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Tax Newsletter

Topics for discussion:

- Working at home – tax issues
- Tax disputes in a Covid-19 world
- Credit for digital news subscriptions (and other help for journalism)
- Gasoline tax refund for charities and for persons with physical disabilities
- Around the courts

Working at home – tax issues

In the context of the COVID-19 pandemic, Canadians doing their work at home may have used their home as an office and incurred extra costs accordingly. What expenses will then be tax deductible for them?

The deductibility of expenses for tax purposes — including home office expenses — depends, first of all, on whether you are an **employee** or **self-employed**. (Many self-employed people were already claiming home office expenses before the pandemic.)

Employees — home office expenses

If you are an employee and are **required by your contract of employment** to maintain an office in your home, you can claim certain home office expenses, but only if you meet certain conditions.

First, your employer must sign a certificate (Form T2200), confirming that the employer requires you to have a home office.

Second, either the home office must be the place where you "**principally perform the duties of employment**", or else you must use it on a regular and continuous basis for **meeting** customers or other people in the ordinary course of your employment.

The effect of the above rules in the past has been that the deduction is rarely available to employees.

However, at time of writing the CRA had not yet indicated whether it may relax these rules for people working at home during the COVID-19 crisis, in a number of possible ways. Many taxpayers may take these positions anyway, forcing the CRA (and if necessary the Tax Court) to decide these issues:

- The determination of "principally perform the duties of employment" has traditionally been based on the amount of time you spend at your home office over the entire year. However, the *Income Tax Act* is not clear on this point. One can argue that home office expenses should be allowed for the weeks or months during the year that you worked at home, because *during that period*, that is where you "principally" performed your duties of employment.

- "Meeting" people has been held by the Tax Court of Canada to include telephone meetings, in at least four reported cases. In the past, the CRA has said that it does not accept these decisions. One hopes that, given the extensive use of video conferencing for meetings during the pandemic, the CRA will change its mind on this and stop trying to overrule the Tax Court.

- Form T2200 has traditionally been considered to be required for the entire year (or the part of the year that you are employed by that employer). However, the *Income Tax Act* is not explicit about this. The CRA (or the Tax Court) might permit the form to apply to only those weeks or months that your employer instructed you to work at home.

If you do qualify to deduct home office expenses, what can you claim?

The allowable expenses are normally based on **the fraction of the home that is used for your office**. You can choose any calculation which is reasonable; calculations based on square footage or number of rooms are usually reasonable.

The expenses you can claim include:

- rent, if your home is rented — but not mortgage interest or capital cost allowance
- utilities: electricity, heat, water
- maintenance, including repairs and supplies (e.g., lightbulbs)

You can't claim any expenses that exceed your total employment income from that employer — but if you do have such an excess, it can be carried forward and you can claim it against income from that employer in a later year.

Employees — other expenses

The Act also allows a number of other expenses that can relate to you working at home — again, only if required by your employer as certified on a Form T2200:

- Salary of an assistant, if this payment is required by your employment contract.

- The cost of supplies that are "consumed directly" in the performance of your employment, if your employment contract requires you to both supply and pay for them (this might be implied by the terms under which your employer told you to work at home). An example is paper and toner cartridges for your printer. Long-distance phone charges and cell phone airtime charges qualify, but not (in CRA's view) flat monthly charges for phone and Internet access.

If you are an employee who works on commission, the allowable expenses are much broader. For example, as part of your home office expenses, you can normally claim a portion of your home insurance premiums and property tax. There are also a number of other special cases where specific employment expenses are allowed.

Employees — reimbursements from the employer

Generally, if your employer reimburses you for costs you have incurred, the reimbursement is a taxable benefit unless you incurred the expense primarily for the employer's business purposes. The CRA has numerous administrative policies as to when reimbursement of a particular expense will be considered a taxable benefit.

In April 2020, the CRA announced that, because of the pandemic, employers can reimburse up to $500 of the cost of personal computer equipment to enable the employee to work at home, without this being a taxable benefit.

Self-employed persons —home office expenses

If you are self-employed, home office expenses are deductible only if you fall into one of the following two categories (similar but not identical to those for employees discussed above):

- Your home is your **principal place of business** — that is, you do not have an office elsewhere. Note that even if you have a major client that provides you with an office on its premises, it is still the client's premises and it will not disentitle you to your claim for a home office.

or

- The home office is used exclusively for your business, *and* is used “on a **regular and continuous basis for meeting** clients, customers or patients”.

You cannot use home office expenses to produce an overall business loss that is deductible against other income. However, losses disallowed because of this rule can be carried forward and used in any later year against income generated from the same business.

The allowable expenses will normally be based on **the fraction of the home that is used for your office**. See the discussion for employees above.

The expenses you can claim are the same as for employees discussed above, but also include mortgage interest.

You may also claim **capital cost allowance** (CCA — depreciation, normally at 4% of the declining balance of the home’s cost excluding the land) on the appropriate fraction of your home, but this is usually not advisable. If you claim CCA, the CRA will take the position that that fraction of your home is not part of your principal residence, and will disallow your claim for the principal residence exemption in respect of that portion of the home when you eventually sell the home.

Self-employed persons — other expenses

If you are self-employed, then for tax purposes you are “carrying on business”, and your business income is calculated using the same principles as any business. Most notably, unlike the rule for employees, you can deduct *any* expense that is required for your business, unless there is a specific rule disallowing it.

Therefore, supplies and other charges that relate *exclusively* to your business are fully deductible and not subject to the restrictions that apply to home office. Fully deductible expenses would normally include:

- a separate business phone line
- printer paper and toner cartridges
- computer repairs (assuming your computer is used for your business)
- stationery, envelopes and other office supplies.

Furniture and equipment (e.g., desks, bookcases, computers) are also fully claimable if purchased exclusively for your business, but only as capital cost allowance (depreciation), prorated over many years at the various allowable rates. Note that the Accelerated Investment Incentive rules introduced in 2018-2019 significantly increase the rate of CCA that can be claimed on purchases of new items.

Tax disputes in a Covid-19 world

The Canada Revenue Agency shut down most operations on March 18, 2020 for an indefinite period.

So what does this mean, if you're dealing with the CRA in a tax dispute or potential dispute?

First, if you're under audit, things will take longer. However, the delay will not necessarily help you if the CRA is auditing a past year. For individuals and for most corporations that are small businesses, the CRA normally cannot reassess you more than 3 years after the original Notice of Assessment (though this does not apply in cases of carelessness, neglect or fraud, and there are other specific exceptions). So, for example, if you filed your 2017 income tax return in April 2018 and the CRA issued your Notice of Assessment on May 5, 2018, then once May 5, 2021 passes you would normally be (mostly) free from being reassessed. However, on May 19, 2020, the Department of Justice released draft legislation which will allow the Minister of National Revenue to extend this deadline by up to 6 months to account for the pandemic. By the time you read this, the legislation (*Time Limits and Other Periods Act*) may have been passed by Parliament, and the CRA may have its extension. So expect that the deadline in the above example will become November 5, 2021.

Nevertheless, with the backlog caused by COVID-19, if the CRA was planning to audit you, the audit could well be delayed to the point where the auditor is unable to reassess you in time.

Second, if you have filed a Notice of Objection, a CRA Appeals Officer will get to it eventually. Objections relating to benefits and credits were considered "critical", and work on them continue during the pandemic. Others will be delayed, however.

If you are late in filing a Notice of Objection during the pandemic, don't worry — unless you're very late. Normally there is a 90-day deadline to file an objection. There is a one-year extension period, after the 90 days, during which you can file an Application for Extension of Time to Object and the CRA can choose to accept your late objection as validly filed. The CRA has announced that all objections due March 18, 2020 or later can be filed until June 30, 2020 — meaning that the objection will be automatically considered to include an Application for Extension of Time, so that the CRA can consider it. No doubt the CRA will also be flexible beyond this date, where the 90 days began running during the pandemic. But beware: **if the one-year extension period expires**, you cannot file an objection — the CRA is legally not permitted to accept it. So, if you were already past the 90-day deadline to file an objection before the pandemic, make very very sure that this one-year period doesn't expire, or you lose your objection and appeal rights.

Similar rules apply to appeals to the Tax Court of Canada. The appeal deadline is 90 days after the CRA sends you its decision on your Notice of Objection. If you miss the deadline, the Tax Court has announced that, as long as you file your appeal within 60 days of the Court reopening, your appeal will be automatically considered to include an Application for Extension of Time to Appeal,

so that the Tax Court can allow the Notice of Appeal to be considered filed on time. If you miss the 90-day deadline and also miss the one-year extension period beyond the 90 days, then you lose your appeal rights, but the proposed *Time Limits and Other Periods Act* announced on May 19, 2020 (discussed above) will extend this deadline for the pandemic period (the specific period of extension has not been finalized, but it can be for up to 6 months). Note you can file an appeal to the Tax Court online even when the Court is closed.

Credit for digital news subscriptions (and other help for journalism)

The March 2019 federal Budget introduced various forms of assistance to Canadian journalism organizations, in light of the massive consumer shift away from paper newspapers to online publications. These have now been enacted and are in effect.

First, there is a **digital news subscription tax credit**, running from 2020 through 2024 (though of course it could be extended). This is a 15% credit for subscriptions you pay for, for costs up to $500 per year (i.e., up to $75 total credit per year). The organization must be approved as a “qualified Canadian journalism organization”, meeting certain conditions. The CRA will publish a list of qualifying subscriptions.

Of course, if you’re self-employed in a field where you can justify needing the subscription for business reasons, you’re better to treat the cost as a deductible business expense. But if you can’t do that, a 15% credit does reduce the net cost for you somewhat.

Second, non-profit journalism organizations can **effectively qualify as charities** for tax purposes. They do not actually become registered charities; instead, a QCJO that meets additional conditions can become a “registered journalism organization” (RJO), which will essentially be treated the same as a charity, and will be exempt from income tax. Most notably, donations to an RJO will qualify for the charitable donation tax credit, typically worth about 40-50% to you (depending on your province of residence), once your total donations exceed $200 per year.

Third, a QCJO that meets certain conditions can receive a tax credit from the government, subsidizing 25% of the organization’s “qualifying labour expenditures” for eligible newsroom employees. The credit is “refundable”, meaning that even if the organization does not make a profit so it pays no tax, the CRA will pay the credit to the organization.

Gasoline tax refund for charities and for persons with physical disabilities

There is a little-known refund of excise tax on gasoline for persons with physical disabilities and for registered charities.

This refund is provided under the Federal Excise Gasoline Tax Refund Program, and is legislated in subsection 68.16(1) of the *Excise Tax Act*. It is a refund of **1.5¢ per litre of gasoline purchased**

(the CRA also allows 1.5¢ per 10 kilometres driven). The gasoline must have been acquired "for the sole use of the purchaser and not for resale".
Any registered charity (or registered Canadian amateur athletic association) can claim the refund. It is also available to "a person who has been certified by a qualified medical practitioner to be suffering from a permanent impairment of locomotion to such an extent that the use of public transportation by that person would be hazardous".

The rebate can be claimed for up to two years from the date of purchase. To apply for the rebate, download Form XE8 from the CRA's web site. The form includes instructions and further details.

For more information on this program, one can also call the CRA's Gasoline Tax Refund Unit at 1-877-432-5472.

Around the courts

What's the value of an interest in a trust?

If you own a unit in a publicly-traded trust such as a mutual fund trust, it's easy to determine the value of your unit, since it trades on the market.

But what if you are one of three beneficiaries of a family trust worth $3 million? And the trustees have full discretion over whether to pay you, or the other beneficiaries, any monies from the trust? Does your "trust interest" have a value that can be determined?

This issue comes up in family disputes, when couples separate, and their assets have to be valued for purposes of equalization. It also comes up for tax purposes, such as when a person emigrates from Canada or dies, and their assets have to be valued for tax purposes so that their accrued capital gains can be taxed.

In the example above, the CRA is likely to say that your interest is worth $1 million because you're one of three "equal" beneficiaries. This may not be correct, however.

S.A. v. Metro Vancouver Housing was a 2019 decision of the Supreme Court of Canada. The question in the case was the value of an interest in a "Henson trust". This is a trust set up for a person X with disabilities, deliberately structured so that X cannot legally force the trustees to make any payments to X. The idea is not to disentitle X to other support they can get from public sources.

In this case, a Henson trust was set up for Ms. A, who had disabilities, from her late father's estate. She and her sister were the sole trustees, and they could allocate any amount of the trust's income or capital to Ms. A's "care, maintenance, education or benefit".

Ms. A lived in a rent-subsidized Vancouver rental housing complex. To qualify for rental assistance she had to show each year that she had less than $25,000 in assets. She said that, since she couldn't force the trustees to pay her anything, her interest in the trust had no value.

The Supreme Court ruled that Ms. A had only "a mere hope that the trustees will exercise their discretion in a manner favourable to her". As a result, her interest was valued at nil, and she qualified for the rent subsidy.

This was not a tax case, but it could have significant implications for tax purposes. In the example above, CRA's view — that your interest in the trust is worth $1 million — might not be correct. In light of the Supreme Court of Canada's decision, it can be argued that your interest is worth less than $1 million — or even nothing.

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This letter summarizes recent tax developments and tax planning opportunities; however, we recommend that you consult with us before embarking on any of the suggestions contained in this letter, which are appropriate to your own specific requirements.