

THE CANADIAN TAXPAYER

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A CRA All Star Tag Team v. Gaston Gauthier: Politics Trumps Transparency

David H. Sohmer

In the case of *Gauthier v. CRA*,¹ the Federal Court refused to grant an injunction preventing the Minister from issuing a reassessment. Mr. Justice Martineau summarized the facts as follows at paras. 4 and 6 of the decision:

In 1978, the applicant allegedly transferred \$300,000 to a bank account in the Bahamas, a tax haven. That amount came from savings. Apparently wanting to put his affairs in order and not pass his tax problems on to his heirs, the applicant voluntarily disclosed the unreported income for the years from 2005 to 2014. The voluntary disclosure was apparently received by the CRA on January 7, 2015, and accepted on June 17, 2015, on behalf of the Minister under [subsection 220\(3.1\)](#) of the ITA and the Circular.

However, in August 2016, based on information provided by the applicant, the CRA began an audit of the applicant's income tax returns from 1980 to 2004. As explained in an affidavit by Michel Audet, a CRA auditor, given the applicant's

inability to provide details or documents regarding the initial transfer of \$300,000 or the management of his bank account beginning in 1978, he evaluated two assessment scenarios, choosing to **[TRANSLATION]** "include total investment income (\$173,460) in taxable income for 2004, distributed among dividends from Canadian sources and interest based on a percentage equal to the distribution of his portfolio for the taxation years from 2005 to 2014 to allow him to claim a dividend tax credit [sic] and only assess the penalty for failing to file form T1135 and the penalties set out in [subsections 162\(10\) and \(10.1\)](#) of the Income Tax Act.

The assessment scenario which the auditor evaluated but did not choose is described in the affidavit by the auditor:

[TRANSLATION] Include the \$300,000 in Mr. Gauthier's income for the 1980 tax year, split the total investment income (\$173,460), namely the difference between the initial transfer and the adjusted cost base of his investment on December 31, 2004 (\$473,460), between each tax year from 1980 to 2004, impose a penalty for failing to file form T1135 for each tax year between 1998 and 2004 (\$2,500 for each form), as well as a gross negligence penalty for each year from 1980 to 2004.

In May of 2016 (i.e. three months before the CRA began the audit of Mr. Gauthier's returns from 1980 to 2004), the House of Commons Standing Committee on Finance

¹ 2017 FC 1173, [2018] 4 C.T.C. 13.

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Editor: Arthur B. C. Drache, C.M., Q.C.
Content Editor: Steve Hostetter
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Editorial Offices:
226 MacLaren St., Ottawa K2P 0L6
Phone: (613) 237-3300 x11
Fax: (613) 237-2786
Email: adrache@drache.ca
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Address all subscription inquiries to:

One Corporate Plaza, 2075 Kennedy Road,
Toronto, Ontario M1T 3V4
1-416-609-3800 (Toronto & International)
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held hearings with respect to the current status of the KPMG Isle of Man file. The hearings were prompted by a leaked confidential offer by the CRA to unnamed participants in an offshore tax scheme which the CRA had previously detected and characterized as a sham and as involving gross negligence.² Tax would be assessed

² <https://www.documentcloud.org/documents/2752975-May-2015-CRA-amnesty-offer-to-KPMG-Clients.html>.

for the 1999 to 2014 years. Interest would be reduced by four percent for the 2004 to 2010 years, penalties would not be assessed for the 2004 to 2013 years and no penalties under **subsections 162(10), 162(10.1)** and **section 163** would be assessed for the 1999 to 2014 years. Testifying at the hearing were Diane Lebouthillier, Minister of National Revenue; Andrew Treusch, Commissioner of Revenue and Chief Executive Officer, Canada Revenue Agency; Ted Gallivan, Assistant Commissioner of the International Large Business and Investigations Branch; Stéphanie Henderson, Manager of the Offshore Compliance Section; Lynn Lovett, Assistant Deputy Minister of the Department of Justice Tax Law Services Portfolio; and Diane Lorenzato, Assistant Commissioner of the Human Resources Branch.

The following are excerpts from the testimony of Ted Gallivan:

1. FINA meeting number 23, held on May 19, 2016³

I think you're asking an important question. Within the CRA we're clear on certain policies and practices in terms of how many tax years we go back. For ordinary salaried Canadians, we focus on the current tax year. We find a mistake. We don't go back to the maximum limit. We just take a perspective approach and say, "Don't make that mistake again."

With businesses and high net-worth individuals, we tend to stay in the two to four year range. Again, it's educational; let's correct it and let's move on. When you get into aggressive tax planning, we start to move to a six-year review. We sought legislative changes to get nine years. In exceptional cases we can justify going to 16 years. The CRA tries to adjust its approach, but that's an internal policy. We haven't had that up on the website where we could point to that to explain to taxpayers what we normally do and in which exceptional cases we would go further.

2. FINA meeting number 18 held on May 5, 2016⁴

A careful reading of the document posted to the CBC website would indicate that we went back 15 tax years. That would be consistent with the CRA's approach to offshore tax evasion, the most serious kind of non-compliance that we detect. We vary our approach based on the seriousness.

³ <http://www.ourcommons.ca/documentviewer/en/42-1/FINA/meet-ing-23/evidence> (page 34).

⁴ <http://www.ourcommons.ca/documentviewer/en/42-1/FINA/meet-ing-18/evidence> (page 20).

3. FINA meeting 23⁵

In that 50% penalty, the gross negligence penalty that we apply very seldom goes back 16 tax years, and applying a gross negligence penalty is something that we do in a fraction of 1% of cases. We save that for the most serious types of non-compliance.

Why the CRA went back 35 years in the case of Mr. Gauthier when the “clear” policy of the CRA is to go back no more than 15 or 16 years and then only in exceptional cases, is a matter for speculation. Perhaps the answer is suggested by the following comments by Andrew Treusch and Minister Lebouthillier:

Andrew Treusch:

In the recent budget, \$440 million was invested in the agency over five years to increase our ability to tackle tax evasion and tax avoidance. We are committed to returning to the government, to the crown, \$2.6 billion in revenue. That’s the proposition.⁶

Minister Lebouthillier:

As a result of the unprecedented announcements that we made, we expect to recoup \$2.6 billion over the next five years.⁷

David H. Sohmer, a frequent contributor to The Canadian Taxpayer, is a shareholder of Spiegel Sohmer Inc., a Montreal law firm, and can be reached at dhsohmer@spiegelsohmer.com.

⁵ <http://www.ourcommons.ca/documentviewer/en/42-1/FINA/meet-ing-23/evidence> (page 28).

⁶ <http://www.ourcommons.ca/documentviewer/en/42-1/FINA/meet-ing-18/evidence> (page 3).

⁷ <http://www.ourcommons.ca/documentviewer/en/42-1/FINA/meet-ing-23/evidence> (page 12).

Federal Cabinet Shuffle

In the wake of the surprise resignation of Scott Brison as President of the Treasury Board, the Prime Minister was forced to re-jig his cabinet and in so doing had a couple of surprises.

Jane Philpott, who was Minister of Indigenous Services and Vice-Chair of the Treasury Board, becomes President of the Treasury Board and Minister of Digital Government. This move was not a total surprise as Philpott has been the deputy head of the Cabinet committee of Treasury Board.

In our view, she had done a fine job in Indigenous Services (or at least as fine a job as could be managed) and this is a well-deserved promotion.

With the departure of Brison, Trudeau had to find a replacement as a Nova Scotia Minister. He chose Bernadette Jordan, currently Parliamentary Secretary to the Minister of Democratic Institutions, who becomes Minister of Rural Economic Development. Jordan will be the first female minister to represent a federal riding in Nova Scotia in Canadian history.

As Minister of Rural Economic Development, Minister Jordan will oversee the creation of a rural development strategy to spur economic growth and create good, middle class jobs in rural Canada. She will also take action to bring high-speed Internet to more rural households and businesses, and work with municipalities, provinces, territories, and Indigenous partners to meet the many infrastructure needs of rural communities. This is a new department obviously designed to try to pry rural voters away from their traditional Conservative leanings.

Seamus O’Regan, currently Minister of Veterans Affairs and Associate Minister of National Defence, becomes Minister of Indigenous Services, replacing Philpott.

The big surprise to us was that Jody Wilson-Raybould, currently Minister of Justice and Attorney General of Canada, was named Minister of Veterans Affairs and Associate Minister of National Defence. By any standard, this is a demotion and in our view was not merited as we have always felt that she had done a first rate job in Justice. It may be that there is some other story behind this move but it is not immediately apparent to us.

Wilson-Raybould was openly and obviously unhappy with the demotion, although the Prime Minister refused to call it such.

David Lametti, currently Parliamentary Secretary to the Minister of Innovation, Science and Economic Development, becomes Minister of Justice and Attorney General of Canada. Lametti is a Yale-educated former Associate Dean at McGill University, where he was a Professor of Law. Since the Liberals formed government in 2015, he has held two parliamentary secretary positions; first to International Trade Minister and then more recently as the parliamentary secretary to the Innovation Minister.

The changes which were forced upon Trudeau are hardly earth shaking and we shall just have to wait and see how

these people perform in the relatively short term leading to the federal election.

The day after the cabinet shuffle, Trudeau announced some shifts in the bureaucracy:

Marie Lemay, currently Deputy Minister of Public Services and Procurement, becomes Senior Advisor to the Privy Council Office, effective January 28, 2019, prior to an upcoming appointment. Lemay, a former CEO of the National Capital Commission, joined PSPC in April 2016, as the new pay system for civil servants was first rolled out across government. Since coming online, Phoenix has botched paycheques for thousands of civil servants.

Bill Matthews, currently Senior Associate Deputy Minister of National Defence, becomes Deputy Minister of Public Services and Procurement, effective January 28, 2019.

Claude Rochette, currently Assistant Deputy Minister of Finance and Chief Financial Officer of National Defence, becomes Associate Deputy Minister of National Defence, effective January 28, 2019.

Federal By-Elections Finally Called

After several months of increasing angst of opposition parties, the Prime Minister announced that by-elections will be held on February 25, 2019, in the following three electoral districts:

- Burnaby South, British Columbia
- Outremont, Quebec
- York-Simcoe, Ontario

The political situation is unusual in the extreme given that none of the three seats is held by the governing party. But the two seats which were held by the NDP are very much in play.

The one which most eyes will be on is of course Burnaby South where Jagmeet Singh is fighting for a seat in the Commons and by common consensus, his political career if he should not be successful. Breaking an often (but not universally accepted convention) the Liberals and the Conservatives are not prepared to give the leader of the federal party a free pass and at the start of the campaign, there seems to be at least a reasonable chance that Singh can lose this seat.

Singh was to be up against Liberal candidate and small business owner Karen Wang, the Conservatives' Jay Shin, a corporate lawyer, and former talk show host Laura-Lynn Tyler Thompson of the new People's Party of Canada. Green Party Leader Elizabeth May has said her party will stand back and respect the "leader's courtesy" by not running a candidate against Singh.

But days after the by-election call, Wang dropped out citing an ill-thought out online comment about Singh's ethnicity.

The Liberals now will run Richard T. Lee, a longtime B.C. MLA, as their candidate for Burnaby South. Lee previously represented Burnaby as a Member of the B.C. Legislative Assembly for 16 years, where he also served as a Parliamentary Secretary. According to a release from the party, Lee was the first Chinese-Canadian to serve as deputy speaker of the Legislature. He's lived in Burnaby for 32 years.

The Outremont seat had been held by former NDP leader Thomas Mulcair who, when he first won it, took what was a traditionally strong Liberal seat. It seems clear that the Liberals are putting significant resources into winning Outremont this time around. The result (one way or the other) will be seen as indicative as to whether the short-lived love affair between Quebec voters and the NDP still exists to any extent or whether most of the NDP seats in the province will be at risk.

Julia Sanchez, a political novice with a background in the humanitarian sector, will try to keep the riding orange while lawyer Rachel Bendayan will carry the banner for the Liberals. Law student Jasmine Louras is running for the Conservative Party and the Greens have tapped deputy leader Daniel Green to run for them. There's no word yet on who is running for Maxime Bernier's party.

The main political parties will also duke it out in the Ontario riding of York-Simcoe, now that Conservative MP and former Harper cabinet minister Peter Van Loan has retired from politics. Our take on the situation is that this is really an easy win for the Tories who nominated business owner Scot Davidson. When the by-election was called, the Liberals and the NDP hadn't even nominated their candidates which suggests that neither party had any illusions about winning that seat.

But when all is said and done, the key result will be the success or otherwise of Singh. Winning for him is the *sine qua non* of continuing to be the leader but even if that

happens, it is not clear whether he can salvage the NDP to the extent of the status quo in seats held in the Commons.

The announcement doesn't address all the vacancies in the House of Commons. Until recently, Sheila Malcolmson held the Nanaimo-Ladysmith riding in B.C. for the NDP, but has left to run in a provincial by-election. A Liberal official said the government won't call the federal by-election there until after the provincial race to replace Nanaimo MLA-turned-Mayor Leonard Krog is over on January 30.

Meanwhile, Liberal Nicola Di Iorio, who has not been seen on Parliament Hill since the House resumed sitting this fall, has said he'll step down as the MP in Saint-Leonard-Saint-Michel January 22. That timeline allows Trudeau to avoid calling a by-election and to leave Di Iorio's seat vacant for the maximum time allowed — nine months before the October 21 general election.

Proposed Tax Changes to Give Relief from Phoenix Pay Fiasco

We have reported on several occasions over the past couple of years of the depredations wreaked on federal public servants because of the Phoenix pay system problems. In a nutshell, some bureaucrats are paid too much, some too little and some don't get their paycheques at all. Hundreds of millions of dollars have been allocated to fixing the system which still isn't working as it should.

We also noted that many civil servants are also getting hit by the tax system which doesn't make allowances for this sort of situation. Now the government has proposed tax changes which will have to be approved by the provinces and which will offer relief from some of the tax issues.¹

The problem in a nutshell is this: when an employer pays an employee, the employer is required to deduct a portion of the salary or wages and remit it to the CRA. These deductions are made on behalf of employees to help cover their income tax and other obligations for the year in which they are paid.

This requirement can create difficulties when employees are accidentally overpaid, due to a system, administrative,

or clerical error on the part of the employer. In these cases, employers still typically make deductions on overpaid amounts, and remit these to the CRA as they would for any payment of salary or wages.

Overpayments are sometimes not identified until after the calendar year in which the overpayments were made. When this happens, under existing rules, the employee is required to repay to the employer the gross (full) value of the overpayment, including the amount of income tax, Canada Pension Plan contributions, and Employment Insurance premiums that had been deducted from the overpayment by the employer and remitted to the CRA. Because these deductions were remitted to the CRA on behalf of the employee, the onus is on the employee to recover the amount of these deductions from the CRA and provide them to the employer as part of the repayment.

This procedure puts an unfair burden on affected employees and may require them to make repayments that are larger than the amount they received from their employer, creating uncertainty and potential financial hardship.

To alleviate this burden and help affected employees, the Feds are proposing changes that would, under certain conditions, permit an affected employee to repay to their employer only the net amount of the overpayment received in a previous year, rather than the gross amount (net amount plus income taxes, CPP, and EI). Under the proposed legislation, the CRA would be able to refund directly to the employer the income tax, CPP, and EI withheld on an overpayment (and remitted to the CRA on behalf of the affected employee) that occurred through a system, administrative, or clerical error. As a result, affected employees who received overpayments through no fault of their own would no longer be responsible for recovering these amounts from the CRA and repaying the gross amount to their employer.

These changes would apply to employees experiencing overpayments of salary or wages, including federal public servants affected by Phoenix pay system overpayments, and are applicable moving forward as a result of the January 15 announcement. For example, they would apply to overpayments made during the 2018 tax year that have not already been processed under current rules.

¹ There is a short consultation period and draft legislation has been posted on the Department of Finance website.

“These proposed changes are part of the Government of Canada’s plan to address existing pay challenges and replace the Phoenix pay system with a system better aligned with the complex federal government pay structure.”

The backgrounder states in part:

Proposed Treatment

The draft legislative proposals released for public comment would effectively extend the existing rules for overpayments repaid within the same year to overpayments repaid within three calendar years after that year (or where arrangements have been made within that three-year period to make such a repayment). This would allow employees, under certain conditions, to repay their employer the net amount of an overpayment (i.e., excluding income tax, CPP, and EI deductions), even where the salary paid in error and the repayment are in different years.

A public or private sector employer could elect to apply these new rules for any overpayment paid after 2015 as a result of a system, administrative, or clerical error as long as they have not previously issued a T4 correcting for this overpayment. For example, they could process overpayments made during the 2018 tax year under these new rules that have not already been processed under current rules.

For these new rules to apply, the employee must have repaid their employer (or made arrangements to repay) within three years following the end of the year in which the overpayment took place. Where these conditions are not met, the current rules would continue to apply.

In light of the joint federal and provincial management of the Canada Pension Plan, proposed amendments to the Plan would be subject to formal provincial consent, and would not be implemented until such time as this consent has been achieved.

New Election Rules for 2019 Enacted

Well, Canadians will still be subject to the “first past the post” regime in the 2019 federal election but now that the Senate has passed Bill C-76, there will be a number of changes in the rules surrounding that election.

The bill passed in the upper house on December 10 on a vote of 54-31 and is expected to receive Royal Assent by the time you read this.

Conservative senators proposed four amendments to the bill but all were defeated. They have been particularly critical of the provision allowing millions of Canadian citizens living abroad to cast ballots, some of whom Conservatives have argued might potentially be compelled to vote a certain way by unfriendly foreign governments.

Chief electoral officer Stephane Perrault estimated that although some two million Canadians live outside the country, only about 30,000 ex-pats will actually take advantage of the right to cast ballots.

Perrault had warned that the much-delayed bill must go into effect by the end of this year if the independent elections watchdog was to have time to implement the reforms for next year’s campaign.

Bill C-76 is an omnibus bill that will reverse a number of changes wrought by the previous Conservative administration’s widely denounced *Fair Elections Act*. It will restore the use of voter information cards as a valid form of identification to prove residency and will do away with measures that critics argued were designed to benefit the deep-pocketed Tories.

It will limit spending by parties and advocacy groups during the three-month period before an election is officially called, as well as during the official campaign. And it scraps a Tory-instituted provision allowing parties to spend \$650,000 for each day a campaign exceeds the minimum 37 days and caps the maximum campaign length at 50 days.

Legislation aimed at preventing foreign interference and constraining the influence of big money in Canadian elections was also approved by the Senate.

The bill represents a first stab at grappling with the spectre of social media being able to manipulate election results, exacerbate societal divisions, amplify hate messages or instill distrust in the electoral system. It comes in the wake of scandal over Russian interference in the last U.S. presidential contest and the misuse of personal information of millions of Facebook users during the United Kingdom’s Brexit campaign.

It will ban advocacy groups from ever using money from foreign entities to conduct partisan campaigns.

And it will require online platforms, such as Facebook and Google, to create a registry of all digital advertisements placed by political parties or third parties during

the pre-writ and writ periods and to ensure they remain visible to the public for two years.

The bill requires political parties to put in place and publish policies designed to protect the privacy of Canadians whose personal information winds up in their massive voter data bases. But there will be no requirement for independent monitoring or enforcement of those policies.

The legislation also beefs up the powers of the commissioner of elections to investigate violations of election laws, including giving the commissioner the power to compel testimony.

Allowances for Vehicles

From the time the concept of a standby charge for automobiles was introduced some decades ago, there have always been complexities as to whether tax is exigible and how much tax is payable. We well remember an early speech on the subject where the presenter promised a solution which guaranteed no taxes payable by the employee. After a series of overheads dealing with various scenarios, after a pause he announced the fail safe approach. . . and unveiled a picture of a horse.

The rules have been fine tuned over the years but the issue remains.

One variant is where the vehicle is owned by the employee and he or she receives a flat amount as an allowance.

This situation was discussed in a recently published (but likely two-year-old) [technical interpretation](#) from the CRA.¹

We are writing in response to your correspondence dated October 3, 2016, and subsequent telephone conversations in which you asked about the tax consequences of an employer-provided motor vehicle allowance under the Income Tax Act. Thank you for your understanding regarding the delay of this response.²

In the situation described, an employee is paid a flat amount of \$X per month, plus, if eligible, an additional variable payment. The allowance works as follows:

- The employee receives the flat amount at the beginning of each month, and if eligible, receives an additional payment at the end of each month;
- The employee is eligible for the additional payment where the actual kilometres driven for employment purposes is greater than the flat amount divided by the per-kilometre rate. The additional payment is computed by:
 1. Multiplying the total employment kilometres driven in the month by the per-kilometre rate; then
 2. Deducting the monthly flat amount (i.e., \$X).

[T]he per-kilometre rate fluctuates depending on the terms of the collective agreements. At this time, the rate agrees to the amounts prescribed in [section 7306](#) of the Income Tax Regulations.

Our comments

Subject to certain conditions, [subparagraphs 6\(1\)\(b\)\(v\), \(vi\), and \(vii.1\)](#) of the Act provide that reasonable motor vehicle allowances received by employees in respect of travelling in the performance of their duties may be excluded from income. Subparagraph 6(1)(b)(x) of the Act deems a motor vehicle allowance not to be reasonable if it is not based solely on a per-kilometre rate. The per-kilometre rate must be reasonable. Furthermore, an allowance is deemed not to be reasonable by subparagraph 6(1)(b)(xi) of the Act if an employee receives both an allowance for the vehicle and a reimbursement for expenses (in whole or in part), for the same use of the motor vehicle. Consequently, any motor vehicle allowance that does not comply with the specific rules in subparagraphs 6(1)(b)(x) and (xi) of the Act will be deemed not to be reasonable and must be included in the employee's income.

Although you administer the motor vehicle allowance by providing up to two separate payments to an employee in a month, the collective agreements provide that an employee who is required to use his or her motor vehicle in the performance of employment duties is entitled to receive the greater of a flat amount or a per-kilometre allowance.

Where an employee receives the per-kilometre allowance in a particular month, provided the per-kilometre rate for employment-related travel is reasonable, the amount would generally be excluded from the employee's income by subparagraph 6(1)(b)(v), (vi), or (vii.1) of the Act. The fact that the employee could have received a flat amount in respect of his or her employment-related travel would not affect this position.

¹ CRA Views [2016-0673831E5](#), "Motor vehicle allowances", released October 31, 2018.

² At least there was an apology for a ludicrously long delay in dealing with what should have been a straight forward query.

However, where an employee receives a flat amount regardless of how many kilometres he or she drives for employment purposes in a month, the allowance would not be considered reasonable for purposes of subparagraphs 6(1)(b)(v), (vi), and (vii.1) of the Act, and must be included in the employee's income. In such cases, subparagraph 6(1)(b)(x) will deem the allowance not to be reasonable because the allowance is not based solely on the number of kilometres driven.

If it is determined that a motor vehicle allowance (per-kilometre or flat amount) received by an employee is not reasonable and the allowance is included in the employee's income, he or she may be entitled to claim a deduction for actual motor vehicle expenses incurred in the course of carrying out his or her employment duties provided the following conditions are also met:

1. The employee was normally required to work away from his or her employer's place of business or in different places.
2. Under the contract of employment, the employee had to pay his or her own motor vehicle expenses.
3. The employee has a copy of Form T2200, Declaration of Conditions of Employment, which has been completed and signed by his or her employer.

There is no really new element to this interpretation but we felt that it will be useful in advising employers who want to fairly reimburse employees who must use their cars with the added complexity of having to take into account a collective bargaining agreement.

Maybe it is time to think about horses!