

Fines and Penalties

By

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Section 67.6: “In computing income, no deduction shall be made in respect of any amount that is a fine or penalty (other than a prescribed fine or penalty) imposed under a law of a country or of a political subdivision of a country (including a state, province or territory) by any person or public body that has authority to impose the fine or penalty.”

An expense is generally deductible for tax purposes if the taxpayer incurs it for the purposes of gaining or producing income. Under accounting principles, a taxpayer may usually deduct expenses incurred from illegal acts to the extent that he or she incurs them for the purpose of earning income. However, for public policy reasons, the *Income Tax Act* limits this principle in the case of fines and penalties.

Section 67.6 denies a deduction for fines or penalties imposed by law. The provision effectively overturned the decision of the Supreme Court in *65302 B.C. Ltd.*,¹ which held that fines and penalties incurred for the purpose of gaining or producing income were deductible expenses and were not caught by the purpose prohibition in paragraph 18(1)(a).

The rationale behind the prohibition is that allowing a deduction for fines and penalties would diminish their deterrence value, which would be contrary to public policy. However, the *Act* leaves open the door for the deduction of prescribed fines where it would be contrary to public policy to deny deductibility.²

¹ In *65302 British Columbia Ltd. v. Canada*, [1999] 3 S.C.R. 804, [2000] 1 C.T.C. 57, 99 D.T.C. 5799 (S.C.C.), an over-quota levy imposed on an egg-producing poultry farm by the B.C. Egg Marketing Board an allowable deduction pursuant to subsection 9(1) and paragraph 18(1)(a) of the Act. The levy was incurred as part of the taxpayer’s day-to-day operations. Furthermore, the business decision to produce over-quota was a deliberate decision made in order to realize income. Since the fine was imposed to remove the profit of over-quota production, it was allowable as a deductible current expense.

² See, for example, Reg. 7309, which prescribes fines under the *Excise Tax Act*.

Apart from the exception prescribed under Regulation 7309, the characterization of the amount under federal, provincial, municipal or foreign law determines whether the amount may be deducted. Hence, if the amount is not characterized as a fine or penalty and is incurred for the purpose of earning income, it should be deductible. For example, section 67.6 does not apply to the purchase of carbon offset credits³ or to penalties or damages under private contracts.

However, section 67.6 does not preclude the deduction of legal fees to defend against prosecutions that may lead to fines if the legal fees are otherwise deductible.⁴

The CRA considers that 67.6 applies to:

- Penalties imposed by self-regulating organizations recognized by a provincial securities commission, such as, the Investment Dealers Association (VIEWS docs 2006-0185611I7, 2007-0256591M4);
- Court-ordered payments to a charity on conviction under workplace safety legislation (2008-0294701E5);
- Penalties under Ontario *Tobacco Tax Act* (but interest on the penalties may be deductible): 2012-0472261E5;
- Administrative penalties under Alberta's *Climate Change and Emissions Management Act* (2012-04404715), but not contributions to the CCEM Fund to comply with that Act (2012-0462621E5).

The section also applies to proceeds of crime forfeited under *Criminal Code* s. 462.37 or the *Proceeds of Crime (Money Laundering) and Terrorist Financing Act*: (See: *Chow*, 2011 CarswellNat 1519 (TCC), para. 29: "Forfeiture of the proceeds of crime is a penalty for illegal activities").

³ See: Folio S4-F2-C1: *Deductibility of Fines and Penalties*, para. 1.7.

⁴ CRA Views Docs 2008-0271801I7, 2008-0294701E5. The provision does not apply to interest charges, including interest on penalties on provincial capital tax (CRA Views Docs 2004-0103901E5 and 2009-0326941I7.).

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