owned a condo in Montreal where he resided before he terminated his employment with CN and developed Management. During the periods in questions, the condo was used on only one overnight stay and this was over a span of twenty-seven months – hardly something which was going to be actively used for the purpose of gaining or producing income. If so, it was certainly a poor investment. Miller himself acknowledged that he kept the condo in part because of its investment value and he was hesitant to part with the condo. From his personal point of view, he thought it would be nice to spend more time in Montreal, especially in the summertime as it is much like Europe and also that real estate was a building block for assets and he was hesitant to part with it. All of this particular evidence rings to me that this was a matter of a personal expenditure, for personal pleasure, and not one incurred for the purpose of gaining or producing income and I find it as such.

V. Medical Expenses:

[85] In the Reply, the following were the key assumptions in relation to medical expenses:

> 32. …
> iii) the medical expenses were not incurred to earn income from a business or property;

jjj) the medical expenses were personal or living expenses;

[86] I conclude that medical expenses incurred by the Appellant were not incurred for the purpose of earning or producing income from the business. The medical expenses were associated with a visit to the Mayo Clinic as well as some dental treatment. These expenses were not for pilot license check-up, but rather were associated with Miller's personal choice to have a check-up done at the Mayo Clinic as opposed to using the medical services available through the Alberta Health Care Insurance plan which was certainly in existence at the time. There was little or any explanation given with respect to the medical expenses except that he thought that he was important for Canada and Management and therefore his health care was of concern to ensure continued success of Management – even if his health was of concern to ensure the continued success of Management, his health could have been looked after through a public health program, just as well as it could be looked after through such clinic as the Mayo Clinic. Miller also felt that his family had a long successful history using the Mayo Clinic which reinforces the finding that this is a personal expenditure and not for the purpose of earning income from a business.

VI. Subscription:

[87] In the Reply, there were several key assumptions with respect to subscription expenses:

32. …

lll) the subscriptions expenses were not incurred to earn income from a business or property;

mmm) the subscription expenses were personal or living expenses;

I am of the view that the subscription expenses incurred by the Appellant were not incurred to earn income for business. I have already reviewed in detail the lengthy personal and significant interest which Miller had in aviation and these subscription expenses were in relation to that life long personal interest.

VII. Travel Expenses:

[88] The Reply refers to several key assumptions with respect to travel expenses:

32. …

cc) the Appellant claimed $11,789.89 and 12,799.58 in travel expenses for its 2002 and 2003 taxation years, respective;

dd) the amounts the Appellant claimed as travel expenses were incurred to enable Mr. Miller to attend air shows, aircraft conventions, medical services at the Mayo Clinic, airplane owners' gatherings, pleasure trips, and training;

Given my findings with respect to the personal aspect of Miller using the TBM-700, for air shows, aircraft conventions, medical appointments, airplane owners' gatherings and pleasure trips and training, I believe that the only portion of the travel expenses which could be used for the purpose of gaining or producing income were the expenses associated with Simcom training. All of these other attendances, whether they be air shows or aircraft conventions or airplane owners' gatherings, as I indicated, were as a result of Miller's lifelong interest in aviation and flying and the business aspects of the trips, if any, were simply the add-ons to accommodate his personal interest in aviation and flying. As such, I am not of the view that these travel expenses were for the purpose of gaining or producing income.

VIII.North Bay Project:

[89] There are several key assumptions relied upon by the Respondent:

32. …
qqq) Paul Miller was a shareholder of 1429424 Ontario Inc. in the taxation years at issue;
rrr) the $38,135.00 was not paid or incurred to earn income from a business or property;
sss) the $38,135.00 related to personal or living expenses of Mr. Miller;

I believe the evidence is clear that this expense was not a personal or living expense, but rather, was an investment opportunity for Management in acquiring technology associated with automated mining underground transportation equipment. This business opportunity was brought up to him by a friend, Ben Brophy, and Management put up approximately $38,000 for the purpose of paying legal fees to acquire the intellectual property for this automated technology. The monies came from the account of Management and were wired to the credit of Mr. Brophy. Miller had taken a couple of trips to North Bay to discuss and investigate this business opportunity and canvass the possible uses of the technology, including possible sales through Canadian Tire or Laidlaw and Ford Motor Company. Management and Brophy, and one other shareholder, were the ones that were involved in the company 1429424 Ontario Inc. Miller did not even realize that he was put down as a shareholder in 1429424 Ontario Inc. until the business venture became unsuccessful and the financial statements were prepared. I accept

the evidence of Miller on this particular point, that the investment had been made on behalf of Management and not on behalf of Miller, and was recorded in error. I find, that this investment was done for the purpose of gaining or producing income and was not a personal expense.

IX. Florida Residence and Hangar:

[90] There were several key assumptions in the Reply relating to the Florida residence and hangar and those were:

> 32. …
>
> www) Mr. Miller's Florida condominium and the hangar were not used by the Appellant for any business purpose;
> xxx) Mr. Miller stored the Aircraft in Florida for his personal use;
> yyy) the rent paid by the Appellant paid for personal or living expense of Mr. Miller; and
> zzz) the rent paid by the Appellant for the Florida condominium and hangar was unreasonable.

Miller asserted that he used the Florida condominium as he was able to work in the house every day, using the internet, satellite TV and telephone and with a dedicated office with the plane also dedicated and parked very close by. I am of the view that this Florida property and hangar were for personal use and were personal living expenses for the Appellant and not for the purpose of gaining or producing income. Furthermore, in the type of business operated by Management there is really no reference at any time to Miller requiring a particular office facility for any purpose anywhere. The internet is available virtually anywhere; satellite TV is not something which is required for the purpose of gaining or producing income in the business that Management was involved, telephones are also available virtually anywhere. Miller testified he could go anywhere and in fact could be off the ground in thirty minutes, There was no evidence whatsoever that there was any requirement for him to be off the ground in thirty minutes. I reviewed in detail the use of the TBM-700 for the purpose of going to and from Florida and the significant time spent in Florida while having the TBM-700 available to him, whether it be to conduct Management's business, or Canada's business, or at the request of CN or anyone else. Miller basically flew the TBM-700 where he wanted, when he wanted and the attendances in Florida were very much tied in to his personal holidays, whether it be on a cruise, or time spent at Spruce Grove. I was not particularly impressed with the explanation given by Miller with respect to his use of the Florida condominium and the hangar, and the necessity that it was

used for the purpose of gaining or producing income. Quite the contrary, the Florida property and hangar were for his own personal pleasure and enjoyment and to satisfy interest in aviation and flying, and as such, I find that the expenses related to the Florida property and hangar were not for the purpose of gaining or producing income.

[91] In summary, in relation to the Management Income Tax appeal, I find:

1. Management was involved in the years in question in commercial activity and conducting an ongoing business.

2. Aircraft expenses:
- for year ending September 16, 2002 of the 19 trips for the TBM—700 – 11.4 trips were personal and 7.6 were commercial;
- for the year ending September 16, 2003 of the 15 trips for the TBM-700 – 7.8 trips were personal and 7.2 were commercial;
- for the stub year ending December 31, 2003,, of the 5 trips for the TBM-700 – 2.55 were personal and 2.4 were commercial;
- However, due to the fact that Management was never going to be a distributor of Socata but rather some other entity – the figures for 2002 are adjusted to 11.4 trips personal and 6 trips deductible to Management.
- the figures for 2003 are adjusted to 7.8 trips personal and 6.1 deductible to Management;
- the figures for December 31, 2003 are adjusted to 2.58 personal and 1 deductible to Management.

3. Capital Cost Allowance: The capital cost allowance expenses are deductible in the same proportions as the aircraft expenses for the years in issue, as noted above.

4. Entertainment Expenses of cruise are allowed as a business expense.

5. Montreal condo expenses are not allowed as a business expense.

6. Medical expenses are not allowed as business expenses.

7. Subscriptions are not allowed as business expenses.

8. Travel expenses are not allowed as business expenses.

9. North Bay project was a business investment for Management and business expenses are allowed.

10. Florida residence and hangar was not a business expense.

B: Management – GST Appeal:

[92] The key assumptions with respect to the GST appeal were sections 16(pp) and (qq) of the Reply.

> 16. …
>
> pp) during the reporting periods at issue the Appellant did not use or resupply the Aircraft in the course of a commercial activity;
> qq) beginning on September 17, 2001, the Appellant used the Aircraft primarily for purposes other than commercial activities (the "change in use"):

I have reviewed the facts in detail in terms of the usage of the TBM-700 in the taxation years of 2002, 2003 and the stub year ending December 31, 2003. The personal usage of the plane was quite high in each of the taxation years – certainly more personal than commercial – this was good reason on the facts to open up the prior tax assessment. The Appellant should have recognized readily the GST problem which arises from the amount of personal use that the plane was put to in 2002. The Minister is entitled to make these reassessments beyond the normal reassessment period by evidencing the inaccuracies in the Appellant's returns.

[93] I believe that Management originally acquired the TBM-700 for use primarily in its commercial activities. However, for the GST relief the Appellant seeks, I have to consider the use of the aircraft during the reporting period ending on September 30, 2001. For the years in question, the numbers show that the majority of flights were, in fact, taken for Miller's personal usage. As a result, I find that during the period in question the aircraft was not used primarily in commercial activities of Management. The Minister's reassessment with respect to the deemed change in use under section 200 of the *Excise Tax Act* stands.

[94] The Minister's reassessment with respect to the disallowed input tax credits on hangar expenses also stands. The Florida hangar was not a business expense. The Appellant is entitled to claim input tax credits on aircraft maintenance expenses to the extent I have found that the aircraft flights were commercial.

C: Miller - Income Tax Appeal

[95] With respect to the expenses in the Management appeal, the results of those finding on expenses flows directly to the Miller appeal. Where I have found expenses not to be for the purposes of gaining or producing income, they are held to be shareholder benefits or indirect payments to Miller in amounts as apportioned above.

D: As both parties were partially successful in the positions they had taken on the issues under appeal, there will be no order as to costs.

Signed at Ottawa, Canada, this 12th day of March, 2010.

"E.P. Rossiter"

Rossiter A.C.J.

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