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TAX TICKLERS… some quick points to consider…

- Canadian controlled **private corporations** accounted for **54%** of all **corporate tax paid**.
- The **1% of Canadians** who earned income in the **top federal tax bracket** paid 26% of the total personal taxes.
- Of the **27.8 million individual** tax filers, **36%** were **non-taxable**.
- The **home buyers' plan maximum** withdrawal increased from $25,000 to **$35,000** for withdrawals made after March 19, 2019. Also, it is now available for use by those experiencing a recent **breakdown in their marriage or common-law partnership.**

REAL ESTATE SALES: Taxable or not?

In general, **gains** are **fully taxable** where the taxpayer **buys a property with the intention to sell** for a **profit** (sold on "account of income"). In **other cases**, **half the gain** is **taxable** (sold on "account of capital"). When a sale on "account of capital" involves the sale of a **principal residence**, the **tax** may be **reduced** or **eliminated** by using the principal residence exemption.

In a December 13, 2019 French **Tax Court of Canada** case, at issue was whether **two apartment buildings** sold by the taxpayer were on account of **capital** (as filed by the taxpayer) or **income** (as assessed by CRA).

After acquiring the two apartment buildings, the taxpayer **paid** the **tenants** to voluntarily **vacate** their **leases**. The buildings were then **renovated** and **sold for a profit**. The taxpayer **argued** that it was only **after** the **discovery of fundamental structural problems** with the properties that the **original plan** to rent the units **changed**, and that the taxpayer decided to resell both buildings.

Taxpayer loses

The Court **did not accept** the taxpayer's argument that the **corporation did not have the funds** to **finance** the **renovations** required due to the substantial structural problems, **as** it **paid large amounts** to the **tenants** to vacate the property. Also, it concluded that it was **highly improbable** that, **at the time of acquisition**, the **taxpayer** was **not aware** of the extent of the **problems** affecting the properties.

The following factors were also considered to indicate the property was acquired for resale:

- the **period of ownership** (up to 18 months) was very short;
- the **director** of the corporation was an **experienced real estate businessman**, indicating that he would likely have known he could make a profit by buying and selling the buildings quickly;
- the buildings were **located** in a **popular and highly sought-after area** of Montreal; and
- one of the buildings was **funded fully by debt**, with the other largely financed by debt. A portion of the purchase price was not due until a number of months after sale.

The Court ruled that, on the balance of probabilities, the **intention** of the taxpayer was to **resell** the properties at a **profit**. The sale was therefore on account of income and **fully taxable**.

ACTION ITEMS: Retain documentation, (emails, letters etc.), which occurred at or around the time of purchase to support your position as to whether the property was acquired on account of income or capital.

CONTRIBUTIONS OF GOODS OR SERVICES TO AN NPO: Tax Implications

In a January 6, 2020 **Technical Interpretation**, CRA considered whether a **deduction** was available to suppliers who **contributed in-kind goods or services** to an **NPO** with the expectation that they would benefit from word of mouth advertising and promotion.

Where the supplier is **providing goods or services** to an NPO in **exchange** for **advertising and/or promotional services**, a **barter transaction** may have occurred. As such, the typical rules for barter transactions would apply. In **arm's length barter transactions**, the **income** is the **price which the taxpayer would normally have charged** a stranger for his services or goods/property. Where **capital property** is provided as part of the barter transaction, the value of the property would be considered proceeds of disposition. The expense for the **goods or services received** by a taxpayer is generally the **same amount** as the value of the **goods or services given up**, adjusted for any cash given or received as part of the transaction. Additional information on barter transactions can be found in Interpretation Bulletin IT-490, Barter Transactions.

For **example**, where a landscaper **barters landscaping services** to an NPO in exchange for **advertising** and promotion for their business, the landscaper would be required to **include the value** of the services provided to the NPO **in its income**. The landscaper would **claim an equal deduction** for advertising and promotion. The landscaper could also deduct costs of providing the landscaping services.

ACTION ITEM: When contributing goods or services, recognize that the deduction, in essence, is limited to the cost of producing and delivering the good or service, rather than its fair market value.

HOME ACCESSIBILITY RENOVATION CREDIT: Increase in Home Value?

When applying for the **home accessibility tax credit** (HATC), valued at **15%** of up to **$10,000 in expenditures** per year, does it matter if the renovation **increases the value** of my **home**? Yes, and No.

In a December 12, 2019 **Tax Court of Canada** case, at issue was whether the taxpayer was eligible for a **HATC** claim for **$10,000** of **qualifying renovations** for the 2016 year, the first year of this credit. The taxpayer's spouse was **76 years old** and **suffered** from **reduced mobility**. The taxpayer incurred $11,000 in renovation costs at the taxpayer's home to **remove steps** the Court referred to as "rickety" and which had no railing or landing area with a very sturdy **deck** including a 5-foot wide stairway and aluminum railings.

CRA denied the claim on the basis that the renovations did **not** meet the definition of a **"qualified renovation"** and even if they did, they would be ineligible as they were made to **enhance** or **maintain the value** of the **house**. Note that a taxpayer is precluded from claiming the HATC where the primary intention of the renovation is to increase or maintain the value of the property. There was no dispute as to the wife being an "eligible individual", the house being an "eligible dwelling", and the taxpayer being a "qualified individual".
Taxpayer wins

Qualifying renovation
The Court indicated that the **taxpayer satisfied almost all**, if not all, of the legislatively required **purposes** that the **renovation assists** with: **gaining access** to a dwelling, or **mobility, access, functionality** or **reduction of harm** within a dwelling (only one of these five purposes is required to satisfy this component of the definition). In addition, the Court observed that the **renovations** were of an **"enduring and integral nature to the dwelling"**. Both of these conditions (the "purpose" and "enduring and integral" tests) are required to meet the definition of a "qualifying renovation".

Increase or maintain value of property
Although the entrance was considered substandard by the taxpayer many years prior, it was not replaced earlier nor in contemplation of a sale. Instead, the **renovations** were **undertaken** when the taxpayer's wife's **mobility from age and affliction demanded** them. The link between the health purpose and the renovations, and the absence of any other clear indication that the purpose was economic, indicated that the primary purpose was not to increase or

maintain the value of the property. The fact that the renovation may also increase or maintain the value of a property was not sufficient to deny the claim.

The Court **allowed the full HATC claim**.
The Court also stated that "if the drain on the federal treasury is too great because of the existing wording, then Parliament can repeal or amend its textually clear provisions. Until then, the Minister and her agents must have some prominent factual basis for asserting a taxpayer's primary economic purpose in undertaking these improvements before this exclusion is invoked."

Note: A "qualifying individual" must either be **65 or older** before the end of the taxation year or eligible for the **disability tax credit** for renovations to their "eligible dwelling" to qualify for the HATC.

ACTION ITEM: Make sure to keep all receipts for renovations that may qualify. Some renovations may also be eligible for a medical tax credit.

WORKING FROM HOME DURING COVID-19: Home Office Expenses

In order for home office expenses to be deductible against employment income, the employee must be required by contract to incur such expenses, and **one** of the **following has to be met**:

i. The home is where the employee **principally** (more than 50% of the time) **does their work**.

ii. The employee **uses the space exclusively** to earn **employment income**, and it is used on a **regular** and **ongoing basis** for **meeting** clients, customers or other people in the course of performing employment duties.

Given that the COVID-19 pandemic has required many **to work from home**, many more will likely be eligible under (i) than in previous years. However, at question is whether the workspace must be the main place of work in **context of the entire year or** just a **specific period**, such as the several months dictated by preventative COVID-19 measures. While CRA has not yet provided their comment, the tax preparation community has been pushing for guidance in time for next tax filing season.

If qualifying under **provision (ii)**, a problematic issue is the requirement for **regular and ongoing meetings**. CRA has stated that those meetings must be **in person**; many tax publishers and journalists have noted that position is outdated and **should include video and teleconference** meetings as well.

What expenses are deductible?
A **portion** of household costs can be deducted, such as **electricity, heating, water, rent, security and maintenance**. If, and only if, the individual is a commissioned **salesperson**, a portion of **property tax and insurance** can also be deducted. **No employee** (neither commissioned sales persons nor regular employees) can deduct **mortgage interest** or **capital cost allowance**.

When calculating the **deductible percentage**, a **reasonable** basis should be used, such as the **area** of the workspace divided by the total finished area (including hallways, bathrooms, kitchens, etc.). Expenditures that **relate solely** to the workspace and employment duties **do not have to be prorated**.

Other cautions
In addition, the employee must:
- obtain a completed **T2200** (Declaration of Conditions of Employment) from the employer;
- **prorate** the **personal usage based on space** (portion of house) and **time** (portion of the day used for work);
- **prorate** expenses that **do not relate to the portion of the year** when working from home; and
- **limit** expenses to the **amount of related income earned during the year**.

For more information, see CRA **Guide T4044**.

ACTION ITEM: If uncertain as to whether your home office expenses are deductible, retain receipts so that a determination can be made as CRA rolls out more guidance and as the filing season approaches.

BUSINESS USE OF THE HOME: Eligible Expenses

A November 27, 2019 French **Tax Court of Canada** case reviewed various deductions claimed against the taxpayer's **business income** derived from **engineering and arbitration** services related to the **business use** of his **home**. The taxpayer and CRA had **agreed** that **35.83% of the home**, mainly the **basement** which was used as a business office, was used for **business purposes**.

CRA had **disallowed gardening** and **swimming pool maintenance** costs which the taxpayer **argued** were **business related** as he **met clients** at his home and sometimes **conducted arbitrations** in the garden. He also argued that there was **no personal use** of the pool, but **clients sometimes used it**. CRA had also **disallowed costs** for repair and renovation of the **living room**, which the taxpayer argued made that room **suitable for hosting arbitrations**.

Taxpayer wins – in part
The Court accepted that the **gardening** expenses were **ordinary home maintenance** costs, deductible in **proportion to business use** of the home (35.83% as noted above), allowing a deduction of $1,271. The **pool expenses** were **not allowed**, on the basis these were **not ordinary expenses** of a business of this nature, and the Court was **not convinced** that **clients used** the pool. It was **not relevant** that the **taxpayer** and his wife **did not use the pool**.

Claims for **repairs and renovations** to the **living room** were **denied** as the taxpayer had **ample space** in the basement office and the garden to **host arbitrations** and conduct his other business activities. The living room was **not part of** the floor space making up the **agreed 35.83% business portion** of the home. As well, the evidence showed the **renovations** were **required** to comply with **city regulations**, including removal of a wood fireplace.

ACTION ITEM: Consider which portions of the home, and which expenditures clearly tie to the business use of your home. Retain and obtain documents (like client emails and photos of work-spaces), which demonstrate how different portions of the home were used for business, and to what extent.

UNCOLLECTIBLE ACCOUNTS: Making Them Valuable

Tax Possibilities – Bad Debt Write-off
As many businesses are **struggling to collect** outstanding amounts, it may be worthwhile to **identify** any receivables which have previously been included in income that can be **written off as bad debts**. This allows for a deductible expense to **reduce taxes**. A number of factors should be considered, including:

- the **history and age** of the debt;
- the **financial position of the debtor**, its revenues and expenses, whether it is earning income or incurring losses, its cash flow and its assets, liabilities and liquidity. These should be compared to prior years as well;
- **changes in total sales** as compared with prior years;
- the **general business conditions** in the country, the community of the debtor, and in the debtor's line of business; and
- the **past experience** of the taxpayer with writing off bad debts.

While the expense as a result of the **bad debt** will provide **relief** on the filing of the tax return associated with **that period**, **GST/HST** can generally be **recovered sooner** on the filing of the return for the period. So, for a monthly remitter with a December year-end, a bad debt with GST/HST written off in April would yield a GST/HST refund when the April GST/HST return is filed. The expense would be claimed in the following year when the tax return for the December 31 year-end is filed.

While a **bad debt** is one that will **not be collected in the future**, a business may claim a **reserve for doubtful account** which is a reasonable amount in respect of doubtful accounts. The reserve for doubtful debts claimed in one year must be included in income in the next subject to a new reserve being taken in that following year. The **GST/HST** on a **doubtful account** is **not recoverable** – the debt must be entirely bad to recover GST/HST.