**GENERAL NOTES**

- 3 main economic functions of govs:

* 1) Allocation.
	+ Public goods and services (school, health, defence, might include carbon taxes, etc.). Funded by tax.
* 2) Distribution.
	+ Market needs to be regulated. Redistribution via tax.
* 3) Stabilization.
	+ Monitoring unemployment etc. through monetary policies (interest rates) and fiscal policies (gov borrowing to spend on infrastructure, etc.). Tax in boom times to pay off debt.

- Horizontal equity: Requires that individuals who are similarly situated wrt income be treated the same.

- Vertical equity: Requires that TPs w differing incomes be treated/taxed differently based on ability to pay.

**- 150(1)(d)** When and how to file:

* Return of income in prescribed form shall be filed w Minister w/out notice or demand (no reminders) for each taxation year of a TP (April 30th).
	+ **248(1)** “Prescribed” = decided by the Minister.
	+ **248(1)** “Minister” = Minister of National Revenue.
* **150(1.1)** Exceptions – 150(1) does not apply unless:
	+ **(b)(i)** Tax is payable.
	+ **(b)(ii)** There is a taxable capital gain or TP has disposed of capital property.

- **Part 1 Division A: Liability for Tax** (s.2(1)).

- **Part 1 Division B: Computation of Income** (ss.3-107):

* Sub A: Office and employment income or loss (ss.5-8).
* Sub B: Biz or property income or loss (ss.9-37).
* Sub C: Taxable capital gains and allowable capital losses (ss.38-55).
* Sub D: Other sources of income (ss.56-59).
* Sub E: Deductions in computing income (ss.60-66).
* Sub F: Rules relating to that computation of income (ss.67-80).

**STATUTORY INTERPRETATION**

**STRICT APPROACH**

- Traditionally, courts adopted a strict approach.

- *Partington v Attorney-General* (1869) HL: Focus on the letter of the law, not the spirit of the Act. If a TP does something that complies w the words, even w the wrong intention, it is legitimate.

* Statutory language is construed literally.
* Ambiguities in taxing provisions are resolved in the TP’s favour.
* Ambiguities in relieving provisions (deductions & exemptions) are resolved against the TP.
* Not about equity.

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| MNR v MacInnes 1954 ExCt-Strict approach-Substituted property | - TP gave $ and bonds to his wife, who put them into her savings account. Several transactions, she eventually invested in other securities. *Income War Tax Act* attributed income earned on $ transferred btwn husband/wife to transferor, including substituted property.* Issue – whether “property substituted therefore” includes property substituted for substituted property.

- No. The language didn’t account for this – “the court has no right to assume that a transaction is w/in the intention…of a taxing Act if it does not fall w/in its express terms.* Other section defined “previous owner” to include series of previous owners, so clearly if Parliament wanted to include a series, it could have.

- NOTE: Multiple substitutions now dealt w under **248(5)**.- NOTE: This type of income splitting now dealt w under attribution rule **74.1**. |

**MODERN RULE**

- SCC rejected the strict approach in *Stubart Investments v Canada* (1984) SCC and adopted Driedger’s modern rule:

* Words of the Act are to be read “in their entire context, and in their grammatical and ordinary sense, harmoniously w the scheme of the Act, the object of the Act, and the intention of Parliament.
* Start w plain meaning, then take other factors into account. Context is essential:
	+ Internal (w/in the sentence).
	+ External (w/in scheme of the Act).
		- Indicates whether the ordinary meaning or legal meaning is intended.

- Scheme of the Act:

* Presumption of economical use of language: Each word is there for a purpose.
* Presumption of consistent expression: If a word is used in more than one place, interpret it the same way.
* Principle of implied exclusion: Imputing meaning into the absence of words (ie. omitted for a reasons).
* Principle of coherent structure: Assume a coherent structure – the more specific provision will govern (*Schwartz*).

- Object/purpose of the Act:

* Raises revenue; Promotes certain behaviours (incentives), and; Equity/fairness (social policy).
* Purposes are often inferred, and intention of Parliament is often presumed – takes the consequences of various interpretations into account.

- Associated words principle: Have to read words as they are connected to the words around them.

* Ex. **56(1)(m)** Scholarship, fellowship, bursary, prize for academic achievement, etc. “Prize” was found to include awards for completing things, not just winning something (now overturned by leg).

- Limited class principle: Have to read words w/in the type of subject implied by the other words around it.

* Ex. **5(1)** Salary, wages, other remuneration. “Remuneration” probably not going to mean damages awards.

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| Will-Kare Paving v Canada 2000 SCCLegal meaning vs ordinary meaning | - TP tried to claim 2 manufacturing/processing tax incentives based on capital cost of an asphalt plant it constructed.* Is using the plant to produce asphalt, supplied in connection w paving services, a use primarily for the purpose of manufacturing/processing goods for sale?

- Parliament did NOT exhaustively define the scope of manufacturing/processing.* Majority looks at ordinary legal meaning, not commercial. Referred to obscure K law (prof: not clear Act was actually using a legal term here).

- Most asphalt produced was supplied in connection w paving services, not sold to 3rd parties. Using it there is not in the legal definition of sale.* So it was used primarily in manufacturing/processing of goods supplied through contracts for services, not for sale 🡪 No tax break.

- Minority used the ordinary meaning, most ppl don’t know legal meanings, diff btwn K for sale and K for services. Prof: Should have referred to plain meaning approach. |

**BASIC STRUCTURE OF THE INCOME TAX**

- An income tax consists of 4 basic elements:

* 1) Tax unit (subject to the tax – in Canada, it’s the individual).
* 2) Tax base (on which the tax is assessed).
* 3) Accounting period (over which period of time income is computed).
* 4) Tax rates (applied to determine the amount of tax payable).

- Always keep in mind the 3 main categories: Income – Capital – Windfalls – and the implications of categorizing an amount as such.

**TAX UNIT**

1) Tax unit (subject to the tax – in Canada, it’s the individual).

* **2(1)** An income tax shall be paid, as required by this Act, on the taxable income for each taxation year of every person resident in Canada at any time in the year.
* **248(1)** “Person” or any word or expression descriptive of a person, includes any corporation…

- Taxing based on the individual gives incentive for **income splitting**:

* Different tax for each earner.
* Aggregate tax for couples where both earn is lower than where there is only one earner.

- Based on residence in Canada. Takes clear and virtually irreversible measures to sever residence in Canada.

* **250(3)** A reference to a person resident in Canada includes a person who was at the relevant time ordinarily resident in Canada 🡪 even if you don’t live here, can be “ordinarily resident” over a longer period of time.
	+ **250(1)(a)** A person is deemed to have been resident in Canada throughout a taxation year if the person sojourned in Canada in the year for a period, or periods totaling 183 days or more.

**TAX BASE**

2) Tax base (on which the tax is assessed).

- Note the impact of “income from a source”. Connotes a periodical/recurring aspect to income + a source (office, employment, biz, property). This makes it different from capital gains and windfalls.

* **248(1) 🡪 2(2)** The taxable income of a TP for a taxation year is the TP’s income for the year plus the additions and minus the deductions permitted by Division C.
* **3** The income of a TP for a taxation year for the purposes of this Part is the TP’s income for the year determined by the following rules (a+b-c-d):
	+ **(a)** total of all income from all sources (compute separately).
	+ **(b)**
		- (i) total capital gains PLUS gain from dispositions of listed personal property MINUS
		- (ii) capital losses (excluding listed personal property) MINUS biz investment losses.
			* Never have a negative – if (ii) exceeds (i), just get zero.
	+ **(c)** [a + b] – [deductions in subdivision e (ex. moving expenses, childcare expenses, etc.)].
		- If something has already been deducted under (a) or (b), can’t deduct it again.
	+ **(d)** [c] – [losses from office, employment, biz or property, allowable biz investment losses].
		- Deduct losses against everything that has come before.
		- Allowable biz investment losses: When you invest everything in a small biz that fails, you can deduct separately from capital losses (disposition of shares or debt).
	+ **(e)** The amount determined under (d) is TP’s income for the year.
		- If the number calculated was positive, that is the amount that gets taxed.
	+ **(f)** Otherwise, income is deemed to be zero.
		- If the number calculated was negative, it is simply zero.
		- Zero income is a non-capital loss – see below (accounting period).

**ACCOUNTING PERIOD**

3) Accounting period (over which period of time income is computed).

* **249(1)** “Taxation year” is a calendar year.
	+ “Calendar year” not defined. Look to ***Interpretation Act*, s.37(1)(a)** = 12 consecutive months beginning on January 1st.

- Bunching – When all the income is stuck in one year (ex. sell a property). A TP can, in certain circumstances, push income to next year or pull credits into current year, etc. to avoid this effect.

- **111** TPs can “carry over” unutilized losses from other taxation years.

* **111(1)(a)** “Non-capital loss”: Unutilized losses that are fully deductible in computing TP’s taxable income for the year to which the loss is carried over.
	+ These can be carried back for 3 years, and forward for 20 = 24 year accounting period.
* **111(1)(b)** “Net capital loss”: Unutilized allowable capital losses, generally deductible only against net taxable capital gains in the taxation year to which the loss is carried over.
	+ These can be carried back for 3 years, and forward indefinitely.

**TAX RATES**

4) Tax rates (applied to determine the amount of tax payable).

* The use of marginal rates creates an incentive to shift income to other people.
* **117(2)** Rates for taxation years after 2008, (annually indexed for inflation under **1171.1**):
	+ **(a)** $40,726 or less = 15%.
	+ **(b)** $40,726 - $81,452 = 15% + 22%.
	+ **(c)** $81,452 - $126,264 = 15% + 22% + 26%.
	+ **(d)** $126,264 or less = 15% + 22% + 26% + 29%.

**CREDITS**

- These come off the bottom – a deduction from tax owing. Apply marginal rates, then subtract the credit amount.

* Can lead to a reduction in tax payable (non-refundable) or, where no tax is owing, a tax refund (refundable).

- **118(1)** Personal credits - exempt a basic amount for TPs supporting a cohabiting spouse or CL partner or related dependant who earns no income.

* Credits for children under 18, for disabled dependants over 17, sharing accommodation w aged or disabled relatives over 17.
* **118.2** Medical expense credit. **118.3** Disability credit. **127(3)** Political donations.

**DEDUCTIONS**

- These come off the top – a deduction from your taxable income. Calculate income, deduct these amounts, and then apply the marginal rates.

* Make sure you only deduct against what the Act allows.

- Deductions are more valuable to high income earners than low income earners.

**EXEMPTIONS**

- Some types of income are exempted all together, never included in computing income in the first place.

* Ex. ½ capital gains, certain disability-related employment benefits, certain eligible housing losses, etc.

**TAX AVOIDANCE**

- Tax avoidance: Legal efforts to order one’s affairs to minimize tax.

* Distinct from tax evasion, which involves an illegal breach of specific statutory duties.

- Generally, if you see the term “reasonable”, you’re looking at an anti-avoidance rule.

- 2 factors:

1) Legal character of the relationship:

* Apply ordinary legal principles (contract, tort, etc.) the Act refers to.

2) Legal vs. economic substance:

* Canada has generally focused on the legal substance only, not the reasons why something was done.
	+ This formalist approach is conducive to tax avoidance.
* US has focused more on the economic reality.
	+ This substantive approach is a more aggressive anti-avoidance doctrine, requiring *bona fide* relationship.

- In using anti-avoidance mechanisms, go in this order: **Doctrines 🡪 SAARs 🡪 GAAR.**

* Legal Substance Over Form doctrine: Nomenclature vs. legal substance vs. economic substance.
	+ In US, economic substance wins. In Canada, legal substance wins.
* Sham doctrine: If the relationship isn’t *bona fide*, it’s a sham. Not ever intended to be acted on, just a cloak.
* Ineffective Transactions doctrine: If you try to set something up and don’t do it right, it’s ineffective. Actually have to create the legal rights and obligations you are trying to rely on.
* Specific Anti-Avoidance Rules (SAARs): See below.
* General Anti-Avoidance Rule (GAAR): See below.

**U.S. APPROACH**

- U.S. uses at least 3 anti-avoidance doctrines:

* Substance over form; Sham; Business purpose test.

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| Gregory v Helvering 1935 USEconomic substance testBusiness purpose test/ Sham | - TP was wife of private secretary of multi-millionaire, who was millionaire in his own right. TP owned all shares of United, which held shares for Monitor. She wanted to buy Monitor shares but that would trigger 2 layers of tax. To avoid this:* TP set up Averill. 3 days later, United transferred all shares of Monitor to Averill, Averill issued shares to TP (TP owned all United shares so ok). 1 week later, Averill is dissolved, TP owns shares directly. She then sells shares, triggering a capital gain.
* TP tried to fit this under old section as a reorganization. Valid?

- USSC ignored the hoops and went to economic substance of what was being done – shares were distributed to the TP and sold, so there should be double tax.* Court read in that you need a “plan of reorganization”, something w a biz purpose. This was just a sham.
 |

**U.K. APPROACH**

- UK & Canada added a fourth anti-avoidance doctrine to US 3:

* Legal substance/Ineffective transactions doctrine.

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| CIR v Duke of Westminster 1936 HLLegal effect doctrine | - UK wouldn’t have allowed deductions for payments to a personal servant b/c it’s not a cost of earning income. So Duke and gardener signed a “deed of covenant”, by which Duke stopped paying salary but gave gardener the same amount “while in the Duke’s service”.* Were these payments of salary or wages, despite the deed?

- No. Looked at the legal effect of the K: In law, the gardener could stop working and still get paid. Legal effect trumped the nomenclature/form.* You are allowed to arrange your affairs, w/in the law, to pay less tax.

- Minority: economic reality is gardener still working for Duke and these are wages.- NOTE: This case affirmed in *Stubart* in 1984. |

**SPECIFIC ANTI-AVOIDANCE RULES (SAARS)**

- These are designed to deal w the room the courts gave to tax avoidance.

- There are rules dealing w:

* **Inclusions**.
	+ Ex. **6(1)(a)**: Have to include employment benefits in income.
* **Deductions**.
	+ Ex. **18(1)(a)**: Can’t deduct personal expenses.
	+ Ex. **67**: Can’t deduct any outlay or expense unless it was reasonable in the circumstances.
* **Timing issues**.
	+ Ex. **12(1)(a) & (b)**; Inclusion of certain receipts in a tax year that might not otherwise be included.
* **Deeming rules** (trump legal substance and impose something else).
	+ Ex. **74.1-74.5** Attribution rules.
	+ Ex. **6(3), 16(1)(a), 68** Something is deemed to be something else “regardless of form or legal effect”.
	+ Ex. **125(7)** Personal services business.

**GENERAL ANTI-AVOIDANCE RULE (GAAR)**

- GAAR will apply where there is a **Tax benefit + primarily tax motivated purpose + misuse and abuse**.

- *Stubart* (1984) affirmed the *Duke* case: no business purpose test in Canada wrt tax avoidance b/c we have SAARs to deal w it. If the Act is insufficient, it should be amended.

* Overturned by the GAAR in **1988**.

**- 245(2)** Where a transaction is an avoidance transaction, the tax consequences to a person shall be determined as is reasonable in the circumstances in order to deny a tax benefit that, but for this section, would result, directly or indirectly, from that transaction or series of transactions that includes that transaction.

**PURPOSE**

* **245(3)(a)** “Avoidance transaction”: A transaction that, but for this section, would result…in a tax benefit, unless it is reasonable to consider that it was undertaken for a *bona fide* purpose other than…tax benefit.
	+ Purpose test. Look at the primary purpose – tax motivated? The focus is always on the impugned transaction itself, even if it’s the transaction as a whole that leads to the benefit.
		- “Reasonably considered” = objective assessment.
		- “Primarily” = comparative. Compare tax vs. non-tax motives.
			* **245(3)(b)** If there is a series of transactions in which the impugned transaction occurred, the court will still look at the individual transaction.
	+ Step Transactions Doctrine: One step is bad, whole thing is bad, even if overall series is *bona fide*.

**BENEFIT**

* **245(1)** “Tax benefit” broadly defined: a reduction, avoidance or deferral of tax or an increased refund, etc.
	+ Consider the benefit of the entire series of transactions (if applicable).
	+ *Canada Trustco* said any deduction is a benefit - too broad. Some things are meant to be deducted.
	+ *Copthorne* said compare what you would have done/what would have happened but for the benefit.
		- This higher threshold makes more sense – use this.

**MISUSE AND ABUSE**

* **245(4)** GAAR doesn’t apply unless there is a (a) misuse or (b) abuse of the Act/Regs (misuse and abuse test).
	+ Something that, although it adheres to the language, violates the spirit or purpose of the Act.
	+ 2 steps:
		- 1) What is the purpose of the provision? 2) Is the purpose violated?

**CONSEQUENCES**

* **245(2)** …Tax consequences shall be determined as is reasonable in circumstances in order to deny benefit.
	+ Extremely broad remedial powers.
		- Between **245(1)** and **245(5),** can authorize adjustments to any amount relevant to a TP’s current or future tax liability.
	+ Only limited by being “reasonable in the circumstances” and to “deny the benefit”.

**INCOME SPLITTING**

- Marginal rates of taxation based on the individual gives incentive for income splitting:

* Different tax for each earner.
* Aggregate tax for couples where both earn is lower than where there is only one earner.

**- 56(2)** An amount that would be included in a TP’s income if received by the TP is taxable to the TP if it is diverted to another person for the benefit of the TP or that other person.

- Specific attribution rules.

- **251(1)(a)** Related persons are deemed not to deal with each other at arm’s length.

* **251(2)** “Related persons” or persons related to each other are:
	+ **(a)** Individuals connected by blood relationship, marriage or CL partnership or adoption,
		- **251(6)** Persons are connected by:
			* **(a)** Blood relationship if one is the child or other descendant of the other or one is the brother or sister of the other,
			* **(b)** Marriage if one is married to the other or to a person who is so connected by blood relationship to the other,
			* **(b.1)** CL partnership if one is in a CL partnership w the other or w a person who is connected by blood relationship to the other,
			* **(c)** Adoption if one has been adopted, either legally or in fact, as the child of the other or as the child of a person who is so connected by blood relationship (other than as a brother or sister) to the other.
	+ **(b)** A corp and (i) a person who controls the corp if it is controlled by one person, (ii) a person who is a member of a related group that controls the corp, or (iii) any person related to a person described in (i) or (ii).
	+ **(c)** Any two corps (i) if they are controlled by the same person or group of persons (ii) each corp is controlled by related persons, etc.

**INCOME FROM AN OFFICE OR EMPLOYMENT**

- **3(a)** says a TP’s income for the year includes income from each “office” and each “employment”, and **3(d)** permits deductions for losses from office and employment.

* Main issue of characterization: Employee or independent contractor?

- **248(1)** “Office” Generally a fixed position that exists independently of the person – exists in law regardless of whether the position is filled or not.

**- 248(1)** “Employment” The position of an individual of some other person.

* Both definitions are only for an “individual”, which, as defined, does not include a corporation.

- Deductions:

* **8** Deductions are allowed **(2)** but only as specifically authorized.

**EMPLOYEE VS. INDEPENDENT CONTRACTOR**

- 3 main tests to use in making the distinction, tied into the total relationship test in *Wiebe Door*.

* Control Test:
	+ Employer has a right to tell an employee not only what to do, but how to do it.
* Entrepreneur Test:
	+ Look at economic factors – who owns tools, who takes the chance of profit or risk of loss, etc.
* Organization/Integration Test:
	+ Look at whether the work done is an integral part of the biz or whether it is ancillary to the biz.

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| Wiebe Door Services v MNR 1986 FCATotal relationship test | - TP assessed wrt 12 persons characterized as employees but Weibe claimed they were independent contractors. Various installers who actually did the work, understanding they were carrying on biz for themselves and would pay their own pension plan, taxes, etc.- Court looked for the **total relationship** of the parties. Considered:1) **Control test**: Wiebe could tell them what to do but not how 🡪 Inconclusive.2) **Ownership of tools**: Installers mostly, Wiebe supplied specific pieces 🡪 Independent.3) **Chance of profit/risk of loss**: Installers paid per-job so on them 🡪 Independent.4) **Integration/organization**: W/out installers, the biz wouldn’t exist 🡪 Employee.* Analyze this piece from the perspective of the worker – do they see themselves as integrated? Can they choose own hours? Work for more than 1 co? Etc.

- Point is to consider the whole operation, consider all factors. Who’s business is it?* Factual determination, look at everything. Specific results (one job for a long period?), degree of responsibility for investment and mgmt., principal workplace, hiring of helpers, exclusivity of employment, etc.
* Intention is not determinative in and of itself. Just one factor.

- Sent back for redetermination. |

**INCORPORATED EMPLOYEES / PERSONAL SERVICE BUSINESSES**

- Employment is the position of an individual – a corp gets business income, which has more deductions.

- NOTE: This kind of tax avoidance has been essentially shut down through 2 new SAARs:

* **125(7)** “Personal services business”:
	+ Where the TP or a related person (**251(2)**) is a specified SH (owns >10% of the shares) of a corp on behalf of which the TP performs services, and If, but for the existence of the corp, the incorporated employee would reasonably be regarded as an O/E of the person to whom the services were provided, it’s a personal services business and the tax benefits of business income do NOT apply.
		- (Unless corp has 5 or more full time employees throughout the year).
* **18(1)(p)** Disallows other deductions if you are an incorporated employee in a personal service business, but you are still allowed to deduct remuneration and benefits paid to incorporated employees.

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| Engel v MNR 1982 DTCPre-GAAR, pre-*Stubart* valid incorporation of employee | - TP was TV journalist w Global. Started his own co, entered employment agreement w it and resigned from Global. His co entered into a contract w Global to “lend” TP’s services. MNR reassessed to include amounts from Global to his co, on top of his salary from his co.* TP said his purpose was to make more (incl. less tax), and to do more freelance work.

- This was pre-GAAR, so have to look at judicial doctrines:* Legal substance over form: K btwn his co and Global, not him and Global.
* Sham: There was actually a K.
* Ineffective transactions: It was sloppy but behaviour suggests it was effective.
* Business purpose test: Not used in Canada.

- Reassessment denied, TP’s set-up was valid. |
| Dynamic Industries v Canada 2005 FCJPersonal service business | - Martindale was an ironworker and only employee of Dynamic, a co he incorporated. Provided services to many diff companies until Dynamic subcontracted for SIIL. SIIL very successful, only source of income for Dynamic for several years.* Issue – Personal service biz? Is it reasonable to regard him as O/E of SIIL, but for existence of Dynamic?

- No. *Wiebe Door* factors point to contractor. Despite exclusively working for SIIL, he absorbed all the risk, didn’t work elsewhere simply b/c he didn’t have time (was free to do so). |
| 533702 Ontario Ltd v MNR 1991 TCJPersonal service business | - TP incorporated a co, his wife was an employee. Co’s only K was w him.- Court found the co had no commercial purpose apart from TP, no independent biz. Both TP and wife would be employees if not for the co.* NOTE: Seems to imply biz purpose test into reasonably regarding as employee.
 |

**INCLUSIONS**

**REMUNERATION**

**- 5(1)** TP’s income for a taxation year from an O/E is the salary, wages and other remuneration, including gratuities, received by the TP in the year.

* **6(1)(c)** Includes “director’s or other fees received by TP…in respect of, in course of, or by virtue of an O or E.
* “Fee” = fixed payments in respect of an office.
* “Salary” and “wages” = Regular payments to employees.
* “Gratuitous payments” = see below. Amounts paid on account of legally non-enforceable claims.

- There is a SAAR here:

* **6(3)** Deems certain amounts to be “remuneration for the payee’s services rendered as an officer or during the period of employment”. **To trigger the SAAR, need either (a) OR (b) AND (c), (d), OR (e**).
	+ **(a)** During a period while payee was O or E of the payer. Or
	+ **(b)** On account, in lieu of payment or in satisfaction of an obligation arising out of an agreement made by the payer w the payee immediately prior to, during or immediately after a period that the payee was O/E of the payer.
	+ Shall be deemed, regardless of form or effect (*Curran* - only applies to c, d, e) to be remuneration if:
	+ **(c)** Inducement pay – as consideration or partial consideration for accepting the O/E.
	+ **(d)** Reasonable to regard as remuneration for services as O/E.
	+ **(e)** Agreement to pay for something done before or after term of employment

**GRATUITOUS PAYMENTS**

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| Goldman v MNR 1963 SCCPayment for services in context of existing source = income  | - TP appointed counsel for SH committee during co reorganization. Committee said no remuneration “as such” but that legal fees would be enough to share. Lawyer got $20K – paid $14 to TP over 2 years and kept the rest. TP claimed it was a gift.* Issue – was the payment to TP income?

- Yes. Income from O/E. It was not a contractually obligated payment but was nonetheless a payment for services. There was always an expectation to be paid in relation to the office. |
| Seary v MNR 1979 CTCNot received while employed | - TP prof was denied tenure, received monthly payments to fend of legal action, plus a lump sum when he eventually got tenure.* TP successfully argued monthly payments were a windfall b/c he was not employee at the time. But lump sum was taxed as gratuity.

- DUFF: Thinks court should have used 6(3)(b). Potential issue w “immediate”. |
| Yaholnitsky-Smith v MNR 1991 TCJNot received while employed | - TP teach at group home got $ from group home to go back to school. She wasn’t employed during studies, and had no obligation to return after completing her program.* Court said it was remuneration under 6(3), arising out of an agreement immediately after she had been employed.

- DUFF: A covenant should include reciprocal consideration – weird characterization. |

**INDUCEMENT PAYMENTS**

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| Curran v MNR 1959 SCC | - TP worked for Imperial, good salary, pension, opportunities for promotion, to sit on board. Brown gave $ in exchange for TP giving up all benefits in Imperial, whether or not he actually took over the co Brown wanted him to (Brown ran the co).* Got out of **6(3)(a)** & **(b)**: Never worked for Brown, who paid him – payee/payer relationship wasn’t the same as employer/employee.
* “Regardless of legal form or effect” only applied to **(c)**, **(d)** and **(e)**!
* Couldn’t satisfy **(a)** or **(b)** so **6(3)** can’t apply – need both halves.

- Not taxable under **6(3)** BUT still taxable: Payment for services, and the service was the resignation, which made him available to provide services to Brown’s cos.* Said it was payment for “personal service”, working directly for Brown & cos, **5(1)**. Substance of the matter was the acquisition of services (economic substance analysis).

- DUFF: Should have just pierced the corporate veil at **6(3)**. They did anyways a bit at **5(1)**. |

**COMPENSATION FOR BREACH/WAIVER OF CONTRACTUAL OBLIGATIONS**

- **6(3)** Deemed remuneration for amounts received while payee is employed by the payer, or arising from an agreement immediately before or after period of O/E.

* Applies where a payment is clearly not for services.

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| Moss v MNR 1963 Ex Ct | - TP had agreement to work for Prairie that gave him an interest in boss’s life insurance policy, and a right to buy shares/assets at 90% of price of an intended sale. Boss entered negotiations to sell, paid TP in exchange for waiving rights under the agreement.* Life insurance policy payments not taxable b/c return of capital.

- Court used **6(3)(b)** – payment in satisfaction of the obgs arising out of employment agreement.* Payment relates back to inducement to accept offer of employment (**6(3)(c)**).

- DUFF: Stronger argument is prob that this was a covenant in which he agreed to waive rights. |

**STRIKE PAY**

- These are payments for not providing services.

- Union dues and unions themselves are generally exempt from tax, so strike funds have not been subjected to tax.

- Earlier cases found strike pay not taxable in itself, but taxable as characterized as something else:

* *Loeb v Canada* 1978 FCTD: There was an employment arrangement to provide various services to the union during course of the strike. Court said that strike pay had the character of employment income.
* *Ferris v MNR* 1977 CTC: Employees on strike published a newspaper during strike, received income. Court said the pay had the character of business income.

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| Canada v Fries 1989 FCAIncome from an unspecified source | - Union paid $ to TP who was employee of Liquor Board. TP and other employees went on strike in support of other striking unionists. $ received was equivalent to TP’s normal net pay.- 1) TP claimed interpretation bulletin at the time basically exempted the pay he got. * Court said the interpretation bulletin is a factor to be considered, but not determinative.
* DUFF: This seems harsh, misleading to the ordinary person.

- 2) TP claimed it was just a return of capital b/c he had contributed to the strike fund.* Court said b/c it was a common, collectivized fund, TP’s input no longer identifiable and therefore not a return of capital. Connection is severed.

- Overall, court said it had the characteristics of income from an unspecified source – periodical character of same amount the income would otherwise be. Just a substitution.* Process of elimination – doesn’t have the characteristics of capital or a gift/windfall – only leaves income. **3(a)** is broad and inclusive.

- DUFF: Bit of a stretch. Not a source like the others, can’t reasonably expect to get paid. |
| **Canada v Fries SCC** | - **OVERTURNED FCA JUDGMENT** in 4 sentences. Just said they weren’t satisfied strike pay comes w/in the definition of income from a source. Benefit of the doubt must go to TP.- DUFF: Not helpful! Don’t know what this stands for. |

**DAMAGES FOR PERSONAL INJURY**

- Generally we don’t tax damages payments made for either physical or emotional injury.

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| Cirella v Canada 1978 FCTDCompensation payments more akin to capital | - TP awarded special damages for injury from car accident for loss of income from time of injury to trial, relative to what he previously earned. Then set up his own light welding biz.- Employment income: *Surrogatum* principle? No. Insufficient connection to employment.- Business income: *Surrogatum* principle? No. Wasn’t in a biz at the time.- Unspecified source: Source is injury? No. Compensation, no characteristics of income.* The character of special and general damages is compensation for the loss of income earning capacity, not the loss of income itself.
* More like capital – income-earning capacity is a capital asset/value.
 |

**TERMINATION PAYMENTS**

- Generally, an implied term of an employment contract is that you won’t be terminated w/out reasonable notice, or payment in lieu of.

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| Quance v Canada 1974 FCTDTermination payments taxable as income | - TP terminated, offered 6.5 mo pay in lieu of notice, then 9. TP refused. Wanted 1 year. Employer unilaterally decided to keep paying him every 2 weeks for 9 mos.* TP accepted payments, not as payment in lieu, but on the basis that they were compensation for damages he would have been suing them.

- Court said **6(3)** can apply to termination payments on facts like these on *surrogatum* principle, suggesting termination payments would be taxable as income. - **NOTE: This case hasn’t been followed.** |
| Canada v Atkins 1976 FCATermination payments not taxable as income | - TP received $ in settlement of all claims relating to termination.* Distinguished from *Quance* b/c there, steady pay, no agreement or waiver.

- If employer continues to pay salary after termination, that is taxable employment income.* BUT if terminated w/out reasonable notice and you sue, damages or settlement amount is severed from the employment relationship and is a capital receipt.
	+ Termination is not subject to **6(3)** b/c it is not payment in lieu of so much as it is damages for breaching the employment K w early termination.

- Doesn’t fit under **3(a)** either b/c not income from a source.- **NOTE: Now dealt w under retiring allowance.** |

**RETIRING ALLOWANCE**

- After *Atkins*, there was an incentive for terminations to be made w/out notice, for employees to “sue” and settle to avoid tax. By 1981 the gov included these amounts as taxable income via retiring allowance.

- **56(1)(a)(ii)** Any amount received by the TP in the year as, on account of or in lieu of payment of, or in satisfaction of a retiring allowance...

* **248(1)** “Retiring allowance” means an amount received
	+ **(a)** On or after retirement of a TP from O/E in recognition of TP’s long service, or
	+ **(b)** In respect of a loss of an O/E of a TP, whether or not received as, on account or in lieu of payment of, damages or pursuant to an order or judgment of a competent tribunal.
* “In respect of” = very broad causal connector (*Mendes-Roux*).

- Retiring allowances only apply if you have started employment – can’t lose what you never had (*Schwartz*).

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| Mendes-Roux v Canada 1997 TCCPayment in respect of loss | - TP worked w court translation bureau in Bathurst. While on maternity leave she was informed the Bathurst office was closing and was told to go to Fredericton or else she would be terminated for “abandonment of position”. Sued for wrongful dismissal, settled. Estimated break-down of $ for salary and unused vacation pay, and $ as damages for pain and suffering.* CRA: “in respect of” = “but for”. If not employed, she wouldn’t have gotten the $.

- Court said no. Damages are in respect of tort, not loss of employment. May be occasioned by the same event, but it’s not compensation for the loss – just putting her back where she was.* Broad connection – payment must simply be linked to an amount that would have otherwise been taxable (damages not taxable).
 |
| Schwartz v Canada 1996 SCCRetiring allowances don’t apply to intended employment | - TP accepted job offer, notified partners he was leaving. K then unilaterally cancelled by prospective employer. Settled, classified $ as damages rather than compensation for loss.* CRA said it was retiring allowance. If not, employment benefit under **6(1)(a)**. If not, income from an unspecified source under **3(a)**.

- TJ said not retiring allowance b/c he didn’t lose O/E – never had it to begin w. Not employment benefit b/c never employed. Not enough evidence to show it wasn’t damages.- SCC said they didn’t have sufficient basis to overrule TJ so non-taxable damages.* Income from another source: Phrasing of **3(a)** and **56(1)** is so broad, meant to include all possible sources of income. But still have to use scheme of the Act. **56(1)(a)(ii)** is a specific solution to a specific problem to therefore takes precedence over general **3(a)**.
* But doesn’t fit as a retiring allowance. Other places in the Act refer to “employment and future employment”, but not here (like *MacInnes*).

- DUFF: Sort of goes back to strict construction. Should have considered Parliament’s intent.- NOTE: Stuff on unspecified source is obiter, so can argue against it even though it’s binding. |

**BENEFITS**

- **6(1)(a)** The value of board, lodging, and other benefits of any kind whatever received or enjoyed by TP, or by a person who does not deal at arm’s length w TP, in the year in respect of, in the course of, or by virtue of TP’s O or E.

**-** 3 Requirements to this:

* 1) Characterization of the benefit.
* 2) Connection to O/E (Nexus).
* 3) Valuation.

- Remember *Pezzalato* – if the employer really wants something done, they can pay for it and deduct it, pay their employees more so they can afford it, etc.

**CHARACTERIZATION**

1) **Characterization of the benefit**: “Any kind whatever” was included to defeat limited class principle here.

* TEST: Advantage must be a material benefit/advantage, more than merely incidental (*Lowe*).
* Simply being restored to your economic situation before incurring an employ-required cost is not enough to be a benefit (*Huffman*).
	+ The fact that the employer requires you to take the benefit doesn’t matter. Focus on the material benefit itself (*Cutmore, Deitch, Dunlap*).
* There are lots of exceptions. See *CRA position* below.

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| Lowe v Canada 1996 FCACharacterization of the biz trip | - TP was exec at co, sent to New Orleans w wife to keep brokers happy. Most of their time booked up w brokers, but still admitted they enjoyed the trip. How to characterize the trip?- Court looked for some material acquisitions that confer a benefit, beyond incidental benefit.* Trip wasn’t instead of pay, so not obviously taxable benefit.
* Look to principal purpose: primarily biz motivated vs. personal enjoyment. Can be both if enjoyment is more than an incidental benefit (if you stay an extra 10 days, that’s taxable).

- This was primarily biz motivated. Worked most of each day, only incidental benefit. |
| Huffman v MNR 1988 FCTDReimbursement | - TP detective, blood on clothes, reimbursed for cleaning/replacing.- Court said no benefit, simply being restored to economic situation he was in before his employer ordered him to incur the expense. |
| Cutmore v MNR 1986 TCCMandatory = benefit | - TP’s employer required employees had tax returns done by accountants. Paid for it.- Court said this is a benefit, even though it is required by the employer.* Motivation behind conferring the benefit doesn’t undo **6(1)(a)**.
 |
| Deitch v MNR 1989 TCCMandatory = benefit | - TP’s employer paid professional liability insurance, was mandatory he had it.- Court referred to *Cutmore* to say it’s not a benefit b/c it’s mandatory.* TP would have had to pay it himself otherwise – was protected from liability so it’s a substantial economic benefit.
 |
| Dunlap v Canada 1998 TCCParty = benefit | - TP reassessed to include benefit in respect of annual Xmas parties hosted by employer.* Court said benefit (several hundred $) was not trivial. Fact that it was unilaterally offered by employer doesn’t take away from the beneficial nature.

- NOTE: Some parties now allowed. See *CRA position* under “Nexus” section. |
| CRA Position | - CRA excludes some “non-taxable privileges” from inclusions of taxable benefits under **6(1)(a)**, provided the privilege doesn’t constitute a form of extra remuneration. Excludes:* Discounts on merchandise and commissions on sales if it’s ordinarily done by employer.
* Transportation to the job if necessary for security or practical reasons.
* Recreation facilities if employee’s generally allowed to use employer’s facilities or where employer pays for membership that is principally for employer’s advantage.
* Transportation passes for airline employees (unless they reserve a seat and pay < 50%). Rail/bus co and retired transport co employees get free passes, never taxable.
 |

**NEXUS**

2) **Connection to O/E (Nexus)**: “In respect of” – broad causal connection. May be received by TP or other:

* **251(1)(a)** Related persons deemed not to deal at arm’s length, **(c)** in all other cases it’s a Q of fact.
* **251(2)** “related person”, **251(6)** “blood relationship” (g/parents, kids, siblings, spouses, in-laws)

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| R v Savage 1983 SCC$ for completing courses in line w co program = nexus | - TP took courses to improve her knowledge in the field, got $100 per course in accordance w co policy do encourage staff to upgrade. TP said it was a prize under **56(1)(n)**, so only included as taxable income if exceeds $500 in one year. MNR said employment benefit.- 1) Is this a benefit under **6(1)(a)**?* Yes. Doesn’t have to be payment for services to fit here, just “in respect of” O/E. Paid in accordance w co policy, sufficient connection. Not a gift either, employer deducted the cost, suggesting not a disinterest gift but rather connected to the biz.

- 2) Is this a prize under **56(1)(n)**? |
| Mindszenthy v Canada 1993 TCC“Gift” from employer | - TP gave presentation using fake Rolex, boss gave him a real one while at dinner at TP’s house. Boss then deducted the cost (several thousand $).* Court said this was a taxable benefit rather than a gift. Fact that boss deducted it suggests it was w biz purpose, establishes the nexus to O/E. Taxable benefit to TP.

- DUFF: Better remedy would have been to disallow employer’s deduction.- NOTE: CRA now allows some gift-giving from employer to employee. See below. |
| Waffle v MNR 1968 Ex CtBenefit from indirect employer | - TP co-owner/employee of Ford dealership, met quota in sales promotion campaign, got free trip to the Caribbean. TP claimed not “in respect of” b/c from Ford, not the dealership.* Court said it doesn’t matter if it’s not the direct employer who pays. He still got his trip “in respect of, in the course of, by virtue of” his O/E.
 |
| Giffen v Canada 1995 TCCFrequent flier | - TP employment required lots of travel, accumulated $36K worth of frequent flier points. TP said they got it through membership in the flier program, not through employment.* Court said connection there b/c only got this big benefit from flying for job.
 |
| CRA Position | - Employers can give 2 non-cash/non-cash equivalent gifts to employees per year tax-free if the total is less than $500. If you go over, whole thing is taxable, incl first $500 (limits *Mindszenthy*).- Can give tax-free parties if everyone is invited and cost is < $100 per person (limits *Dunlap*). |

**VALUATION**

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| Detchon v Canada 1995 TCCSearch for objective valuation test | - TP teacher at private school, sent their kid their for free. Couldn’t have afforded it otherwise.- Did they get a benefit? Clearly yes.- What’s the value? Fair market value (i.e. usual cost of tuition)? Cost to employer (cost to school per student, cost to TP of public school, cost if tuition scaled to income, etc.)?- Most fair option might be public school cost, but that’s not the actual benefit TP received.* Court went w average cost per student. Just took the middle ground.

- **NOTE: THIS CASE HAS BEEN OVERTURNED** by following cases. Just: Looking for objective test, how to find the right valuation once you move away from fair market value. |
| Spence v Canada 2010 FCAFair market value | - TP teachers got 50% off kids’ tuition.- What is at issue isn’t the cost to the employer, but the value of the benefit received by the TP. So value is fair market cost of tuition minus what TP paid.- Eliminated the bargaining. If it’s valuable enough for the school to have those kids go there, they should pay the teachers more so they can afford it (*Pezzalato*). |
| Schroter v Canada 2010 FCAFair market value | - TP had free parking pass downtown that he didn’t use.- Court said it doesn’t matter that he didn’t use it. Again, it’s not the benefit to TP, it’s the value of the benefit. Fair market value. |

**SCHOLARSHIPS, FELLOWSHIPS AND BURSARIES**

- **56(1)(n)** TP has to include the total of all amounts received…as or on account of a scholarship, fellowship or bursary, or prize for achievement in a field of endeavor ordinarily carried on by the TP, other than prescribed prize.

* **(3)** Scholarship exemptions:
	+ **(a)** Any scholarship etc. that relates to post-secondary, elementary or secondary school.
		- Exempts scholarships!!! Unless received in respect of O/E (taxable employment income) or in the course of biz (taxable biz income).
	+ **(b)** Allows deductions for the production costs of an artistic work (including prizes).
	+ **(c)** $500 in other circumstances (ex. *Savage*).
* **(3.1)** Scholarship etc. only considered to be for school if it is reasonable to conclude that the award is intended to support the TP’s enrolment in the program, must be in pursuit of the degree.

NOTE: *DiMaria* overturned by leg changes and the introof “someone who doesn’t deal at arm’s length” in **6(1)(a)**.

* BUT then specifically exempted in **6(1)(a)(vi)**: Excludes benefits received/enjoyed by a person other than the TP under a program provided by TP’s employer designed to assist individuals to further their education, provided TP deals w employer at arm’s length and it is reasonable to conclude the benefit isn’t a sub for salary, wages, or other remuneration.
	+ This is a bad route for supporting higher education though b/c only gives tax benefit to people who already have jobs that can pay scholarships. Just widens the gap.

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| DiMaria v Canada 2008 TCCEmployer provided scholarship | - TP employee of co, son got award from that co. Nexus test pretty clearly satisfied. Was there a benefit to TP, or just his son? - NOTE: At the time, scholarship deduction only $3K, not whole thing. And wording of **6(1)(a)** didn’t include “someone who doesn’t deal at arm’s length w TP”. That was added after this case.- Court said no. No obligation to send your kid to uni and pay tuition – no direct benefit to TP.* He was sending him anyways, but this doesn’t matter. Son got the money, dad had no obg to pay, co had no obg to pay, etc. No benefit to TP.
* Doesn’t matter that threshold for getting the scholarship was low, can be awarded for whatever reason the donor chooses.

- Decision turns on fact there is no legal obg to provide a uni education. Taxable to son, exempt. |

**SPECIFIC BENEFITS**

**INTEREST FREE AND LOW INTEREST LOANS**

**- 6(9)** Where an amount in respect of a loan or debt is deemed by **80.4(1)** to be a benefit received by an individual, the amount of the benefit shall be included in computing the income of the individual as income from an O/E.

* **80.4(1)** Where a person receives a loan/incurs a debt b/c of or in consequence of the previous, current or intended O/E of the individual, or in a personal services biz, they are deemed to have received a benefit.
	+ Note the nexus test to O/E: Narrower than “in respect of”.
	+ **The amount of the benefit is the amount, if any, by which [(a) + (b)] exceeds [(c) + (d)]**.
		- The effect of this section is to require an individual to whom the provision applies to include as a benefit an amount equal to the difference between the prescribed rate and amounts paid by the debtor either as interest or a reimbursement paid by the employer.
		- Prescribed rates in **Reg 4301**.
	+ **(a)** Amount of interest that would be payable at the prescribed rate for the year.
	+ **(b)** The actual amount of interest paid by the employer.
	+ **(c)** The amount of interest actually paid to the lender.
	+ **(d)** Interest paid by the employer which is reimbursed by the TP.
* **80.4(1.1)** A loan or debt is deemed to have been received or incurred b/c of an individual’s O/E if it is reasonable to conclude that, but for an individual’s previous, current or intended O/E
	+ **(a)** The terms of the loan or debt would have been different, or
	+ **(b)** The loan would not have been received/debt would not have been incurred.
	+ This section reverses *Krull*.

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| Krull v Canada 1995 FCANexus test | - TP relocated from Calgary to Toronto, employer paid mortgage interest subsidy to the bank to make up the diff TPs had to pay in more expensive housing market.* Issue – is this a taxable benefit under **6(9)**/**80.4(1)**?

- No. The causal relationship/nexus btwn loan and E/O is not there. Didn’t have to buy a house in Toronto b/c of E/O – could have rented, etc.- NOTE: This is overturned by **80.4(1.1)** and **6(23)**. |

**DEBT FORGIVENESS**

- **6(15)** There is a deemed benefit to TP under **6(1)(a)** any time a debt is settled or extinguished.

* **6(15.1)** “Forgiven amount” The amount left to be paid (principal obg minus what has been paid).

- The nexus here depends on the general rule in **6(1)(a)**.

* *McArdle v MNR* 1984 TCC: Connection is very broad, courts generally find debt forgiveness to be in respect of O/E and therefore taxable.

**HOME RELOCATION LOANS**

- There are some breaks for home relocation loans

- **248(1)** “Home relocation loan” Means a loan received by an individual or their spouse, where the individual has commenced employment and by reason thereof has moved from one place of ordinary residence to another IF:

* **(a)** The distance is more than 40 km,
* **(b)** The loan is used to acquire a dwelling or the right to acquire a dwelling,
* **(c)** The loan is received in circumstances of **80.4(1)** or would have been s if **80.4(1.1)** had applied, AND
* **(d)** The loan is designated by the individual as a home relocation loan (can’t designate > 1 at a time).

- INTEREST LOCKED IN: **80.4(4) & (6)** For a home relocation loan, in each 5-year period, with the first beginning on the date the loan is taken out, the rate of interest determined under **80.4(1)(a)** cannot go above the prescribed rate of interest as it was at the beginning of the 5 year period.

**-** DEDUCTION: **110(1)(j)** Where TP has, by virtue of **80.4**, included an amount in respect of a home relocation loan, they can deduct **(iii)** The amount of the benefit deemed to have been received under **80.4**.

**HOUSING LOSS**

- General rule: If you have a housing loss that is compensated, it is fully taxable.

* Exception for “eligible housing loss” (then first $15K tax free, and only ½ the amount over that is taxable).

- **6(19)** An amount paid in respect of a housing loss is deemed to be a fully taxable benefit under **6(1)(a)** if it was paid to or on behalf of TP (or non-arm’s length person) in respect of, in the course of or b/c of, an O/E.

**- 6(21)** “Housing loss” Means the amount by which:

* The greater of **(a)** ACB of the residence (capital cost plus value of renos, etc.) and **(b)** it’s fair market value during previous 6 months] exceeds
* **(c)** If the residence is disposed of before the end of the tax year that begins after the disposal: the lesser of proceeds of sale and fair market value at that time, OR
* **(d)** If the residence is not disposed of: the fair market value at that time (of computing the loss).

**- 6(22)** “Eligible housing loss” In respect of a residence designated by TP means a housing loss in respect of an eligible relocation of the TP (or non-arm’s length person). Can only designate one residence.

* **248(1)** “Eligible relocation” Means a relocation of TP where:
	+ **(a)** Relocation enables TP to be employed at new work location or to be full-time uni student
	+ **(b)** Before relocation TP ordinarily resided at old residence at after relocation, ordinarily resides at new residence.
	+ **(c)** the new residence is >40km closer to the new work location.
* **6(20)** Deems an amount paid in respect of an eligible housing loss to or on behalf of TP (or non arm’s length person) in respect of, in the course of or b/c of, and O/E to be a benefit under **6(1)(a)**.
* **The first $15K is not a taxable benefit, and only half of any amount above that is included as a benefit.**

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| Thomas v Canada 2005 FCAEligible relocation requires enablement to carry on new employment | - TP was recruited by JD and moved from Ottawa to St. John’s. Bought property and built a house on it for total $850K. Terminated 1 year later, FMV of house dropped to $758K. As part of termination agreement, JD bought it for more than FMV (loophole wrt retiring allowance).* Issue – is this an eligible housing loss?

- Eligible relocation: Left St. John’s b/c no other jobs for him there, got a job in Ottawa.* Did it enable him to carry on a biz or be employed at a new work place? Yes.
* Did he ordinarily reside at a place before an after? Yes.
* Did he move >40km closer to his new job? Yes.

- Court said still not eligible housing loss though b/c the loss happened b/c of his termination, not to enable him to get to his new employer.- If it had been an eligible housing loss, would have been:* Diff in house value = $91K. Minus $15k. ½ of that = $38K taxable.
 |

**HOUSING SUBSIDIES**

- **6(23)** An amount paid or the value of assistance provided by any person in respect of, in the course of or b/c of, and individual’s O/E in respect of the cost of, the financing of, the use of or the right to use, a residence is a benefit.

* *Phillips v MNR* 1994 FCA: TP’s place of residence closed, transferred him elsewhere and gave him a “relocation payment”. TP said it was for higher living costs. Court found the payment allowed him to acquire a more valuable asset and increase his net worth, so a taxable benefit.

**-** NOTE: Reimbursements of moving expenses are not taxable benefits under **6(1)(a)**:

* *Pollesel v Canada 19*97 TCC: TP reimbursed for move, court said TP received no economic benefit.
* *MacInnes v Canada* 2003 TCC: TP got lump-sum upon retirement from military to cover cost of returning him from the base to his original home. Court said “no economic gain, advantage or benefit”.

**OPTIONS TO ACQUIRE SECURITIES**

- Giving securities is one way for companies to compensate employees.

- The right to acquire the security is the option. Actually acquiring the security is exercising the option.

- Options are generally given for free, but if you have to pay for it, you pay the “option price”.

- Options usually only last for a certain period of time.

* Not exercisable until the option has vested, then exercisable until it expires.

- The price at which you exercise the option (acquire the security) is the “exercise price/strike price”.

* Generally the difference between the FMV and the exercise price is treated as an employment benefit and is taxed at ½ value as a capital gain.

- **7(3)(a)** If qualifying person agreed to issue securities to their employee, only use **7**. Ousts **6(1)(a)**.

* **248(1)** “Employee” includes an officer (*Taylor*).
* **7(5)** Section **7** doesn’t apply unless the benefit was received “in respect of, in the course of, or by virtue of, the employment” – nexus test (ex. *Busby*).
	+ NOTE: **7(5)** refers to “employment”, but **7(3)(a)** refers to “employee”. See *Taylor*.
* **7(7)** “Qualifying person” means a corp.
	+ *Robertson v Canada* 1990 FCA: Options granted by non-corp so **7** doesn’t apply. Go to **6(1)(a)**.
* **7(7)** “Security” of a qualifying person means (a) if person is a corp, a share of the capital stock of the corp.

**COMPUTATION & TIMING OF BENEFIT**

- **7(1)(a)** If an employee has acquired securities, the benefit is equal to the amount by which:

* **(i)** The value at which the *securities* were acquired (FMV) EXCEEDS
* **(ii)** The exercise price PLUS **(iii)** The option price.
* The benefit is deemed in the year of acquisition.

- **7(1)(b)** If the employee has disposed of the option to acquire securities:

* **(i)** If disposed of to arm’s length person, benefit is deemed to be the amount paid minus option price.
* **(ii)** Deemed in the year in which the option was disposed of.
* **7(1.7)** Deems the cancellation of an option to constitute a transfer or disposition and deems amounts received on cancellation to be proceeds of disposition.

- **7(1.1)** Timing: If, as an employee dealing at arm’s length w the corp, you get shares from a Canadian controlled private corp, the benefit will be deemed to have been enjoyed in the year in which you dispose of the shares, rather than in the year in which you acquire them.

* Defers the tax for Canadian controlled private corp shares w which TP deals at arm’s length.
* These shares also qualify for deduction under **110(1)(d)** if they meet the requirements, or else under **110(1)(d.1)**. See below.

**DEDUCTIONS**

- **110(1)(d)** If the shares have particular characteristics (a prescribed share), the benefit that would be fully taxable under **7(1)(a)** or **(b)** is only ½ taxable. Characteristics:

* **(i.1)** Refers to **Reg 6204**. Security must be a “prescribed share”. **6204(a):**
	+ **(i)** The amount of dividends is not limited to a max amount or fixed min amount.
	+ **(ii)** No fixed entitlement to an amount on liquidation of the co.
	+ **(iv)** Can’t redeem your share in exchange for your money back.
	+ Essentially, a common share that is tied to the co that you expect to hold for 2 years.
* **(ii)(A)** The exercise price must be more than the difference between 1) FMV at the time the agreement was made and 2) the option value (i.e. shares can’t be “in the money”).
	+ Ex. FMV is $100, you only pay $2 as option value. Exercise price can’t be less than $98.
* **(ii)(B)** TP must deal at arm’s length so as to avoid abuse of the section.

- **110(1)(d.1)** If TP is deemed under **7(1.1)** to have received a benefit in a year, and they hold on to the share for 2 years, they can get the ½ tax deduction.

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| Taylor v MNR 1988 TCC“The employment” in 7(5) includes office, as in “employee” | - TP sole SH of co that provided consulting services to cos Bianca and Greenwood. TP became director for both, got stock options which he eventually exercised.- Bianca. Option for 50,000 shares: Option price = $0, Exercise price = $2.70/share.* Exercised for 20,000 when FMV was $5.40, and other 30,000 when FMV was $4.40.
* Benefit under **7(1)(a)**:
* $5.40 – ($2.70 + $0) x 20,000 = $54K // $4.40 – ($$2.70 + $0) x 30,000 = $51K // $54K + $51K = $105K total benefit.

- Greenwood. Option for 15,000 shares: Option price = $0, Exercise price = $3.75/share.* Exercised all 15,000 when the FMV was $16.50.
* Benefit under **7(1)(a)**:
* $16.50 – ($3.75 + $0) = $12.70 // $12.70 x 15,000 = $191,250 total benefit.

- TP said he wasn’t an employee so doesn’t fit in **7(3)**.* Court said **248(1)** definition of “employee” includes “officer”, which includes director.

- TP also said he wasn’t in “the employment” of the cos under **7(5)** so **7(1)** doesn’t apply.* Court said “the employment” assumes people are “employees”, so incl director. Said the stat defs are not all-inclusive, can go broader if necessary to give effect to a provision.

- DUFF: This is shaky, ignores the statutory definition of “employment” in **248(1)**,  |
| Busby v Canada 1986 FCTD**???????????** | - TP had personal relationship w biz-man who persuaded her to serve as nominal director of a co. She got options, which she exercised.* Court said Parliament didn’t intend for “the employment” to stand on its’ own, separate from the other definitions. Seems like a drafting mistake.
* Here, benefits were received extraneous to employment, a personal gift.

- Court in *Taylor* considered this but said it was just obiter, didn’t follow it. |

**ALLOWANCES**

- **6(1)(b)** All amounts received by TP as an allowance for personal or living expenses or as an allowance for any other purpose. Lots of exceptions in (i) – (ix). “Allowance” not defined in the Act.

**-** *CRA* distinguishes among:

* Allowance: Any periodic or other payment that an employee receives from an employer, in addition to salary or wages, w/out having to account for its use. See *MacDonald*.
* Reimbursement: A payment by the employer to the employee to repay the employee for amounts spent by the employee on the employer’s business.
* Accountable advance: An amount given by an employer to an employee for expenses to be incurred by the employee on the employer’s business and to be accounted for…

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| MacDonald v Canada 1994 FCADefinition of allowance | - TP in RCMP, transferred from Regina to Toronto. He got $700/mo as housing subsidy from RCMP for “cost of living adjustment”.- Court defined an allowance:* 1) For a purpose (from the statute).
* 2) Arbitrary amount (as opposed to a reimbursement).
* 3) No duty to account (discretion).

- Here, arbitrary amount for the purpose of housing, and discretionary (didn’t have to prove he used the money, etc.). Fits character of an allowance, taxable under **6(1)(b)**. |
| North Waterloo Publishing v Canada 1988 FCAAllowance vs. reimbursement | - TP newspaper editor at two locations. Got meal allowance, excluded them on basis they were reimbursements for meals consumed while working at the 2 locations.* Court characterized it as an allowance b/c no detailed receipts etc. as for reimbursements.
 |

**EXEMPTIONS**

**TRAVEL & MOTOR VEHICLE EXPENSES**

- The following are exemptions to inclusion under **6(1)(b):**

- TRAVEL: **6(1)(b)(vii)** Reasonable allowances for travel expenses (other than for motor vehicle) received by the employee for travelling away from the municipality or metropolitan area where the employer’s establishment at which the employee ordinarily worked was located, if the travel was done in performance of the employee’s duties.

- MOTOR VEHICLE: **6(1)(b)(vii.1)** Reasonable allowances for the use of a motor vehicle received by an employee for travelling in the performance of the duties of the O/E.

* **6(1)(b)(x)** An allowance here will be deemed not to be reasonable where the measurement of the use of the vehicle for is not based solely on the number of Km for which the vehicle is used.
	+ Not a reimbursement b/c still a rough, measurement (doesn’t include gas prices, repairs, etc.), still has a discretionary aspect.

- Both of these exceptions refer to “travelling”, which is not defined in the Act.

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| Blackman v MNR 1967 TABTravelling vs. sojourning | - TP worked for co that transported goods and passengers, had to move a lot for work. Got a daily amount for food etc. designed to cover expenses incurred for being away from home. TP lived in Montreal for 240 days of each year for 3 years.* It was an allowance b/c discretionary, for a purpose, and arbitrary. Exempt as a travelling expense?

- No. Court said they weren’t travelling, but “sojourning” b/c it was an extended period of time, lived there temporarily. Sojourning vs. travelling: Consider:* Time: Travelling is more temporary. 240 days was sojourning.
* Accommodation: Hotel or apartment or something?
* Number of places visited: More is indicative of travelling.

- NOTE: Act was subsequently amended to provide some tax-free benefits under **6(6)** – below. |
| Bouchard v MNR 1980 TRBIn performance vs. to and from | - TP lived in city, part time job at Sherwood Uni, got allowance for travelling there & back.- Court said they were 2 separate jobs, so not travelling in the performance of his duties, only to and from the job. This is taxable.- NOTE: Reversed by **81(3.1)** – see below. |

**PART-TIME WORK & SPECIAL WORK SITE**

- **81(3.1)** Exempts a reasonable allowance or reimbursement for travel expenses incurred in respect of part-time employment, provided the part-time duties are performed at a location not less than 80km from the individual’s ordinary place of residence and place of other employment or biz.

* TP must have other employment for this to apply.
* Captures travel not in the performance of duties, just getting to and from the job.

- **6(6)** Exempts any benefit or allowance received or enjoyed in respect of things for:

* **(a)**Board and lodging at a special work site:
	+ **(i)** A location where TP performs temporary duties, if TP maintained a self-contained domestic establishment elsewhere as a principal place of residence but, due to distance, can’t travel back and forth all the time.
	+ **(ii)** Only applies if TP was required to be away from principal residence or at the special work site for > 36 hours.
	+ **248(1)** “Self-contained domestic establishment” Means a dwelling-house, apartment or other similar place of residence in which place a person as a general rule sleeps and eats (i.e. home).
* **(b)(i)** Can exclude a benefit or allowance for transportation between the principal place of residence and the special work site.

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| Guilbert v MNR 1991 TCCMade-up definition of special work site | - TP accepted permanent position in Quebec on anticipation he would be appointed to another position soon in Ottawa. Employer provided apartment free of charge. Worked there for 3 years, quit after found out he wouldn’t get the promotion. Maintained his home a considerable distance away, split time 50/50. Kids lived w him in Quebec, wife at other place.* Is this a “special work site” under **6(6)**?

- Court said 3 main elements to a special work site:1) Duties must be temporary in nature:* Can be permanent job w temporary duties. CRA says temporariness is to be assessed on expected duration as anticipated at the outset. TP here seems to meet this.

2) TP must maintain “self-contained domestic establishment” at another location: Met.3) “Self-contained domestic establishment” must be TP’s principal place of residence:* Consider time spent (TP went back every wknd), where family is (half and half), ownership (TP owned house, rented in Quebec), and exclusive use (other people used the apartment when he wasn’t there). Seems TP meets this.

4) Was it available to TP and not rented out? Yes.5) Would it be unreasonable for TP to commute daily by virtue of distance? Yes.- Additional from statute: Did he have to be away for >36 hours? Yes.- DUFF: This is pretty made-up. Other cases have looked more to the statute. |
| Jaffar v R 2002 TCCModern interpretation of special work site | - TP and IT guy, K said he’s to work at employer’s office or office of clients. Did a 1.3 year stint in New York, co paid for his apartment and for travelling expenses to visit his family.- Court found this was a special work site, exempt from tax.* Not his usual place of work, so “special”. Performed temporary duties for a limited period. A special work-site doesn’t have to be remote, in the bush, etc.
 |
| Rozumiak v Canada 2005 TCCAs above | - TP hired by Vancouver co for 3 year term to go to Chicago.* Court said this was a “special work site”, so amounts received for rent and expenses while in Chicago were exempt under **6(6)**.
 |

**DEDUCTIONS**

- Deductions are calculated, and then taken out.

- **8(1)** In computing TP’s income from O/E there may be deductions for amounts as may reasonably be regarded as applicable to the O/E duties.

* **8(2)** BUT no deductions except as permitted by the Act.
* **8(10)** Certain deductions require a certificate from the employer **(1)(c), (f), (h), (h.1)** and **(1)(i), (ii), (iii)**.

- Always keep **67** “reasonableness” in mind as a possible limit. No deduction shall be made in respect of an outlay or expense unless the outlay or expense was reasonable in the circumstances.

**TRAVEL & MOTOR VEHICLE EXPENSES**

- For both categories, the most important part is the “mid-amble” that says the expenses must be incurred in the course of the O/E.

* “In the course of” is a close nexus.

- **8(10)** applies here – need a certificate from the employer – costs required by K.

**TRAVEL EXPENSES**

- These expenses generally include costs of transportation, accommodation, and meals.

- **8(1)(h)** TP can deduct if TP was:

* **(i)** ordinarily required to carry on their duties of O/E away from employer’s place of biz or in diff places AND
* **(ii)** contractually obliged to pay the travel expenses so incurred.
* WON’T get the deduction if:
* **(iii)** TP got an allowance already deducted under **6(1)(b)(v) or (vi)** OR
* **(iv)** Claimed a deduction under **(e), (f) or (g)**.
* ALSO **8(10)** applies – employer has to certify the expenses, saying they expected employee to pay them.

**MOTOR VEHICLE EXPENSES**

**-** These expenses generally include things like costs of maintenance, gas, etc.

- **8(1)(h.1)** TP can deduct on the same requirements as **8(1)(h)**.

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| Luks v MNR 1958 Ex CtTravel in the course of employment | - TP was electrician, worked for 3 diff employers in various places, many projects all over. Had to bring his own tools – no place to store them so brought them to and from everyday. Deducted travelling expenses for gas, oil, repairs, and various car expenses.* Issue – were the expenses incurred travelling in the course of his employment?

- No. He was travelling to and from, not during. Carting his tools around occurred before and after his duties. Just b/c it was the practical thing to do doesn’t mean it’s part of his duties. Might be “in respect of” his employment, but doesn’t meet “in the course of”.- DUFF: This is a very strict approach. Court lightened up after this. |
| Chrapko v Canada 1988 FCATravel itself doesn’t have to be in course of employment | - TP worked at 3 racetracks – lived in Niagara Falls, worked 25% at Fort Erie, 75% Toronto. Tried to deduct travel costs as being incurred in the course of his employment.* He didn’t report to the same place everyday. Court found he “ordinarily worked” in Toronto, so gave him travel deductions to Fort Erie only.

- This case lightened the test to allow travel that is not in performance of a E/O duty but that is still for work: See *Merton*. |
| MNR v Merton 1990 FCTDAs above | - TP was electrician, travelled to different work sites, often went directly to or left directly from the sites before/after going to employer’s permanent office.* Court allowed deductions b/c *Chrapko* qualified the test so you can deduct expenses for travelling from home to a place of work other than the place of usual work. The travel itself need not constitute the performance of a service for the employer.
 |
| Evans v Canada 1998 TCCImplied K to bring everything, no alternative. All travel deductible | - TP school psychologist for various school, had to bring files w her in her car. Allowance only covered travel btwn schools, not to and from home. Sought to deduct those costs.- Normally would look at where she ordinarily reported and make that normal commute non-deductible. If you go somewhere else first, would make the same distance non-deductible and would allow deductions for the rest of the commute.* But here she had no option but to bring the paperwork everywhere. No alternative. So court found implied K term that she have a car and bring the materials.

- All the travel was in the course of her duties, even to and from home.* Moving away from *Luks*.
 |

**MEALS**

- **8(1)(h)** for travelling expenses generally includes the cost of meals that are consumed during the period of travel.

**- 8(4)** Assumes you have satisfied **8(1)(h)**. It requires TPs who seek to deduct the cost of meals as travelling expenses under **8(1)(h)** to satisfy a further requirement that:

* Meal must be consumed during period that TP is required to be away for >12 hours from the municipality or metropolitan area where employer’s establishment to which TP ordinarily reported for work was located.
	+ “Ordinarily” in this context is interpreted to mean “usually” (*Healy*).
		- This is a different interpretation of “ordinary” than in **8(1)(h)**.

- Note that this section is subject to limitation in **67.1** that the amount paid or payable in respect of the human consumption of food or beverages or the enjoyment of entertainment is deemed to be 50% the lesser of:

* **(a)** The amount actually paid or payable in respect thereof, and
* **(b)** An amount in respect thereof that would be reasonable in the circumstances.

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| Healy v Canada 1979 FCAInterpretation of “ordinary” | - TP worked at jockey clubs in Fort Erie and Toronto, lived in Toronto, head office in Toronto. Worked at Fort Erie for a total of 10 weeks, lived in a hotel. Sought travel expenses from Toronto plus costs of accommodation and all meals. Clearly in course of employment.* Was he away from employer’s establishment to which he “ordinarily” reported?

- Yes. He ordinarily/commonly/usually reported to and worked in Toronto so it doesn’t matter that employer also had establishment in Fort Erie.- NOTE: Could also have tried an exempt travel allowance from employer, or special work site. |

**LEGAL EXPENSES**

- Under **8(1)(b)** TP can deduct amounts paid as or on account of legal expenses incurred by the TP to collect, or to establish a right to, an amount owed to TP that, if received by the TP, would be required to be included as income.

* This includes establishing a right to salary or wages, or anything else taxable under (a).
* But does not apply to a retirement allowance b/c that is not employment income.
	+ BUT **60(o.1)(e)** Can deduct the total of all legal expenses paid in the 7 preceding taxation years to collect or establish a right to a retiring allowance.

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| Werle v The Queen 1995 TCCAttempt to establish a right | - TP sued employer for wrongful dismissal, lost. He claimed legal fees as a deduction.* Court allowed the deduction. Wording of **8(1)(b)** allows for an attempt to establish a right, so don’t have to be successful.

- Only allowed the deduction for costs to establish his right to 9 months pay. Not for the actual wrongful dismissal claim b/c that would be for damages, not something required to be included as income. |
| Loo v Canada 2004 FCA | - TP was part of group suing their employer to get same payment as employees in Toronto.- Deductions of legal fees allowed b/c TP was trying to establish that the is entitled to be paid more than he has been paid. |

**HOME OFFICE EXPENSES**

- **8(10)** applies here, require certificate from employer – costs required by K.

- Deductions allowed for:

* **8(1)(i) (i)(i)** Annual professional membership dues the payment of which was necessary to maintain a professional status recognized by statue (ex. law society fees).
* **8(1)(i) (i)(ii)** Office rent the payment of which was required by the K of employment.
	+ These deduction not likely allowed where TP owns the property (*Prewer, Felton, Thompson*).
* **8(1)(i) (i)(iii)** The cost of supplies that were consumed directly in the performance of the duties of the O/E that were required by K of employment to be supplied and paid for.
	+ These include things like fuel, electricity, light bulbs and cleaning supplies (*CRA Bulletin*).

**- 8(13)** imposes a further limitation:

* **(a)** No deduction except to the extent that the work space is either **(i)** the place where TP principally performs the duties of O/E OR **(ii)** Used exclusively or regularly for carrying on the duties.
* **(b)** Where (a) is met, deductions can’t exceed the income calculated before deductions.
* **(c)** Any loss not deductible b/c of (b) can be carried over to deduct against income from the same O/E in the next year, over and over. Unlimited carry-over.

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| Prewer v MNR 1989 TCCHome office rent expense - reasonable deduction allowed | - TP was admin assistant, co in trouble, agreed to do sales work during normal biz hours and do her admin work from home. Converted a bedroom into office, deducted 1/3 of the cost of operating her condo. Implied K to do this, but had a form satisfying **8(10)**.* She didn’t deduct any mortgage interest costs.
* Even though employer provided a work space w/in reasonable distance, it wouldn’t have been reasonable for her to stay so long

- Court found she was entitled to deductions, but that what she claimed was not reasonable under **67**. Said she only used 1/12th of the actual space, so no major hydro costs etc.* Considered square footage and big draws on utilities. 10% of costs deductible.

- TP owned the home so not really rent. But court said it would be absurd if you could rent from your neighbour and deduct, but couldn’t do it from your own home.* DUFF: Probably the right answer but should have left it to the leg to make the change.
* Generally, can’t deduct rent if you own the home.
 |
| Felton v MNR 1989 TCCIf you own, no rent to deduct | - TP had home office as required by K, deducted expenses for “rent”.- Court disallowed, said “rent” can only arise from a landlord-tenant relationship.* Better off deducting office costs under supplies (iii) if you own your home office.

- NOTE: This approach favoured in *Thompson v MNR* 1989 FCJ over the *Prewer* approach. |

**MOVING EXPENSES**

- Requirements:

* 1) Eligible expense (**62(3)**).
* 2) Eligible relocation (**248(1)**).
* 3) Limitations (**62(1)**).

- **1)** TP can deduct **62(1)** amounts paid by TP as or on account of moving expenses incurred in respect of an eligible relocation, to the extent that:

* **(a)** Not paid on TP’s behalf in respect of, in the course of or b/c of TP’s O/E.
	+ If your employer pays, it’s a non-taxable benefit. Hasn’t been included, so can’t be deducted.
* **(d)** All reimbursements and allowances received in respect of those expenses are included.
	+ Again, if it hasn’t been included, it can’t be deducted. Allowances are a fully taxable benefit, so if you include it there, can deduct it as a moving expense.
* **(c)** The total moving expenses can’t exceed either:
	+ **(i)** If moving for employment/biz reasons: the amount you are getting for the taxation year in the new work/biz location.
	+ **(ii)** If moving for school reasons: the amount you are getting in scholarship, grants, etc. at the new school location.
* **(b)** If you were limited by (c), unlimited carry-forward.

**- 2) 248(1)** “Eligible relocation” Means a relocation of TP where:

* **(a)** Relocation enables TP to be employed at a location (new work location) or to be full-time uni student
* **(b)** Before relocation TP ordinarily resided at old residence, after relocation, ordinarily resides at new one.
* **(c)** the new residence is >40km closer to the new work location.

**- 3) 62(3)** “Moving expenses” includes any expense incurred as or on account of:

* **(a)** Travel costs (including a reasonable amount expended for meals and lodging) in the course of moving.
* **(b)** Transport/storage costs in the course of moving.
* **(c)** Cost of meals and lodging near old or new residence for TP and member’s of TP’s household for <15 days.
	+ Doesn’t specifically say “reasonable” but subject to **67** reasonableness limit anyhow.
* **(d)** Cost of cancelling the old lease.
* **(e)** Cost of selling the old residence.
* **(f)** If the old residence is sold as a result of the move, the cost of legal services regarding the purchase of the new residence and any tax, fee or duty imposed on the transfer or registration of title to the new residence (ex. property transfer tax, not GST).
* **(g)** Cost of interest, property tax, insurance and heating/utility premiums of old residence up to the lesser of $5,000 or the total of those costs while the residence is unoccupied & TP is making reasonable efforts to sell.
* **(h)** Cost of changing licenses (and other legal documents that need to be changed) and the cost of disconnecting or connecting utilities.

**MOVING EXPENSES**

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| Storrow v Canada 1978 FCTDMoving expenses | - TP moved from Ottawa to Vancouver, claimed excess cost of new house (more expensive in Vancouver) as a moving expense, as well as new appliances and door locks. Claimed on the basis that the list in **62(3)** is not exhaustive.* Court agreed it’s not exhaustive but said moving expenses are only things that effect the transfer of the person and their stuff. Doesn’t include costs incurred w the acquisition of the new residence.
 |

**PURPOSE OF RELOCATION**

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| Dierckens v Canada 2011 TCCNo time limit on “new” work location | - TP a school bus driver in Winnipeg. Worked there for many years while living in Selkirk. Eventually moved 47km closer to work.* Is this an eligible relocation by which she can claim moving expenses?

- Yes. New wording says “new work location” but doesn’t specify “new”, and is only included in bracket in the definition of eligible relocation, indicating it is defining something else in the provision, rather than creating a time limit.* If there is a work location and a move, you should get the deduction.

- DUFF: Ignores the wording of “enables”. Even then could be too broad if just “make easier”. |
| Beyette v MNR 1989 TCJOld language | - REFERRED TO IN *DIERCKENS*, DECIDED UNDER OLD ACT.- Under old Act, a person had to have commenced to be employed at a location and by reason of that commencement, must have moved. Closer nexus.* Under that language, *Dierckens* might have been out of luck, but there was still no time limit, so might be ok.
 |
| Abrahamsen v Canada 2007 TCCLooking for work | - Under old language, couldn’t deduct if you hadn’t commenced employment.- This case said, under the new language, you CAN deduct moving expenses in the search for employment, as the move would “enable” you to be employed at a new location. |

**REQUIREMENT FOR “NEW WORK LOCATION”**

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| Grill v Canada 2009 TCCNew location | - TP commuted for 10 years, sought to deduct moving expenses after he and his wife separated and he moved into a new residence more than 40km closer to work.- Court said no. Emphasized requirement of “new” work location. Contrary to *Dierckens*. |
| Moreland v Canada 2010 TCCNew location | - TP assigned new duties at same location. Court disallowed the deduction on same wording as *Grill*, emphasized the “new” part as well.* Said you need a new location.
 |
| Gelinas v Canada 2009 TCCNew location | - TP a part-time nurse, commuted 65km each way. Got full time job at same hospital, moved more than40 km closer. Sought to deduct moving costs.- Court allowed the deductions on the basis that “new work location” are not the operative words, just define preceding words.* You just need a change at work that reasonably results the move.

- DUFF: Again, completely ignores “enables”. |

**RESIDENCES BEFORE AND AFTER RELOCATION**

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| Rennie v MNR 1989 TCCOnly 1 residence at a time, ordinary mode of life | - TP worked at McGill, took position in Edmonton. Worked there for 2 years. Kept his house in Montreal but deducted expenses for taking his stuff to Edmonton. TP then took a contract in Victoria and tried to deduct costs of selling Montreal house and new house in Victoria.* Issue – what are his old and new residences?

- Court said you can only reside in 1 location – where your ordinary mode of life is. This was Edmonton, not Montreal, so no deductions allowed.- NOTE: Big oops for TP – couldn’t deduct big ticket items now (buying/selling costs) and didn’t deduct them when he had the chance. Should have maintained Montreal as ordinary place of residence and claimed other jobs were temporary, sojourning. Then deduct in stages – nothing in the Act says you can’t move over 3 years/have a drawn-out relocation.  |
| Jaggers v Canada 1997 TCCRenting before selling | - Court allowed deductions for cost of selling former residence sold more than 2 years after the acquisition of a new one.* Kept and rented out the old one until he was sure the job would work out. That shouldn’t prevent deductions.
 |
| Neville v MNR 1979 TRBRenting before buying | - TP accepted appointment in Winnipeg while on sabbatical. TP and family lived in Winnipeg in rented accommodation for 2 years before buying a house and moving and seeking deductions.* Court allowed deductions. Rental for 2 years only temporary in nature, so the other house remained the “old residence”.
 |
| Pitchford v Canada 1997 TCCOrdinary routine, normally live = residence | - TP moved from Victoria to Moose Jaw, then to Saskatoon. Stored most stuff while in Moose Jaw, sought deductions for moving it from Victoria to Saskatoon.* Court allowed deductions. Family didn’t have a “settled routine of life where they regularly, normally or customarily lived” until they settled in Saskatoon. Old residence remained the one in Victoria.
 |
| Ringham v Canada 2000 TCCOrdinary residence | - TP accepted work on project in Budapest. Sold his hope in Ottawa and rented a condo there while travelling weekly to Thornhill where he stayed at a hotel. Budapest project fell through, TP moved to Thornhill condo & worked full time at Thornhill office. Sold Ottawa house.* Court allowed deductions. Realistically, there was only 1 move. At first, the Thornhill residence wasn’t considered by TP as an ordinary residence – didn’t unpack boxes, changed mailing address just for convenience. Expected to move soon.
 |
| Calvano v Canada 2003 TCCOrdinary residence | - TP moved from Brampton to rented house in Coquitlam. Didn’t sell Brampton house for 16 months after renting it out. Then moved all his stuff out.* Court disallowed deductions b/c he was ordinarily resident in Coquitlam in meantime.
 |
| Turnbull v Canada 1998 TCCOrdinary residence factors | - TP maintained home in NFL, worked in Edmonton, then BC, then Yellowknife. Sought deductions for moving to and from BC.* Court disallowed deductions b/c he was ordinarily resident in NFL at all times – returned every year, listed it as residence on tax return, rebuilt the house, etc.
 |
| MacDonald v Canada 2007 TCCOrdinary residence factors | - TP couldn’t find work on Cape Breton island, so worked in AB for 6 weeks. * Court disallowed deductions b/c he was ordinarily resident in Cape Breton the whole time – CB drivers license and health insurance, left most of his stuff there, CL spouse stayed in CB, had 3 houses in NS but didn’t buy anything in AB, didn’t change bank accounts or mailing address.
 |
| Cavalier v Canada 2001 TCCFactors | - TP accepted teaching K that required him to move from BC to AB for 4 months.* Court allowed deductions even though his spouse stayed in BC, no change to mailing address or bank account.
 |

**DISTANCE REQUIREMENT**

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| Giannakopoulos v MNR 1995 FCAAssess distance on shortest normal route | - TP moved w/in Edmonton, calculated distance difference by driving between locations. CRA reassessed based on straight line analysis of distance.* Court allowed deduction – “as the crow flies” isn’t practical. Have to calculate the 40km using real and usual methods of travel.
* BUT use the shortest normal route (not scenic route when highway is shorter, for ex.).
 |
| Nagy v Canada 2007 TCCShortest *practical* route | - TP claimed deductions, CRA denied on the basis he had moved only 34.6km closer.* Court allowed deductions, said TP’s method of calculating the distance was more reasonable. Can’t just pick the shortest route, bar none. Have to pick the shortest practical, realistic, normal, common sense route.
 |
| Lund v Canada 2010 TCCShortest by distance, not time | - TP calculated old distance at 53km, CRA at 33. New distance was 9.8km so important call. TP said his route was a longer distance but short time due to traffic.* Court disallowed deductions: Since both routes could be considered normal, have to go w the shorter one. Has nothing to do w time.
 |

**CHILD-CARE EXPENSES**

- **63(1)** Can deduct **amounts paid as or on account of child care expenses incurred for services rendered in the year in respect of an eligible child of the TP**.

* **63(3)** “Eligible child” of a TP means a child that is:
	+ **(a)** a child of the TP or of the TP’s spouse or CL partner OR
	+ **(b)** a child dependent on the TP or the TP’s spouse or CL partner for support and whose income for the year doesn’t exceed the amount used under **118(1)(c)**.
	+ Provided that, at anytime during the year, the child was:
	+ **(c)** under 16 OR
	+ **(d)** dependent on TP or TP’s spouse or CL partner and has a mental of physical disability.
* **63(3)** “Supporting person” of an eligible child of a TP means a person, other than the TP, who is:
	+ **(a)** A parent of the child,
	+ **(b)** The TP’s spouse or CL partner, OR
	+ **(c)** An individual who deducted an amount under **118** for the year in respect of the child,
	+ If they resided w TP at any time during the year and any time w/in 60 days after the end of the year.
* **63(3)** “Earned income” means the total of salaries/wages/other remuneration from O/E, employment benefits, stock options, scholarship, etc., income from a biz actively engaged in, and disability payments.
	+ These are all active things, no income from property etc.
* **252(1)** Extended meaning of “child” Words referring to a child of a TP include:
* **(a)** A person of whom the TP is the legal parent,
* **(b)** A person who is wholly dependent on the TP for support and of whom the TP has, or immediately before the person attained the age of 19 years had, in law or in fact, the custody and control.
* **(c)** A child of the TP’s spouse or CL partner, and
* **(e)** A spouse or CL partner of a child of the TP.

- **63(3)** “Child care expense” means an expense incurred for the purpose of providing, for an eligible child, child care services including baby sitting services, day nursery services or services provided at a boarding school or camp if the services were provided:

* **(a)** To enable the TP, or the supporting person of the child for the year, who resided w the child at the time the expense was incurred:
	+ **(i)** To perform the duties of an O/E,
	+ **(ii)** To carry on a biz either alone or as a partner actively engaged in the biz,
	+ **(iv)** To carry on research or any similar work in respect of which the TP or supporting person received a grant, or
	+ **(v)** To attend a designated educational institution or a secondary school, where the TP is enrolled in a program of not less than 3 consecutive weeks duration and has to spend **(A)** >10 hours per week on courses or work in the program OR **(B)** 12 hours per month on courses.
* You only get the deduction to the extent that you incurred the expense in order to carry on these things. Must be the primary purpose, but can have other incidental benefits (*Levine, Bailey, Jones*).
	+ Also note possibility of “good help is hard to find” fees, and the waffling by the court (*D’Amours* etc.).
* **(b)** Provided that the services are performed by a resident of Canada other than **(i)** the mother or father of the child, **(ii)** a supporting person of the child or **(iii)** a person under age 18 who is related to the TP, or a person in respect of whom an amount is deducted under **118**.
* **(c)** Dollar limit on boarding schools and camps (based on weeks).
* **(d)** Medical expenses are not included unless they are explicitly included elsewhere in the definition (ex. it’s included in nursery care, etc. – can’t be pure medical care).
* Note possible use of a corporation run by an otherwise ineligible provider (*Clogg*) (possible GAAR issues).

- **63(3)** allows for deductions by dollar amount per eligible child, varying depending on age and disability. These amounts will be going up by $1,000 each in the next year or two:

* **(a)** Disabled child = $10K max per year.
* **(b)** Child under 7 years old = $7K max per year.
* **(c)** And other child up to age 16 = $4K max per year.

- **63(1)** Childcare expenses as defined above can be claimed by the TP or a supporting person if they meet the reqs:

* **(e)** Can only deduct the lesser of 2/3rds of your earned income and the total of all expenses.
	+ So can only deduct up to 2/3rds of your earned income.

- **63(2)** The expenses must be deducted by the lower income-earning spouse.

* **(b)** The higher earner can only deduct if the supporting person is **(A)** a student, **(B)** disabled & certified to be incapable of caring for children b/c of disability, **(C)** in prison (or similar institution), or **(D)** b/c of breakdown of marriage or CL partnership, was living apart from TP at the end of the year and for >90 days.
* In some cases the lower income-earning spouse may be actively working but not making “income” as defined in the section. They are the one who must claim the deduction, but w 0 income, can’t use it.

**EXPENSE INCURRED FOR CHILD CARE**

|  |  |
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| Levine v Canada 1995 TCCPrimary purpose must be CC and enabling work | - TP was flight attendant, on call on days off. Husband also worked on short notice. They had 2 kids, ages 7 & 4, had a live-in nanny. Then had twins and nanny quit, had trouble finding a new one. Eventually paid agency a $500 finders fee and found a new nanny. TP took maternity leave.* Deducted finders fee & costs of many “recreational” activities. Deductible?

- Court allowed deductions for finders’ fee b/c it was paid for the purpose of providing child care services. Falls w/in the spirit of the section.- But disallowed recreational expenses. Took French version, interpreted CC to mean “guarding”.* Primary purpose of these things was recreation and new skills, CC was only secondary to that purpose. These would have been done whether or not TP was working, only lasted an hour or so, not the whole day – not enabling TP to work.
 |
| Acharya v Canada 1996 TCCCC + education | - CRA disallowed deductions for expenses in respect of a 13 year old child on the basis that they were tutorial rather than CC, and a 13 year old doesn’t need much care/supervision.* Court allowed the deductions. Even if some education, musical or other teach was involved, that is not sufficient in itself to find the amounts are not CC.
 |
| Bailey v Canada 2005 TCCCC + education | - TP sent kid to private school that cost less than CC center, as kids was 10 days too young to go to kindergarten. CRA reassessed on the basis that it was education, not CC.* Court allowed the deductions. Expenses were paid not for education but for reasonably priced CC services – any education was an incidental benefit. Primary purpose was CC.
 |
| Jones v Canada 2006 TCCCC + recreation | - Court allowed deductions for gymnastics class fees for the kids after school and during spring and summer breaks. No prohibition on recreational activities being deducted, as long as the primary purpose was CC so TP can perform duties of O/E. |
| Lessard v Canada 2003 TCCUp to parent | - TP deducted residence fees paid for daughter while studying at Royal Winnipeg Ballet School.* Court allowed deductions on the basis that the choice of CC services is up to the parent. Doesn’t have to be justified by parent’s work needs.
 |

**PURPOSE OF SERVICES (ENABLING)**

- DUFF: These decisions seem to map onto the gender of the judge.

- DUFF: No one seems to have actually looked at “enable” and analyzed what the limits of that are.

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| D’Amours v MNR 1990 TCCGood help is hard to find | - TP had 3 kids, took maternity leave for 4th. Hired a babysitter who worked during the first 4 months of TP’s maternity leave. Deductible?* Court said yes on basis that “good help is hard to find”. Sitter worked for her before mat leave, and TP had to keep her on in order to ensure she would be there when she went back to work. So those 4 months were still enabling TP to work. Economic reality.
 |
| McCluskie v Canada 1994 TCCStandby fee | - TP hired nanny from another country immediately when she arrived in Canada, rather than waiting until the end of TP’s mat leave. Deductible?* Same argument as in *D’Amours*, but court here called it a “standby fee” and disallowed the deduction. It is a cost of personal convenience rather than necessity.
 |
| McLelan v Canada 1994 TCCGood help | - TP hired nanny immediately when she became available, when TP was still on mat leave.* Court allowed deductions on the basis that good help is hard to find (*D’Amours*).
 |
| Sawicki v Canada 1997 TCCPersonal but enabling | - TP had depression, paid her nephew to look after her kids on weekends and holidays. She claimed, due to her illness, this enabled her to work.* Court disallowed, said it’s a personal expense rather than CC even if, in the end, it enables TP to work.
 |

**CHILDCARE PROVIDERS**

|  |  |
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| Clogg v Canada 1997 TCCProprietorship vs. corporation | - TP put kid in daycare run by TP’s spouse. Claimed payment was to the proprietorship, not to his wife. Is this an ineligible provider?* Court said ineligible. Payments were really to wife – sole proprietorships are carried on personally by the individual who owns them. Not a distinct entity like a corporation.
 |

**INCOME FROM A BUSINESS OR PROPERTY**

- **3(a)** Inclusion of income from all sources includes income from biz and property.

- Main issues: 1) Characterization. 2) Inclusions. 3) Deductions. 4)Timing.

**CHARACTERIZATION**

- What is a biz and what is a property?

* **248(1)** “Property” means property of any kind whatever, including **(a)** a right of any kind whatever (ex. a share), **(b)** money, **(c)** timber resource property, and **(d)** the work in progress of a biz that is a profession.
* **248(1)** “Business” includes a profession, calling, trade, manufacture or undertaking of any kind whatever, an adventure or concern in the nature of trade (ACNT), but does not include an office or employment.
	+ Ordinary meaning of business = organized activity carried on for the purpose of profit.
		- Subjective and objective 🡪 Reasonable expectation of profit test.
		- NOT gambling gains (*Morden, Leblanc*), YES treasure hunting gains (*McEachern, Tobias*).
	+ Extended definition includes ACNT: A speculative activity that has the nature of buying and selling.
		- Can be isolated, but there must be an intent to profit (inherent in “speculative”).
		- The difficulty is often trying to distinguish inventory from capital.
			* Short holding period and soliciting orders/customers generally indicates inventory.
			* Holding property for a longer period and earning income from it generally capital.
		- See *Taylor* for relevant tests to use.

**CHARACTERIZATION OF BUSINESS**

|  |  |
| --- | --- |
| MNR v Morden 1961 Ex CtGambling = not a biz | - TP owned a hotel and racing stable w up to 12 horses. Spent a lot of time and attention betting on horses and gambling on all kinds of things. Were gambling winnings taxable as biz income?* Court looked at subjective and objective elements:

- Subjective element: Court looked at TP’s “dominant objective”. Commercial or entertainment?* TP said he wasn’t in it for profit, was a compulsive gambler, would do it even if no $.

- Objective element: Court looked at the fact that he put a lot of time, attention and labour into it, but also that it wasn’t sufficiently organized or active. Also said gambling isn’t capable of being a biz, differentiated from a bookie, who calculates odds, expects to win, is organized, etc.- Overall, just a windfall, non-taxable. No reasonable expectation of profit. |
| Leblanc v Canada 2006 TCCGambling | - TPP bros set up a system and made lots of money on sports lotteries. They figured out how to beat the odds and got away w it for a time. It was their only occupation during that time.* Court said not taxable. Just gambling, even if they had a system. Compulsive.
 |
| MacEachern v MNR 1977 TRBTreasure-hunting | - TP treasure hunter. Sold things he found, was characterized as biz income on the basis that at all times he was intending to sell anything he found for profit.* More than a hobby b/c it had clear potential for substantial profit, well-organized.
 |
| Tobias v Canada 1978 FCTDTreasure-hunting | - TP unsuccessful treasure-hunter. Court said it was a commercial operation, allowed costs to be deducted as losses from a biz.* Regardless of high degree of uncertainty, there was a prospect of a very substantial award to compensate TP for time, money and risk involved. Like investing in risky biz.
 |
| Cameron v MNR 1971 TABWhale catching | - TP was a fisherman, joined others twice to catch killer whales and sell them to aquariums.* Court said not taxable. He was a fisherman, not a whaler, it was more of a fortuitous event than a business venture in the usual sense. But said if there had been a 3rd catch, might have swung it into category of biz.

- DUFF: What about ACNT? |
| MNR v Taylor 1956 Ex CtAdventure or Concern in the Nature of Trade | - TP was prez of Canadian sub that was only allowed to have a 30-day supply of raw metals on hand. Lead prices dropped, he asked to buy a 3-month supply, parent co said no. He bought it himself and sold it to the co over time, made big profit.* Issue - Was it an ACNT? Court went through the relevant tests:

1) Manner of dealing: Was the thing done in the same way it would be by someone actually in the biz? (ex. soliciting customers, not held for a long period of time, REOP).2) Nature and quantity of the subject matter: Huge quantities of things not generally for personal use, and certain things clearly for trade (ex. lots of iron, whiskey, toilet paper, etc.).3) Intention and secondary intention doctrine: Intent to sell. Secondary: Might have bought it to enjoy it but realized it may go up in value and could sell for profit.* NOTE: This case said intention isn’t important, has been overturned by CRA.

- Overall court found TP was doing ACNT. Nature and amount of lead, left it in rail car waiting for time to sell, found a buyer right away, etc.- Things that don’t matter:* Frequency of transaction (“an” ACNT).
* Doing something w it (don’t have to manufacture or anything, just buy and sell).
* Being engaged in other similar activities – can be relevant, but not necessary.
 |
| Regal Heights v MNR 1960 SCC Secondary intention | - TP bought then resold parcel of vacant land. SCC characterized it as biz income from ACNT b/c of secondary intent to resell, notwithstanding the primary intent was to build a shopping mall.- NOTE: Subsequent cases have said it can be ACNT where “the possibility of re-sale at a profit was one of the *motivating considerations* that entered into the decision to acquire the property” |
| Steward v Canada 2002 SCCREOP only for transactions w a personal aspect | - TP was salaried employee looking for tax shelter investment. Bought condos to earn rental income, w projected losses for 10 years. He incurred expenses (interest, mgmt. fees, CCA, etc.) against the rent he earned, and deducted them to offset other income. Eventually would get a capital gain, only half taxable.* SCC said the REOP test does NOT apply to transactions that are clearly commercial.
* Only if there is a personal aspect can you use the REOP test.

- So have to distinguish between commercial use and personal use.* Here it was clearly commercial (no personal use even argued), so no REOP test.
 |

**INCLUSIONS**

- **9(1)** TP’s income for a taxation year from a biz or property is the TP’s profit from that biz or property for the year.

* “Profit” is a net concept – inclusions and deductions.

**INCOME FROM BUSINESS AND OTHER INCOME**

- Note that illegal businesses are taxable:

* *No.275 v MNR* 1955 TAB: TP was prostitute. First, determine if the income is from a business (here yes). If so, it is taxable. Otherwise, big incentive to illegal businesses.

**DAMAGES AND OTHER COMPENSATION**

- Possible characterizations for payments:

* Compensation for lost profits = business income.
* Compensation for lost assets (ex. *HA Roberts*) = capital receipt.
* Punitive damages (*Bellingham, Cartwritght and Sons*) = non-taxable receipt.

- *H.A. Roberts* makes it clear a TP can have more than one business, have to separate them out. *CRA Bulletin*:

* Factors to consider:
	+ Type of operations (same processes, products, customers, inventories, etc.?).
	+ Operations carried out on the same premises.
	+ If one operation exists primarily to supply the other.
	+ Etc.

- Whether the K lost ended the biz or was a loss of a capital asset is a big area of litigation. *CRA Bulletin*:

* Factors to consider:
	+ *Surrogatum* principle.
	+ Nature of contracts in the business
		- Can the loss of a K be absorbed by the biz as a normal incident?
	+ Size of the contract relative to the size of the business.
		- Does the loss of the K cripple the whole profit-making apparatus?

|  |  |
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| London & Thames Haven Oil Wharves 1967Surrogatum | - TP got $ in claim for negligence for loss of use of an income earning asset during its period of repair. Court developed the *surrogatum* principle, w 2 requirements:* 1) Compensation received pursuant to a legal right.
* 2) Amount for which the compensation substitutes would have been taxable income.

- NOTE: Damages are neutral, don’t tell us if the underlying thing is income/capital/windfall. |
| Canada v Manley 1985 FCASurrogatum | - TP entered agreement w Levy to find a purchaser for controlling shares of Levy Ind. to buy them from Levy and family members. TP would get 2% finders’ fee. Turned out Levy didn’t have the authority to enter into this agreement – Manley sued and won for breach of K.* Is the damage award taxable?

- Court looked to *The Queen v Atkins* 1976: An amount paid as damages for wrongful dismissal isn’t taxable as income from an O/E. Not income from a source in O/E, but disposition of capital.* TP used this to argue that it’s a capital gain, no “source” of income.

- Court rejected this. Said damages fall under *surrogatum* – TP got in damages exactly what he would have got in profit from ACNT. If it was earned as finders’ fee it would have been taxable.* *Atkins* rejected this in the O/E context, but the court went w it here for biz.
 |
| H.A. Roberts v MNR 1969 SCCSeparate biz/huge K lost – capital receipt | - TP had real estate biz to manage mortgages for clients. A client terminated a long-term K and paid TP ~$75K. Is that income from a biz?* Court characterized the mortgage biz as a separate biz that ceased to exist when the Ks were cancelled (basically the only client), and therefore a capital receipt (at the time not taxable at all). AND K was so big it was a capital asset to the biz anyways.

- NOTE: Relevant *CRA Bulletins* above, this is a big area of litigation. |
| Bellingham v Canada 1995 FCAPunitive damages | - Gov expropriated TP’s property, didn’t pay him enough. TP sued, got punitive damages.* Court said this was a non-taxable windfall. The payment wasn’t compensation for the loss of the land, it was to punish the gov.
 |
| Cartwright and Sons v MNR 1961 TAB As above | - TP got punitive damages for infringement of copyright.* Court said this was a non-taxable windfall. TP wasn’t being compensated for loss, it was to punish the infringer.
 |

**VOLUNTARY PAYMENTS**

- Voluntary payments are made *ex gratia*, w/out any legal entitlement on the part of the recipient.

* Note the difference from *surrogatum*, where you have to get the amount pursuant to a legal right.

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| Federal Farms v MNR 1959 Ex CtGift | - TP had farm, hurricane flooded his crops and caused a lot of property damage. Charity relief fund was set up for the area, TP got ~$40K, mainly for corp loss but also to fix property damage. This covered about ½ TP’s losses.* MNR argued it was compensation for lost crop income under the *surrogatum* principle.

- Court said it was just a voluntary personal gift. Characteristics of the payment:* TP had no legal right to it.
* No expectation of getting anything.
* In no way did this arise out of the biz – wholly unrelated.
* Unlikely to recur.
 |
| Campbell v MNR 1958 TABVoluntary compensation for services | - TP was a swimmer, entered K w newspaper to attempt to swim Lake Ontario for $600, would get a further $5,000 if she did it. Coach pulled her from the water w 1 mile to go. Despite not completing the swim, newspaper gave her the $5,000 for her “magnificent effort”.* Court said that despite there being no legal right to this etc., it was a payment made in compensation for services – voluntary, but arose out of services rendered.
 |
| Canada v Cranswick 1982 FCAWindfall | - TP was minority SH of Canadian branch of US co. Majority offered to either buy the shares or pay an amount per in order to avoid litigation after a bad sale of part of the co. TP didn’t sell, took the extra money option.* Court held this was a non-taxable windfall to which TP had no enforceable claim. Hadn’t expected it and non-recurring.
* Note that if the TP had sold their shares, they would have triggered a capital gain.
 |
| Frank Beban Logging v Canada 1998 TCCWindfall | - TP had biz as logging/road contractor, got $800K from gov after their agreement ended due to a disagreement in levels of gov.* Court held this was a non-taxable windfall. Payment was not pursuant to a legal right. Whether gov paid to keep him happy or to compensate him doesn’t matter. It was done voluntarily so nothing more than a windfall.
 |
| Mohawk Oil v MNR 1992 TCADon’t bank on the parties’ characterization | - TP got $ as settlement for a negligence claim for damages.* Court held it was received partly on account of lost profits and partly on account of capital – taxable.

- Can’t characterize payments based on what the involved parties call them. Payor can have multiple varying motives. Just b/c this amount exceeded the amount provided for in the termination of damages clause of the K. Payee was “made whole” in income etc. |

**PRIZES AND AWARDS**

- Often received w/out any legal entitlement on the part of the recipient. But in some cases, the recipient may have provided valuable consideration in exchange for which the grantor confers either a prize itself or the opportunity to receive a prize or award.

- **ANALYSIS**:

* 1) Is this prize received in the course of a biz or in respect of an O/E?
	+ Yes 🡪 Fully taxable as biz or O/E income (got to **9(1)** or **6(1)(a)**).
	+ No 🡪 Proceed to 2.
* 2) Is this prize for achievement in a field of endeavor ordinarily carried on by the taxpayer under **56(1)(n)**?
	+ No 🡪 Not taxable, just a windfall.
	+ Yes 🡪 Taxable unless 3 applies.
* 3) Is this prize a prescribed prize under **Reg 7700**?
	+ No 🡪 Taxable over $500.
	+ Yes 🡪 Not taxable.

- Prizes from lucky draws are generally not taxable as biz income. (*Abraham, Poirier*).

- Prizes from competitions may be taxable as biz income (*Rother, Watts*).

* DUFF: Note that in both these cases the competitions were part and parcel w the biz, so should have been taxable as biz income. This was not followed in either case.
* Feds responded w **56(1)(n)**.

- Prizes not received in respect of employment or in the course of a biz may be taxable under **56(1)(n)** if they are for achievement in a field of endeavor ordinarily carried on by the TP.

* **56(3)** There is a $500 exemption.
* Note that “in respect of” is the nexus test, as in **6(1)(a)**, very broad. This nexus piece was added after *Savage*.
* See *Savage* for what counts as a prize and what doesn’t.

**- 56(1)(n)** exempts “prescribed prizes”.

* **Reg 7700** “Prescribed prize” is any prize that is recognized by the general public and that is awarded for meritorious achievement in the arts, the sciences or service to the public but does not include any amount that can reasonably be regarded as having been received as compensation for services.

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| Abraham v MNR 1960 TABLottery winning | - TP owned an IGA, got all products from Loeb. Loeb distributed lottery tickets for a draw w their deliveries in anticipation of anniversary party. TP won a car, took cash instead.* Court said it was won by change so a windfall. May have gotten the lottery tickets via his biz, but he didn’t pay for them and didn’t request them, just showed up.
* Won by pure chance, no remuneration for services. Not taxable.

- DUFF: How much chance is required to break the connection w the biz? |
| Poirier v MNR 1968 TABLottery winning from work | - TP was prez of a Ford dealer. Met sales quota, won a draw for free trip to Caribbean.* Court said just won by chance, windfall, not taxable. Said the trip wasn’t income b/c the origin of it didn’t have the characteristics of taxable income. Benefit wasn’t rent, interest, dividend, profit or salary.
 |
| Rother v MNR 1955 TABCompetition | - TP was 1 of 6 architect finalists in a design competition, got $2,000 for being a finalist.* Court said it was a gratuitous award received in the course of a competition, not taxable. He didn’t get it as a fee for services rendered, or purchase price of the design or anything like that. No legal right to it, etc.
 |
| MNR v Watts 1966 Ex CtCompetition | - TP architect entered design competition, got $4,000 for being 1 of 5 asked to submit further drawings, and he got the $15K final prize.* Court said taxable income b/c they came from a “contractual relationship” that had been created by virtue of TP entering into the competition that enabled him to win the prize. Court found a separate biz entity/venture, so taxable.
 |
| Canada v Savage 1983 SCCOld section“Prize” is broad | - **NOTE** this was before the exemption in **56(1)(n)** for prizes received in the course of or by virtue of O/E. So if employment, fully taxable, if a prize, only taxable of $500.- TP got $300 from employer for completing courses. Court decided it was received in the course of office or employment, so then had to see if it was a prize or employment.* Court interpreted “prize for achievement” broadly, doesn’t have to be a competition etc.
* BUT does NOT include chance, athletic achievement, or costume party things.

- In this case, $500 exemption applied, so this amount not taxable. |
| Turcotte v Canada 1997 TCCField of endeavor | - TP won $ for trivia on a game show.* Court found it wasn’t a prize under **56(1)(n)** b/c it wasn’t for “a field of endeavor ordinarily carried on by the TP”. So not taxable.
 |
| Foulds v Canada 1997 TCCPrescribed prizePublic recognition | - TP had music mgmt biz, primarily for 1 band. The band won 2 music prizes for outstanding achievement in the music field, TP got a cut. Were these prescribed prizes?* Court said yes. It was not income (not recurring, not for services rendered, etc.), there was meritorious achievement, and it was an art, and was sufficiently recognized by the public thanks to heavy advertising over radio, posters, etc. in the area in which the prize was given out.
 |
| Labelle v Canada 1994 TCCPrescribed prize | - TP prof won a writing award. Question whether it was a prescribed prize:* Court said no. Not recognized by the general public.
 |

**INCOME FROM PROPERTY**

**INTEREST INCOME**

- **12(1)(c)** TP must include any amount received or receivable in the year as, on account of, in lieu of payment of or in satisfaction of, interest.

* Note the use of *surrogatum* words. Remember interpretation principle that if words are used in one place and not another, there is a presumption that the omission is deliberate.

- “Interest” is not defined in the Act. Dictionary definitions reveal **3 elements to legal interest**:

* 1) Compensation for the use or retention of a principal sum (the amount of the loan),
* 2) Interest is referable to the principal (ex. is a percentage of the principal sum), AND
* 3) Accrues day-today (ex. if you charge 5% a year you can break it down and see how much is owed on a daily basis, even if it is not payable until the end of the year).
	+ Can agree to make interest accrue day-to-day on a principal sum determined retroactively (*Perini, Miller*). This is different than when a payment has an element of compensation (*Huston, Bellingham*). The difference has to do with legal entitlement to the sum.
* *Sherway* expanded the concept of interest to include amounts not directly referable to the principal, but clearly connected to it. DUFF thinks this is too broad.

- **16(1)(a)** Where, under a K or arrangement, an amount can reasonably be regarded as being in part interest or other amount of an income nature and in part an amount of a capital nature, the part that can reasonably be regarded as interest shall be deemed to be interest on a debt obligation.

* This adds “deemed interest” to **12(1)(c)** – have to include legal and deemed interest.
* The application of this provision turns on the terms of the agreement, course of negotiations, relationship between price paid and FMV, and common practice (*Groulx, Vanwest Logging*).

**LEGAL INTEREST**

|  |  |
| --- | --- |
| Perini Estate v MNR 1982 FCACan retroactively agree to make interest accrue day-to-day | - TP owned all shares of co, sold them on a 3 stage agreement:* 1) Initial payment of $660K on closing date (Nov.27 1968).
* 2) Earn-out (buyer to pay % based on profits for the year) for 3 years, not exceeding $400K each year, $1.2mil cumulative.
* 3) 7% interest on earn-out amounts from closing date (Nov.27, 1968).

- Issue – is #3 truly an interest payment? (got $14K, $28K, and $119K over the 3 years).- TP argued it was a capital payment (b/c it was part of the purchase price), despite use of the word “interest”. Said it doesn’t meet the legal interest requirement of accruing day-to-day b/c the principal sum only came into existence once calculated at the end of the year.* Court disagreed - You can retroactively agree to make the interest accrue day to day.

- Have to look very carefully at what the agreement is – here there was a legal obligation from the closing date to pay a price to be determined once a condition was met. The condition was met (profits), and then it kicked in retroactively. |
| Miller v Canada 1985 FCTDRetroactive | - TP got retroactive salary increase w “interest” payable for periods to which the salary related.* Court said those payments were referable to a principal sum, even though the amount was not determined prior to the period to which the interest related.
 |
| R.G. Huston v MNR 1962 Ex CtCompensation | - Payments received from a war claims fund were called and calculated as interest.* Court said they weren’t though – simply grants b/c TP had “no property or legal or equitable right of any kind in the amount on which the alleged interest was computed”.

- There is an element of compensation here, rather than retro-activity – not interest. |
| Bellingham v Canada 1995 FCACompensation | - TP got an amount b/c gov expropriated his land. Got punitive damages b/c gov didn’t pay him nearly enough.* Court characterized the payment as a punitive damage award rather than interest.

- There is an element of compensation here, rather than retro-activity – not interest. |
| Sherway Centre v Canada 1998 FCAExpanded concept of interest | - TP borrowed lots of $ to finance a commercial development. The loan had various elements:* 1) Interest payment, 9%.
* 2) “Participatory interest”, 15% of the operating surplus.

- #2 here was a formula related no just directly to the amount borrowed, but to the income earned by the development. Court expanded the definition of interest to include this:* Amounts like this are clearly referable to the principal sum in the sense that it’s only payable so long as the principal sum is outstanding.

- DUFF: Bad decision, extended the concept too much. Now interest can include amounts that are not directly related to the principal, but are clearly related to it in some way. |

**DEEMED INTEREST**

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| --- | --- |
| Groulx v MNR 1967 SCCObjective and subjective elements | - TP owned a farm, had been approached to sell several time. Then approached w good offer, negotiated to $395K on a schedule of deferred payments:* 1) $85K on closing (1956).
* 2) $15K in 1958, $25K in 1959, $50K from 1960-1963, and $40 in 1964.
* 3) Buyer to pay 6% per year on late payments.
* 4) Buyer to get 5% discount per year on early payments.

- TP reassessed on basis that, in 1958, it’s reasonable to regard payments after that as interest.- Court agreed w CRA:* TP was savvy biz guy. Sold above FMV and suggested they forgo interest and do this type of payment schedule instead. Basically looks like he was trying to avoid interest.

- The part of the payment that would represent interest at 5% (prevailing rate at the time) is interest under **16(1)(a)**. Can be reasonably regarded as interest b/c:* Objective: Almost universal biz practice to charge interest on land transactions.
* This is supported by MNR’s evidence that the purchase price exceeded FMV.
* Subjective: TP’s obvious interest in not doubling his taxable income.
 |
| Vanwest Logging v MNR 1971 Ex CtUse of *Groulx* approach | - TP sold logging rights for $7.5mil. $1.5mil due on closing, rest $1.2mil per year for 5 years.- Looks like *Groulx* but the court differentiated:* Interest never discussed – doesn’t seem shady like in *Groulx*.
* Nothing in K about allowing discounts or penalties based on time of payment.
* Sale wasn’t above FMV.
* No practice of charging interest in transactions w timber.

- Said only use **16(1)(a)** when something in the evidence indicates that it was the intention of the vendor to avoid taxation on interest by including it as part of a larger capital payment.* Here, it’s all a capital payment, not interest.
 |

**DISCOUNTS AND PREMIUMS**

- Discount: Where a debt obligation is acquired at a price less than the principal amount payable on maturity (buy the right to be paid for less than you will get), this “discount” is an economic return, in addition to interest payable on the debt.

- Premium: Debt obligations may also provide an economic return in the form of a bonus in excess of the principal amount payable at maturity. This is a “premium”.

- These kinds of payments can substitute for interest/are functionally equivalent. In order to characterize them as “legal interest”, the courts have traditionally said they must not only compensate for the use of borrowed money, but refer to the principal amount and accrue day-by-day.

- Factors to consider:

* See *Peter Dixon & Sons*. Where there is a reasonable commercial rate of interest on a fairly secure loan, there is no presumption that a discount or premium has the character of interest.
* Where there is no stipulated rate of interest payable, it will be characterized as interest (*O’Neil*).

|  |  |
| --- | --- |
| Lomax v Peter Dixon & Sons 1943 KBCharacterization of discount or premium vs. interest | - Notes issued by a co at a discount, and redeemable at a premium. Notes also bore a reasonable commercial rate of interest. Court found the discount and premiums were capital sums. To get at the true nature of the discount/premium, look at:* The term of the loan (longer = higher risk).
* Stipulated rate of interest (reasonable indicates capital).
* Nature of capital risk (buying a house or just a loan to go travelling, for ex.).
* Extent to which parties took the nature of the capital risk into account in the terms of K.

- Where there is a reasonable commercial rate of interest on a fairly secure loan, there is no presumption that a discount or premium has the character of interest. |
| O’Neil v MNR 1991 TCCNo rate of interest = interest | - TP bought treasury bill for $189K, cashed in for $200. Did it twice. Are his earnings interest?- Court use factors from *Peter Dixon & Sons*:* Reasonable rate of interest being charged? No, no interest rate at all. So might be reasonable to see all of it as interest. Court deemed it to be interest.
 |

**ROYALTIES**

- **12(1)(g)** Any amount received by the TP in the year that was dependent on the use of or production from property. There are 2 main aspects to this:

* 1) The manner in which amounts received must “depend on” the use of or production of property (*Morrison*)
* 2) The relationship between “amounts received in the year” and use of/production from property (*Huffman*)
* NOTE: Such an amount could include rent.

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| MNR v Morrison 1966 Ex CtDependent on use = referable to timeDependent on production = referable to quantity | - TP owned a bunch of land. Gov wanted to build a causeway, made an agreement w TP to get rock from his property. Basically said they could take however much they wanted and build structures on the land, so long as they repaired everything etc.* K said TP would get 2.5 cents per ton of rock moved. Instead, gov gave him an advance payment of $2,500 and a lump sum after, of $14,500 for rock and damages.
* Issue – was TP’s money dependent on the use or production from the property?

- “Dependent on use” means it has to be in some way referable to the use over time (ex. rent).- “Dependent on production” means it has to be in some way referable to quantity or value, the amount taken from the property.* Here they had no records to show payment according to amount taken. Instead it was a lump sum, not dependent on the actual amount taken.
* No *surrogatum* wording either to be able to say the lump sum was a substitute. And anyways, it seems the payment was in large part for damage to the property rather than for the rock. How to split it up?
 |
| Huffman v MNR 1954 TABCap on amount doesn’t matter | - TP sold gold mine leases for $25K, payable in installment of 25% of the value of the gold removed until the full price was paid + 2½% per year. The wording of the Act changed just before the last payment to include “in the year”. Clearly reliant on use of the property.* Issue – were the amounts “received in the year”?

- Court said the payments under the old language were not “rents, royalties, annuities, or other like periodical receipts” so they were not included as royalties due to the global cap amount.- The last payment, however, under the new wording which is broader, just “amounts received”, could be counted as a royalty payment despite the global cap, as they were dependent in a way.- Under the new wording, a global cap payment is not a bar to **12(1)(g)**. |
| Porta-Test Systems v Canada 1980 FCTDTop-ups aren’t royalties | - TP sold exclusive rights to manufacture, use and cell certain inventions w/in a specific area in exchange for a 15% royalty, w a min payment of $150K over the first 3 years.* Where the royalty is equal to or less than the min payment, the aggregate amount doesn’t depend on the use or production from property. So any “top-ups” required to reach the minimum won’t be dependent on use and so not a royalty (just a capital receipt), the rest will.

- When the royalty payments exceed the minimum, both the total amount of all payments and the timing of each specific payment depend on the use/production of the property, so royalty. |
| CRA Bulletin (s.5(d))Minimum amount | - If an agreement for sale includes royalties as well as a minimum sale price (lump or annual), the payments based on production are royalties, regardless of whether they are less than, or in excess of, the minimum. But any other payments which must be made to meet the min requirements are treated as proceeds of disposition (capital). |
| Pacific Pine v MNR 1961 TABReasonable price w downward adjustment doesn’t count as royalty | - Property can be sold for a fixed price (lump or installment), w a proviso that the price will be adjusted down if certain expectations wrt revenue or profitability aren’t met.- TP bought timber license and sold it to a logging contractor for a fixed amount, payable in installments, subject to an agreement that the price would be reduced if the quantity of timber was less than the TP had represented.* Issue – does such an adjustment make the price dependent, as a royalty?

- Court said no, based on the CRA Bulletin above (s.9). Says that if there is a reasonable expectation that the condition will be met (i.e. no downward adjustment), and the original price was FMV, proceeds will be capital. Original max amount is considered to be the sale price.* Essentially just ignoring the adjustment.
 |

**DEDUCTIONS**

- **9(1)** Is a net concept of profit, revenue minus expenses.

* Deductions are permitted if they are consistent w “ordinary principles of commercial trading or well-accepted principles of business practice” – Business Practice Test.
* This section is the source of authority for deductions.

- **18(1)** No deduction shall be made unless authorized.

- **18(1)(a)** Can’t deduct an outlay or expense unless it was incurred by TP for the purpose of gaining or producing income from the biz or property.

* Income-Producing Purpose Test.
* 2 pieces – objective business practice test + subjective income-producing purpose test.

- **18(1)(h)** No deduction for personal and living expenses, other than travel expenses incurred by the TP while away from home in the course or carrying on the TP’s biz.

* **248(1)** “Personal or living expenses” includes:
	+ **(a)** The expenses of properties maintained by any person for the use or benefit of the TP or any person connected w TP by blood relationship (251(6)), marriage or CL partnership or adoption, and not maintained in connection w a biz carried on for profit or w a REOP.
		- REOP test for properties maintained for use of TP or related individuals.
	+ **(b)** The expenses, premiums or other costs of a policy of insurance, annuity K or other like K if the proceeds of the policy or K are payable to or for the benefit of the TP or a person connected…
	+ **(c)** Expenses of properties maintained by an estate or trust for the benefit of the TP as one of the beneficiaries.

- **67** In computing income, no deduction shall except to the extent that it was reasonable in the circumstances.

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| Symes v Canada 1993 SCCTest for deductible expensesRelationship of statutory sections | - TP working mom, employed a nanny. Sought to deduct nanny costs from computer her professional income. MNR prohibited it saying they were personal or living expenses.* 5 men said not deductible. **63** on CC expenses is the more specific provision so has to be used over the more general **9** provision. Doesn’t fit CC, so not deductible.
* 2 women said deductible. Have to make yourself available for biz. Calling them personal expenses is old-fashioned.

- **9(1)** is the starting point for deductions. Then look at the income-earning purpose test under **18(1)(a)**, and then analyze if it’s a living expenses under **18(1)(h)**.- So to start, is this a “well-accepted” expense? Didn’t want to decide on this b/c times change.* Used to be that the decision to have a kid or to participate in the work force was considered a personal choice, and any costs associated were therefore living expenses.

- For **18(1)(a)** look to subjective manifestations of the objective purpose. Consider:* “But for” the biz, would the need to incur the expense have existed? Yes.
* “But for” the biz, would the expense have been incurred? No.
* Is the expense ordinarily incurred by others in the biz? Yes, lawyers.
* Is that expense ordinarily allowed? No.
* Does the expense arise from a personal consumption choice? No. Having kids doesn’t fit the concept of “personal choice” in this context.

- **63** on CC expenses is more specific anyways, so uses that.* The point in **63,** as in **18(1)(a)**, is an income-earning purpose test, directly on point. **63** addresses the exact question and is intended as a complete code for CC (limited, “carefully controlled terms”, in a different section, etc.). Can’t claim a deduction under **9** when such a deduction is already accounted for more specifically somewhere else.
 |

**RECREATION, MEAL, AND ENTERTAINMENT EXPENSES**

- These types of expenses are often incurred for the purpose of biz promotion, but they also confer personal benefits both on the objects of the promo and on the promoters themselves.

- Some specific limitations to deductions:

* **18(1)(l)(i)** Can’t deduct an outlay or expense made or incurred by TP for the use or maintenance of property that is a yacht, a camp, a lodge or a golf course or facility, unless the TP made or incurred the outlay or expense in the ordinary course of the TP’s biz of providing the property for hire or reward.
* **18(1)(l)(ii)** Can’t deduct an outlay or expense made or incurred by TP as membership fees or dues (whether initiation fees or otherwise) in any club the main purpose of which is to provide dining, recreational or sporting facilities for its members.

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| Royal Trust Co v MNR 1957 Ex CtGeneral | - TP was a trust co. Part of the biz strategy was to encourage sales reps to make personal contacts, so had a policy requiring employees to join various social clubs in their communities and paid the membership fees. Common, successful practice. Deductible?* Court again emphasized that **9(1)** is the starting point for authorizing deductions, and pretty much everything else is a limitation.

- Income earning purpose test: This was a well-accepted business practice and regularly deducted by others in the biz.* Evidence clearly showed this was for the purpose of earning income. Don’t need evidence you actually made income, it’s the purpose that matters, not the result.
* Limitation used to be stricter, had to be “wholly and solely” for the purpose of earning income. That wording is no longer included, so this was ok.

- NOTE: After this case, **18(1)(l)(ii)** was enacted. |
| Sie-Mac Pipeline Contractors v MNR 1992 SCC**18(1)(l)(i)** Lodge | - TP sent customers and employees on a trip to a fishing lodge to show appreciation and inform them of new equipment and techniques.* Court disallowed the deductions b/c this was a “lodge” under **18(1)(l)(i)**. There is no need for the property to be “owned” or “rented” or “exclusively controlled” in order for it to be “used” under this section. Can be for just a period of time.
* And, the cost included food, canning fish, etc. Any direct, indirect, or incidental effect is swept up in the “lodge”, no deductions.

- DUFF: If they had gone to a fancy hotel or gone out for dinner though it would have been ok. |

**PARTIES AND FOOD**

- The cost to entertain biz guests at persona parties is non-deductible unless specifically identified as biz guests.

- **67.1** An amount paid or payable in respect of the human consumption of food or beverages or the enjoyment of entertainment is deemed to be 50% of the lesser of:

* **(a)** The amount actually paid or payable in respect thereof, and
* **(b)** An amount in respect thereof that would be reasonable in the circumstances.
* **Exceptions:**
	+ **62** and **63** are not subject to this 50% deduction limitation (moving expenses and CC expenses).
	+ It is part of your business (ex. you run a restaurant and are paying for food).
	+ Fund-raising events.
	+ Expenses for which TP is specifically compensated (ex. take a client for lunch and bill for it).
	+ Expenses for food & beverages that would be exempt under **6(6)(a)** (special work site).
	+ <6 special events in a calendar year open to all employees at a particular place of biz
* Still have to satisfy **9(1), 18, 67**…whatever is paid after that = 50% deductible.
* Note that food can be deductible as fuel (*Scott*).

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| Roebuck v MNR 1961 TABWell-accepted | - TP and his bro had a law firm, had a party for their clients to TP’s daughter’s bat mitzvah.* Court said this wasn’t in accordance w the principles of commercial trading or accepted biz practice, nor incurred for the purpose of gaining or producing income. Purely social.
 |
| Fingold v MNR 1992 TCCBiz guests | - TP was primary SH, co paid part of receptions for son’s bar mitzvah and daughter’s wedding. Co only paid a proportionate share of the expenses based on the % of biz guests invited.* Court disallowed the deductions b/c there was no indication the biz guests knew they were there as biz guests, so TP wasn’t actually promoting his biz.
 |
| Grunbaum v Canada 1994 TCCBiz guests | - TP prez and primary SH of co. Co paid part of his daughter’s wedding reception in proportion to the number of biz guests. The invitations were sent through the co and identified the co on the invitations, and all correspondence through the co.* Court allowed the deductions b/c the biz guests knew they were biz guests.
 |
| Stapley v Canada 2006 FCAConsumption/ enjoyment by other person | - TP real estate agent. Bought gift certificates for food & beverages and tickets to concerts etc. for clients. Wanted to deduct this as a marketing expense.* Court only allowed 50% deduction under **67.1** despite the fact that the TP didn’t consume or enjoy the things he bought. Just has to be “in respect of” human consumption, doesn’t say who has to consume it.
 |
| Scott v Canada 1998 FCAFood as fuel | - TP was courier who delivered by foot/public transit. Sought to deduct extra food consumed as part of his daily routine.* Court allowed deductions as analogous to fuel. But only allowed for extra food, not the stuff he would have had anyways.
 |

**CLOTHING EXPENSES**

- Like recreation, meals and entertainment, clothing that is acquired for business purposes may also provide a personal benefit.

* If they are clothes you also wear in everyday life, not deductible.
* If they are costumes or something though that you can’t wear outside of work, deductible.

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| No.360 v MNR 1956 TABOtherwise wearable | - TP actress. Deducted expenses for wardrobe and accessories.* Court disallowed deductions as personal and living expenses b/c she could wear the clothes every day, even though they may have cost more, and she had to buy more, than she otherwise would have bought.
 |

**HOME OFFICE EXPENSES**

- In addition to other general principles:

- **18(12)(a)** prohibits otherwise deductible expenses for any part of a self-contained domestic establishment (248(1)) unless the work space is either:

* **(i)** The TP’s principal place of biz OR
* **(ii)** Used exclusively to earn income from a biz and used on regular and continuous basis to meet clients, customers, or patients (includes phone contact – *Vanka*).
* **18(12)(b)** if you meet either of the requirements in (a), can’t deduct more than the income amount.
* **18(12)(c)** a loss disallowed in the previous year b/c of (b) can be deducted in the current year, again subject to (b), in respect of the same biz (unlimited carry-forward).

- If the base of operations is the TP’s home, travel involved in leaving home is deductible.

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| Locke v MNR 1965 TABGeneral | - TP lawyer, office at his house where he did work in the evenings (had other office). He met clients at home about twice a week, kept some files there, took some phone calls, etc. No sign on the door. Sought to deduct 1/6th of expenses of running the house (utilities, etc.).- Under **18(12)(a)**:* Is this his principal place of biz? No.
* Is it used exclusively for the purpose of earning income from a biz? Maybe.
* Is it used on a regular and continuous basis to meet clients? No.

- Deductions not allowed. |
| Vanka v Canada 2001 TCCPhone calls | - TP was doc. Had office downtown where he saw patients regularly, but also worked from home where he saw ~1 patient per week, but received ~7 phone calls per evening. Said he used that room in his house exclusively for his biz.* Phone calls is sufficient to satisfy “meeting patients”.
 |
| Ellis v Canada 1994 TCCHome office | - TP had pottery biz. Had a studio/store connected to the rest of her house. Sought to deduct.* The work space was clearly part of the house, met all requirements for **18(12)** to apply. For it to be a home office don’t need “the smell of home-baked break wafting into the work space”.
 |
| Dufour v Canada 1998 TCCHome office | - TP had notary biz in office in TP’s garage.* This workspace fits “self-contained domestic establishment” b/c it was attached to the house, shared utility connections, and was accessible through the interior of the house.
 |
| Maitland v Canada 2000 TCC | - TP had bed and breakfast, lived on top floor and part of the 2nd floor. * Court found the residence was their home, not a separate office. **18(12)** applies.
 |
| Sudbrack v Canada 2000 TCC | - TP operated country inn. He and his family resided in the same building* Court found the separate living quarters were a self-contained establishment separate from the biz, **18(12)** doesn’t apply.
 |
| Brockerick v Canada 2001 TCC | - TP lived in basement apartment, operated B&B in the rest of the house.* Court found it was self-contained, distinguished *Sudbrack* on the basis that the biz was largely seasonal, making the residence fully available to TP and family most of the year. Not separated enough, **18(12)** applies.
 |
| Lott v Canada 1997 TCC | - TP had day-care they operated out of their home.* Court said **18(12)** applies even though the biz is carried on *throughout* the house. Wording “any part” includes the whole.
 |

**TRAVEL EXPENSES**

- Certain travel expenses are specifically excluded from the category of non-deductible personal and living expenses in **18(1)(h)** if they were incurred by TP while away from home in the course of carrying on the TP’s biz.

* In the employment context, travel expenses are very limited.
* In the biz context, no specific statutory rule, just based on the above.

- As a general rule:

* Deductible where travel is in the course of the biz from the TP’s “base of operations” (*Cumming, Hnery, Cork*), even if choosing that base of operations involved an element of choice (*Forestell*).
* Deductible when in the course of a single biz but not when from one biz to another (*Randall, Wasserman*).
* A portion may be deductible and a portion non-deductible if travel involves both biz and pleasure (*A-1 Steel*).

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| Cumming v MNR 1967 Ex CtBase at home | - TP was doc at hospital ½ mile from his house. Didn’t have an office space at the hospital so did all his admin work from home. Had to go in on call sometimes. Sought to deduct car expenses for driving back and forth from home to the hospital.* Court found his base of operations is at home, not the hospital. Any cost of going between is therefore a cost incurred in the course of biz.
* Found it relevant that he lived close to the hospital – makes it less of a personal choice, keeps it very reasonable.
 |
| Henry v MNR 1971 SCCBase elsewhere | - TP doc at hospital, sought to deduct travel costs from home and back, same as in *Cumming*.* Court disallowed, based on the fact that he had an office elsewhere nearby where he could do all his admin work etc. So a personal expense, not incurred for biz purpose.
 |
| Canada v Cork 1990 FCABase at home | - TP mechanical-design guy who had an office in one room of his house. Sought to deduct expenses incurred in travelling to construction sites where he performed services on drafting tables supplied by the clients.* Court allowed the deduction b/c his home was his base of operations.
 |
| Forestell v MNR 1991 TCCChoice to have base at home ok | - TP was independent contractor working for museum in Toronto. Commuted in from a different town every week, rented a small apartment in Toronto he claimed was his office.* Court accepted that the rented apartment was the base of operations, and that his use of his home office in the different town was not significant to his operations and was, to a large degree, his own choice. But it met the requirements, so deductions allowed.
 |
| Randall v MNR 1967 SCCSingle biz | - TP lived in Vancouver, managed horse races at a number of tracks. Had an agreement w a co in Portland to manage their track as well.* Court said these were deductible travel expenses b/c they were incurred in carrying on a single biz located in different geographical places. Activities were similar enough to be considered one business.
 |
| Wasserman v MNR 1969 TABSingle biz | - TP had furrier shop in Pembroke, lived in Ottawa. Sought deductions.* Court said it was all part of the same biz, had offices in both places, ads, bank accounts, storage services, etc. in both locations.
 |
| A-1 Steel and Iron Foundry v MNR 1963 TAB | - TP sought to deduct expenses of a trip to Europe taken by the prez, controlling SH and wife.* Court found that only a small portion of the trip was biz related, and allocated the amounts. Allowed deductions for biz portions but not for pleasure portions.
 |

**INTEREST EXPENSES**

- Interest expenses are explicitly allowed to be deducted.

- **20(1)(c)(i)** An amount paid in the year or payable in the year, pursuant to a legal obligation to pay interest on borrowed money used for the purpose of earning income from a biz or property.

* The wording here implies that the income earned must be taxable income.
* There is also an implied reasonableness limitation in **20(1)** which only allows deductions for amounts that may reasonably regarded as…This is arguably different from **67**.
	+ So if **20(1)(c)(i)** applies, no **67** reasonableness limit!
* The concept of income implicitly contemplated here is profit.
* Direct use/economic substance test (*Bronfman Trust, Tennant*), w possibility of indirect use (*Trans-Prairie, Grenier* – not popular).

- **20(3)** If TP borrows money to repay money previously borrowed for the purposes of **20(1)(c)(i)**, the money is deemed to be used for the same purpose as the original amount was borrowed for.

* Emphasis on economic substance to determine the purpose for which borrowed funds are used (*Bronfman Trust, Mark Resources, Robitaille*). This approach has now been rejected (*Shell Canada, Singleton, Ludco*).
	+ Under *Ludco*, “income” is “gross revenue”, so even some income is ok. Don’t need a *bona fide* income-earning purpose – an ancillary income-earning purpose is enough to satisfy the statutory test now!
		- NOTE possible application of the GAAR now to transactions entered into after Sept.13, 1988.
	+ **The Direct use test from *Bronfman* is still the main test. Disregard economic realities.**

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| Bronfman Trust v Canada 1987 SCCDirect useEconomic substancePossible indirect use for *bona fide* income-earning purpose | - Trust set up by TP for his daughter as B She was to get 50% of income, and capital at discretion of trustee. Assets had grown significantly in capital value, but there was only tiny income. Trustees wanted to give her some capital but bad time to sell. Instead, borrowed from the bank, put into trust, then out to B. But there was a very high interest rate on the loan.* Issue – can they deduct the interest expense, as being on borrowed funds for the purpose of earning income from a biz or property?

- TP argued they preserved the assets, the income-earning potential, so it was income purpose.* Court said this analysis would allow almost any transaction. Can’t do it.
* Court read into the provision a purpose to encourage investment and the accumulation of income-earning capital. But even on this, the interest payments were far higher than the income, so it doesn’t work.

- Emphasis is on the direct use of the borrowed funds. Distinguished *Trans-Prairie* by saying in that case, it was all done for clearly biz reasons, dominated by a biz purpose. * There may be an indirect biz use, but only if there was a *bona fide* income earning purpose in the bigger picture.
* Preserving capital assets to earn income off of is not the same as an income-earning purpose, so it’s only an indirect use. Need *bona fide* purpose to do this.
* Here, the income generated compared to the interest payments was super low, paid more than they saved, so not a *bona fide* income earning purpose.
* The economic substance of the transaction was not to earn income but to pay B.

- Doesn’t matter what they could have done and got away w, it matters what they actually did. |
| Trans-Prairie Pipelines | - Co replaced equity w debt. Court found the borrowed funds were used to pay off the SH, filling a hole in the co. Deductible as interest based on the indirect purpose |
| Grenier v MNR 1992 TCCIndirect use | - TP borrowed $66K against his house (mortgage) to invest in a mechanic shop. Moved – used proceeds from the sale of his house to repay the original loan. Borrowed $151K to purchase new house, and sought to deduct the interest on the full amount of his new loan on the basis that is had replaced the original $66K loan that was taken out for an income-earning purpose.* Court allowed deductions on $66K of the loan b/c that was the part replaced.
* If you trace the funds, the direct purpose was to buy the house.
* But if you take a step back, it looks more like earning income – just swapping out security. The indirect use here won out.

- NOTE: Indirect use test not very popular. Stick w direct use. |
| Tennant v MNR 1996 SCCTracing | - TP borrowed $1mil and bought 1mil shares of an arm’s length corp. Sold to another at a declared FMV of $1,000, in exchange for 1,000 shares of another co. TP then continued to deduct interest on the full $1mil. All eligible uses.* Court traced the full amount of the borrowed funds to TP’s interest in his new shares. Found interest was deductible b/c he could “establish a link between the current eligible use property, the proceeds of disposition of the original eligible use property, and the money that was borrowed to acquire the original eligible use property.”
 |
| Mark Resources v Canada 1993 TCCEconomic substance | - TP was Canadian co w US subsidiary that incurred a lot of losses. In the US, carry-forward is limited, was about to expire – TP wanted to take advantage of the losses. Took out US $, transferred it to the sub. Sub then invested in secured investment, paid dividends to Canadian co, who can then deduct the losses of its’ sub.* Issue – can Canadian co deduct interest on the borrowed funds?

- Court said no. Real purpose was to sop up the US losses, import them to Canada. No *bona fide* income earning purpose, so not deductible.* Court looked at the economic substance for which the borrowed funds were used
 |
| Robitaille v Canada 1997 TCCEconomic substance | - TP partner in law firm. Withdrew $100K from his partnership account in order to buy a home. Then borrowed $100K against the house to put back into the partnership account.* Court looked at the economic substance of the transactions, the ultimate economic objectives sought. Here it was to buy the house, not to earn income. No deduction.
 |
| Shell Canada v Canada 1999 SCCForeign currency | - TP needed $ for general corp purposes. Elaborate series of transactions – borrowed NZ$ expecting it would depreciate against the US$. Then entered into an exchange agreement to buy NZ$ as needed to make interest payments on the loan. So incurred much higher interest expenses than they would have if they did it w US$. Interest payments deductible?* Court found the borrowed funds were used for the purpose of earning non-exempt income from its’ biz, notwithstanding the purpose for which the NZ$ was borrowed (tax avoidance), and the negotiated interest rate was reasonable.
* The fancy exchanges didn’t alter the basic character of the borrowed funds. Changed only value, not substance. The link between the borrowed money and the income-producing purpose remains. Deductible.
 |
| Singleton v Canada 2001 SCCDirect use | - TP partner in law firm. Borrowed $300K from the capital account to buy a house, bought it, borrowed from the bank, put $300K back in the capital account.* Court allowed deductions b/c TP had used the borrowed funds to refinance his capital account. Used the direct use test from *Bronfman* to get here, ignoring the broader economic substance – said there is nothing in the Act about a series of transactions.
 |
| Ludco Enterprises v Canada 2001 SCCAncillary direct purpose enough | - TP incurred interest expenses on $6mil borrowed funds. Funds were used to acquire shares in cos in tax havens (Panama). Only paid out $600K in dividends, making a $5.4mil loss to TP over life of the investment. But then sold for $9.24mil (capital gain, only half taxable). Overall, TP had a next loss on the investment but in reality made $3.8mil.* Court allowed the deduction based on an interpretation of “income” as “gross revenue”, rather than “profit”. B/c they earned some income, so deductible

- Under this interpretation, just have to prove you’re getting some revenue from the use to which you put the borrowed funds. Just need some income, along w anything else.* The “purpose” requirement therefore doesn’t need to be *bona fide*, can just be ancillary. So an ancillary, direct purpose to earn income is sufficient, even if the primary purpose is to obtain a capital gain or avoid tax.

- NOTE: Possible application of the GAAR now. |
| Lipson v Canada 2009 SCC | - TP had family corp. W borrowed $ from the bank 🡪 uses it to buy shares from H, paid FMV 🡪 H uses the $ to buy the house 🡪 H&W mortgage the house. 🡪H uses mortgage proceeds to repay the loan. W wants to deduct interest on the loan.* The dividends were less than the interest payments, so there was a loss generated.

- TP said the original loan was used to buy shares, which is an eligible income-producing use. Then borrowed some more against the house to repay the loan. **20(3)** deems those funds to be for the same use as the originally borrowed funds (to buy the shares). So deduction? |

**TIMING ISSUES**

- In the E/O context, amounts are generally received when you receive them, and deductible when you pay.

* This is known as the cash basis accounting method – indicated by “received/enjoyed” and “paid”.

- In the biz/property context, amounts are generally included and deducted on an accrual basis:

* This means that an amount is not included when it is received, but when it is “receivable” – when someone has a legal obligation to pay you. This is simply a legal right to receive, not necessarily an immediate right to receive, provided the amount is sufficiently ascertainable (*West Kootenay*).
* And you deduct an amount when the expense is actually “incurred”, which is not necessarily the same as when it is paid.

- This is all done under **9(1)** “profit for the year”.

* Courts use the True Picture Principle.
* They will look at what accountants say, but it is not determinative.

- There are also more specific rules on timing:

* **12(1)(a)** Have to include amounts received by TP in the year in the course of a biz, including:
	+ **(i)** Advance payments: Amounts received on account of services not rendered or goods not delivered before the end of the year.
	+ **(ii)** Deposits: Amounts received under and agreement or understanding that it is repayable in whole or in part on the return or resale to TP.
* **12(1)(b)** Have to include any amount receivable by the TP in respect of a property sold or services rendered in the source of a biz in the year. But, if the method used for computing tax is a cash basis, and that method is accepted, then you can use the cash basis and don’t have to include amounts receivable. An amount will be deemed receivable on the earlier of:
	+ **(i)** Sending out the bill, or
	+ **(ii)** The day the bill would have been sent if you hadn’t delayed sending it out in order to delay tax.
* Note that even if you choose your own method, the court can always override it and choose the best method for you (*West Kootenay*).

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| West Kootenay Power & Light v MNR 1991 FCATrue picture principle (guideline of matching)Amounts receivable | - TP is electric power co, had 2 month billing cycle. At the end of the tax year, there was some electricity that had been provided that hadn’t been billed for yet, but it was possible to estimate the cost of the amount that had been provided. Until 1979 TP didn’t include those amounts in tax return, used the “billed method” instead. Then changed to the “accrual method” and included the unbilled amounts in tax return. Stayed on accrual for accounting purposes, switched back to billed method for tax.* Issue – can TP use two different methods for accounting and tax?

- Court said no, there is no “conformity principle” to say you have to use the method for both.* All you need is the “true picture”. This is a legal principle that takes precedence over accounting principles. Just want to "fairly and accurately portray income on the basis of sound business or commercial principles”.
* Court also called this the “matching principle”, matching expenses to revenue.

- **12(1)(b)** says TP can use a non-accrual based method if that’s their regular practice. TP tried to argue this, saying, as a regulated co, they couldn’t send their bills out earlier, so it shouldn’t have to be included yet.* BUT this is always subject to the court choosing the right method for you, not absolute.

- Court found the unbilled revenue should be included (accrual method) in order to provide a true picture. As the amount not billed was both receivable and calculable, it should be included.* “Receivable” simply means you have a legal, if not immediate, right to receive it. Must simply be sufficiently ascertainable.
 |
| Canderel Ltd v Canada 1998 SCCMatching principle just interpretive tool | - The matching principle is merely an interpretive aid, not an established rule of law. The true picture principle from *West Kootenay* does not mean it’s been elevated to a rule of law, still simply a tool to use in reaching a determination of profits.* The goal of the legal test of “profit” is to determine which accounting method best depicts the reality of the financial situation of the TP. If this is done by the matching principle, great. But don’t use it as a go-to.
 |

**DEDUCTIONS**

- **18(1)(a)** disallows any deduction in respect of an “outlay” (an actual payment) or an “expense” (the assumption of an obligation to pay an amount), except to the extent that it was “made” (paid) or “incurred” (assumed) by the TP for the purpose of gaining or earning income.

* This contemplates deductions being made on either a cash or accrual basis.
* **18(1)(e)** prohibits deductions for contingent liabilities b/c those are not amounts payable.

- Based on the “truer picture” of income, you have to try to match your revenue to your expenditures.

* So if you have a significant expense that gives rise to a benefit over several years, you should spread the expense out over the years rather than deduct it all at once.
* **18(1)(b)** Not allowed to deduct capital expenses.
* **20(1)(a)** Not allowed to deduct depreciable expenses.

**INTEREST INCOME**

**- 12(1)(c)** Have to include any amount received or receivable by TP in the year (depending on the method regularly followed by TP in computing income) as, on account of, in lieu of payment or in satisfaction of, interest.

* This contemplates both a cash and an accrual method.
* However, many interest payments are now subject to the accrual rules in **12(3) & (4)**, which set up a third kind of accounting for interest income – Pure Accrual.
	+ This method includes amount that are not received or receivable, but that accrue over time, day-by-day. It requires you to include amount accrued to the end of the year.

- **12(3)** In computing the income of a corp or partnership, there shall be included any interest on a debt obligation that accrues to it to the end of the year, or becomes receivable or is received by it before the end of the year.

* Doesn’t apply to individuals.
* Inclusion happens at the end of the fiscal year of the business entity.

**- 12(4)** If an individual TP holds an interest in an investment K, on any anniversary day of the K there shall be included in computing the TP’s income the interest that accrued to the end of that day.

* Applies to individuals.
* Date depends on when the individual acquired or disposed of the debt obligation.
* **12(11)** “Anniversary day” means one year after you loaned the $, and every year after that on that date. If you sell the debt obligation, the selling date is also a date on which you have to include accrued amounts.

**TRANSFER OF DEBT OBLIGATIONS**

- Where a TP sells a debt obligation on which interest has accrued but hasn’t been collected, the sale price is likely to include an amount equal to the value of that unpaid interest.

**- 12(3)&(4)** require that accrued interest up to the time of the sale must be included in the vendor’s income.

* **20(14)** accounts for this, permitting accrued interest to be allocated between the vendor and purchaser on the transfer of a debt obligation.
	+ **(a)** The accrued interest amount shall be included in the transferor’s income, AND
	+ **(b)** The accrued interest amount may be deducted from the transferee’s income.
* **52(1)** Accrued but unpaid interest that is included under **12(3)** or **(4)** OR **20(14)(a)** may be added to the cost of the debt obligation, thereby reducing the amount of any gain on disposition.
* **53(2)(1)** Reduces the cost based of the debt obligation by any amount that is deductible under **20(14)**.
	+ The amount deductible from the transferee’s income under **20(14)(b)** is subtracted in computing the taxable cost base, essentially eliminating any capital loss on the part of the transferee.
* Changes the hypothetical cost of the debt obligation, adjusts it to match so you don’t get a capital gain or loss.

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| Canada v Antosko 1994 SCC**20(14)(a)&(b)** not dependent on each other | - 2 TPs entered into an agreement w finance to take over a failing co, Atlantic. Board owned most of the shares of Atlantic and Atlantic owed the board $5mil, w interest accruing. TPs agreed to buy the shares for $1, on the promise they would operate Atlantic in a good and biz-like manner for 2 years. At the end of the 2 years, they could then by the debt plus interest for just $10. They do this – debt + interest now owing to TPs.* TPs get paid a lot in each year, looks like taxable income. TPs rely on **20(14)(b)** to say it’s not. They say it was interest that accrued before they bought the debt obligation, so it can be deducted from their income.

- Court said that in order to get the deduction under **(b)**, you don’t need someone to have done the inclusion under **(a)**. Not dependent on each other.* Also said that, b/c this kind of fell outside of what the provision was meant to deal w (seems like big windfall), the court should look at whether the transaction was legit or not. Here, it was all done honestly and *bona fide*, so deductions allowed.

- NOTE: The GAAR may prevent this now. |

**INVENTORY**

- **248(1)** “Inventory” Means a description of property the cost or value of which is relevant in computing a TP’s income from a biz, or would have been so relevant if the income from the biz had not been computed in accordance w the cash method.

* Basically anything that, when you sell it, gives rise to biz income.
* Gross profits from sale of inventory = proceeds – cost.

- The costs of inventory are not deductible until the inventory is sold (*Neonex*).

* This can be somewhat problematic for homogenous inventory – how do you know what exact piece of inventory has been sold?
	+ Instead, deduct the cost of inventory acquired/produced during the year, and then add back the cost of unsold inventory in the year.
* 3 methods:
	+ FIFO (first in first out): First inventory you buy is the first to be sold (oldest sold first).
	+ LIFO (last in first out): Last inventory you buy is the first to be sold (newest sold first).
	+ Average cost.
		- You can choose any one of these methods, but it has to actually track on to the flow of your commodities (*American Brass*).

- There may also be situations where what is left in the warehouse has gone down in value (ex. iPhones, new version has come out). This loss of value is reflected in **10(1).**

* **10(1)** When you add back the value of what’s left in your inventory, add the lower of cost of FMV.
	+ This allows a TP to trigger a loss w/out having actually sold the product.
	+ Deduct the loss of value against your overall income in the year in which the loss occurs.
* **10.01** Lower of cost or FMV does not apply to inventory held in a biz that is ACNT. If it’s ACNT, the inventory will be added back simply at cost.
	+ This reverses *Friesen v Canada* 1995 SCC where TP bought a single piece of land w the intent to develop it for biz income. This was a ACNT. Value of the property went down, and he was able to rely on **10(1)** to deduct his loss, as FMV was lower than his cost.

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| Neonex International v Canada 1978 FCAMatching principleInventory expenses not deductible until sold | - TP made electric signs, custom built. No inventory of completed signs, but at the end of the year there are some works-in-progress. This meant there were some amounts payable (employees making the signs etc.) but not all paid. For several years TP didn’t deduct the expenses, carried the costs over to the next year. Then changed, keeping that approach for accounting purposes but, for tax purposes, began deducting all expenses in the year, even on signs he hadn’t sold yet.* Court said the purpose of the expenses incurred was to earn income in the next year. The expenses could effectively be matched to the revenue. So a truer picture could be had by deferring the expenses until the revenues were earned – matching principles applies.

- Don’t have to have the same accounting and tax approach, but it’s harder to accept a TP’s argument that their tax method is a true picture when they do something else for accounting. |
| MNR v Anaconda American Brass 1955 PCMethod of valuing has to track onto commodity flow | - TP buys copper in order to make brass. Copper prices rising, so TP switches from FIFO to LIFO. This means that they could deduct the cost of copper, and then add back the cost of the older, cheaper copper, giving them a lower income return.* Court said no go. You can use any accounting practice you want, but you have to be able to demonstrate that it actually tracks onto the flow of your commodities.

- Here, the court didn’t believe the copper in the warehouse was from 20 years ago, and the TP couldn’t demonstrate the flow in the warehouse. |

**RUNNING EXPENSES**

- These are currently deductible where the expense cannot be easily matched w subsequent revenues (ex. *Oxford Shopping Centres*) or the expense produces benefits in the current period as well as future periods (ex. *Canderel*).

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| Oxford Shopping Centres v Canada 1980 TCACan’t match expense to revenue, uncertain return | - TP owned a shopping center, worried about traffic congestion and competition from a new mall down the road. Paid the city $500K as an inducement to build a road to his mall, which was described as being a payment “in lieu of local improvement rates and taxes that might be payable” by reason of the works. On financial statements, amortized the expense over 15 years so as not to show a huge loss in one year. But for tax purposes, deducted all at once.* Court allowed the full deduction in one year, again rejecting the idea that your accounting and tax methods have to be the same.

- It was allowed b/c the deduction isn’t really related to anything, can’t map it onto something specific. It has an uncertain outcome, like an advertising campaign – it’s an expense in this year w/out a certain connection to a revenue stream.* This is therefore a “running expense”, an expense of doing biz.
 |
| Canderel v Canada 1998 SCCCurrent period benefits | - TP in biz of building shopping centers, needed tenants. To get a good lead tenant, paid an inducement payment for the tenant to sign the lease agreement, and deducted it all in one year.* Court allowed the deduction b/c it would simply be arbitrary to spread it out over many years, as this expense gave rise to various current period benefits (easier to get other tenants, better loan rates, etc.).

- DUFF: Court probably could have allocated some now and some later. Also, if it wasn’t a lead tenant, probably easier to match to revenue b/c not the same big, ambiguous benefits. |

**PREPAID EXPENSES**

- After *Oxford* above, the Act was amended to include a provision for prepaid expenses, that says you have to spread certain kinds of expenses out over time.

* **18(9)(a)** No deduction for:
	+ **(i)** Prepaid services in respect of a period after the end of the year.
	+ **(ii)** Prepaid interest, taxes, rent or royalties in respect of a period after the end of the year.
	+ **(iii)** Prepaid insurance in respect of a period after the end of the year.
* **18(9)(b)** Instead, deduct in the year in which the prepaid expense reasonably relates.

- Note: This arguably reverses *Oxford* but not *Canderel*, as there is nothing in this section about inducement payments, only rent etc. Nothing about paying inducements to get rent.

**CAPITAL EXPENSES**

- **18(1)(b)** No deduction for a capital outlay, loss or replacement of capital, a payment on account of capital or an allowance in respect of depreciation, obsolescence or depletion except as expressly permitted by the Act.

* So can’t deduct capital expenses that give rise to depreciable property.

- But if capital property is depreciable, you can deduct a percentage of it over time, as a Capital Cost Allowance (CCA) under **20(1)(a).** See below.

* If the property is non-depreciable, no deduction – just offset against the proceeds (if sold) to determine whether you have gain or a loss.

- Characterization of capital property by the courts has generally relied on 2 tests:

* 1) *British Insulated and Helsby Cables v Atherton* 1926 England: If the expenditure is “once and for all”, w a view to bringing into existence an asset or an advantage for the enduring benefit of the trade, it is a capital expense.
* 2) *BP Australia v Commissioner of Taxation* 1966 Australia AND *Sun Newspapers Limited v Federal Commissioner of Taxation* 1938 Australia: Sums expended on the structure w/in which the profits were to be earned vs. expended as part of the money-earning process. Distinction between the acquisition of the means of production and the use of them.

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| Canada v Johns-Manville Corp 1985 SCCApplication of tests | - TP had open-pit asbestos mine, had to keep buying up land to expand the mine, not to get more asbestos, but to prevent cave-ins. Did this regularly for 40 years, cost of the land was ~3% of the annual revenue of the mine. TP deducted the cost of acquiring the land as an ordinary biz expenses. MNR said it was capital, not a deductible current expense.- Court set out the test to see if you have a capital expense:* Objective: *British Insulated -* Recurring/annual payment? Or is it “once and for all”?
* Subjective: *BP Australia & Sun Newspapers -* Is the purpose simply to keep operating the biz, or is it to acquire a capital asset/set up the structure of the biz?

- Here, annual expense to allow the mine to continue operating, not buying the land for the ore or anything. Recurring, relatively small amount.- NOTE: If they had bought all of the land at the start, it would have been a capital expense, and only deductible as an offset when sold. They turned a non-deductible capital expense into a deductible biz expense by doing it this way. |
| Canada Steamship Lines v MNR 1966 Ex CtRepairs vs. upgrades vs. acquisitions | - TP owned steamships, spent a lot on repairs – replaced the floors and walls of cargo holds and the boilers that powered the ships.* Court said that even if it’s not regular, the repairs to the cargo holds were just that, repairs, not a capital expense. Currently deductible.
* However the boilers are a separate capital asset, not built-into the ship in an integral way as the cargo holds are. They have their own stand-alone value. Capital expense.

- NOTE: If what you do is more of an upgrade/renovation than a repair, might be capital. |
| Canaport v Canada 1993 TCCAs above | - TP put new fiberglass liner on an oil pipeline to prevent leakage and extend the life expectancy of the pipeline.* Court said this was a capital expense, based on *Canada Steamship* reasoning.
* NOTE: This could easily have gone either way.
 |
| Canadian Reynolds Metals v Canada 1996 FCAAs above | - TP replaced carbon cathode lining in steel pots used to produce aluminum.* Court said this upgrade increase the life of the linings from 20 months to several years. Characterized it as capital expenditure to acquire “capital assets of an enduring nature”.

- Upgrade vs. ordinary repair. But NOTE: Use can use new technology for a repair – blurs the line between an upgrade and a repair. |
| Shabro Investments v MNR 1979 FCAAs above | - TP had building that was built on a landfill. Basement shifted so TP replaced it. Installed steel pipes, made a new floor, and repaired/replaced water lines, etc.* Court said the steel pipes etc. are upgrades (new addition to the building), but the rest (water mains, new floor) were just ordinary repairs.
* Ordinary repairs don’t have to be gradual wear and tear, can be the result of something sudden and destructive.
 |
| Gold Bar Developments v MNR 1987 FCTDAs above | - TP had apartment building, wall falling off. Replaced it w metal cladding (better technology).* Court said this was just a repair. The issue was about the purpose for which the repair was done – here it wasn’t to upgrade and have a nicer building, it was to deal w the fact that it was falling apart. Can use new technology for this. Repair crisis, not optional.

- NOTE: This is inconsistent w the idea that if your building burns down and you rebuild it, that’s a capital expense. |

**CAPITAL COST ALOWANCES**

- If capital property is depreciable, notwithstanding that it is a capital expense under **18(1)(b)**, you can deduct a percentage of it over time, as a Capital Cost Allowance (CCA) under **20(1)(a)**.

* If the property is non-depreciable, no deduction – just offset against the proceeds (if sold) to determine whether you have gain or a loss.

- Straight-line method of depreciation:

* If you have something worth $1,000 that will last for 10 years, you deduct $100 every year for 10 years.
* The amount you record after deducting the $100 is the undepreciated capital cost (UCC). In this example, after 5 years, the UCC would be $500. Eventually will get to a UCC of $0.

- Declining balance method of depreciation:

* This takes a percentage off of the UCC every year rather than a hard amount. In the above example, rather than deducting $100 every year, would take off (for ex.) 40% per year.
* This leads to more deductions up front, not spread out evenly over time. Never get to UCC of $0.

- **The Act** generally uses the declining balance method of CCA.

* Applies to groups of assets (class method), rather than individual assets.
* CCA under the Act is optional. You don’t have to claim it in a year, leaving a higher UCC for the next year, which can then be deducted in a later year.

**DEPRECIABLE PROPERTY**

**- 39(1)(b)** The disposition of depreciable property cannot trigger a capital loss.

**- 13(21)** “Depreciable property” Means property acquired by the TP in respect of which the TP has been allowed a deduction under paragraph 20(1)(a).

**- 20(1)(a)**: Can deduct from biz/property income such part of the property, or such amount in respect of the capital cost to the TP of the property, if any, as is allowed by the regulation.

* **Reg 1100(1)** Fort the purposes of **20(1)(a)**, can deduct, subject to (2), the listed classes of property at the listed rates. With respect to each class, can claim a percentage of the UCC at the end of the year.
* **Schedule II** lists different kinds of properties and puts them into classes:
	+ Class 6: Buildings of frame, log, etc.
	+ Class 20: General manufacturing or processing equipment and other kinds of tangible property.
	+ Class 10: Automobiles.
	+ Etc.
* **Reg 1102** Has important limitations. Things not deductible:
	+ **1102(1)(a)** If it’s already been deducted.
	+ **1102(1)(b)** Inventory.
	+ **1102(1)(c)** Property not acquired for the purpose of gaining or producing income.
		- So the things listed in **Schedule II** do not becomes depreciable property unless they are being used for the purpose of gaining or producing income.
	+ **1102(1)(f)** Property under **18(1)(l)** (yachts, lodges, etc.).
	+ **1102(2)** Land.

**RENTAL PROPERTIES**

- Certain property is designated in it’s own class, and there will never be more than one asset in the class.

* **Reg 1101(ac)** Rental properties w a capital cost of at least $50K are designated to be each in their own class.

- The Act prohibits you from using CCAs to produce net losses for rental properties:

* **Reg 1100(11)** In no case shall the aggregate of deductions for rental properties generate a CCA loss (pool all rental properties together, even if they are in different classes).
	+ CCA can’t exceed **(a)(i) – (b)(i)** (income minus losses).
		- Compute income from rental properties w/out CCA and subtract the losses w/out CCA. You can then claim CCA up to that amount.
		- This prevents people from using CCA on rental properties to shelter income.
* **Reg1100(14)** “Rental properties” Means a property owned by the TP if it was used principally for the purpose of gaining or producing gross revenue that is rent.

**UNDEPRECIATED CAPITAL COST**

- **13(21)** “Undepreciated capital cost” is a notional balance that changes over time depending on what you do w property of the class.

* Things to add: ex. if you buy a new car, the cost gets added to class 10 and the UCC goes up.
* Things to subtract: ex. If you claimed a CCA on something, UCC goes down.
* Note the definition of “proceeds of disposition” in **13(21)** and “disposition” in **248(1)**.

- Terminal loss: If you sell your last asset in a class for less than it’s UCC (ex. UCC is $20K and you sell for $14K), you have depreciation that is unaccounted for in the Act. Only works if you have a negative UCC.

* This is simply a loss generated on the disposition of depreciated property.
* **20(16)** Gives you a deduction on your income for that amount ($6K in my example), as a terminal loss.

- Recaptured depreciation: If you sell an asset for more than it’s UCC (ex. UCC is $20K and you sell for $25K), you haven’t used all of your depreciation the Act gave you.

* If there are other assets in the class, you are unlikely to get recaptured depreciation b/c those other assets can “sop up” the extra depreciation – defers the recapture, in a sense.
* **13(1)** Adds this back in to your income.

**- UCC = cost of assets – CCA claimed**.

* **A – E – F + B**
* **A: The total capital cost of every asset in the class acquired before that time**.
	+ Capital cost includes the ordinary cost + installation costs etc. Buy a new asset in a class, add it in.
* **E**: **The total depreciation**.
	+ CCAs that have already been claimed under **20(1)(a)**.
* **F: The lesser of 1) the disposition of the property (proceeds minus transaction costs) OR 2) the capital cost of the property**.
	+ This means you can only claim proceeds up to the capital cost, never more.
	+ Deduct either the proceeds of sale or the capital cost, whichever is less.
* **B**: **The total amount of recaptured depreciation.**
	+ If there is any recaptured depreciation under **13(1)** (you sold for more than the UCC), add it in.

**CASES**

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| Ben’s Limited v MNR 1955 Ex CtIncome-earning purpose | - TP had bakery, bought 3 neighbouring properties w houses on them. The intention was to tear down the houses and expand the bakery. Had to wait for re-zoning, which it got. There was a renter in 1 building; TP got $140 in rent before rezoning. In tax return TP apportioned costs primarily on buildings, deducted CCAs (land not eligible).* Issue – how to allocate the expenditure between different kinds of property that were purchased together?

- CRA reassessed on the basis that TP really only wanted the land and didn’t meet the income-producing purpose test for the buildings as required to claim a CCA. TP argued they bought it all for the purpose of earning income, b/c bought it to expand the bakery.* Court sided w CRA. Said TP only wanted the land in order to expand, didn’t want the buildings. Getting $140 in rent is not enough to satisfy the income-earning purpose, and besides, getting rent was not part of the person.

- NOTE: This was before *Ludco*, which said income-producing now doesn’t have to be the only purpose, and that income is gross revenue. If *Ludco* was before this case, TP here could have kept renting, advertised for tenants, etc., made it part of their purpose – then the fact that the deductions would be larger than the income wouldn’t matter. |
| Hickman Motors v Canada 1997 SCCIncome-earning purpose | - TP had a car dealership, sought to deduct CCA on leasing equipment that it bought on the windup of one of it’s subsidiaries that was in the biz of leasing equipment. TP parent co essentially inherited the UCC, help onto the property for 5 days, then sold to someone else. Then claimed CCA on it, on top of the income it received from renting it for those 5 days.* Court allowed the deductions. Reg 1102 doesn’t require that you hold on to the depreciable property for any particular length of time. While the TP had the assets they produced revenue, and it doesn’t matter that it was small or short.
 |

**TAXABLE CAPITAL GAINS AND ALLOWABLE CAPITAL LOSSES**

- The main issue here is to determine whether the property is capital or inventory.

* **248(1)** “Inventory” Property the disposition of which gives rise to biz income. Can be ordinary biz or ACNT.

- **3(b)** Income includes the total of a TP’s capital gains minus their capital losses. Net amount. Allowable capital losses are generally only deductible against capital gains.

* **54 Definition of “Capital property”:**
	+ **(a)** Any depreciable property, and
	+ **(b)** Non-depreciable property, any gain or loss from which would be a capital gain or loss.
	+ This is basically property acquired for the purpose of acquiring income from it.
		- Ex. Getting rent (building is the capital property).
		- Ex. Store of value (land is the capital property).
* **38** Inclusion rate for capital gains and losses:
	+ **(a)** Capital gains are ½ taxable.
	+ **(b)** Allowable capital loss is ½ the loss.
* **39** Definitions. They are framed as residuals:
	+ **(1)(a)** “Capital gain” If you sold something and it did not give rise to biz income (aka. not inventory), the proceeds are a capital gain.
	+ **(1)(b)** “Capital loss” A loss from the disposition of property, other than depreciable property (that is a terminal loss under **20(16)**, fully deductible).
	+ These are essentially gains and losses that would not be recognized for tax purposes if the Act were read w/out paragraph **3(b)**.
	+ **39(1)(b)** The disposition of depreciable property is not included in capital losses.

- General computational rules are found in **40**:

* **40(1)(a)**: Gains.
	+ **(i)** If property was disposed of in the year, Gain = proceeds – (ACB + selling costs). If this gives you a positive number, you have a gain.
* **40(1)(b)** Losses.
	+ **(i)** If property was disposed of in the year, Loss = proceeds - (ACB + selling costs). If this gives you a negative number, you have a loss.

- These definitions turn on their being a disposition of property:

* **248(1)** “Disposition” Stuff that gives you proceeds of disposition.
* **54** “Proceeds” The sale price of property (includes more than just money).
* **54** “Adjusted cost base (ACB)”
	+ For depreciable property, the ACB is the original capital cost.
	+ For non-depreciable property, the ACB is the original capital cost adjusted in accordance w **53**.

**PERSONAL USE PROPERTY**

- This is property that is primarily used for personal used and enjoyment **(54)**.

* If this type of property goes down in value, it’s assumed that’s b/c you’ve been using it (wear and tear).

- **40(2)(g)(iii)** Deems loss from personal use property to be nil.

* Can’t claim a capital loss on personal use property.
* However, you may claim a terminal loss.

**CHARACTERIZATION AS CAPITAL VS. INVENTORY**

- Where property is not characterized as capital property, it is characterized as inventory (*Friesen*).

- Factors to consider in determining whether real property is capital or inventory include:

* Holding period.
* Circumstances responsible for disposition (ex. unsolicited offer).
* Method of financing.
* Reasonable expectation of profit.
* Other activities carried on by TP or principal SH(s).
* Secondary intention doctrine (which operates as a but-for test) (*Regal Heights, Racine*).

- Note the administrative rules for the change of use from investment purpose to inventory or vice versa.

* The CRA takes the position that, where real estate has been converted to inventory, capital gains/losses will be calculated on the basis that a notional disposition occurred on the date of the conversion. The amount so determined will be the difference between the ACV and the FMV at the date of conversion. The amount of income gain/loss on final, real disposition will be determined on the basis that it is inventory.

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| Regal Heights v MNR 1960 SCCSecondary intention | - TP bought land being used as a golf course. Wanted to build a shopping center but it never worked out. Ended up selling the land at a gain of ~$135K.* Issue – is this a gain from inventory from a ACNT biz, or is it a capital gain?

- TP said capital gain (not taxable at all at the time) b/c their intention was to build a mall and derive rental income.* Court said no. Recognized that building the mall was unquestionably the primary purpose, but also found a secondary intention to sell if it didn’t work out. The venture was speculative to being w, and land prices were rising at the time.

- So if you have a primary intention to use property for investment purposes, but it’s all preliminary and you have a secondary intention to sell for a profit, that can be a ACNT that gives rise to taxable biz income.* Courts have subsequently clarified that the secondary intention only counts if it was a motivating intention, sort of “but-for”.
 |
| Racine v MNR 1965 Ex CtSecondary intention | - TPs experienced in real estate biz, borrowed $ to buy land and machinery of a bankrupt corp. They sold it 4-6 weeks later at a big profit. Biz income in ACNT or capital?* Court said capital based on TP’s uncontradicted testimony that it had been their intention to carry on the biz indefinitely as a long-term investment.
* Secondary intention was not present here.
 |

**ALLOCATION OF PROCEEDS ON DISPOSITION**

- **68**: If an amount received or receivable from a person can reasonably be regarded as being in part the consideration for the disposition of a particular property of a TP,

* **(a)** the part of the amount that can reasonably be regarded as being the consideration for the disposition shall be deemed to be proceeds of disposition of the particular property irrespective of the form of legal effect of the K or agreement, and the person to whom the property was disposed of shall be deemed to have acquired it for an amount equal to that part.
	+ Essentially, if a part of global proceeds is reasonably for one thing, the cost of that thing is deemed to be that part. The proceeds are re-allocated wrt both the vendor and the purchaser.
	+ Ex. *Ben’s Limited* (CCA bakery case).
* Since an assessment under **68** has reciprocal effects on both parties, an allocation agreed to between arm’s length parties is entitled to considerable weight, absent sham or subterfuge (*Golden*). Nonetheless, if the agreement doesn’t meet the test of reasonableness, it may still be challenged under **68** (*Transalta Corp.*).
* Reasonable consideration must be viewed from the perspective of the vendor AND the purchaser. The test looks to reasonable consideration, not value (*Golden*).
* Reallocation is more likely where agreed amounts differ substantially from FMV and where there is no hard bargaining over the allocation (*Peterson, Leonard*).

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| Golden v Canada 1983 FCAAgreement by the parties |  - Apartments in Edmonton, owner approached by potential buyer. Global offer of $5.6mil:* $2.6mil for land // $2.4mil for buildings // $0.6mil for vehicles.

- The parties negotiated and in the end, global price of $5.85mil:$5.1mil for land // $$0.75mil for buildings & vehicles.- Court found that the allocation agreed upon by the arm’s length parties was reasonable, so **68** didn’t apply. It’s not about FMV, just reasonable disposition and proceeds. It’s open to the owner to dispose of their property as they see fit.* Have to look at the perspectives of both the vendor and the purchaser b/c the apportionment they decide on affects both of them. So what they decide is entitled to considerable weight.
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| Petersen v MNR 1988 TCCPatently unrsbl | - TP sold daycare for $157K, allocated $45K to goodwill (only partly taxable).* Court said not go. There is no goodwill here – the license had been revoked and it had been losing money for years.
* It Patently/clearly unreasonably to allocate anything at all to goodwill, so **68** applies.
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| Transalta Corp v Leonard 2012 FCARsbl agreement | - TP sold regulated electricity transmission biz for a negotiation price 1.3 times the book value of it’s tangible assets, for a total of $190mil allocated to goodwill.* Court said ok. There isn’t really goodwill in regulated industries, but here the TP’s efficient mgmt. and the potential for new biz opportunities from TP’s network constitutes goodwill. So the agreement was reasonable.
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| Leonard v Canada 1990 TCC | - TPs bought a farm after selling one elsewhere. There was no real negotiation on the price over the allocation. For tax purposes, TP used FMV for deductions, was actually arguing to have **68** apply so they could get more deductions.* Court allowed **68** to apply b/c there was no real negotiation and certain things were just thrown in last-minute w/out real consideration by the TP.
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