Jones Thomblison LLP
Chartered Professional Accountants

Dear Clients/Friends:
This is a quarterly newsletter which we send to clients, referral sources and friends. The information is meant to be educational and application of the concepts should be on an individual basis.Please do no hesitate to contact us should you require further clarification of any item.

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This publication is a high-level summary of the most recent tax developments applicable to business owners, investors and high net worth individuals. Enjoy!

Tax Tidbits

Some quick points to consider…

- On June 19, 2022, individuals suffering from **Type 1 diabetes** became automatically entitled to the **disability tax credit**. This change is **retroactive** to 2021.
- The **Tax Gap**, which measures the difference between what is actually collected and the taxes that would be paid if all obligations were fully met, is between **$18.1 billion and $23.4 billion**.
- On June 23, 2022, legislation was passed which would allow the **full and immediate expensing of many capital assets** purchased on or after April 19, 2021.
- CRA is currently reviewing how and when **crypto asset holdings** need **to be disclosed** on form T1135.

Poker Playing: Hobby or Business?

In a June 21, 2022 French **Tax Court of Canada** case, **CRA assessed** the taxpayer's **poker winnings** from 2010 to 2012 as business **income**. In 2010, the taxpayer **won almost $9 million** in the No Limit Hold'em Championship (The Main Event) at the World Series of Poker. His **net winnings** that year were **about $5 million**. In **2011 and 2012**, the other two years under review, his **net winnings** were about **$400,000 and $100,000** respectively. These amounts were not in dispute, and details of amounts deducted were not included in the case.

The **taxpayer argued** that he played poker as a **hobby**. He cited Paragraph 1.15 of Folio S3-F9-C1 (Lottery Winnings, Miscellaneous Receipts, and Income (and Losses) from Crime) to support his view that his **winnings** should **not** be **taxable**. That document provides the following **four factors** that would be considered in determining whether **gambling** was a **business**:

- the **degree of organization**;
- **special knowledge** or inside information that the taxpayer possesses that allows the **element of chance** to be **reduced**;
- the **intention** to gamble for **pleasure** or as a **profitable livelihood**; and

- the **extent** of the **gambling activities**, including the number and frequency of bets.

After his Main Event win in 2010, PokerStars, **an online poker business**, engaged him as a spokesperson through a taxable corporation created for this purpose. The taxpayer had no other sources of income during the period in question.

Taxpayer wins

A high **volume** of **gambling activity** is **not**, by itself, **sufficient** to result in a **business**. CRA and the taxpayer each presented testimony from **expert witnesses in game theory** discussing **steps** that **poker players** can and do take to **minimize and manage** the **risk of loss**. The taxpayer testified that he **did not follow** these strategies, contrary to claims from a **book** published in 2011 that was **ghostwritten** for him. The book contained **several factual errors**, and the Court accepted that it presented the taxpayer in a manner **designed to promote PokerStars** in concluding that the **taxpayer's testimony** was more accurate. The taxpayer **did not** use statistics software or **study his opponents** – strategies the expert witnesses suggested would be undertaken by a professional poker player.

When **playing in tournaments** in Las Vegas, the taxpayer **partied with friends**. Despite having taken **business courses** during his university studies before taking a sabbatical to play poker, he **did not maintain** formal **accounting records** to track **revenues and expenses**. There was **no evidence** of **formal training or preparation** to play poker beyond watching videos on internet gaming sites.

The Court concluded that the **taxpayer's success** did **not** result from **prudent business practices** and instead occurred purely by **chance**. The taxpayer **did not behave** in a manner **consistent with** conducting a **business** – he played for **entertainment** with **no reasonable expectation of profit**. His **good fortune** in defying the odds **did not** result in a source of **income** – his gambling winnings were **not taxable**.

> **ACTION:** While positive earnings from most taxpayer activity is considered taxable by CRA, this case gives an example of where the Courts found otherwise. When generating cash from a hobby, consider these factors when determining whether tax should be paid.

Required Travel: Between Home and Work

A June 21, 2022 **Tax Court of Canada** case considered whether **motor vehicle costs** of $1,642 associated with a construction foreman's travel between **home and various job sites** were **deductible** against employment income. The taxpayer worked on many of his employer's 50 projects, located at numerous construction sites. The taxpayer was responsible for **ensuring that the workers** were **in place each morning** and were ready to work with **properly functioning tools**, materials and equipment. This meant that the taxpayer was required to **take the tools, materials and equipment home each night** for inspection and **repair**, and then **bring them back** in the morning. The taxpayer also testified that this process was necessary to **protect the assets** from job site theft at night. Storage and repair took place in a designated spot in his garage.

To be eligible for a deduction, the taxpayer **must** be:

- **ordinarily required** to carry on the employment duties away from the employer's place of business **or in different places**; and
- required by employment contract to pay motor vehicle travel expenses in **the performance of employment duties**.

Generally, travel from one's **home to one's place of work** is **personal**; therefore, motor vehicle expenses would **not be deductible**. However, a few exceptions to this position have been determined by the courts, such as where the taxpayer's home was found to be an essential place of business as mandated by the employer.

Taxpayer wins

First, the Court found that the taxpayer was **ordinarily required** to carry on **employment duties in "different places,"** being his garage and the various worksites. While CRA argued that the taxpayer must have carried on the majority of employment duties at home for it to constitute a place of work, the Court disagreed, finding that he only had to be required to **"ordinarily"** carry on duties at home. This meant that he had to perform employment duties at home in the **ordinary or usual course of events or state of things**. Although the taxpayer spent most of his work day at construction sites, he was still **required to fix and store** business assets at home **on an ordinary basis**, and therefore this condition was met.

Second, the Court found that the **travel** between these different places was **conducted in the course of the taxpayer's employment**. The Court specifically noted that his **day did not end when he left the construction site**. Rather, it ended **after he had completed the storage and repair** duties at home. Likewise, his day **started at home** when he loaded the tools, materials, and equipment, and not just when he arrived at the job site. As the travel occurred after his employment duties had commenced and before they ended, the Court determined that the travel was conducted **in the course of employment**.

The taxpayer was allowed to **fully deduct the expenses** associated with travelling between his home workspace and the construction sites.

> **ACTION:** This case is a noteworthy exception from the general rule that travel between home and the workplace is normally personal, and non-deductible. As the circumstances allowing the deduction were fairly specific, CRA will likely generally continue to assess most travel between home and the workplace as personal.

Principal Residence Exemption: Land in Excess of One-half Hectare

The definition of a **principal residence** limits the amount of **land** that qualifies for the **principal residence exemption** to **half a hectare unless** the taxpayer establishes that the **excess land** was **necessary for the use** and **enjoyment** of the housing unit as a residence.

In a January 28, 2022 **Technical Interpretation**, CRA reiterated that it is a **question of fact** as to whether the excess land is **necessary** to the use and enjoyment of the residence. CRA considered their position in light of the use of a **rural property** for a variety of **recreational activities** (such as skating, fishing and horseback riding) and for **farming** to grow fruits and vegetables for personal enjoyment and consumption by the taxpayers' friends and family, such that the taxpayers could **"enjoy country living."**

In referencing Folio S1-F3-C2, Principal Residence, CRA stated that using **excess land** in **connection** with a particular **recreation or lifestyle** (such as keeping pets or country living) does **not** mean the land is **necessary**. Excess land may still be **necessary** where either of the following conditions are met:

- the location of a housing unit requires such excess land to **provide** its occupants with **access to** and **from public roads**; or
- where the **size or character** of a housing **unit** and its **location** on the lot make such excess land **essential** to its **use** and enjoyment as a residence.

In addition, if a **minimum lot size** or a severance or subdivision restriction **existed** in a given year, the **excess land** would **normally** be part of the **principal residence for the year**. If the restriction was released in a particular year, the excess land would generally no longer be considered necessary for that and subsequent years. In those cases, it will then be necessary to determine the portion of the capital gain on disposition that would benefit from the principal residence exemption.

Where a portion of the property is **primarily used** for **income-producing purposes** (such as farming), that portion would **not** be considered **necessary**, **regardless** of whether there was a **minimum lot size** or severance or subdivision restriction in place. While most of CRA's comments are supported by jurisprudence, it does not appear that this particular position is.

The **determination** of whether the excess land is necessary should be done on an **annual basis**.

> **ACTION:** Where a residence is on land in excess of half a hectare, maintain a record (including supporting documentation if possible) of the reasons the additional land was necessary to live on the property.

Personal Services Business (PSB): CRA Education Initiatives

In some industries it is common for employers to **require their workers** to provide services through their **own corporation** rather than directly as employees. In general, a PSB exists where an individual would be **considered the employee** of the hiring entity if it were **not for the existence** the **worker's corporation**. In a recently released 15-minute video, CRA stated that PSBs are more common in trucking, IT consulting, accounting, construction and catering.

If considered a PSB, not only is the **small business deduction not available**, but the corporation is subject to an **additional 5% tax rate, resulting in corporate taxes well over 40%**. Further, **many deductions** available to offset income of regular business activities are **not available** to offset PSB income.

On July 21, 2022, CRA released a stakeholder email announcing the **launch** of an **educational project** in respect of **PSBs**. The email indicated that businesses from specific sectors would be selected; however, the specific industries were not provided. Participation in the project was stated to be **voluntary**.

CRA officials will **contact businesses** and ask them **to provide documentation** on the nature of their **payer/payee relationship**. As part of the project, CRA will also inform payers and payees of the tax obligations. CRA finally noted that **no compliance action** will result from review; however, businesses will be advised to **ensure** that **errors** are **corrected** and comply with the Income Tax Act. The project is expected to run until December 2022.

> **ACTION:** If your corporation provides services to a single client, you may want to watch the video noted above to assess your risk of being considered a PSB. There are several strategies that can be employed to both reduce the risk of PSB classification and reduce the negative consequences of such a classification. If at risk of PSB classification, contact your advisor for analysis and risk mitigation.

TFSA Overcontribution: Relying on Information in Your CRA Online Account

One challenge when relying on CRA-provided **information online** in respect of **TFSA contribution room** is that the information is **not** updated on a **real-time** basis due to the delay in receiving information from TFSA issuers. Although CRA has many disclaimers surrounding this issue, some individuals may be unaware or misinterpret their comments.

A July 14, 2022 Financial Post article (**Taxpayer relying on CRA website info gets hit with penalty for contributing too much to TFSA**, Jamie Golombek) indicated that financial institutions are required to **submit information** on all contributions and withdrawals for each calendar year by the **end of February** of the **following year**. CRA may **not process** and update this information **until April or later**. As such, for example, the contribution room available online in January 2022, would likely only consider transactions from 2020 and earlier, with the 2021 transactions only being included later in the Spring of 2022.

In a June 15, 2022 **Federal Court** case, the Court addressed an application for **judicial review** of CRA's decision to **deny relief** for taxes on **excess TFSA contributions** (1%/month for each month the TFSA is overcontributed) where a taxpayer **misunderstood** the **contribution room** as published online in **CRA's My Account**. This case appears to be the one discussed in the Financial Post article above.

In **2019**, the taxpayer contributed a total of $26,002, while her contribution room was only $7,849, resulting in a **penalty tax of $1,784**. Only $400 of interest income was earned on the overcontribution. The taxpayer made contributions in **January and February 2019** based on what the **taxpayer misinterpreted** to be her **contribution room** at that particular **point in time**, resulting in an over-contribution. The taxpayer argued she **did not intend** to make an over-contribution and that the **information** on My Account was **"very confusing"** and gave rise to a reasonable error.

The taxpayer previously made excess contributions which were withdrawn after correspondence was received from CRA. It appeared that CRA assessed no excess contributions tax at that time.

Taxpayer loses

While the Court was **sympathetic** to the taxpayer's position, in the **self-reporting tax system** in Canada, **individuals** are **responsible** for **understanding** their **TFSA** accounts, and thus the Court ruled that **CRA** was **reasonable** in denying relief to the taxpayer.

Had this been the taxpayer's first excess contribution, the result may have been different as CRA generally offers a little more relief in such situations.

> **ACTION:** Do not rely solely on the information presented in your online CRA account. Additional verification should be conducted to ensure that recent contributions have been incorporated into the contribution room number. If you discover you have accidentally contributed too much, the excess should be withdrawn without delay to minimize exposure to this punitive tax.

CPP Disability Benefit: Following the Doctor's Advice

In a June 6, 2022 **Federal Court of Appeal** case, the Court addressed an application for **judicial review** of the Social Security Tribunal's **decision** to **deny** the taxpayer's **CPP disability benefits** claim on the basis that he did **not** have a **severe and prolonged disability**. The General Division of the Social Security Tribunal stated that while the taxpayer **had significant impairments** (chronic back pain and osteoarthritis in both knees), he had **not** made **reasonable efforts** to follow the **treatments recommended by his physicians**. The taxpayer's doctors had **advised him** for 12 years to **lose weight and exercise**, but the General Division held that he had **not attempted to do so** until 2020.

Taxpayer loses

The Court found that the taxpayer had a **duty to mitigate the severity of his ailments** by following the **treatment recommendations**, and the taxpayer did **not** provide a **reasonable explanation** for failing to do so. As such, it found that the General Division did **not err** when it found that the taxpayer did **not** meet the requirements for a **severe and prolonged disability**, making him ineligible for CPP disability benefits.

> **ACTION:** Not following a doctor's advice to lose weight and exercise may impact eligibility for CPP disability benefits. Heed their advice!