Tax Notes

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ARE YOUR CLIENTS PLANNING ON RENOVATING? HERE ARE TWO TAX CREDITS THAT MAY HELP WITH THE COST

— Wolters Kluwer Canada

Now that the real estate market is cooling, perhaps your retired clients, or those approaching retirement, have at least temporarily shelved plans to downsize and cash-in on the value of their homes. For many, especially those with health challenges, renovations may be on the horizon. Or perhaps some of your clients are considering renovations to make life easier for a disabled family member, or even renovating their homes to allow a family member to move in with them. While renovations can be expensive, there are two tax credits which may assist with the cost: one, the Home Accessibility Tax Credit ("HATC"), which was introduced in the April 21, 2015 federal Budget (with the amount of the credit being doubled in this year's budget); and the other, the Multigenerational Home Renovation Tax Credit ("MHRTC"), just being introduced this year.

Home Accessibility Tax Credit

An individual meeting certain conditions may claim a non-refundable home accessibility tax credit under section 118.041 of the *Income Tax Act* ("ITA"). The credit is calculated at the rate of 15% of renovation expenditures incurred for the benefit of a senior person who is 65 or more at year-end or of a disabled person who is entitled to claim the disability tax credit.

More specifically, the conditions are the following:

- the claimant is a qualifying or eligible individual;
- the expenditures are qualifying expenditures;
- the home being renovated is an eligible dwelling;
- the renovation undertaken is a qualifying renovation; and
- the credit is currently calculated on up to $10,000 of expenditures.

The terms "qualifying individual", "eligible individual", "qualifying expenditure", "eligible dwelling", and "qualifying renovation" are defined below.

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If an expenditure qualifies for both the HATC and the medical expense tax credit ("METC"), both credits may be claimed by the qualifying or eligible individual.

Even if both the qualifying and eligible individuals can claim the HATC, the total credit currently cannot exceed $1,500 ($10,000 x 15%).

The credit is calculated on up to $20,000 of expenditures after 2021 and $10,000 of expenditures before 2022. The total credit that may be claimed by qualifying and eligible individuals is $3,000 ($20,000 × 15%) after 2021 from $1,500 ($10,000 × 15%) before 2022.

Definitions

An individual must refer to the definitions below to determine if they are eligible for the HATC.[1] Only qualifying and eligible individuals may claim the HATC for a particular taxation year.

Qualifying Individual

An individual (other than a trust) is a qualifying individual and may claim the HATC for the year if:

- they are 65 or older at year-end, or
- they are disabled (i.e., eligible for the disability tax credit) for that year.

Eligible Individual

An individual is an eligible individual and may claim the HATC for the year if they claimed one of the following personal amounts for the qualifying individual for the year:

- the spouse or common-law partner amount,
- the eligible dependant amount, or
- the Canada caregiver amount.

Even if an individual cannot claim one of the above amounts, they will still be eligible for the HATC if they:

- could have claimed the spouse or common-law partner amount if the qualifying individual had no net income in the year,
- could have claimed the eligible dependant amount if the qualifying individual had no spouse or common-law partner and had no net income in the year, or
- could have claimed the Canada caregiver amount if the qualifying individual was over 17 and had no net income in the year.

An eligible individual would normally include any of the following persons who could claim one of the above personal amounts for a qualifying individual:

- the spouse or common-law partner of the qualifying individual, or
- the parent, grandparent, child, grandchild, brother, sister, aunt, uncle, niece, or nephew of the qualifying individual or the qualifying individual's spouse or common-law partner.

[1] See subsection 118.041(1) of the ITA.

Eligible Dwelling

To be considered an eligible dwelling for the purpose of claiming the HATC in a particular taxation year, a home must meet all the following conditions:

- the home must be the principal residence of the qualifying or eligible individual at any time in the year;
- the home must be a housing unit located in Canada, including the subjacent land and one-half hectare of contiguous land;
- the qualifying or eligible individual must own, jointly or otherwise, the housing unit itself or a share in a cooperative housing corporation acquired to live in a housing unit owned by the corporation;
- if the qualifying individual owns the unit, they must ordinarily live in it at any time in the year; and
- if the eligible individual owns the unit and the qualifying individual does not own another unit at any time in the year, both of them must ordinarily live in the unit at any time in the year.

A trust of which the individual is beneficiary may also own the unit or share of capital stock.

Qualifying Renovation

To be considered a qualifying renovation for the purpose of claiming the HATC in a particular taxation year, the renovation must be:

- related to the eligible dwelling owned by a qualifying or eligible individual;
- of an enduring nature (i.e., a capital vs. a current expenditure); and
- undertaken to improve the qualifying individual's mobility within the dwelling, to improve its accessibility and functionality to them, or to reduce the risk of harm for them in living or accessing the dwelling.

Qualifying Expenditure

To be considered a qualifying expenditure for the purpose of claiming the HATC in a particular taxation year, the expenditure must be:

- incurred during the year; and
- directly attributed to the qualifying renovation of the eligible dwelling of a qualifying or eligible individual.

The costs of the following items are specifically included as "qualifying expenditures":

- goods and services received to complete the qualifying renovation;
- permits required for the renovation; and
- the rental of equipment needed for the renovation.

On the other hand, the costs of the following items are specifically excluded from "qualifying expenditures":

- property for general improvement of the dwelling independent from the renovation;
- routine repairs and general maintenance of the dwelling;
- the purchase of household appliances or electronic home-entertainment devices;
- housekeeping, security monitoring, gardening, or outdoor maintenance services;

- mortgage interest or other similar costs of financing the renovation;
- renovation of a portion of a dwelling which is used to earn business or property income;
- goods or services provided by a person related to the qualifying or eligible individual, and not registered for GST/HST purposes; and
- expenses reimbursed by a person other than the government.

You can still qualify for the HATC if you do the renovation work yourself. In that case, eligible expenses will include expenses for building materials, fixtures, equipment rentals, building plans, and permits. However, eligible expenses would not include the value of your labour or tools.[2]

Credit Calculation

Once Bill C-19 is passed, the HATC claimed for a particular taxation year will not be permitted to exceed $3,000 for expenditures after 2021 and the current amount of $1,500 for expenditures before 2022, and will be calculated at the rate of 15% on the lesser of two amounts:

(1) $20,000 after 2021 and $10,000 before 2022; and

(2) the qualifying expenditures incurred during the year.

Qualifying expenditures are expenditures incurred for the qualifying renovation of the eligible dwelling of a qualifying individual or eligible individual.

Documentation

As for the type of documentation the Canada Revenue Agency ("CRA") will be asking for to substantiate a claim for the credit, they have published the following guidelines:[3]

> Documentation such as agreements, invoices, and receipts, must clearly identify the type and quantity of goods purchased or services provided, including, but not limited to, the following information, as applicable:
>
> - information that clearly identifies the vendor/contractor, their business address, and, if applicable, the GST/HST registration number;
> - a description of the goods and the date when the goods were purchased;
> - the date when the goods were delivered (keep your delivery slip as proof) and/or when the work or services were performed;
> - a description of the work performed, including the address where the work was performed;
> - the amount of the invoice; and
> - proof of payment (receipts or invoices must indicate that they are paid in full or be accompanied by other proof of payment, such as a credit card slip or cancelled cheque); and
> - a statement from a co-operative housing corporation or condominium corporation (or, for civil law, a syndicate of co-owners) signed by an authorized individual identifying,
>   - the amounts incurred for the renovation or the alteration work,

[2] See the CRA website at: www.canada.ca/en/revenue-agency/programs/about-canada-revenue-agency-cra/federal-government-budgets/budget-2015-strong-leadership/home-accessibility-tax-credit-hatc.html (Item 12).

[3] See the CRA website at: www.canada.ca/en/revenue-agency/programs/about-canada-revenue-agency-cra/federal-government-budgets/budget-2015-strong-leadership/home-accessibility-tax-credit-hatc.html (Item 11).

- as a condominium owner, your portion of these expenses if the work is performed on common areas,
- information that clearly identifies the vendor/contractor, their business address and, if applicable, their GST/HST registration number, and
- a description of the work performed and the dates when the work or services were performed.

The CRA also suggests people consult the CRA's underground economy webpage for tips to protect themselves when hiring a contractor. In order to verify whether someone is registered for GST/HST, see the CRA's GST/HST Registry.

Special Situations

Combined Credit Limit for Qualifying and Eligible Individuals

If both the qualifying and eligible individuals are entitled to claim the HATC in respect of qualifying expenditures for a particular taxation year, they cannot "double-dip" and claim the credit twice for that year. In this case, the maximum qualifying expenditures must be claimed by one individual, or shared between them.

Where the qualifying and/or eligible individuals become bankrupt during the year, they will not be considered to have two taxation years in the year of bankruptcy for the purpose of calculating their combined HATC. This rule applies to calculate the bankrupt's taxable income before and after the date of bankruptcy, but not to calculate the credit claimed by the qualifying and eligible individuals.

Expenditure Eligible for the HATC and METC

If a qualifying individual is eligible to claim both the HATC and METC, the qualifying or eligible individual can claim both credits.[4]

Eligibility for the HATC in Death or Bankruptcy Situations

A qualifying individual who dies in a year in which they would have turned 65 will be deemed to be 65 at the beginning of that year for the purpose of determining their eligibility for the HATC.

An individual becoming a qualifying individual and bankrupt in the same year is deemed to be a qualifying individual at the start of the year for the purpose of determining their eligibility for the HATC. The same rule applies if the eligible individual, not the qualifying individual, becomes bankrupt in the year.

Multigenerational Home Renovation Tax Credit

Effective January 1, 2023, an "eligible person" can claim the multigenerational home renovation tax credit for a "qualifying renovation" if the renovation work is performed and paid for, or the goods acquired, after 2022. The credit for a year is equal to 15% of the lesser of: (1) $50,000; and (2) "eligible expenses" for the year.

Definitions

Eligible Person

An "eligible person" is a person who, at the end of the year including the end of the "renovation period", is:

(1) over 64 (i.e., a senior person); or

(2) over 17 and eligible for the disability tax credit under subsection 118.3(1) (i.e., a disabled person).

[4] See the CRA website at: www.canada.ca/en/revenue-agency/programs/about-canada-revenue-agency-cra/federal-government-budgets/budget-2015-strong-leadership/home-accessibility-tax-credit-hatc.html (Item 18).

Qualifying Renovation

A "qualifying renovation" is one establishing a secondary dwelling unit allowing an "eligible person" to live with a "qualifying relation". A "qualifying renovation" involves a renovation or alteration of, or an addition to, an "eligible dwelling", and meets the following conditions: (1) it is of an enduring nature and integral to an "eligible dwelling"; and (2) it is undertaken to allow an "eligible person" to live in the dwelling with a "qualifying relation" by creating in the dwelling a "secondary unit" that will be occupied by the "eligible person" or "qualifying relation". Only one "qualifying renovation" may be made during an "eligible person's" lifetime.

Renovation Period

A "renovation period" begins when the application for the building permit to complete a "qualifying renovation" is submitted and ends when the "qualifying renovation" passes final inspection.

Eligible Expenses

The "eligible expenses" include expenses meeting the following conditions:

- they are reasonable;
- they are made or incurred during a "renovation period" to complete a "qualifying renovation";
- they are not reimbursed; and
- they are not subject to any financial assistance.

"Eligible expenses" include the following:

- labour and professional services;
- building materials;
- fixtures;
- equipment rentals; and
- permits.

However, they specifically exclude the following expenses:

- furniture;
- tools;
- construction equipment;
- recurring or routine repair or maintenance;
- household appliances and devices;
- electronics;
- outdoor maintenance and gardening;
- housekeeping or security;

- financing costs of renovation;
- expenses not supported by receipts;
- expenses used to claim the medical expense tax credit; and
- expenses used to claim the home accessibility tax credit.

Qualifying Relation

A "qualifying relation" is an individual who is:

- over 17 at the end of the year that includes the end of the "renovation period"; and
- a parent, grandparent, child, grandchild, brother, sister, aunt, uncle, niece, or nephew of the "eligible person", or a spouse or common-law partner of any of those persons.

Eligible Dwelling

An "eligible dwelling" is a housing unit owned (jointly or not) by the "eligible person", by their spouse or common-law partner, or by a "qualifying relation" if the "eligible person" and "qualifying relation" ordinarily reside or intend to reside in the housing unit within 12 months after the end of the "renovation period".

Secondary Unit

A "secondary unit" is a self-contained dwelling unit (which has a private entrance, kitchen, bathroom, and bedroom) that is newly built from an existing living space not previously meeting the requirements of a "secondary unit". The permits to build the "secondary unit" must be obtained and the renovation work must be done in accordance with the laws of the jurisdiction where the "eligible dwelling" is located.

Claiming the Credit

The credit must be claimed, for the year including the end of the "renovation period", by:

(1) A "qualifying relation" in respect of the "eligible person" owning the "eligible dwelling", or

(2) An individual ordinarily residing (or intending to reside) in the "eligible dwelling" within 12 months of the end of the "renovation period" and who is an "eligible person", their spouse or common-law partner, or their "qualifying relation".

More than one person may claim the credit, but the annual "eligible expenses" cannot exceed $50,000 and the annual credit cannot exceed $7,500. If the claimants disagree on how to split the credit, the CRA will make the decision.

CURRENT ITEMS OF INTEREST

Progress of Legislation

The Standing Senate Committee on National Finance reported Bill C-19 without amendment on June 21, 2022. On June 23, the bill received Third Reading in the Senate and received Royal Assent on the same day.

Bill C-241, *An Act to amend the Income Tax Act (deduction of travel expenses for tradespersons)*, received Second Reading in the House of Commons on June 8. If enacted, the bill would allow tradespersons and indentured apprentices to deduct from their income amounts expended for travelling where they were employed in a construction activity at a job site that is located at least 120 km away from their ordinary place of residence.

After the Senate Committee report was presented without amendment on June 8, Bill C-8, *Economic and Fiscal Update Implementation Act, 2021*, received Third Reading in the Senate and Royal Assent on June 9. This enacted the new small business air quality tax credit, the enhancement of the northern residents deduction, the expansion of the school supplies tax credit, the new refundable fuel charge tax credit for farmers, and the new *Underused Housing Tax Act*.

Bill C-22, *Canada Disability Benefit Act*, received First Reading in the House of Commons on June 2. Bill C-22 reintroduces Bill C-35, which died when Parliament was dissolved last year. The bill includes consequential amendments to the *Income Tax Act*.

CRA's Annual Processing Review Program Begins

The CRA began sending annual post-assessment letters for individual income tax returns on May 26. If a client's tax return has been selected for review, the CRA will send out letters to a representative's office if:

- they are designated as the client's representative; and
- they indicated that the Processing Review Program letters should be sent to them.

Electronic filers, who are representatives authorized by taxpayers to receive CRA letters, can sign up for online mail to receive Processing Review letters for these taxpayers in Represent a Client.

Letters may be received from National Verification and Collections Centres other than those you have dealt with in the past. The CRA asks to please send the requested information to the centre indicated in the letter.

New T2 Forms

The CRA has published the 2022 version of the T2 *Corporation Income Tax Return*, and new T2 SCH 65, *Air Quality Improvement Tax Credit (2022 and later tax years)*.

COVID-19 UPDATE

Given the rapidly changing information related to COVID-19 we are providing continuously updated information at blog.intelliconnect.ca/.

Federal

Remission Order for Students Required To Repay CERB (June 22, 2022)

A new federal remission order will provide partial relief of debts owed by students who were found to be ineligible for the Canada Emergency Response Benefit ("CERB") or the Employment Insurance Emergency Response Benefit ("EI-ERB") (i.e., the CERB delivered via the EI system). The CRA estimates that up to 98,000 individuals who were ineligible for the CERB or EI-ERB they received may have been eligible for the Canada Emergency Student Benefit ("CESB"). However, the deadline to apply for the CESB has passed.

To remedy this situation, this order provides relief to those individuals who applied for the CERB or the EI-ERB, but who could have been eligible for the CESB. The order ensures that individuals with CERB or EI-ERB overpayments who can show that they would have met the eligibility criteria for the CESB do not have to repay amounts equivalent to the benefits they could have received under CESB. Accordingly, these individuals would only repay CERB/EI-ERB overpayments that are more than the CESB amounts that they could have received.

FOCUS ON CURRENT CASES

This is a regular monthly feature examining recent cases of special interest, coordinated by Tony Schweitzer of Dentons Canada LLP. The contributors to this feature are from Dentons Canada LLP, Montreal, Toronto, Calgary, and Vancouver.

Kimery v. Canada (Justice), 2022 DTC 5066 (Federal Court) — Request Under the *Access to Information Act*: Refusal of Access May Exist Where Record Merely Alleged

Background

The taxpayer (Mr. Kimery) submitted a request to the Department of Justice ("DOJ") under the *Access to Information Act*, RSC 1985, c A-1 (the "AIA"), seeking accounting records related to a Crown prosecutor's time and expenses (the "Request") in connection with a Canada Revenue Agency ("CRA") investigation and prosecution of Gunner Industries Ltd. ("Gunner Industries"), a company in which Mr. Kimery is interested. Following receipt of the Request, the DOJ responded to Mr. Kimery, communicating that a search of the records under the control of the DOJ revealed that no records existed in response to the Request. Mr. Kimery proceeded to submit a complaint to the Office of the Information Commissioner ("OIC"), alleging that, despite the DOJ's claim that no records existed in response to his request, they did have possession of responsive records. The OIC concluded that the complaint was not well founded, stating that it was satisfied that the DOJ's search for the records was reasonable and that no records could be located.

Mr. Kimery filed a Notice of Application to the Federal Court for a review under section 41 of the AIA.

Issues and Decision

The issues before the Court were:

(1) Does the Court have jurisdiction to hear this application?

(2) If so, are there grounds to grant the relief sought by Mr. Kimery in the circumstances of this case?

The Court's jurisdiction to review matters of this sort under the AIA is conferred by section 41 of the AIA. The determination regarding whether the Court had jurisdiction in the context of the present application was thus determined to fall on whether the circumstances of this application involved refusal of access to a record. In answering this question, the Court made a brief comparison of the former and current versions of section 41 of the AIA. The Court stated that its analysis did not depend on which version of the legislation is applied.

Mr. Kimery took the position that a refusal to disclose a record is a condition precedent to the Court having jurisdiction to conduct a review under the AIA and grant requested relief. The Court followed the conclusion in *Lambert v. The Minister of Canadian Heritage*, 2022 FC 553, finding that an alleged record that does not exist in the records of the relevant government institution is nonetheless a record, and the OIC's response constituted a refusal of access such that the requester was permitted to seek judicial review under section 41 of the AIA. The Court therefore found that it had jurisdiction to hear the application.

Thereafter, the Court analyzed the supporting documents submitted in support of Mr. Kimery's position that the alleged record in fact existed. The documentation commenced with a page entitled "Client Slip", which references Gunner Industries, a file number, and Horst Dahlem as lead lawyer, and appears to relate to travel disbursements. The Court found that there was insufficient evidence explaining the relevance of this documentation to the existence of the alleged records.

The Court held that there was insufficient evidence submitted to reach a finding of bad faith, tampering, or similar alleged egregious behaviours on the part of the DOJ in responding to Mr. Kimery's request, and that Mr. Kimery's position amounted to mere speculation that responsive documents exist in the DOJ's possession.

Conclusion

Taking into account the evidence before the Court, including the evidence of the DOJ's efforts to search for responsive information, there was simply no basis in fact or law for the Court to grant Mr. Kimery relief that would amount to an order that the DOJ conduct a further and better search. It is notable that the Court did not find that it was necessary for it to make a finding as to why the DOJ would not be in possession of the requested records.

— David Blain

Astro Consulting Inc. v. The Queen, 2022 DTC 1038 (Tax Court of Canada) — Corporation Carrying on a Personal Services Business Deprived From Benefitting From the Small Business Deduction and the General Rate Reduction

Background

Astro Consulting Inc. ("Astro") is in the business of providing engineering, consulting, and management services in relation to the oil and gas sector. Mr. Aaron Glazier was the sole director and officer of Astro. Mr. Glazier provided all of the engineering, consulting, and management services rendered by Astro. Lanmark Engineering Inc. ("Engineering") is in the business of providing engineering services and solutions to oil, gas, petro-chemical, and energy industries and ancillary services. Lanmark Petroleum Holdings Ltd. ("Lanmark") owned 100% of the shares of Engineering. As of January 1, 2012, Astro owned 20% of the voting shares of Lanmark. Mr. Glazier became the vice-president of business development and part of Lanmark's senior management team on June 1, 2012, and a director of Lanmark on December 13, 2012. Payments received from Engineering and Lanmark were Astro's main source of revenue. The Minister assessed Astro on the basis that it was a personal services business ("PSB") rendering it ineligible for the subsection 125(1) of the *Income Tax Act*, R.S.C. 1985, c.1 (5th Supp.) (the "ITA") small business deduction and for the subsection 123.4(2) general rate reduction.

Issues and Decision

The issue considered by the court was whether Astro was a PSB, rendering it ineligible for the small business deduction provided for in subsection 125(1) and for the general rate reduction provided for in subsection 123.4(2). Pursuant to paragraph 125(7)(*d*), Astro was not a PSB if the amount it received in the year when the services were rendered was paid by a corporation with which it was associated in the year. Astro's primary ground of appeal was that the Minister's assessment of it as a PSB was in error because Astro was associated with Engineering and Lanmark.

Entitlement to the small business deduction for associated Canadian-controlled private corporations

Pursuant to subsection 125(2), a corporation's business limit for a year for purposes of the small business deduction is $500,000 unless the corporation is associated in the taxation year with one or more Canadian-controlled private corporations, in which case the limit is nil. While the small business deduction can be shared among associated companies if they file a joint election under subsection 125(3), no election had been filed with the Minister in this case. Applying subsection 125(2), the court decided that Astro was not entitled to the small business deduction independently of whether Astro was associated with Engineering and Lanmark.

Entitlement to the general rate reduction

Pursuant to subsection 123.4(1) of the ITA, which provides the definition of "full rate taxable income" (applicable to taxation years that begin after October 31, 2011), the general rate reduction is not available on income earned by a corporation from a PSB. For this reason, the court still proceeded to consider whether Astro was associated with Engineering and Lanmark.

Associated corporations for tax purposes

Application of 256(1)(a) and (b)

Astro argued that pursuant to paragraph 256(1)(*a*), Lanmark was associated with Engineering since it had *de jure* control of Engineering as its sole voting shareholder. Astro also argued that Lanmark was associated with it because either by itself, or together with Engineering, it had *de facto* control of Astro. Astro further argued that since each of Engineering and Astro were associated with Lanmark, they were associated with each other under paragraph 256(1)(*b*). Citing *McGillivray Restaurant Ltd. v. R.* (2016 DTC 5048 (FCA)), which provides that *de facto* control, like *de jure* control, is concerned with control over the board of directors and not with control of the day-to-day operations of the corporation or its business, the court found that none of the evidence filed by Astro supported a finding that Lanmark and Engineering had *de facto* control over Astro.

Application of 256(2.1)

Astro further argued that it was associated with Lanmark as a result of the application of subsection 256(2.1). In order for subsection 256(2.1) to apply, the court was required to find that one of the main reasons for the separate existence of Astro and Lanmark was to reduce the amount of taxes that would otherwise be payable under the ITA. The lack of evidence leading to such a conclusion, combined with the fact that Astro existed five years before it had any contact with Lanmark, led the court to conclude that their separate existence had nothing to do with reducing taxes.

Source of Astro's revenues

Astro argued that the revenues it received from Lanmark were not for services rendered by it since Lanmark's Unanimous Shareholders Agreement provided that the consideration for the services rendered by each shareholder would be calculated and paid monthly to each shareholder based on the profit realized by Lanmark and its subsidiaries. The court found that it is common for owners of a business to be paid for their contribution to the business, including for the services rendered to it, based on the profit of the business. Furthermore, the court was not convinced by Astro's argument given that Astro recorded all of the revenue that it received from Lanmark and Engineering as fees for services rendered in respect of an active business and invoiced Lanmark for such services.

Astro's business was a PSB with respect to the services that it rendered to Lanmark ("but for" test)

Pursuant to subsection 125(7) of the ITA, Astro was a PSB if Mr. Glazier, who performed all services on behalf of Astro, would have reasonably been regarded as an officer or employee of Lanmark *but for* the existence of Astro. The court cited *Ivan Cassell Limited v. The Queen* (2016 DTC 1048 (TCC)) for the proposition that the determination is to be made by asking whether, taking into consideration all of the circumstances, Mr. Glazier would reasonably be regarded as carrying on a business on his own account if Astro did not exist. Given Astro had conceded that its business was a PSB with respect to the services it rendered to Engineering, the court found that Astro also qualified as a PSB with regard to the services it rendered to Lanmark. The court relied on the fact that Astro's relationship with Lanmark was identical to its relationship with Engineering, with the exceptions that Astro's role with Lanmark was to grow and manage its business and that Lanmark paid Astro a monthly sum based upon Lanmark's consolidated profit. The court found that both of these exceptions supported a finding that Mr. Glazier would reasonably be considered to be an employee of Lanmark if Astro did not exist and concluded that all of the revenue Astro received from Lanmark and Engineering was received in respect of a PSB.

Conclusion

In this case, subsection 125(7) of the ITA applied to qualify the taxpayer as a PSB ineligible for the general rate reduction provided for in subsection 123.4(2). The case reiterates the fact that a personal services business is ineligible for the small business deduction provided for in subsection 125(1). The case highlights the importance for associated corporations to file a joint election under subsection 125(3) to be able to share the small business deduction provided for in subsection 125(1). The case also restates the fact that the test for *de facto* control, like *de jure* control, is concerned with control over the board of directors and not with control of the day-to-day operations of the corporation or its business.

— *Anass Benchekroun*

National R&D Inc. v. The Queen, 2022 DTC 5051 (Federal Court of Appeal) — The *Northwest Hydraulic* Test Is Relevant When Assessing SR&ED Eligibility Under S. 248(1)

Background

National R&D Inc. ("National") appealed from a judgment of the Tax Court of Canada in which the Court dismissed National's appeal of the Minister of National Revenue's decision to deny tax credits claimed by National for scientific research and experimental development ("SR&ED") under subsection 248(1) of the *Income Tax Act* (the "ITA"). In its reasoning, the Tax Court explained that the appellant's project did not qualify as SR&ED under subsection 248(1) as well as the criteria set out in *Northwest Hydraulic Consultants Ltd. v. The Queen*, 98 DTC 1839 (TCC) (*Northwest Hydraulic*), mainly because it did not follow the scientific method, which can be read as follows:

> (. . .)
>
> 3. Did the procedure adopted accord with the total discipline of the scientific method including the formulation[,] testing and modification of hypotheses?
>
> (. . .)

The Tax Court judge agreed that National satisfied the first requirement under the *Northwest Hydraulic* test but failed to meet the remaining requirements.

Issues and Decision

The Federal Court of Appeal ("FCA") was faced with the question of whether the Tax Court applied the correct criteria in determining if a taxpayer was properly denied tax credits pursuant to subsection 248(1) of the ITA.

In its appeal, National contended that the judge made legal errors in her understanding of subsection 248(1), made palpable and overriding errors in the assessment of the evidence with respect to the appellant's project, misunderstood the burden of proof on the taxpayer in proceedings before the Tax Court, and erred in ruling the expert report tendered by the appellant to be inadmissible.

With respect to the first issue, the appellant took the position that the judge erred in her understanding of subsection 248(1) by applying the *Northwest Hydraulic* test, specifically with respect to the third criteria: the "scientific method". According to National, the "scientific method" is not a requirement for SR&ED eligibility as per section 248. The FCA disagreed and found that this argument failed. Indeed, in *Kam-Press Metal Products Ltd. v. Canada*, 2021 DTC 5050 (FCA), the FCA also found that the *Northwest Hydraulic* criteria were appropriate when interpreting the meaning of "scientific research and experimental development" under subsection 248(1) of the ITA. Notwithstanding the appellant's contention that the "scientific method" criterion is inconsistent with the CRA guidance, the FCA rejected this argument, noting that while the CRA guidance is useful, it is not binding. Furthermore, the FCA found that the appellant was mistaken in its contention that the "scientific method" is not a proper eligibility requirement on the basis that it comes from jurisprudence and not from the wording of section 248. Moreover, the FCA refused to adopt a restrictive approach as to what constitutes "scientific method", noting that any distinction that the taxpayer wished to make as between scientific research and engineering methodology should have been addressed at trial.

Regarding the second issue, the FCA confirmed that the applicable burden of proof is "balance of probabilities". Thus, National had to prove, on a balance of probabilities, that its activities were within the meaning of subsection 248(1).

Finally, regarding the third issue, the FCA found there was no palpable and overriding error in the judge's finding with respect to the evidence or the decision to exclude expert testimony. In assessing the admission of an expert report, subsection 145(2) of the *Tax Court of Canada Rules (General Procedure)* must be followed as well as the general threshold of admissibility, which was not the case.

The appeal was therefore dismissed.

— *Anne-Sophie Veillette*

RECENT CASES

Minister's opinion re s. 247(10) outside jurisdiction of Tax Court

The Minister of National Revenue reassessed Dow Chemical Canada ULC's ("Dow") 2006 taxation year by adding approximately $307 million to its income as a result of certain transfer pricing adjustments made under section 247 of the *Income Tax Act* ("ITA") in relation to intercompany transactions involving Dow and Dow Europe GmbH, a Swiss operating company with whom Dow was not dealing at arm's length. The Tax Court (2021 DTC 1001) had determined that where the Minister has decided, pursuant to subsection 247(10) of the ITA, to deny a taxpayer's request for a downward transfer pricing adjustment, that decision is not outside the exclusive original jurisdiction granted to the Court under section 12 of the *Tax Court of Canada Act* and section 171 of the ITA provided that the assessment resulting from that decision has been properly appealed to the Court.

The appeal was allowed. In determining whether the Minister's decision under subsection 247(10) of the ITA is outside the exclusive jurisdiction granted to the Tax Court, the Court observed that paragraph 247(2)(*c*) of the ITA provides that the amounts will be adjusted to reflect the terms and conditions that would have been agreed upon by persons

dealing with each other at arm's length. The Court observed that the barrier to having a reassessment that reflects the downward adjustment to Dow's income is the absence of a favourable opinion of the Minister under subsection 247(10) of the ITA. Even if the Tax Court could review the opinion without quashing it, since the existing opinion would remain in place, there was no basis on which the assessment could be referred back to the Minister. The Court held that the opinion rendered by the Minister under subsection 247(10) of the ITA was outside the exclusive jurisdiction of the Tax Court and allowed the appeal.

The Queen v. Dow Chemical

2022 DTC 5050

Appellant's second withdrawal not "eligible amount" under HBP

The Appellant had sought to dismiss her 2017 reassessment, which included in her income subject to tax $5,000 that she withdrew from her RRSP as part of her home buyers plan ("HBP"). Her $5,000 was within the $5,000 maximum amount permitted to be withdrawn as part of an HBP, and the $5,000 was used to pay for her new Toronto condo. The Appellant had agreed to purchase the Toronto condominium pre-construction in 2015 and the agreement contemplated a December 2015 completion. The Appellant had withdrawn $20,000 from her RRSP as an HBP in 2015 and used that amount to pay the deposit in 2015.

The appeal was dismissed. In determining whether the $5,000 second withdrawal satisfied the definition of "regular eligible amount" in subsection 146.01(1) of the *Income Tax Act* (the "Act"), the Court observed that the Appellant had contacted the CRA in early 2016 to explain the situation of delays in closing and was told that she would be able to withdraw the remaining $5,000 amount as part of her HBP and use it to pay the closing costs. The applicable HBP legislation is clear that the Appellant's $5,000 second withdrawal cannot be an "eligible amount" under the HBP regime as it was not withdrawn in the same year as her initial $20,000 HBP withdrawal or in the following year. The Court further held that the $5,000 withdrawal was not a "regular eligible amount" under the HBP provisions and it was therefore an RRSP withdrawal to be included in her income in 2017 in accordance with the provisions of the Act. The Court concluded by opining that the fact that the Appellant had diligently spoken with the CRA regarding the very issue of delayed closings and HBP withdrawals does not give power to the Court to make exceptions to statutory provisions on the grounds of fairness or equity. In holding so, the Court dismissed the appeal.

Dunn v. The Queen

2022 DTC 1029

Federal Court grants jeopardy order in CEWS case

The Respondent claimed $482,160.97 representing six Canada Emergency Rent Subsidy ("CEWS") claims for properties it asserted were leased for industrial purposes. The claims were paid in December 2021; the money was deposited in January in a newly opened account at Scotiabank. After Scotiabank raised questions, CRA investigations determined that the Respondent was not a tenant of any of the leased properties, that RBC had no record of the account from which the Respondent purportedly paid rent for the properties, that there was no activity in the Scotiabank account other than bank deductions, there was no record of the Respondent in a real property search, none in a motor vehicle search, and no T4s or required corporate filings. Subsection 225.1(1) of the *Income Tax Act* provides that the CRA may not undertake collection action until 90 days after a notice of assessment has been mailed. Section 225.2, however, provides that if reasonable grounds are obtained for thinking that delay may jeopardize collection, the Court may authorize the CRA to take immediate action; this is known as a jeopardy order. Here, the CRA sought an *ex parte* jeopardy order to authorize collection of the CEWS amounts.

The order was granted. The standard of proof is that the CRA have a *bona fide* belief on credible evidence in a serious possibility that granting the delay would jeopardize the collection of the debt. The Court held that the CRA had met this burden. Under Federal Court precedent, any of five factors could justify a jeopardy order. The first factor is that there were reasonable grounds to believe that the taxpayer has acted fraudulently. Here, the Scotiabank account was opened seven days before the money was deposited and there had been no transactions since; the leases the Respondent cited were all based on a checkoff form; and the landlords advised that the Respondent was not one of their tenants. Above all, the RBC account did not exist. This was enough to establish the first factor. In addition, the Respondent appeared to have no assets the CRA could seize, indicating that the fourth (assets that could diminish in value over time) and fifth (the size of the debt relative to income and expenses) factors were satisfied. Finally, Scotiabank had restricted the account but could not withhold the money if the Respondent requested it, meaning that delay would jeopardize collection.

Canada (MNR) v. 11421417 Canada Inc.

2022 DTC 5049

TAX NOTES

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