CORPORATE Newsletter

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Recent CRA Thinking on Topics of Interest

IN THIS ISSUE

The Canada Revenue Agency (CRA) regularly releases its responses to queries from the general public on varying tax matters. The responses given to these queries by the CRA gives us an insight their approach to the law, including actual practices and policies of the government on such issues. Some recent queries and responses of interest are summarized below.

Insurance Proceeds—Can they replace Business Income?

This situation involved two associated corporations, an operating company, and a specified investment holding company. The investment holding company owned the real estate from which the operating company carried on its business and the operating company paid the holding company rent. As a result of the association between the operating company and the holding company, the rent received by the holding company from the operating one constituted active business income under certain provisions of the *Income Tax Act* (the "Act").

As a result of a fire in the building, the operating company had to relocate its operations until such time as the premises were repaired. Under the terms of its insurance coverage, the holding company was paid an amount to compensate it for the lost rental revenue. The question that was asked was this: do the insurance proceeds for the lost rent constitute active business income as it replaces the rental revenue from its associated corporation which was afforded active business income status under the Act?

The CRA's position was that the insurance proceeds paid to the holding company would not be treated as active business income, but rather as property income, as rental income is properly reflected as property income in most circumstances. The only exception to that rule was instances where the rent was being paid by an associated operating company. Since the insurance company making the payments was not associated with the holding company, that exception to the general rule no longer applied and the replacement funds paid by the insurance company would constitute property income and be taxed at the higher rate.

Outstanding Cheques

This situation involves a Canadian Controlled Private Corporation (a "CCPC") attempting to qualify as a Small Business Corporation (an "SBC") under the provisions of the Act. The owner of the corporation wanted to avail himself of the capital gains exemption and he needed to reduce the cash on hand in the company by $50,000 so that it would meet the qualification that 90% or more of its assets were used to produce active business income. There was too much cash on

hand in the company and he needed to have cash removed from the company so that it could meet the test. The question put to the CRA was that if the company was to issue cheques to suppliers in advance and they remained outstanding, would those outstanding cheques reduce the balance of cash on hand for the purpose of the SBC test?

Revenue Canada took the position that outstanding cheques on the books of a company at any particular time do not reduce the cash on hand or in the bank at the time a test for the purpose of determining SBC status is done. Outstanding cheques on the books of a company are not considered to reduce the cash of a company for the purpose of the SBC test. The issuance of a cheque was not considered to be a payment until such time as the cheque is cashed and settled by the bank.

Employee Benefits—Meal Allowances

The CRA was asked if a meal allowance paid to an employee at a work site where they did not have a cafeteria constituted a taxable benefit or if it could be treated the same as subsidized meals paid for by employees served in company cafeterias. The CRA ruled that meal allowances and meal certificates must be treated as a taxable benefit. The exemption of subsidized meals applicable in situations where an employer provides a cafeteria for its employees and the employees pay a reasonable amount for their meals is not applicable in situations where the employer does not provide a cafeteria.

Employee Benefits—Free Staff Parking

The CRA was asked if an employer provided free parking to an employee who was frequently required to use his own vehicle for business purposes, whether such free parking was an employee benefit to be included in the employee's income. The CRA stated that generally the fair market value (if it can be determined) of the free parking, less any amount paid by the employee would be required to be included in the employee's income as a taxable benefit. However they also stated that if the following conditions existed, then there would be no taxable benefit.

- Parking was provided free for all employees and customers on a first-come, first-served basis and it was not possible to attribute a fair market value to the parking as parking was offered to everyone free.
- The parking provided to the employee free of charge so that the employee could use the vehicle for use in the performance of his or her employment. In such a case the free parking was of benefit to the employer.

The CRA stated that where an employee was granted free parking and provided his or her own vehicle, or a company-owned vehicle to perform their duties, they would be considered to be regularly using their parking space for employment duties if they were required to use their vehicle on at least three separate occasions per week.

Employee Benefits—Fitness Club Fees

The question posed to the CRA was whether fitness memberships, made available to employees by an employer who had contracted such services with a fitness facility, were considered taxable employee benefits. In this instance the employee would pay the employer for the service by payroll deduction. The employer was able to negotiate special rates for this service for all its employees, such services being available to them at the various locations of the fitness club. The employer has control over issuing membership cards, cancellations, and renewals. The fitness club is independent and simply provides the service.

In the CRA's view, the provision of such a service as described above is not considered a taxable employee benefit. The CRA specifies that the membership fees will not be taxable if the following conditions apply:

- the employer pays an organization separately to provide the fitness facility;
- the contract is between the employer and the fitness provider; and
- the fitness membership is made available to all employees.

In this instance, the CRA concluded that there was no taxable benefit in making the fitness club membership available to its employees.

Employee benefits—Employee Awards

The CRA is frequently asked about the taxability of awards given to employees under various different circumstances. In this instance, the CRA was asked to comment on whether the giving of certificates to employees who meet certain performance targets was to be treated as income for those employees.

The CRA has an administrative policy that non-cash gifts given to an arm's length employee in certain circumstances are not taxable to the employee provided that they do not exceed a value greater than $500 annually. The circumstances under which they would be considered taxable would be in situations where such non-cash awards were presented to employees to reward them for meeting certain performance objectives for employment-related activities. In this instance the employees were given certificates that they could redeem for goods and merchandise offered by the employer. The CRA, therefore, ruled that the awards would be taxable as income to the employee involved.

The CRA cited some of their administrative policies respecting the taxability of awards. These are as follows.

An arms-length employee can receive any number of non-cash gifts and awards from the employer as non-taxable, provided that they do not exceed $500 in total annually and they are not awarded as performance-related awards. If they are deemed to be performance-related awards (e.g., an award given for meeting a sales target), then they are taxable in their entirety and no exemption applies.

In addition to the $500 annual limit on general non-cash gifts and awards, an employee can also receive, free of tax, a non-cash long service or anniversary award of up to $500, provided that the award cannot be for less than five years or that the last award was presented at least 5 years ago. These awards are separate and one cannot be used to enhance the limit for the other.

Awards granted to employees who are non-arm's length employees (i.e., related to the company), will have all awards treated as taxable regardless of their nature.

Gifts of items of an immaterial nature, such as t-shirts, caps, mugs, trophies, etc., will not be considered a taxable benefit to employees.

The giving of gift cards or stock certificates, although being non-cash, will be considered to be a gift of near cash and will be considered taxable regardless of how they are given .