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First Quarter 2023

Kurt Rosentreter Tax Planning Tips 1st Quarter 2023

Tax Tidbits... Some Quick Points to Consider

- For 2023, the maximum amount that may be deducted for non-taxable allowances paid to an employee using a personal vehicle for business purposes has increased by 7₵ to 68₵/km for the first 5,000 kms driven and to 62₵ for each additional km. For Yukon, the Northwest Territories and Nunavut, the tax-exempt allowance will continue to be 4₵/km higher.
- Rapid inflation has resulted in a significant increase of 6.3% to personal income tax and benefit amounts for 2023. For example, the income level at which OAS repayments commence is now $86,912 (from $81,761), the capital gains exemption for the sale of certain small businesses is now $971,190 (from $913,630), and the annual TFSA contribution limit has increased to $6,500 (from $6,000).
- Legislation that requires more trusts to file trust returns and more information to be disclosed has been enacted. The commencement date was recently deferred by a year to apply to fiscal years ending on or after December 31, 2023. These filing requirements include bare trust arrangements, such as in-trust bank accounts that a parent or grandparent may have with their child or grandchild, unless a specific exception applies.

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Covid Benefits: Review/Audit Activity

Kurt's Comments:

Review and audit activity in respect of COVID benefits is likely to increase. Ensure to have all supporting documentation ready for claims made.

On December 6, 2022, the Auditor General of Canada released its report on COVID benefit compliance enforcement. The report reviewed a total of $210.7 billion in payments with the following breakdown among programs.

- Canada Worker Lockdown Benefit (CWLB) – $0.9 billion
- Canada Emergency Wage Subsidy (CEWS) – $100.7 billion
- Canada Recovery Sickness Benefit (CRSB) – $1.5 billion
- Canada Recovery Childcare Benefit (CRCB) – $4.4 billion
- Canada Recovery Benefit (CRB) – $28.4 billion
- Canada Emergency Response Benefit (CERB) and related EI program – $74.8 billion

The report indicated that $4.6 billion in overpayments were made to ineligible individuals, and an additional $27.4 billion of payments to individuals and businesses should be investigated further. This included an estimated $15.5 billion in CEWS received by employers that did not suffer a significant drop in revenue, extrapolated from a review of monthly GST/HST filers' reported revenues. The report noted that GST/HST filings were far from a perfect measure but were still useful for risk assessment.

CRA has indicated that they have completed audits of $2.8 billion in CEWS claims (1,739 applications), but this only led to $200 million being redetermined post-payment. $11.6 million in penalties had been issued as of October 28, 2022.

The report also indicated the following in respect of CERB paid to recipients likely ineligible:

- $1.6 billion was provided to 190,254 individuals who had quit their jobs;
- $6.1 million was provided to 1,522 people who were in prison and $1.2 million to 391 dead people; and
- $2.2 million was provided to 434 children under 15 years old at the time of application.

Just before the release of the report, a November 30, 2022 National Post article (CRA clawing back $3.2 billion from suspect COVID-19 aid payments, but that's just the start, Christopher Nardi) noted the following, based on comments from two top CRA officials:

- CRA has issued notices of redetermination disallowing $3.2 billion in COVID-19 benefit overpayments;
- CRA sent out 825,000 notices of redetermination to individuals it suspected of receiving ineligible or excess payments from several COVID-19 benefit programs as of November 18, 2022;
- post-payment reviews are set to continue until at least 2025; and
- 25,000 cases of fraudulent payments were tied to identity theft.

Many of the overpayments stemmed from confusion and challenges associated with the attestation-based programs.

One of the CRA representatives also noted that "we want to recover money, but we don't want to create financial hardship" and "it's going to be based on the capacity of each and every individual to repay."

Unreported Real Estate Dispositions: Multiple Issues

Kurt's Comments:

Ensure to report all dispositions of real property on your personal tax return.

A September 12, 2022 Tax Court of Canada case reviewed the gain on a residential property purchased in 2007 and disposed of in 2011. The property was substantially rebuilt during the ownership period. The proceeds, cost and gain were all determined by CRA as the sale was unreported. These amounts were largely unchallenged by the taxpayer and accepted by the Court. The Court noted that the taxpayer's tumultuous relations with her ex-husband, whom she divorced in 2014, resulted in "an off-again/on-again cohabitation" during much of the relevant period.

Although the taxpayer argued that the property was her principal residence, CRA denied it, assessing the gain as an adventure in the nature of trade and, therefore, fully taxable. CRA also assessed outside the normal reassessment period of three years and applied gross negligence penalties.

Capital property or adventure in the nature of trade?

The Court accepted that the taxpayer lived at this property from time to time during the ownership period, a personal use inconsistent with a business venture of acquiring, improving and selling the property for a profit. In addition, the taxpayer was a teacher not connected to the real estate sector. Her marital difficulties demonstrated a plausible reason for acquiring this larger residence for personal use as a residence in which to start a family. There was no suggestion that the reconstruction was undertaken for purposes other than for personal use. The nature of the property, length of ownership, lack of prior or subsequent activity in real estate and her personal circumstances all led to the conclusion that the property was acquired for personal use and not resale, so it was a capital property.

Principal residence?

The property was used as an intermittent refuge and was never occupied with regularity. In the absence of evidence such as a change of address, domestic expenses beyond mandatory utilities or other permanent hallmarks, the Court could not conclude that the property was ordinarily inhabited, preventing it from being the taxpayer's principal residence. As such, the taxpayer could not claim the principal residence exemption on the disposition.

Statute-barred?

The Court acknowledged that a fully exempt principal residence sale was not required to be disclosed in the taxpayer's 2011 personal tax return. However, the taxpayer provided no details to show a reasonable basis for believing the gains were fully exempt. Without such evidence, she could not support her defense that the failure to report the gain was based on a reasoned and thoughtful assessment of her filing position rather than a result of carelessness or neglect, as CRA asserted. As she could not disprove CRA's assertions, the return could be assessed outside the normal reassessment period.

Continued: Unreported Real Estate Dispositions

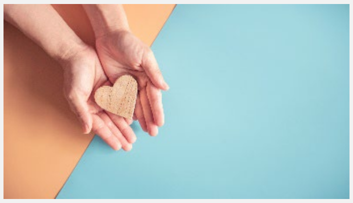
Note that all principal residence sales were required to be disclosed in an individual's tax return starting in 2016. If not reported, the individual could not claim the principal residence exemption on the disposition of the property and would be liable for the tax on the gain on disposition. As the taxpayer's disposition was in 2011, this issue was not addressed in the Court case.

Gross negligence?

The Court noted that CRA's gross negligence penalty assessment (50% of the understated tax) was linked to three factors: the conclusion that the property was held in the course of an adventure in the nature of trade; the assertion that the taxpayer never lived in the property; and the magnitude of unreported income. All three of these assertions were incorrect. The taxpayer's belief that she could navigate the tax laws related to personally held real property was incorrect; however, it was not tantamount to a deliberate act demonstrating indifference to compliance with the law. The gross negligence penalties were therefore reversed.

Kurt's Comments:

Consider whether these updates will affect the taxability of current benefits offered.



Employee Gifts and Parking: Updated CRA Policies

CRA updated several administrative policies in respect of employment benefits, effective January 1, 2022. Two of the key changes relate to employee gifts and parking. These updates were released in late 2022.

Gifts, awards and long-service awards

Under CRA's existing gifts and awards administrative policy, the first $500 of annual gifts and awards provided to arm's length employees is non-taxable. This policy does not apply to cash or near-cash gifts. Historically, CRA had considered all gift cards to be cash or near-cash gifts and, therefore, a taxable benefit.

However, CRA will now accept certain gift cards to be non-cash and eligible to be a non-taxable benefit provided all of the following requirements are met:

- the gift card comes with money already on it which the terms clearly state cannot be converted to cash;
- the use of the gift card is limited to purchases from a single retailer or a group of retailers identified on the card;
- the employer maintains a log to record all of the following details:
  - name of the employee;
  - date the gift card was provided;
  - reason for providing the gift card to the employee (e.g. gift, award, social event);
  - type and amount of gift card; and
  - name of retailer(s) at which the gift card can be used.

Continued: Employee Gifts and Parking

Parking

Generally, employer provided parking is a taxable benefit to employees unless a particular exception applies, such as where there is scramble parking. As a COVID-19 relieving measure, CRA stated that where there was a closure of the place of employment (including situations where employees were given the option to work from home full-time) due to COVID-19 between March 15, 2020 and December 31, 2022, no taxable benefit arose in respect of employer-provided parking in this period. When the employee returns to their regular place of employment to perform their duties, including returning on a part-time basis, the policy no longer applies, meaning that the parking benefit becomes taxable (unless another exception applies).

CRA also discussed many other policies related to parking benefits, such as the exception for scramble parking such that no taxable benefit arises. This policy requires that parking spaces are not assigned and are available to all employees who want to park. Not more than two parking spaces can be available for every three employees who want to park. CRA indicated that this ratio would be based on the average number of parking spaces and employees, calculated at least annually, with a recalculation if there is a significant change.

Witnesses For Legal Documents: Choose them Wisely

A June 17, 2022 Ontario Superior Court of Justice case considered whether a will had been appropriately witnessed. In 2020, the owner of an insurance agency was diagnosed with terminal cancer and drafted a final will and testament. As it was the height of the COVID-19 pandemic, she chose two of her employees to meet her outside of the agency to sign the document as witnesses. She left everything to two children and nothing to the third. She died later that year.

Subsequent to her death, one of the beneficiaries wound up the agency and provided severance to the employees. One of the employee witnesses was not happy with the 14 weeks of severance pay offered and refused to affirm that she had witnessed the will signing until the dispute over her severance was completed. The Court also noted that she was quickly rehired by another insurance agent, the deceased's child who had not received anything from the will. Later, the witness argued that she was not physically close enough to confirm that she had actually witnessed the document being signed.

The circumstances indicated that the witness was present at the signing, was close enough to see what was happening, and as a clerk in an insurance agency, would not have originally signed the will inappropriately. The Court found that the witness was lying about not having witnessed the signing with the likely motivation of increasing her severance.

Kurt's Comments:

When selecting an individual to witness the signing of a legal document, consider whether they would be available and willing to properly verify their signature in the future, if required.

Canada Dental Benefit: Support for those with Young Children

Kurt's Comments:

Eligible individuals must apply for this benefit on their own as accountants and representatives cannot apply on the client's behalf.

The Canada dental benefit, announced in September 2022, provides up-front tax-free payments to cover dental expenses for children under age 12 without dental coverage. The program began December 1, 2022, with expenses retroactive to October 1, 2022 being covered.

The program is available for two periods: December 1, 2022 to June 30, 2023, and July 1, 2023 to June 30, 2024. While the program expires in mid-2024, the government has stated that it is committed to fully implementing a dental program for all households with income under $90,000 by 2025.

Services that dentists, denturists or dental hygienists are lawfully able to provide, including oral surgery and diagnostic, preventative, endodontic, periodontal, prosthodontic and orthodontic services, are eligible for the benefit.

Amounts

The amount of payments that are provided annually (per period) per child under age 12 are based on adjusted family net income (AFNI) as follows:

- $650/child if AFNI is under $70,000;
- $390/child if AFNI is between $70,000 and $79,999; and
- $260/child if AFNI is between $80,000 and $89,999.

AFNI for the benefit's purpose is the same as for the Canada child benefit, with the annual income period ending on December 31, 2021 for the first period and December 31, 2022 for the second period.

Shared-custody parents at the beginning of the relevant period are each eligible for 50% of the benefit, based on whether they incur or will incur eligible expenses in the period and their respective AFNI.

The benefit does not reduce other federal income-tested benefits (for example, the Canada workers benefit, the Canada child benefit, and the GST credit).

Eligibility

To qualify, parents need to attest that the following conditions are met:

- their child does not have access to private dental care coverage (for example, through a parent's employer or coverage that is paid for personally); and
- the child has received, or is intended to receive, dental care services during the relevant period.

Parents also need to provide documentation to verify that out-of-pocket expenses occurred (e.g. show receipts) if required by CRA.

To qualify, the child must be under 12 on December 1, 2022 for the first period and under 12 on July 1, 2023 for the second period.

Continued: Canada Dental Benefit

Application

The application portal for the benefit is available online through CRA's My Account. Those unable to apply online can call 1-800-715-8836 to complete their application with an agent. In addition to an individual's standard identifying information and the above-noted attestation, parents need to provide CRA with the name, address and telephone number of their and their spouse or common-law partner's employer. They also need to provide information about the dental service provider from which they received or intend to receive services for their child.

Poker Winnings: Taxable or Not?

A November 25, 2022 French Tax Court of Canada case considered whether a taxpayer's poker activity constituted a source of business income and therefore the winnings were taxable, as argued by CRA. The taxpayer argued that his winnings were non-taxable as they were derived from his hobby rather than a business. The taxpayer generated poker winnings each year from 2008 to 2011, ranging from $156,855 to $573,882.

Taxpayer Loses

Where an activity can be considered both a hobby and a business, the Court will examine whether it is carried on in a sufficiently commercial manner. If carried on in a sufficiently commercial manner, the activity would be from a business and therefore proceeds taxable. The Court analyzed various elements of the taxpayer's gambling activities, noting the following.

- The taxpayer's activities were much more than entertainment; he played for a living. It was his sole source of income and he devoted almost all of his time to it. Although the taxpayer reported to CRA that he only played 10 hours per week, CRA was able to demonstrate that he was playing over 50,000 hands per month at a rate of 765 hands per hour, averaging over 30 hours/week for at least two of the years in question.
- The taxpayer had demonstrated over the four years an ability to make profits on a consistent and regular basis even though he could not predictably control each specific game. The purchase of a residence in Quebec and a condo in Florida indicated confidence in his ability to generate income.
- Despite an unusual lifestyle (frequent parties and travelling), he behaved like a serious businessman by, for example:
    - using various strategies depending on table limits and strength of opponents;
    - playing high volumes of games at low-limit tables against weaker players;
    - using software that provided information on the tendencies of opponents;
    - tracking and analyzing his own monthly statistics;
    - buying and selling shares of player entries in large poker tournaments (such as a 5% purchase in Jonathan Duhamel's 2010 world poker championship win); and

Kurt's Comments:

Earnings from gambling and hobbies may be taxable depending on the intention and circumstances surrounding the earnings. If in doubt as to the tax status, consult a tax advisor.

Continued: Poker Winnings

- constantly reinvesting a portion of winnings into gambling.

The Court found that the taxpayer "had a subjective intention to make a profit, and that he used his expertise and ability to earn a living in poker, a game of chance where skill is a strong consideration." Therefore, the earnings were taxable as business income. Further, the Court noted that this result was not inconsistent with another recent poker winnings case in which the much larger winnings were not considered taxable. The results in that case were different as, although the evaluation criteria were the same, the facts were different.

How Can Kurt and Team Help with Taxes?

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