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CESTNICK

TAX MATTERS

# If you want the tax breaks, make sure you meet the right tests for self-employment

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Ever since the pandemic started, the employment of thousands of Canadians has changed. Many people are without work, others are now self-employed.

One gentleman e-mailed me recently. His employment was terminated in May, but he's been hired back as an independent contractor (IC). Whether you're an employee or an IC changes your tax picture significantly. An IC is self-employed and can deduct any reasonable costs incurred to earn income from their business.

Yet not everyone who looks like an IC will be considered self-employed in the eyes of the taxman. A decision of the Tax Court of Canada handed down on July 24 sheds new light on the criteria that determine your working status. Let me explain.

## THE CASE

The Insurance Institute of Ontario (IIO) is an organization that, among other things, provides professional education to the insurance industry in the province. For three years, Peter Barlow worked with the IIO as an instructor. Mr. Barlow entered a series of contracts with the IIO that clearly stated that the intention was for him to be an IC – not an employee. The taxman disagreed and concluded that Mr. Barlow was an employee. The IIO appealed that ruling in the case Insurance Institute of Ontario vs. H.M.Q. (2020 TCC 69).

## THE TWO-STEP TEST

In making its judgment about whether Mr. Barlow was an employee or an IC, the Tax Court of Canada (TCC) relied on a two-step test – from a prior case, Connor Homes v. Canada (2013) – that should be applied in these situations.

The first step is to determine the subjective intent of each party. This can be determined either by the written contract between the parties, or by the actual behaviour of each party (such as invoices rendered for services, registration for GST/HST purposes, and

income-tax filings as an IC). In the case of Mr. Barlow, his contract with IIO specifically stated that the parties agreed he would be an IC, not an employee. Pretty clear.

The second step is to ascertain whether an objective reality sustains the subjective intent of the parties. That is, in the case of Mr. Barlow, did the behaviour of both parties support the intention that Mr. Barlow should be an IC? Past court cases – Wiebe Door Services Ltd. v. MNR (87 DTC 5025), and 671122 Ontario Ltd. v. Sagaz Industries Canada Inc. (2001 SCC 59) – have provided factors to consider when looking at the behaviour of the parties.

When looking at Mr. Barlow's situation, the factors involved in the two cases could lead to the conclusion that he was an employee, and not an IC. This was the view of the Canada Revenue Agency.

The judge, however, sided with IIO and declared Mr. Barlow to be an IC. Why? Because the factors did not point conclusively to Mr. Barlow being an employee. The judge said that if the Wiebe Door and Sagaz factors are inconsistent with the common intention of the parties (which is the case here), but the parties nonetheless act and carry on their relationship in a manner that is somewhat consistent with their intentions, then the relationship will be characterized as they intended – with Mr. Barlow being an IC in this case.

## THE MORAL

Here's the bottom line: If you want to be considered by the taxman as an IC, then you should structure your working relationship such that (1) you have a contract which clearly spells out that you are intended to be an IC, not an employee, and (2) your behaviour supports the conclusion that you're an IC. How? By understanding the Wiebe Door and Sagaz factors and setting up your arrangement to look like an IC.

Those factors are as follows: 1) The degree of control exercised by the worker over when and how they work; 2) Whether the worker provides the tools to perform the work; 3) Whether the worker reaps the rewards of profit, or assumes the risk of loss. A fourth factor – whether the worker is integral to the success of the business – was deemed by the judge to be an outdated factor not to be considered any longer.

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