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In this article, Vern Krishna explains and analyses employee taxable benefits and gives examples and court cases involving non-taxable benefits such as haircuts, business suits, tuition fees, and much more.

Taxable Benefits (Vern Krishna)

Date: May 12, 2016

 [Taxable Benefits](#)

The taxation of benefits is one of the more troublesome questions for employees, which frequently engages them in long disputes with the Canada Revenue Agency (CRA) over small amounts. An employee's standard of living has two components: salary (bonuses, stock options), and perquisites of office. Salary and bonuses are generally fully taxable; stock options can receive special favourable tax treatment. But non-taxable perks of office are the mother lode that can substantially improve one's standard of living.

There are two types of exempt perks of office: those that the common law exempts, and those that the *Income Tax Act* exempts for various policy reasons. With few exceptions, employees are taxable not only on their salary and wages, but also personal benefits of any kind whatever. Typically, perks include economic advantages—such as, free housing, low cost loans, personal vacations, school fees, cosmetic surgery, and clothing—that derive from the employment relationship. The underlying principle is simple: individuals in equal financial circumstances should pay equal taxes. We refer to this as horizontal equity. In practice, however, it is not always easy to identify whether the economic advantage is for the benefit of the employee or the employer. The situation is complicated by the fact that the CRA uses its discretion in some situations to exempt some benefits.

A benefit is an economic advantage or material acquisition measurable in monetary terms that an employee receives from his employer in his capacity as an employee. Thus, we ask four questions:

1. Did the employee, or a person with whom he does not deal at arm's length, receive or enjoy an economic advantage?
2. Is the economic advantage measurable in monetary terms?
3. Is the advantage for the benefit of the employee or the employer? and
4. Did the employer confer the advantage on the employee by virtue of his employment relationship with the employee?

If the answer to all these questions is affirmative, the economic advantage or material acquisition, no matter how small, is taxable as employment income unless the *Income Tax Act*, or the CRA through administrative discretion, exempts the perk from taxation.

For example, employer provided cell phones are non-taxable if the employee uses it primarily for business purposes, even if there is some incidental personal use within a flat package of minutes. However, the CRA will tax payments without receipts by an employer to the employee. The distinction may be small, but the consequences are great.

Similarly, childcare is non-taxable if the employer provides it at the workplace, and it is available to all employees, and employees only, at a minimal or zero cost. The individual is not taxable, even though the service improves her economic well being by saving costs. However, childcare is taxable if the employer pays for it to a third party. Thus, employees should negotiate their benefits from employment with great care to avoid unexpected tax bills. In contrast, the Prime Minister's nanny care is tax exempt by virtue of a special statutory exemption.

The amount of the economic advantage is not material, unless it is *de minimus*. In *Savage*, for example, the CRA assessed an employee of a life insurance company on \$300 that her employer reimbursed for her tuition fees for pursuing a course of studies directly related to her work. The employee voluntarily took the courses, which provided her with a better understanding of the life insurance business, on her own time. The payment was clearly not salary or wages. However, it was a "benefit" that the taxpayer received or enjoyed in respect of employment. The amount would not have been a taxable benefit if the employer had sent the employee to take the courses so that she would be better informed in her employment.

Fortunately for the taxpayer, the amount was exempt from tax by virtue of special exemption for prizes for achievement under paragraph 56(1)(n) of the Act.

It is understandable that employees will attempt to enhance their standard of living by taking their employment income indirectly through perks. Bernard Ebbers of WorldCom, for example, received \$408 million (U.S.) in loans from his company at 2.3 percent interest rate, which saved him nearly \$28 million each year, compared with the company's corporate interest rate. Even if taxable at 40 percent, the net after-tax benefit was worth nearly \$17 million (U.S.) annually in the pocket. Similarly, the company rented another of its board members a corporate jet for \$1 a month, nearly \$1 million below its normal annual cost.

However, there is a good deal of administrative discretion in taxation and one agency of government can give a wink and a nod to another depending on the nature of the particular perk and the status of the recipient. Parliamentary perks, of course, are in a class of their own: subsidized restaurants, hair cuts, gym facilities, and the like are all necessary for the proper administration of onerous legislative duties.

The traditional approach of the tax authorities and the courts has been that reimbursements for personal clothing are taxable benefits unless the employee can use the clothes only for employment purposes without personal use. Hence, employees, such as prison guards, police workers, firefighters, doctors and dentists who use their clothing only for work related purposes are not taxable if they are reimbursed for their special uniforms. Generally, to constitute a uniform, the clothing would have a logo. This is entirely fair since uniforms are of little use outside the workplace.

Can lawyers and accountants exclude clothing benefits if reimbursed by their employers? Reimbursements for business suits and dresses are normally taxable benefits because one can use them for personal purposes. Similarly, expenditures for business clothes are not deductible as business expenses because they are personal expenses. Unlike the security guard, a lawyer in his or her blue pinstripe suit or dress can go the office, and then go out for a personal evening function in the same outfit.

If the stereotypical business suit is no different from a uniform, it is arguable that any reimbursement or expenditure for such expenses is "representational clothing appropriate to local circumstance", and not a taxable benefit. It should also be deductible as a business expense. However, taxpayers can expect push back from the CRA, or a statutory amendment, if they try to deduct such expenses in order to improve their standard of living.

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