

Docket: 2011-1396(IT)G

BETWEEN:

OM P. MITTAL,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeals heard on November 14, 2012, at Toronto, Ontario

By: The Honourable Justice Campbell J. Miller

Appearances:

For the Appellant: The Appellant himself
Counsel for the Respondent: Ernesto Caceres

JUDGMENT

The appeals from the reassessment made under the *Income Tax Act* for the 2006 and 2007 taxation years are allowed and the reassessments are referred back to the Minister of National Revenue for reconsideration and reassessment on the basis that the losses of \$35,226 and \$23,659 incurred by the Appellant in 2006 and 2007 respectively are business losses. Costs to the Appellant.

Signed at Ottawa, Canada, this 28th day of November 2012.

"Campbell J. Miller"

C. Miller J.

Citation: 2012 TCC 417
Date: 20121128
Docket: 2011-1396(IT)G

BETWEEN:

OM P. MITTAL,

Appellant,

and

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Respondent.

REASONS FOR JUDGMENT

C. Miller J.

[1] Mr. Mittal claims to be a trader in securities and, as such, deducted business losses from that activity of \$35,226 in 2006 and \$23,659 in 2007. The Minister of National Revenue (the "Minister") denied those losses as business losses, assessing on the basis that they were capital losses, as Mr. Mittal was neither a trader or engaged in an adventure in the nature of trade.

Facts

[2] Mr. Mittal's losses from 2004 and 2005 were assessed on capital account but Mr. Mittal and the Respondent reached a settlement agreement in which the Respondent allowed Mr. Mittal's 2005 losses as business losses. Apart from indicating that he had approximately 100 trades of 49,591 shares in 2005 representing a dollar amount in purchases and sales of over \$1,000,000, I heard no further evidence of the circumstances involving Mr. Mittal's 2005 trading activity.

[3] Mr. Mittal is an engineer by profession, having worked as such for Shaw Canada from 1998 to 2012. In 2006 and 2007 he averaged approximately 32 hours a week working at Shaw.

[4] Mr. Mittal indicated that he had his own trading account as early as 2000, but maintained he actually started trading in 2004. He provided a business plan prepared in 2005 which is worth reproducing:

Business Plan – Security Trading

1. Personal Growth
Maintain a great positive attitude and decrease negative influences. Make an effort to becoming deaf to negativity and choosing not to read or listen to negative inputs, while also adding position input.
 - a. I will read material on positive mental attitudes
 - b. Positive self talk
 - c. I will exercise to stay healthy physically and mentally
 - d. I will practice YOGA for an average of 5 days a week.

2. Mission Statement
 - a. I will invest my time into financial newspapers, books and market research
 - b. I will watch selective business programs on TV such as BNN
 - c. I will focus on the price action of the current market conditions for trading.
 - d. I will always expand my mind with new ideas.
 - e. I am going to be trading "Online" on TSE stock exchange.
 - f. I shall not trade in futures, commodity and currency.
 - g. I will limit my risk.

3. Goal Setting
 - a. I will try to complete an average of 3 trades a week.
 - b. I will maintain a solid mental and emotional state.
 - c. I will I improve my knowledge and skills

4. Financial Commitment
 - a. I will fund my account out of my savings with a minimum of \$100,000.00.
 - b. I will use margin as and when required for short durations.
 - c. I will borrow about \$50,000.00 from Veenu Mittal and Neil Mittal.
 - d. I will use TD Canada Trust Line of Credit for short durations.

5. Time Commitment
 - a. I will commit my time an average of 25 hours per week.
 - b. I will trade analysis on daily basis.
 - c. I will do market analysis on daily basis.
 - d. I will watch selective business programs on TV as required.
 - e. I will keep record of my account books weekly basis.
 - f. I will read financial newspaper and books.

6. Record Keeping
 - a. I will keep a record of all business transactions.
 - b. I will track profits and losses on monthly basis.

7. Trading Plan Methodologies
 - a. Analyse recommendations and risk analysis from financial institutions such as TD Waterhouse and BMO Investorline.
 - b. Analyze recommendations of top picks from business programs on TV such as BNN.
 - c. Analyze recommendations of "Buy and Sell" from financial newspapers.
 - d. Analyze if certain stock is dropped or appreciated considerably.
 - e. Analyze if there is significant news about any stock such as takeover etc.
 - f. I will further review based on
 - Stock valuation – EPS, P/E, ROIC, P/S, Market Cap, EBIDTA, BVPS etc.
 - Volatility
 - Yield, revenue stability, payout ratio, business outlook, liquidity, interest rates scenario, debt ratio (D/E)
 - Growth history and Potential of earnings, dividends and business
 - Geopolitical conditions
 - Cyclical stocks
 - Management issues, such as insider buying
 - g. Decision time – buying, selling, price target, financing
 - h. Exit – Sell the security, if the analysis indicates to sell and cut further losses or take profit.

8. Drawdown Rules
 - a. Stop trading immediately if the account balance exceeds a 50% drawdown of base capital and review what went wrong? For example:
 - Not executing trades when signals occur.
 - Executing trades when there is no entry signal.
 - Allowing losses to exceed predetermined amounts.
 - My contingency plan should any of those possibilities occur is "Take one week off from the markets to reevaluate my trading, current market conditions, my risk management and my mental and emotional stability. If a vacation is necessary, take one."

9. Compensation

- a. I will not draw any money from the business until I decide to retire from my employment. I will use all proceeds to further develop my business.

[5] Mr. Mittal described himself as something of a workaholic. He read extensively (he listed 16 finance related books) and used various sources to obtain the financial knowledge he deemed necessary to engage in his trading activity. He studied internet sites such as TD Waterhouse and BMO InvestorLine, as well as watching financial and business related television programs and attending numerous financial seminars. He kept logs of his time devoted to his trading activities including this research, as well as his actual trades, his recordkeeping, his banking and all incidental related activity. His logs showed an average of 25 hours a week devoted to this activity. He kept detailed records of all his trades.

[6] Mr. Mittal took me through his trades in 2006. There were several, Alcan, Bank of Montreal, Bank of Nova Scotia, Canadian National Railway, Enervest, ING, Loblaws, ISHARE, National Bank, Riocan, Royal Bank of Canada, Shoppers Drug Mart, Sun Life, TSX Group X, Teranet, Toronto-Dominion Bank, Yellow Pages and Toronto-Dominion RR Bonds, in which he acquired the shares in 2006 and sold either the same day, within a few days or certainly before year-end: all short-term holdings. There were seven sales in 2006 of shares (Advantex, Homeserve, Northgate Exploration, TS Telecom, TD Monthly Inc., TAL China and AGF Aggregate growth) which had been held since before 2005. In 2006, Mr. Mittal engaged in about 60 days of actual trading representing 160 trades with a value of \$3,237,279.

[7] 19 of the 27 stocks traded in 2006 were non-dividend bearing. Many were blue chip: a couple Mr. Mittal described as adventures, Northgate Exploration and TALVEST China Plus. The stock portfolio consisted of 18 publicly traded shares, four mutual funds, four income trusts and one bond.

[8] Mr. Mittal financed this activity from his own savings (approximately \$100,000), non-interest bearing demand loans from his two sons (one for \$41,000 and one for \$10,000 – one son was paid back in 2008), a line of credit used occasionally in short-term investments and a margin account rarely used.

[9] Mr. Mittal also invested for other family members including his wife, his sons and daughter-in-law, totalling investments of over \$700,000.

[10] The volume of trades in 2007 was considerably less (29 trades over 10 days of active trading). Most of these were sales with only a handful of purchases. Most activity was in the first three months of the year.

[11] Mr. Mittal explained that his research suggested a real concern with the U.S. market and household debt in 2007 and heading into 2008. He therefore significantly curtailed his activity. He claims he was proven right by the events of 2008.

[12] It was Mr. Mittal's intention that upon retirement he would rely on the trading activity as his business.

Issue

[13] Was Mr. Mittal in 2006 and 2007 a trader in securities or engaging in an adventure in the nature of trade, which would entitle him to deduct business losses of \$35,226 and \$23,659 respectively?

Analysis

[14] A non-capital or business loss is the taxpayer's loss from a business, business being defined in section 248 of the *Income Tax Act* (the "Act") to include a profession, calling, trade, manufacturing or undertaking of any kind whatever...and an adventure or concern in the nature of trade.

[15] There has been considerable jurisprudence on what constitutes engaging in stock market activity, entitling a taxpayer to deduct losses from that activity. The seminal decision of *Her Majesty the Queen v. Vancouver Art Metal Works Ltd.*¹ contains the oft-listed factors necessary to weigh in addressing this issue:

- a) Frequency of transactions.
- b) Duration of holdings.
- c) Intention to acquire for resale at a profit.
- d) Nature and quantity of securities.

¹ 93 DTC 5116 (FCA).

e) Time spent on activity.

[16] In the recent Federal Court of Appeal decision of *Baird v. Canada*,² the Court relied on the old Supreme Court of Canada case of *Irrigation Industries Ltd. v. Minister of National Revenue*³ to define an adventure in the nature of trade with both positive and negative principles:

...

The positive tests to which he refers as being derived from the decided cases as indicative of an adventure in the nature of trade are: (1) Whether the person dealt with the property purchased by him in the same way as a dealer would ordinarily do and (2) whether the nature and quantity of the subject-matter of the transaction may exclude the possibility that its sale was the realization of an investment, or otherwise of a capital nature, or that it could have been disposed of otherwise than as a trade transaction.

21. Thorson P., in *Taylor, supra*, also formulated a number of propositions which he characterized as negative propositions. These propositions were set out by Cartwright J. in his dissenting reasons in *Irrigation Industries, supra*, at paragraph 49 of his Reasons:

On the negative side:

- (i) The singleness or isolation of a transaction cannot be a test of whether it was an adventure in the nature of trade—it is the nature of the transaction, not its singleness or isolation that is to be determined.
- (ii) It is not essential to a transaction being an adventure in the nature of trade that an organization be set up to carry it into effect.
- (iii) The fact that a transaction is totally different in nature from any of the other activities of the taxpayer and that he has never entered upon a transaction of that kind before or since does not, of itself, take it out of the category of being an adventure in the nature of trade.

² 2010 FCA 35.

³ [1962] S.C.R. 346.

- (iv) The intention to sell the purchased property at a profit is not of itself a test of whether the profit is subject to tax for the intention to make a profit may be just as much the purpose of an investment transaction as of a trading one. The considerations prompting the transaction may be of such a business nature as to invest it with the character of an adventure in the nature of trade even without any intention of making a profit on the sale of the purchased commodity.

[17] In the Tax Court of Canada decision of *Rajchgot v. Canada*,⁴ Chief Justice Rip succinctly summarized the task facing the judge in these cases as follows:

... It is not the lack or presence of one or more factors that will determine whether a transaction is on capital or income account; it is the combined force of all of the factors that is important. There is no magic formula to determine which factors are more or less important. Some factors complement each other. Each case is different. A judge must balance all the factors.

...

[18] Finally, there has been a recent case, *Zsebok v. Canada*,⁵ in which Justice Sheridan suggested that to be a trader the Appellant "had to prove in addition to the above factors that he had a particular or special knowledge of the market in which he trades". Justice Sheridan was relying upon comments of Justice Noël in the decision of *Kane v. Canada*.⁶ In that decision, however, Justice Noël was dealing with whether the taxpayer was caught by the exception in subsection 39(4) of the *Act*⁷, precluding traders from using the election. Justice Noël did however state the following:

⁴ 2004 TCC 548.

⁵ 2012 TCC 99.

⁶ [1995] 1 C.T.C 1.

⁷ Except as provided in subsection 39(5), where a Canadian security has been disposed of by a taxpayer in a taxation year and the taxpayer so elects in prescribed form in the taxpayer's return of income under this Part for that year,

- (a) every Canadian security owned by the taxpayer in that year or any subsequent taxation year shall be deemed to have been a capital property owned by the taxpayer in those years; and

... The factors highlighted by the Court of Appeal have traditionally been applied indiscriminately to identify both persons who carry on a business in the true sense, as well as persons who are in business by virtue of having engaged in an adventure or adventures in the nature of a trade. Because they are badges or indicia of trade, they must be found to exist to a degree or another under either analysis before a conclusion as to the existence of a business for tax purposes can be reached. Usually, the distinction matters little as the tax treatment of profits or losses arising from a business is generally the same whether a business is found to exist as such or whether its existence is premised on the extended definition of the word "business". Hence, the Courts have paid little or not attention to it. ...

[19] With these principles in mind, was Mr. Mittal either a trader in securities, that is carrying on a business, or engaged in an adventure in the nature of trade? Following Justice Noël's observation it is unnecessary, for purposes of determining whether Mr. Mittal is eligible to claim business losses, to distinguish between the two. It is enough if he meets the less onerous requirement of being engaged in an adventure in the nature of trade. While I will go through the usual factors, it is appropriate to step back and get an overall impression of what Mr. Mittal was doing, his whole course of conduct as it were: the overall impression is of an individual spending a great deal of time, energy and money in a very organized and businesslike fashion in investing in the stock market, to the extent that he intended this to be his retirement business. Unfortunately for Mr. Mittal, it proved not to be as lucrative as he had hoped. Being unsuccessful, however, does not make it any less an adventure.

[20] I turn now to a review of the factors to support the overall impression that leads me to conclude Mr. Mittal was at the very least engaged in an adventure in the nature of trade.

(b) every disposition by the taxpayer of any such Canadian security shall be deemed to be a disposition by the taxpayer of a capital property.

a) Frequency of transactions

[21] I agree that there is no magic formula, no bright line test, that if you engage in say over 50 transactions it must be an adventure. At one end of the spectrum is the purchase of one stock, held for some lengthy period of time: at the other end of the spectrum is the purchase and sale of dozens of stock on a daily basis throughout the year, with few if any held for any considerable period of time. Where does Mr. Mittal fit along that spectrum vis-à-vis the frequency of transactions? I conclude that he resembles far more the day-trader with his 160 trades scattered throughout the year, than someone simply making the occasional isolated transaction. The Respondent argues that only 60 days of actual trading, with an average of only approximately three trades a week is not enough to justify the "adventure" status. So, is 100 days of trading with an average of five trades a week enough? As already indicated, the test cannot be reduced to such a mathematical formula. I find Mr. Mittal's number of trades and number of days trading is evidence of someone engaged in an adventure. This factor alone however is not determinative.

b) and c) Duration of holdings and intention to acquire for a profit

[22] From a review of Mr. Mittal's trades, it is clear the vast majority were short-term holds. Yes, there were some stocks sold in 2006 or 2007, acquired in 2005 or earlier, but not many (approximately 7) compared to the overall number of trades. This reflects an intention on Mr. Mittal's part to earn a profit on resale. Regrettably for Mr. Mittal, he does not appear to have played the market as effectively as he would have liked, but I have no doubt that is what he was doing - playing the market.

[23] Mr. Mittal's intention in this regard was confirmed by his evidence that upon retirement, trading would be his only business. The Respondent interpreted this evidence as suggesting the market was Mr. Mittal's retirement fund, that is, invest now to yield gains in retirement. That is not how I interpreted Mr. Mittal's evidence. It was not his intention to invest now to reap gains in retirement. It was his intention to be a good enough trader to earn ongoing profits from trading activity, something that in retirement he could devote all, not just part, of his time towards.

[24] I find this factor points decisively to someone engaged in an adventure, if not indeed to an actual trader.

d) Nature and quantity of securities

[25] Certainly there were some blue chip stocks acquired by Mr. Mittal, but this fact is overshadowed by the quick sale of most of these stocks. They do not appear to have been acquired for the long-term. I find that Mr. Mittal had a rather diversified portfolio. He did not limit himself to simply a handful of bank stocks for example. He only had the one bond and four mutual funds, somewhat safer bets, investing the greatest amounts in publicly traded shares. The Respondent argues that Mr. Mittal was not venturing in high risk stock. I agree the majority, though not all, of his stock investments were blue chip, but I do not find this factor alone is a clear indication that Mr. Mittal was not engaged in an adventure. I view this factor as neutral.

[26] With respect to risk, the Respondent argued that Mr. Mittal was not highly leveraged, relying primarily on his own funds. Yes, however, he did borrow from his family and did use a line of credit and margin account, though sparingly. I see this financing arrangement as a neutral factor.

e) Time spent on activity

[27] Mr. Mittal's uncontradicted evidence was that he put in approximately 25 hours per week on his trading activity, if all his research and study time was included. Mr. Mittal clearly attempted to become as steeped in the market as time permitted, not only on his own behalf but also for members of his family. This was not the occasional call or check the newspaper's listings, this was a daily devotion to following the market, studying the market and, as I have already characterized it, playing the market. It is a classic example of an adventure in the nature of trade.

[28] While I have referred primarily to 2006, my view is the same for 2007. Yes, there were less trades, less activity, but most of that activity was in the first few months of the year. I accept Mr. Mittal's testimony that his research led him to proceed with caution in the latter half of 2007. It would make little sense to view his activity in 2007 to be any less of an adventure than it was in 2006.

[29] The Appeals for 2006 and 2007 are allowed and referred back to the Minister for reconsideration and reassessment on the basis that the losses incurred by Mr. Mittal in 2006 and 2007 are business losses. Costs to the Appellant.

Signed at Ottawa, Canada, this 28th day of November 2012.

"Campbell J. Miller"

C. Miller J.

CITATION: 2012 TCC 417

COURT FILE NO.: 2011-1396(IT)G

STYLE OF CAUSE: OMP. MITTAL AND HER MAJESTY THE QUEEN

PLACE OF HEARING: Toronto, Ontario

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REASONS FOR JUDGMENT BY: The Honourable Justice Campbell J. Miller

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APPEARANCES:

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