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Employee expenses claimed by shareholders

CRA backs down from *Adler*

Under the *Income Tax Act* ('ITA'), a business can generally deduct any expenses that are incurred to earn business income, except where specifically prohibited. Employees, by contrast, are only allowed to deduct expenses that are specifically allowed by the ITA. Most of the rules allowing expenses contain various conditions and restrictions.

One condition that applies to many deductible employee expenses is that the employee be "required under the contract of employment" to pay the expenses. Normally, to claim such expenses, the employee needs to be able to demonstrate that the employment contract states that the employee is required to incur the costs in question. Generally, the employer needs to certify on Form T2200 that this condition is met, as required by ITA subsection 8(10).

What happens if you own the company, and you are also an employee? Can the company 'require' you to incur specific expenses?

In the 2009 *Adler* decision, the Tax Court of Canada ('TCC') ruled that a sole shareholder was not 'required' by his company to incur expenses, even though the employment contract said he was, since there were no consequences to his breaching the agreement. (He was not going to fire himself, for example.)

Although *Adler* was an Informal Procedure decision—meaning that it's not legally binding on either the Canada Revenue Agency ('CRA') or taxpayers—the CRA decided last year to start applying it. Beginning September 2017,

Charitable donation receipts must meet *every* technical requirement



The **Income Tax Regulations**—subsection 3501(1)—state that charitable donation receipts issued must contain all of the required information (as described in the checklist at right) for the tax credit to be allowed.

Two recent decisions of the Tax Court of Canada ('TCC') demonstrate how important it is to check your charitable donation receipts, in case the Canada Revenue Agency ('CRA') challenges them on audit.

TECHNICAL FLAWS IN A RECEIPT CAN CAUSE THE CREDIT TO BE DENIED

In ***Okafor v. The Queen***, 2018 TCC 31, the receipts were otherwise correct, but were missing the "place or locality where the receipt was issued." It was not enough that the charity's address was shown. The donation credit was denied.

In ***Ruremesha v. The Queen***, 2018 TCC 57, the charity's address was shown on the receipts, but it was not the same as the "one recorded with the Minister" (i.e., the CRA). Again, the donation credit was denied.

Often, in these cases, there are other problems as well, and the CRA and the TCC suspect the donation was bogus (e.g., not really paid for, or that there was a cash kickback to the taxpayer). But the case law makes it clear that any technical flaw in a donation receipt can cause the credit to be denied.

So make sure the receipts you receive from charities have all the information listed in the charitable donation receipt checklist (at right)! And if you're involved with running a charity, make sure the receipts it issues comply with *all* the requirements. ■

Charitable donation receipt checklist

- ☐ **Name** and **address** in Canada of the **organization** as recorded with the Minister
- ☐ **Registration number** assigned by the Minister to the organization
- ☐ **Serial number** of the receipt
- ☐ **Place** or locality where the receipt was issued
- ☐ **Date** on which the receipt was issued
- ☐ **Name** and **address** of the **donor** including (in the case of an individual) the individual's first name and initial

FOR A GIFT OF **CASH**

- ☐ **Date** or year during which the gift was received
- ☐ **Amount** of the cash gift

FOR A GIFT OF PROPERTY **OTHER THAN CASH**

- ☐ **Day** on which the gift was received
- ☐ Brief **description** of the property
- ☐ **Name** and **address** of the **appraiser** of the property (if an appraisal is done)
- ☐ Amount that is the **fair market value** of the property at the time that the gift is made

- ☐ Description of the **advantage** (if any) in respect of the gift, and the amount of that advantage
- ☐ **Eligible** amount of the gift
- ☐ **Signature** as provided in subsection (2) or (3) of a responsible individual who has been authorized by the organization to acknowledge gifts
- ☐ Name and Internet **website** of the **CRA**

Canada Child Benefit indexed as of July 2018

■ **In the 2016 Budget**, the newly-elected Liberals announced a large increase in the Child Tax Benefit, renamed the Canada Child Benefit ('CCB'). It is now \$6,400 per year for each child under six, and \$5,400 for each child age six to 17.

The CCB is gradually phased out once the parents' net income exceeds \$30,000, but the phase-out is quite slow. For example, with four children age six to 17, the benefit disappears entirely only when the family net income reaches \$211,375.

As originally announced, the CCB is not going to be indexed to inflation. Possibly, the Liberals wanted future political credit for announcing increases, or else wanted the real cost eroded over time to reduce the federal deficit. However, in September 2016, the Parliamentary Budget Officer publicized the fact that the new program would cost the government less than the old program by around 2025. As a result, indexing was restored, but it would not start until July 2020.

However, in its October 2017 Economic Statement, the government announced that indexing of the CCB would begin in July 2018 (instead of 2020). The earlier indexing was attributed to a "growing economy and improved fiscal track." ■

UNDER 6
YEARS OF AGE
\$6400
BENEFIT
PER YEAR
PER CHILD



6-17
YEARS OF AGE
\$5400
BENEFIT
PER YEAR
PER CHILD



the CRA wrote to many employees who were major or sole shareholders of their companies, and reassessed them to deny employment expenses.

This caused an uproar among small business owners and their advisors, and many complaints were made to the CRA about this interpretation. It would become impossible for any major shareholder to claim these deductions, because they could never prove that the employment contract 'required' them to incur the expenses. Numerous taxpayers were planning to appeal this issue to the Tax Court of Canada, but whether they could win was very uncertain.

A welcome reprieve

Fortunately, the CRA has now backed down, will no longer issue these reassessments, and will reverse those already issued. On 20 February 2018, the CRA issued a notice entitled 'Employment Expenses Review', stating:

// Effective immediately, the Agency will stop reviewing and disallowing 'other employment expenses' claimed on line 229 of the T1 [...] by shareholder-employees. We will also reverse those reassessments specific to line 229 already issued during the review period 1 September 2017 to 10 February 2018 [...] Consultation will be undertaken with stakeholders in the tax professional community to clarify the requirement of employer certification under subsection 8(10) [...] as it relates to shareholder-employees. It is expected that clarification will be issued to take effect in the 2019 tax year. //

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