Docket: 2010-3668(IT)I

BETWEEN:

JERRY KUHLMANN,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

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Appeals heard on August 16, 2011, at Toronto, Ontario

By: The Honourable Justice E.A. Bowie

Appearances:

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|---|---|
| For the Appellant: | The Appellant himself |
| Counsel for the Respondent: | Erin Strashin |

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**JUDGMENT**

The appeals from reassessments made under the *Income Tax Act* for the 2005, 2006 and 2007 taxation years are dismissed.

Signed at Ottawa, Canada, this 1st day of September, 2011.

"E.A. Bowie"

Bowie J.

Citation: 2011 TCC 410
Date: 20110901
Docket: 2010-3668(IT)I

BETWEEN:

JERRY KUHLMANN,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

**REASONS FOR JUDGMENT**

**Bowie J.**

[1] Section 3 of the *Income Tax*[1] (the *Act*) mandates that taxpayers compute their income each year by aggregating their income from all sources, including net taxable capital gains, and deducting from that total their losses, if any, from any office, employment, business or property. When he filed his income tax returns for the 2005, 2006 and 2007 taxation years Mr. Kuhlmann declared his aggregate income from a number of sources, principally pension benefits, and he deducted from that what he claimed to be his share each year of the business losses sustained by a partnership called JHK& BK Enterprises (Enterprises). The results may be summarized this way:

| | 2005 | 2006 | 2007 |
|---|---|---|---|
| Income from various sources | $52,643 | $51,213 | $51,513 |
| Less share of partnership losses | 16,508 | 15,059 | 10,848 |
| Total income | $36,135 | $36,154 | $40,665 |

[1] R.S. 1985 c.1 (5th supp.), as amended.

[2] Initially the Minister assessed Mr. Kuhlmann on the basis upon which he had filed his returns, but upon further reflection he took the view that Enterprises was not a source of income, and so he reassessed Mr Kuhlmann for the years in question to disallow the deduction of the partnership losses from his aggregate income. Mr. Kuhlmann objected to the reassessments, the Minister confirmed them, and Mr. Kuhlmann now appeals from those reassessments.

[3] The appellant was the only witness at the trial. His evidence was, for the most part, candid and credible. I do, however, have some difficulty accepting his evidence that he simply gave all his receipts to his accountant,[2] and that he signed the income tax returns that she prepared for him without giving any consideration to their contents. It seems unlikely that someone with a degree in business administration would not be inclined to question some of the very obviously exaggerated claims for expenses that were made, such as vacation trips and theatre tickets for the appellant and his wife.

[4] Mr. Kuhlmann is an engineer, and also has a business administration degree. He was employed for almost 30 years by the Dow Chemical Company. In 1995 he retired from Dow under an arrangement by which he would be paid a deferred pension starting at age 60. At that time, with a view to starting a consulting business, he and his wife registered a partnership by the name of JHK & BK Enterprises. During the next few years Mr. Kuhlmann worked as a consultant under that partnership name. His major client was Vulsay Industries Ltd., for which he did consulting work that he invoiced monthly for several years. At some point Vulsay offered him full time salaried employment as a sales manager, and he worked in that position until 2005. In 2005, following a change in control of Vulsay Industries, Mr. Kuhlmann again retired, with a pension from Vulsay.

[5] At this point Mr. Kuhlmann, in his words, started looking for either fulltime or part time work. Although Enterprises had been dormant since Mr. Kuhlmann became an employee of Vulsay, it was still extant as a registered partnership. Had the appellant found work that could be carried on as an independent contractor rather than as an employee, then no doubt he would have done it in the name of Enterprises, as he did prior to the period of his employment by Vulsay. In his words, his efforts

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2 The appellant referred numerous times in his evidence to his accountant, and blamed her for the numerous inflated claims of expenses in the computation of the partnership losses each year. She was not called to testify, and I have no idea what qualification she has, if any. Judging by the income tax returns that she prepared for the appellant I think her claim to the designation “accountant” is spurious at best.

were fruitless – he did not find any opportunities, and in 2008 or 2009 he gave up looking and retired. He testified that he did incur expenses in looking for work, however, and, encouraged by his "accountant", he claimed those expenses, and many that had no connection to his search for work, as the expenses of Enterprises. As Enterprises had no revenue whatsoever during the years under appeal the statements of business activities for the partnership which the appellant filed as part of his income tax returns show losses equal to the amount of the claimed expenses each year. For some unexplained reason the appellant claimed 100% of these losses as his share in 2005, and 80% in each of 2006 and 2007.

[6] Enterprises certainly was a source of income for some period of time before the appellant took employment with Vulsay. Was it that in 2005 to 2007? Some assistance with this question can be had from the judgment in *Kaye v. The Queen*.[3] There Bowman J., as he then was, said this:

> 4 I do not find the ritual repetition of the phrase ["no reasonable expectation of profit"] particularly helpful in cases of this type, and I prefer to put the matter on the basis "Is there or is there not truly a business?" This is a broader but, I believe, a more meaningful question and one that, for me at least, leads to a more fruitful line of enquiry. No doubt it subsumes the question of the objective reasonableness of the taxpayer's expectation of profit, but there is more to it than that. How can it be said that a driller of wildcat oil wells has a reasonable expectation of profit and is therefore conducting a business given the extremely low success rate? Yet no one questions that such companies are carrying on a business. It is the inherent commerciality of the enterprise, revealed in its organization, that makes it a business. Subjective intention to make money, while a factor, is not determinative, although its absence may militate against the assertion that an activity is a business.
>
> 5 One cannot view the reasonableness of the expectation of profit in isolation. One must ask "Would a reasonable person, looking at a particular activity and applying ordinary standards of commercial common sense, say 'yes, this is a business'?" In answering this question the hypothetical reasonable person would look at such things as capitalization, knowledge of the participant and time spent. He or she would also consider whether the person claiming to be in business has gone about it in an orderly, businesslike way and in the way that a business person would normally be expected to do.
>
> 6 This leads to a further consideration -- that of reasonableness. The reasonableness of expenditures is dealt with specifically in section 67 of the *Income Tax Act*, but it does not exist in a watertight compartment. Section 67 operates within the context of a business and assumes the existence of a business. It is also a component in the question whether a particular activity is a business. For example, it cannot be said, in the absence of

[3] [1998] 3 C.T.C. 2248.

> compelling reasons, that a person would spend $1,000,000 if all that could reasonably be expected to be earned was $1,000.
>
> 7 Ultimately, it boils down to a common sense appreciation of all of the factors, in which each is assigned its appropriate weight in the overall context. One must of course not discount entrepreneurial vision and imagination, but they are hard to evaluate at the outset. Simply put, if you want to be treated as carrying on a business, you should act like a businessman.[4]

[7] When the matter is viewed in this light it is evident that there was no business here during the years under appeal. There is no commerciality and no businesslike activity here. There is simply someone looking for work, either as an independent contractor or as an employee, either full time or part time. It is not reasonable to expect the fisc to subsidize the search for employment, otherwise than through the employment insurance system created for that purpose.

[8] *Kaye* was, of course, decided before the Supreme Court of Canada's decision in *Stewart v. The Queen*.[5] The test applied by Bowman J., however, is totally consistent with the Supreme Court's restatement there of the approach to be taken:

> We would also emphasize that although the reasonable expectation of profit is a factor to be considered at this stage, it is not the only factor, nor is it conclusive. The overall assessment to be made is whether or not the taxpayer is carrying on the activity in a commercial manner. However, this assessment should not be used to second-guess the business judgment of the taxpayer. It is the commercial nature of the taxpayer's activity which must be evaluated, not his or her business acumen.[6]

[9] Nor does it assist the appellant that Enterprises at one time carried on a business and so was a source of income. In *Moufarrège v. Quebec (Deputy Minister of Revenue)*[7] The Supreme Court of Canada said this at paragraphs 4-5:

> 4 *Stewart v. Canada*, 2002 SCC 46 (CanLII), [2002] 2 S.C.R. 645, 2002 SCC 46, did not alter the principle that when a reasonable expectation of income disappears, so does the

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4 Ibid., paras. 4 -7.

5 [2002] 2 S.C.R. 645.

6 *Ibid*. para 55.

7 2005 SCC 53.

> right to a deduction. In that decision, the Court stated that "the deductibility of expenses presupposes the existence of a source of income" (para. 57).
>
> 5 In the instant case, once the properties were sold, the source of income ceased to exist and the loan was no longer being used to earn income from property in accordance with ss. 128 and 160. With regard to the shares, the company in question is bankrupt, and nothing in the record indicates a possibility of a resumption of activities, so here too the source of income has disappeared even though the company has not been dissolved.

When Enterprises ceased to be a source of income, as it did when Mr. Kuhlmann became an employee of Vulsay, Mr. Kuhlmann's right to deduct its supposed losses came to an end.

[10] In view of this conclusion it is not necessary to consider which of the numerous items making up the supposed losses of Enterprises are personal expenses. There being no business, the expenses are all personal and therefore are not deductible.

[11] The appeals are dismissed.

Signed at Ottawa, Canada, this 1st day of September, 2011.

"E.A. Bowie"

Bowie J.

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|---|---|
| CITATION: | 2011 TCC 410 |
| COURT FILE NO.: | 2010-3668(IT)I |
| STYLE OF CAUSE: | JERRY KUHLMANN and<br>HER MAJESTY THE QUEEN |
| PLACE OF HEARING: | Toronto, Ontario |
| DATE OF HEARING: | August 16, 2011 |
| REASONS FOR JUDGMENT BY: | The Honourable Justice E.A. Bowie |
| DATE OF JUDGMENT: | September 1, 2011 |

APPEARANCES:

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| For the Appellant: | The Appellant himself |
| Counsel for the Respondent: | Erin Strashin |

COUNSEL OF RECORD:

For the Appellant:

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| Name: | N/A |
| Firm: | N/A |
| For the Respondent: | Myles J. Kirvan<br>Deputy Attorney General of Canada<br>Ottawa, Canada |