

FOR YOUR CONSIDERATION In the 3rd quarter of 2013

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This publication is a high-level summary of the most recent tax developments applicable to business owners, investors, and high net worth individuals. Enjoy!

AUTO ALLOWANCES: Fixed Payments for Small Trips Can be Costly!

In a March 28, 2013 Technical Interpretation, the Canada Revenue Agency (CRA) notes that:

1. An **allowance** received for the use of a **motor vehicle** is deemed **not** to be **reasonable** (and therefore taxable to the employee) unless based solely on the **number of kilometres** travelled.



2. In this case, the employee was provided \$4.60 **per trip** of less than 10 kilometres. CRA concluded that this payment would be **taxable to the employee**, however, certain expenses may be deductible by the employee.

Because it is a taxable allowance, the **employer** will **not be entitled** to the GST/HST **Input Tax Credit**. However, the **employee**, in addition to deducting employment expenses, may be **entitled to a GST/HST rebate**.

Action Item: Motor vehicle allowances are a common target of CRA review because many detailed rules apply. Give us a call if you want to review the tax implications of your motor vehicle allowances.

DISASTER RELIEF PAYMENTS: What Is the Tax Impact?

In a June 27, 2013 Technical Interpretation, CRA indicated that there would be **no immediate tax** consequences for payments respecting **personal losses** received as a result of Alberta **flood relief** assistance.

In a July 12, 2013 Technical Interpretation, CRA commented on an employer's **emergency assistance plan**, under which the **employer would match** voluntary employee contributions to create a relief fund directed to assist employees in their recovery efforts. All **payments** would be **based exclusively on need** and the extent of damage to the employee's property.

CRA indicated that disaster relief payments received in the individual's capacity **as an employee** would be **taxable**. However, payments received **as an individual** would **not** be subject to taxation. CRA would generally consider the payments to be received on an individual, non-taxable basis provided **all of the following** criteria are met:

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- the recipient was **affected by a disaster** (CRA refers the reader to <http://www.publicsafety.gc.ca/prg/em/cdd/index-eng.aspx> in this regard);
- the **payment is philanthropic** and intended to compensate for personal losses or damage suffered during a disaster;
- the payment is made in **a reasonable period of time** following the disaster;
- the payment is **voluntary, reasonable** and **bona fide**;
- the recipient deals **at arm's length with the employer**, and not to a shareholder, connected person or person of influence such as executives with the power to control company decisions (CRA notes that payments to such persons may still be received in capacity as an individual, where the **facts demonstrate** the receipt was on the **same basis as** payments to other **individuals who deal at arm's length** with the employer);
- the payment **is not based on employment factors** such as performance, position or years of service;
- the payment is **not made** in exchange **for past or future employment services** or to compensate for **loss of income**;
- the payment **is not in respect of regular salary** for a period in which the individual is unable to report to work due to a disaster; and
- the **employer does not claim** a business **deduction** in respect of the payment (CRA notes it would not be a charitable contribution as it is not paid to a registered charity).

Action Item: *Structure relief payments to employees correctly or they may be hit with a big tax bill.*

EMPLOYMENT INSURANCE: Which Working Hours Count?

The number of hours or weeks one needs to qualify for EI are based on where the person lives and the unemployment rate in that economic region at the time the claim is filed. In an April 12, 2013 Tax Court of Canada case, at issue was how many of a teacher's hours worked were **insurable hours** under the **Employment Insurance Act** (EIA).

Taxpayer wins

The government originally did not include hours spent

attending meetings assigned by a principal, **preparation and planning** of courses, **marking** student work, and **recording student achievements** in determining eligible employment hours.

The Court noted that:

The EIA defines hours of insurable employment and notes that where a person's earnings are **not paid** on an **hourly** basis but the employer provides evidence of the **number of hours** that the person actually **worked** in the period of employment and for which the person was **remunerated**, the person is **deemed** to have worked that number of hours in **insurable employment**.

The Court increased the number of hours from 509 (as conceded by CRA) to 547 hours for this extra time.

Action Item: *Although this case refers to a teaching scenario, consider whether it also applies to you or your employees.*

BUSINESS EXPENSES – Prove It!

In a June 20, 2013 Tax Court of Canada case, at issue was whether the taxpayer, Mr. L, **operated a business** activity providing consulting services, whether the expenses he claimed were deductible, and whether **gross negligence penalties** should be applied.



In his 2007 Tax Return, \$2,000 in professional gross revenue and \$17,154 in expenses for a loss of \$15,154 were reported. In 2008, no gross income and \$12,190 of business expenses were claimed.

Taxpayer loses

The Appeal was denied and the costly gross negligence penalty left in place. The Judge noted, "There was **no credible explanation** that would indicate that any of the amounts that Mr. L reported on his tax returns in respect of his purported consulting business were incurred for the purpose of gaining or producing income. At best, I believe that Mr. L was indifferent as to whether the expenses that he claimed on his tax return were accurate or not. More likely, I believe that Mr. L knew the expenses he claimed on his returns were false and claimed them anyway."

Action Item: *Ensure that you are maintaining the necessary support in an efficient manner before the Tax Man comes to call! We can assist with a review of your recordkeeping system if needed.*

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3RD PARTY DISCLOSURE OF UNREPORTED INCOME

In an April 10, 2013 Tax Court of Canada case, CRA reassessed a taxpayer to **include** approximately \$28,000 of income. CRA based this income inclusion on the results of the audit of a different company which listed the taxpayer as a Subcontractor.

Taxpayer wins

The Court indicated that, "It is simply **insufficient to tax** a person solely because **another person under audit points** to them and provides their name and address. Names and addresses are readily available publicly and the companies **could** just as easily **have given** CRA almost **any** Canadian's **name**, this would include mine." In allowing the appeal, the Court indicated "it is unfortunately **entirely possible** that **the taxpayer** did work for, and **got paid** by, these companies. However, the **evidence** of that, such as it is, **falls very short** of allowing me to conclude that, on a balance of probabilities, he did."

Action Item: CRA's assessments can be challenged – make sure you contact us to review any surprises from the CRA. While the win is positive, it bears noting that the taxes were only reversed because the taxpayer went to court.

OLD TAX RETURNS: They can be reopened!

In a May 31, 2013 Tax Court of Canada case, at **issue** was whether **shareholder withdrawals** of \$28,791, \$32,173 and \$23,351 for the 2004, 2005 and 2006 taxation years, respectively, could be added as **personal income**.

CRA generally has **three years from** the date of their initial **assessment** to revise its assessment of an individual or Canadian-controlled private corporation's income tax return. At the time of reassessment, the 2004 and 2005 years were **past this deadline**. Any **misrepresentation** that is attributable to **neglect, carelessness** or **willful default** is subject to reassessment, even if the usual deadline has passed.

Taxpayer loses

The Judge noted that, **meaningful books do not exist** for the Company or the Appellant, and if they do, they were not produced at the Hearing nor were any source documents regarding actual receipts, vouchers or invoices relevant to specific business expenses. As the reconciliation of the shareholder's loan account was rendered impossible by the **absence of an ascertainable flow of funds**, the Court did not allow for a reduction in personal benefits received other than for a minor amount.

The Judge found that the CRA discharged its onus of proof thereby **allowing the reassessment** of these years **past the usual deadline** on the basis that the returns were signed with such **imprecise expenses**, shareholder advances and benefits that a misrepresentation was presented due to **carelessness**.

Taxpayer wins

The Court, however, did **not** find that the errors were the result of **dishonesty or deceit** and, therefore, did **not** fall within the threshold for the imposition of **gross negligence** penalties of 50% of the underlying taxes.

Action Item: While the taxpayer lost his case, removal of the penalties reduced his tax cost by a third of what CRA had assessed – it can be worthwhile challenging CRA's assessments.

RENTAL PROPERTY: Receipt Retention Issue – more than 6 years!

On August 31, 2010, CRA had advised the taxpayer that his income tax return for the 2007 year was under review and that he was required to provide information and documents concerning a rental property sold in 2007.

The taxpayer had **disposed of the rental property** for \$285,000. CRA included this amount on the **2007** Personal Tax Return but **reduced the Adjusted Cost Base** (ACB) claimed by the taxpayer by the estimated \$52,810 of renovation expenses which the taxpayer had added.

The dispute was settled in a July 3, 2013 Tax Court of Canada case. The taxpayer could **not provide any corroborating evidence** of the renovation costs, therefore, the Court did not accept this as part of the ACB.

The taxpayer referred to the expiration of **six years** as being the **time** for which he had to **keep receipts**.

CRA successfully argued that this **six years** commences **after the year** to which the **costs relate**. Therefore, costs which become part of the ACB of the property must be maintained for **six years** after the property is **disposed**, not six years after the costs are incurred.

Related to the above, in a June 14, 2013 Technical Interpretation, CRA noted that permanent documents must be kept for a period ending two years following the dissolution of the corporation and the **general documents** must be kept for a period ending **six years** following the last year for which they **relate**, unless the corporation is dissolved, in which case the period ends two years following the dissolution of the corporation.

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It should be noted that, at the Tax Court, the **onus is on the taxpayer to prove the CRA is wrong**, not the other way around. "Innocent until proven guilty" is a principal of criminal law, and most tax disputes are not criminal in nature.

Action Item: Don't throw out the receipts for improvements to property! Keep them separate from regular expense receipts.

U.S. SNOWBIRD: Watch Out for the new U.S. Visa!

U.S. immigration reform legislation proposing to allow Canadians aged 55 and older to spend **240 days in the country** without a Visa is still on track to become law.



It is, however, noted that **provincial healthcare limits** on time spent out of the country ranging from 6 to 7 months could reduce the amount of time that an individual could spend regardless of the U.S. Visa changes.

Although immigration reform is being proposed, **taxation law** is not likely to significantly change. This means that individuals staying in the U.S. more than, say, 121 days in a year (based on complicated calculations) may still be deemed resident and find themselves exposed to **additional U.S. filings, tax**, and an assortment of other taxation issues. Individuals may be able to obtain some relief if they stay up to 183 days if they are considered to have a closer connection with Canada and complete the appropriate form.

Action Item: The IRS can be quite aggressive in pursuing filings. Please let us know if you are, or will be, spending a significant amount of time in the U.S.

TEMPORARY EMAIL ACCOUNTS – www.10minutemail.com

When registering for an online service or acquiring information on the internet, users may be required to provide a **valid email address**. However, there **may be a risk** associated with providing this information due to spam, junk and viruses.



10minutemail.com is a free online service that may alleviate this problem by providing a **temporary email address**. Users of 10minutemail.com can access their personal temporary email account for a short period, **10 minutes**, without risking the security of their own personal or work email accounts.

This service also allows users the option of **forwarding emails** from their temporary account to their real email accounts should they wish to retain the information.

Lastly, users can extend the life of the 10 minute email account by simply clicking on 'Give me 10 more minutes'.

Action Item: Protect your email address using 10minutemail.com.

DROPBOX – Dropbox.com

Dropbox.com is a popular service which enables users to **synchronize, share** and **back-up files** via computer, tablet or iPhone.

The service is fairly **easy to use** thanks to its smooth integration with Windows and other platforms. Once installed, Dropbox appears as a folder in My Documents and similarly functions like any other regular folder.

Users are able to share documents in the folder, whether or not they use Dropbox, making it a great **medium to collaborate with friends** and co-workers.

Dropbox.com offers **2GB of free storage**, however, paid upgrades are available if users require more space.

Prior to employing this service, it is important to **consult with your IT Representative** to ensure it complies with your organization's IT policy.

Action Item: Data security is a common issue in the electronic age. Consider obtaining permission from the other party when transferring information via services like Dropbox.com.

GST/HST: CRA Spring Release (No.88) - A Potpourri of Issues

Some points mentioned include:

1. The **2013 Federal Budget** expands the **exemption for homecare services** made after March 21, 2013 to include publicly subsidized or funded **personal care services**, rendered to an individual who, due to **age, infirmity or disability**, requires such **assistance at home**.



Accordingly, the Budget adds a new term, "home care

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service”, which includes **personal care** services such as bathing, feeding and assistance with dressing and taking medication. Also included are **household services** such as cleaning, laundering, meal preparation, and child care.

Where a service provider charges GST/HST on an exempt supply of a homecare service made after March 21, 2013, the **supplier may refund or credit the GST/HST** to the purchaser. **Alternatively**, purchasers who have paid an amount as GST/HST on exempt supplies **may claim a rebate** of tax paid in error using **Form GST189**.

2. Currently, **basic business identification information** is required to be provided at the time of GST/HST Registration. This includes the legal and operating name of the business, type of ownership, ownership details, business activity, and contact information.

In the likely future, the Minister of National Revenue will have the discretionary authority to **withhold the**

payment of GST/HST refunds to a person **until all** of the person’s prescribed business identification information has been **provided and is accurate**.

3. CRA discusses **music programs** and notes that the supply of a service of tutoring or instructing an individual in **music lessons** is **exempt** from the GST/HST. Music lessons involve formal instruction that develops skills in musical performance involving the use of the human voice or musical instruments, conducting an orchestra, or musical composition.

Whether a particular activity or program is a music lesson is a question of fact. The CRA has developed a number of questions to help make this determination. See Excise GST/HST News No. 88 for the criteria.

Action Item: The GST/HST rules change frequently. A regular review of your accounting systems to ensure they properly identify GST/HST on your invoices, and on your expenditures, can avoid costly errors.

The preceding information is for educational purposes only. As it is impossible to include all situations, circumstances and exceptions in a newsletter such as this, a further review should be done by a qualified professional.

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For any questions... give us a call.

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