

PERSONAL TAX

71(1)

COSMETIC SURGERY

The Income Tax Act permits a *medical*



expense credit for an amount paid to a *medical practitioner* in respect of *medical services* - this could include items such as cosmetic surgery, botox injections, calf implants, hair transplants, rhinoplasty and breast augmentation, facelifts, liposuction and tooth bleaching.

PERSONAL CARE HOMES

In a May 5, 2005 *External Technical Interpretation*, Canada Revenue Agency (CRA) note that if an individual is *certified* as suffering from a *physical or mental handicap* and, as a result, receives care, or the care and training, at a particular place, which has the required equipment, facilities or specially trained personnel, the expenditures may qualify as a *medical expense*.

For *example*, fees paid to an institution which has staff specially trained to deal with *Alzheimer's* disease will usually qualify as a medical expense.

TUITION FEES

In a June 7, 2005 *External Technical Interpretation*, CRA notes that *tuition fees* may be eligible for a *medical expense* tax credit if the student is suffering from a *physical or mental handicap*, the severity of which is such that the student "*requires*" (not merely "benefits from") the *equipment, facilities* or *personnel* specially provided by the school and, which is not available in the public school system.

An appropriately *qualified person* must *certify* this.

PARENTS

In a May 31, 2005 *Internal Technical Interpretation*, CRA confirm that where a *parent* is *dependent* on *more than one child*, *each child* could claim their *portion* of the permissible *medical expense* such as nursing home fees.

EMPLOYMENT INCOME

71(2)

MOTOR VEHICLE LOG BOOK

In a March 14, 2005 *External Technical Interpretation*, CRA *reminds employers* that they are required to *maintain records* so that the employee's total employment income can be reported. This includes making every reasonable effort to ensure that an employee maintains a *log book* in respect of the use of an employer-provided

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motor vehicle.

OVERSEAS EMPLOYMENT TAX CREDIT

A Canadian resident employee may receive an *income tax credit* if employed throughout at least *six consecutive months* with a *specified employer* for the performance of services *outside Canada* in connection with a contract related to, among other things, *engineering* activities.

SPECIAL WORKSITE

The Income Tax Act excludes from income allowances for *board, lodging* and *transportation* paid to employees at *temporary special worksites*.

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In an *Internal Technical Interpretation*, CRA notes that even though a contract may extend *beyond two years*, the duties could still be of a “*temporary*” nature, thereby resulting in a *tax-free allowance*.

TRUCKERS

In a May 19, 2005 *Tax Court* of Canada case, the taxpayers



were married and employed to drive the employer’s trucks on *long distance trucking* in Canada and the United States.

CRA *disallowed* their deduction for *meals, showers* and *incidental expenses* on the basis that the Income Tax Act only permits a travel expense deduction if the taxpayer must make disbursements for meals *and lodging*. In this case, most of the time the taxpayers slept in the truck cab.

Some Good News!

The Court noted that CRA’s objection is incorrect.

Now Some Bad News

The taxpayers deducted \$61.50 per day for meals, *without receipts*, on the basis that these were the *rates* established by the *Treasury Board* at that time to be paid as a non-taxable travel allowances to employees of the Government of Canada.

The Court noted that this is *not relevant*. However, the *Court permitted \$40.00 per day* with a 50% addback because of Section 67.1.

Also, the cost of the *showers* was *deductible* as a component of *lodging*.

Editor’s Comment

CRA now permits, without receipts, under the *Simplified Method* \$15.00 per meal times three meals for a total of \$45.00 per day, subject to a 50% addback.

HOME OFFICES

In a May 26, 2005 *External Technical Interpretation*, CRA was asked for guid-

ance as to whether an *employer* should complete *Form T2200* where there is no contract of employment but the employee does incur *home office expenses*.

CRA notes that where it is *tacitly understood* by the employer and the employee that the *office in the home be provided* and that the required conditions are met, the employer should *issue a T2200* and the employee should be able to *deduct expenses*.

CRITICAL ILLNESS INSURANCE (CII)

A June, 2005 *Supreme Court* of Canada case in Quebec struck down a law prohibiting private health coverage in Canada. This has made *CII coverage* a more attractive option by introducing the possibility of *private health coverage in Canada*. Currently, private health coverage is mostly accessed through the United States or, more recently, Asia.

CII policies are a *hedge* against the *public medical system* deteriorating, or not being available on a timely basis.

In a December 9, 2003 *External Technical Interpretation*, CRA note that if the *CII policy* is provided by the corporation to the owner-manager in his/her capacity as a *employee*, and not a shareholder, the premiums will be *deductible* to the employer. Assuming that the premiums only provide for *group CII*, and do not contain any return of premium, there would be *no taxable benefit*.

Also, a lump-sum payment received under a CII policy may be non-taxable.

BUSINESS/PROPERTY INCOME

71(3)

OFFICE IN THE HOME

In a *Tax Court* of Canada case, the Court accepted the deductions for the *office in the home* on



the basis that it was used on a regular and continuous basis for *meeting clients*.

The fact that this *doctor* met most of his patients at the *Clinic* or at the *nursing homes*, and only had about *one or two appointments per week* at his own home *did not prohibit* the deduction.

The Court noted that *meeting with patients* may occur by *telephone*. *Patients and staff telephoned the doctor* often and *regularly* at his home office for consultation, advice and to discuss cases.

LEASES

The Income Tax Act permits a lessee and a lessor to *jointly elect* to treat a lease as a *capital lease* in computing the income *of the lessee* such that the rental payments made by the lessee will be treated as blended payments of *principal* and *interest*. The *lessee* will be able to claim *capital cost allowance* and deduct the *interest portion* of each rental payment.

This only applies for leases of *more than one year* and does *not* apply on “*prescribed property*” including property that has a value less than \$25,000, intangible property, and *exempt property* - office furniture or office equipment, electronic data processing equipment, motor vehicles, trucks or tractors and certain buildings.

INTERNET FEES

In a May 30, 2005 *Internal Technical Interpretation*, CRA notes that *internet connection fees* paid by a *self-employed person* to earn income may be allowed under the Income Tax Act. However, if the fees are related to a *home office* and contain varying degrees of *personal* and business elements, a *pro-ratio* must be made.

MANAGEMENT FEES PAID TO A SPOUSE

In a May 24, 2005 *Tax Court* of Canada case, Mrs. W deducted a *\$32,000 management fee* to her *husband* from her *self-employed* real estate business income. No

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record was kept for the services performed.

Taxpayer Loses

CRA successfully argued that for an *expense* to be *deductible* there must be a “*legal obligation to pay*”.

IMPORTANCE OF RECORDKEEPING

In a June 17, 2005 *Tax Court* of Canada case, the taxpayer carried out a discount store as a proprietorship in which many of the *expenditures* and *revenues* were on a *cash basis*.

Taxpayer Loses

The Court noted that because of the *CRA auditor’s methodical and thorough examination* of the records available, the taxpayer was *unable to rebut* the Minister’s assumptions. The taxpayer’s difficulties stemmed from *inadequate record-keeping*.

INDEPENDENT CONTRACTOR VS. EMPLOYEE STATUS

CRA is *aggressively reassessing* in this area and have *revisited* same companies over and over again - for example, in one case, the workers were found to be independent contractors in 1995 and 2000 and are again being attacked by CRA in 2005.

There are a number of *important issues* such as liability for Employment Insurance (EI), Canada Pension Plan (CPP), withholding taxes at source, preparation of T4s, and deductibility of expenses by the workers. Important *side issues* include the worker’s *entitlement* to employment-related benefits such as *vacation pay* and *wrongful dismissal* settlements.

The Courts are now looking at the *joint intention* of the worker and the payer as one of the important factors in determining the status.

In certain industries (example, entertainment), workers/performers may wish to be *classified as employees* so that they can claim *EI* benefits when they are not work-

ing. However, other workers want *independent-contractor status* to *increase deductions* against business income and to access *corporate tax advantages* such as lower tax rates, non-taxable employment benefits, and income splitting (National Post, June 28, 2005, FP12).

OWNER-MANAGER REMUNERATION

71(4)

SOURCE DEDUCTIONS

If a corporation declares a *bonus payable* to an employee, the bonus must be paid within *179 days* after the yearend. Therefore, the income tax, CPP and, if applicable, employment insurance must be paid in the *following month*, either on the 3rd, the 10th or the 15th, depending on the remittance period.

If the source deductions are *not paid on time*, the corporation may be assessed a *late filing penalty*.

SALARIES TO ADULT CHILDREN

In an April 15, 2004 *Tax Court* of Canada case, Mr. F owned all the shares of a corporation which employed as *key significant employees* his *adult children*. In *bonusing down* to the annual business limit, bonuses were declared to the children \$136,639 and \$50,000 respectively. *CRA disallowed* as a deduction most of the bonuses on the basis they were not incurred to earn income.

Taxpayer Wins!

The *Court permitted* the bonuses and noted that the *services provided* by the adult children played a *material role* in the financial success of the business.

DIRECTOR LIABILITY

In a May 19, 2005 *Tax Court* of Canada case, Mr. M bought a flower shop from Mr. C and *left Mr. C to manage the corporation*.

The corporation was “*run extremely*

poorly” and was *deficient* in *GST* remittances by \$61,216. Mr. M, the *sole director*, was assessed with *personal liability* for the \$61,216.



Taxpayer Loses

The Court noted that Mr. M was a *knowledgeable director* with a strong business background. This was not a case of a naive or unaware director. Under these circumstances, the duty to take *reasonable care* to prevent ongoing defaults requires *significant effort* on the director’s part. The efforts need not guarantee success but, must be immediate, forceful and have some reasonable likelihood of success.

MARRIAGE BREAKDOWN

71(5)

THIRD PARTY PAYMENTS

In a March 24, 2003 *Tax Court* of Canada case, the taxpayer paid \$19,828 *to third parties* in respect of the family residence including mortgage, insurance, taxes, electricity, telephone, cable service, repairs and maintenance as stipulated in the *Marriage Separation Agreement*.

The Income Tax Act *permits a deduction* for *third party payments* if the Court Order or Agreement specifically refers to these tax implications. The *purpose* is to ensure that the parties in question are *fully aware* of the fiscal consequences resulting from the payments.

Taxpayer Loses

The Court disallowed the deduction because there was no written document confirming the tax consequences.



RETROACTIVE CHILD SUPPORT AWARDS

An *Alberta Court of Appeal* case Ruled that when the *income* of a person *paying*

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child support goes up, the *obligation* to pay higher child support would generally *commence at that time*. Therefore, a child support payor could *owe substantial amounts* for *retroactive child support* if his/her income has increased since the original settlement date.

Ontario Disagrees

On May 19, 2005, the *Ontario Court of Appeal repudiated* the Alberta Ruling by directing Judges *not* to routinely order payor parents to pay *retroactive child support* to custodial parents.

The Ontario Court Ruled that Trial Judges should only "*sparingly*" order child support for the months prior to the date on which a custodial parent formally applies for support.

ARREARS

In a February 25, 2005 *Supreme Court* of Canada case, the Court found that a *lump-sum* "disability payment" for *arrears* was *taxable*.

Even though there have been a number of *alimony arrears* cases that found that an *arrears settlement* was *non-taxable/non-deductible*, this status *may* change in the future because of this finding.

CRA are in the process of *reviewing* their *policies* because of this case. This makes settlements of arrears quite risky as the *tax implications* to both the payor and the recipient are *uncertain*.

CHARITIES

71(6)

FORM T3010A

Persons filing a Charitable Organization return for a fiscal period that begins after March 22, 2004 should use new *Form T3010A(05)*.

NEW FUNDING PROGRAM

On May 17, 2005, the Minister of National Revenue launched the *Charities Partnership and Outreach Program* to support

compliance-related education and *training* projects for charities.

Up to *\$3 million* in funds will be available to the voluntary sector *annually* for *education and training* on charities regulations to a *maximum* of *\$500,000 per year* per project.

Any registered charity or non-profit organization serving the charitable sector *can apply* to CRA for *funding*.

PRIVATE GIVING FOUNDATION

For a list of *Community Foundations* that provide a structure for tax deductible charitable giving see www.community-fdn.ca.



DONATION THROUGH THE WILL

The Income Tax Act permits a *donation* made *through the Will* to be claimed on the *Terminal Return* of the deceased taxpayer. CRA usually considers that a gift by the Will of a *specific percentage* of the *residue* will be *eligible*.

However, if the *residue* of the Estate is *dependent* on decisions to be made by the *Executor* (for example, amounts to be paid to grandchildren) then the *donation* is in the *Estate*, not the Terminal Return of the deceased.

ETHNOCULTURAL COMMUNITIES

In a June 30, 2005 *Release*, CRA notes that a group that provides *assistance to an ethnocultural community*, or that *educates* the public about a particular culture, may be *eligible* for *charitable registration*. This 14-page Release discusses the options for such groups.

ESTATE PLANNING

71(7)

ROLLOVER TO FINANCIALLY DEPENDENT CHILDREN

Where a *financially dependent child or grandchild* receives, on the death of a person, a distribution from the



deceased's *RRSP or RRIF*, the *child*, not the deceased taxpayer, includes the amount in *income*. However, an *offsetting deduction* is permitted if the amount is used to acquire a specific type of *annuity*, including a *life annuity* where the child or grandchild is dependent by reason of *physical or mental infirmity* or, an annuity payable up to *the age of 18* for other dependent children or grandchildren.

In an April 6, 2005 *External Technical Interpretation*, CRA noted that a "*Henson*" style *Trust* could be used to *safeguard* a disabled beneficiary's entitlement to *social assistance*.

U.S. DIVIDENDS AND INTEREST

Where a Registered Retirement Savings Plan receives U.S. dividends or interest, there should be *no U.S. withholding tax*.

REGISTERED RETIREMENT INCOME FUND (RRIF) BENEFICIARY

An article in the *National Post* noted that because the *spouse* was *not* designated as the *direct beneficiary* of the *RRIF*, the RRIF proceeds went into the *Estate* and they were forced to *obtain probate* which cost more than \$1,000 and took about six weeks (June 11, 2005, FW6).

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FARMING

71(8)

FULL FARMING LOSS DEDUCTION

In a May 6, 2005 *Tax Court* of Canada case, the taxpayer was a *full-time employee* earning employment income of \$45,000. At the same time, he operated a *barley grain farm* on 320 acres and had *losses* in the year which he *claimed fully* against his employment income. CRA restricted the losses on the basis that farming was not his principal preoccupation.

Taxpayer Wins!

The Court *permitted* the *full deduction* for the *farm losses* and noted that the losses had to do with circumstances *beyond the taxpayer's control*.

CANADIAN AGRICULTURAL INCOME STABILIZATION (CAIS) DECISION

Farmers can now *withdraw* 2003,



2004 and 2005 *CAIS deposit funds*. These are funds either *deposited* directly by farmers into CAIS or *transferred* from their *NISA* accounts.

WEB TIPS

71(9)

TELEPHONE SERVICE

Nowadays, most computers come with energy saving modes that allow you to *keep your computer on* without a break. Why would you want to leave your computer on? One reason is to use it as a *free telephone*.



Yahoo has introduced a *free beta test* computer *phone service*. This is basically an extension of the current Yahoo Messenger service (similar to MSN Messenger). If you have clients or coworkers that are located in offices to which *long distance charges would apply* to telephone communications, consider using this *free service*.

What one needs to do:

1. *Download* the Yahoo Messenger beta 7 program from www.yahoo.ca
2. *Install* the program
3. Plug in a *Microphone*
4. Sign up for a free Yahoo email account if you don't already have one (*1 Gigabyte of space*)
5. *Add* your friends or contacts

How it works:

1. You select the contact you would like to call and then hit the "*call*" ICON.
2. The other person's *computer will then begin to ring like a normal telephone*.
3. The other person would then click "*accept*" on the pop-up message that appears on the screen.
4. Both parties could then *start talking as if they were on a normal telephone call*.

PHOTOS – SHARE WITH FRIENDS AND COLLEAGUES ONLINE

One way to *share electronic pictures* with friends, family and colleagues is to send them by *email*.

Although convenient, one encounters two problems: The first is that you have to spend time waiting for each photo to attach to the message. If you send the photo 10 different times, you would have to wait for that one photo to attach each of those 10 times. The second problem is that some email service providers have limits on the size and number of files you can send. In order to send a series of photos you might have to waste your time sending

several messages.

Solution

Consider *storing your photos online* and simply *sending a link to them* every time you want to share them. This can be done by opening a *free account* at one of the following websites:

www.hpphoto.com (being transferred to www.snapfish.com)

www.dotphoto.com

After downloading your pictures to the site once, you have the *ability to remove, organize and title them*. For example, in the hpphoto.com website, you can organize your photos into folders. From there you have the option to send links that allow the recipient to *view only certain photos or certain albums*.

GST

71(10)

VENDOR DOES NOT REMIT GST

In an Excise Tax Act case, the taxpayer bought vehicles and paid GST to the vendor but the *vendor did not remit* the GST to CRA. CRA argued that the purchaser must then remit the GST for which they claimed an input tax credit.

The Court concluded that this is *ludicrous*, as long as the purchaser can *prove that they have paid the GST*, because the *vendor is acting as the agent* of CRA (The Bottom Line, January 2004, Page 20).

CARRYING ON BUSINESS IN CANADA

Every *non-resident* person who carries on *business in Canada*, other than a small supplier, *must register for GST/HST* if the non-resident person makes a *taxable supply* in Canada.



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GST/HST REGISTRATION CANCELLATION

GST/HST Memoranda Series 2.7 discusses *Cancellation of Registration* including the required conditions, responsibilities and obligations upon *GST/HST cancellation*.

COMPUTERIZED RECORDS

In June, 2005, CRA introduced GST/HST Memoranda 15.2 Computerized Records.

The 11-page Guide discusses *electronic records*, retention of records, inspections, audits and examinations, and lost, damaged or inadequate records.

Also, in June, 2005, CRA introduced *GST/HST Memoranda 15.1* General Requirements for Books and Records.

DID YOU KNOW...

71(11)

CANPASS AIR - BORDER CLEARANCE



On March 24, 2005 CRA introduced *Guide RC4344* which discusses the *CANPASS Air Service* for pre-approved commercial airline travellers.

Members are allowed to use the *self-service kiosk* when entering Canada to avoid the regular customs and immigration line-ups. For more information call **1-800-**

461-9999 or see website
www.cbsa.gc.ca/canpass.

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