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## When Does a Hobby Become a Business?

Many Canadians working full-time jobs or regularly engaged in business also pursue personal endeavours on the side. For example, you may enjoy photography, painting, collecting, or gardening. At first, these activities might resemble personal hobbies, but if they produce revenue or result in expenses, the question arises of whether the revenue is income and therefore taxable, and whether the expenses are deductible in calculating income.

With the rise of the online digital economy, it's tempting and simple to make a few extra bucks from renting out a spare room,

selling handmade mittens or old trading cards, or picking up passengers for a couple of hours each night. There can be a very fine line between a lively hobby and a business. The distinction is further complicated where bricks and mortar storefronts are replaced by apps, websites, or online accounts.

There are a variety of ways to earn revenue from online platforms:

- **Sharing economy**

Using or sharing personal assets to earn revenue. For example, ridesharing is an arrangement in which a

driver uses a private vehicle to offer passenger transportation services for a fee, arranged through an online platform such as Lyft or Uber. Accommodation sharing is renting part or all of a property, usually for a short period, and includes any rentals facilitated by a third-party website or application such as AirBnB, CanadaStays, FlipKey, or VRBO.

- **Gig economy**

The gig economy generally refers to services provided through short-term contracts, freelance work, or other temporary work. Gig workers operate as independent contractors and freelancers. Frequently, arrangements are made through an online platform or mobile application such as:

- Fiverr;
- Clickworker;
- Crowdsource;
- Uber Eats; and
- Skip the Dishes.

Contracted services can range from a micro-task to larger, specialized services.

- **Peer-to-peer ("P2P")**

The P2P economy includes situations where third-party sellers connect with buyers through online platforms such as websites, applications, and

marketplaces to sell their products. Commonly used platforms include:

- Kijiji;
- Etsy;
- eBay; and
- Amazon.

#### • **Social Media Influencers**

A social media influencer is an individual who has created a significant influence or presence on a social media platform and has an audience of users who interact with the influencer's content. Influencers can work as content creators, bloggers, photographers, journalists, fitness coaches, fashion promoters, business consultants, entertainment workers, and many other occupations. Platforms an influencer may use include:

- Facebook (Meta);
- Instagram;
- Twitch;
- Twitter (X);
- YouTube; and
- Independent blogs.<sup>1</sup>

Influencers can earn income in a number of ways, both monetary and non-monetary (barter transactions), including but not limited to:

- subscriptions to their channel(s);
- advertising (clickbait and brand advertisements);
- sponsorships;
- calls to action;
- merchandise sales or commission on sales;
- tips;

- perks such as products, clothes, trips, or other gifts; and
- referral codes.<sup>2</sup>

In most situations, Airbnb, Uber, and gig revenues are clearly a source of income – these are activities undertaken in pursuit of profit with a limited to non-existent personal element. But what about receipts from more casual activities like the sale of collectibles or handmade crafts on eBay or Etsy? So, when exactly does a hobby become a business?

In some situations, a taxpayer may prefer their hobby to be regarded as a business by the CRA, especially when there are significant expenses to deduct.<sup>3</sup> In other cases, could there be an unpleasant shock for taxpayers who are assessed on the takings from what they thought was a personal hobby? Fortunately, as the practice and jurisprudence reveal, the deliberate actions which establish that an undertaking is a business rather than a hobby make surprise unlikely.

In general, a personal endeavour is undertaken for motives other than for profit. The hobbyist seeks a personal benefit rather than a financial one. On the other hand, there is frequently a personal element in the carrying on of a business. A person may derive great personal satisfaction from the activity, but this doesn't make the activity any less a business. Even lawyers and accountants may derive great satisfaction from what they do, but their activities are commercial, intended to yield a profit, and unmistakably are businesses.

In *Stewart v. Canada*, the Supreme Court explained the distinction between personal and business activities:

... in order to determine whether a particular activity constitutes a source of income, the taxpayer must show that he or she intends to carry on that activity in pursuit of profit and support that intention with evidence. The

<sup>1</sup> CRA Publication, "Taxes and the platform economy", March 8, 2023.

<sup>2</sup> CRA News Release, "Are you a social media influencer? Here's what you need to know", March 8, 2023.

<sup>3</sup> The CRA may still question whether a particular expense is reasonable in the circumstances.

purpose of this test is to distinguish between commercial and personal activities, and where there is no personal or hobby element to a venture undertaken with a view to a profit, the activity is commercial, and the taxpayer's pursuit of profit is established. However, where there is a suspicion that the taxpayer's activity is a hobby or personal endeavour rather than a business, the taxpayer's so-called reasonable expectation of profit is a factor, among others, which can be examined to ascertain whether the taxpayer has a commercial intent.<sup>4</sup>

For income tax purposes in Canada, an activity that includes a personal element like a hobby may constitute a business if: (a) it is carried on with the intention—sometimes described as a “predominant intention”—of earning profit, and (b) there is a reasonable expectation of profit. Call this the “Hobby Test”.

Part (a) of the Hobby Test is a subjective assessment, part (b) is objective. Both are determined based on an analysis of the evidence. Intention is indicated by the taxpayer's conduct and the nature of the activity—look for evidence that reveals “indicia of commerciality” or “badges of trade”. Part (b), a reasonable expectation of profit, is determined by the performance of the activity—has the activity been carried on in accordance with objective standards of business-like behaviour?

*Stewart* identified several factors to be considered when determining if there is an intention to profit:

- the profitability of prior years;
- the taxpayer's training;
- the taxpayer's intended course of action; and
- the capability of the venture to show a profit.

However, this list is not exhaustive, and the factors will differ with the nature and extent of the activities. Look for other indicators such as capitalization, the participant's knowledge, and time spent.

Turning to part (b) of the Hobby Test, the assessment of “reasonable expectation of profit”, ask: Would a reasonable person, looking at this activity and applying ordinary standards of commercial common sense, say “yes, this is a business”? Has the person undertaken the activity in an orderly, businesslike way, in the way a businessperson would normally be expected to do? 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 their business acumen.

In *Brooks v. The Queen*,<sup>5</sup> Brooks purchased all sorts of ephemera online (Beanie Babies, football and Royal Navy memorabilia, VHS tapes, and so on). He hoped to resell these items at a profit but never sold a single one. His claim for business losses was rejected because there was no evidence he made any concerted and serious efforts to sell his wares. Brooks' activities were merely a hobby, and he did not carry out those activities under “objective standards of businesslike behaviour”.

Two recent Tax Court cases addressed the hobby vs. business tension in relation to “professional” poker players: *Bérubé v. The King*<sup>6</sup> and *D'Auteuil v. The King*.<sup>7</sup> The sole issue was whether gains earned by the gamblers while playing poker qualified as business income for income tax purposes.

Bérubé had abandoned his studies to play poker. It was his only source of income during the years in issue, and the quasi-totality of his available time was spent playing or learning and studying about poker. Regardless of his unusual lifestyle, Bérubé behaved like a seri-

<sup>4</sup> 2002 SCC 46.

<sup>5</sup> 2007 TCC 557. *Lang v. The Queen*, 2006 TCC 412 (writing and sales of memorabilia), *Lakeway Truck Centre Ltd. v. The Queen*, 2007 FCA 160 (auto racing), *Varcoe v. The Queen*, 2007 FCA 159 (auto racing), and *Kelly v. The Queen*, 2005 TCC 130 (auto racing) also failed to make the leap from a personal hobby to a business.

<sup>6</sup> 2023 CCI 12.

<sup>7</sup> 2023 CCI 3.

ous businessman. His playing was more than a hobby or playing for fun. Accordingly, the Tax Court found that, on a balance of probabilities, Bérubé had the subjective intention of earning a profit from his poker activities and he used his skills and expertise to earn a living playing poker. His poker earnings were business income. D'Auteuil also pursued his activities as a poker player in an organized, methodical way, much like Bérubé. The Tax Court determined his poker gains were also business income.

Even if a hobby or personal undertaking does not constitute a business for purposes of the *Income Tax Act*,<sup>8</sup> if you sell personal-use property related to your hobby activity for more than \$1,000 per sale, any gain received from the transaction may be subject to income tax as a capital gain from a personal-use property.<sup>9</sup> Generally, personal-use property is, as the name suggests, property owned by a taxpayer that is used primarily for the personal use or enjoyment of the taxpayer and related individuals.<sup>10</sup>

For example, take an amateur artist who creates a painting that hangs in his house for years which he later sells on Etsy. Any gain realized on the sale could be taxable. If the adjusted cost base ("ACB") of the painting is less than \$1,000, its ACB is deemed to be \$1,000. If the

proceeds of disposition are less than \$1,000, the proceeds are deemed to be \$1,000. If both the ACB and the proceeds of disposition are \$1,000 or less, you do not have a capital gain or a capital loss. This rule effectively exempts small personal property gains from taxation. However, if either the ACB or the proceeds of disposition are more than \$1,000, you probably have either a capital gain or a capital loss. Capital gains must be reported on Schedule 3, *Capital Gains (or Losses)*, which is filed with your T1 return. Capital losses on personal use property, on the other hand, are typically not able to be claimed, unless the property is listed personal property, which would include the painting in this example.

Applying the two-part Hobby Test to a digital enterprise can be incredibly difficult. Fortunately, detailed records are retained by most apps or online services. In the digital economy, there are almost no cash transactions, and an electronic payment record will be produced for every sale, ride, or stay. If it turns out your hobby does constitute a business, this income must be declared and reported on Form T2125, *Statement of Business or Professional Activities*, and filed with your T1 income tax return. And as always, when in doubt, consult a tax professional.

<sup>8</sup> *Income Tax Act*, ss. 3, 4, 9(1), 248(1) "business".

<sup>9</sup> *Income Tax Act*, s. 46.

<sup>10</sup> *Income Tax Act*, s. 54 "personal-use property".