

TAX COUNSEL

MISSION POSSIBLE:

CHARACTERIZATION OF EMPLOYMENT RELATIONSHIPS

“Good morning Mr. Phelps. Your mission, should you choose to accept, is to infiltrate the enemy organization, frame the kingpin, blow up the munitions dump, seduce the seductress, and ensure freedom in the Western Hemisphere – all while maintaining your anonymity.”

As the tape self-destructs to jazzy music, Phelps has a decision to make: Should he remit his own source deductions?

The Mr. Phelps of whom I speak is, of course, of the fictional Mission Impossible¹ television and movie series; and the question of his source deductions arises from the issue of whether he, like countless others in less dramatic occupations, is truly an employee or subcontractor.

To reduce the clutter, let's suspend reality a bit and assume that Mr. Phelps and the mysterious IMF organization that sends him those perishable tapes are Canadian residents. We will also assume that Mr. Phelps does not conduct his business through a personal service corporation defined under section 125(7) of the *ITA*.

There are many occasions when it would seem to be in the best interests of both the hirer and hiree that they characterize their relationship as one of contractor and subcontractor, as opposed to one of employer and employee. Hirees are looking for ways to work several jobs with competing employers and to deduct their expenses. Those hiring subcontractors as opposed to employees are not bound by labour legislation, have greater flexibility and do not have to concern themselves with tax, E.I. and C.P.P. payroll remittances (this is a real bother for spy agencies). In general, the rights of employees and the obligations of employers are highly regulated whereas the rights of subcontractors are not. Presumably this is because contractors and subcontractors are on a more even playing field and so those supplying subcontractor services are less in need of legislative protection.

Canada Customs and Revenue Agency (the “Agency”) insists that employers not escape their statutory withholding and remittance duties by improperly characterizing their relationship with their employees as something else.

In the early days before Mr. Phelps started his espionage career, the test applied to distinguish between employee and independent contractor was one of control. If a taxpayer did not have control over what work he or she performed, or how it was performed, that person was labeled an employee. The courts considered four aspects in assessing the nature and degree of worker control: (1) his power of selection, (2) his receipt of wages, (3) his control over the method of work, and (4) the employer's right of suspension or dismissal. This test assumed that an employee must perform all reasonable orders from the employer. For example, a person being paid an hourly wage, obliged to do anything his or her supervisor requests, and subject to dismissal or suspension for failure to comply with those requests, would be labeled an employee under the traditional control test.

However, the law (as well as trade unions) often limits an employer's right to interfere with or control the work of its employees. Therefore, the traditional control test is only one of the tests now applied.

Another test that has been tried by the courts is that of integration. This test assumes that, under a contract of employment, a person is employed as a cog in the business wheel, and that his work is done as an integral part thereof. On the other hand, a contractor's work is assumed to be an accessory only, and not an integrated part of the business. Unfortunately, the integration test is difficult to apply and a relationship of mutual dependency does not always involve an employer and employee.

A currently accepted test for an employment relationship stems from *Wiebe Door Services Ltd. v. M.N.R.*² In that case, the appellant was in the business of installing and repairing overhead doors through the services of an installer. Initially the Tax

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“CCRA insists that employers not escape their statutory withholding and remittance duties”



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“Is the person who has engaged himself to perform these services performing them as a person in business on his own account?”

Court found that the employees were engaged in insurable employment by applying the integration test. However, the Federal Court of Appeal in *Wiebe* preferred this test: “Is the person who has engaged himself to perform these services performing them as a person in business on his own account?” If the answer to that question is “yes”, then the contract is a contract for services. If the answer is “no” then the contract is a contract of employment. Control will always be considered but it is not the sole determining factor. Other factors are: whether the person performing the services provides his own equipment, hires his own helpers, undertakes a degree of financial risk and responsibility and whether and how far he or she has an opportunity of profit from sound management in the performance of the task.

So back to Mr. Phelps' question – should he be remitting his own tax? I think so. (1) He has the choice to accept or reject every week's assignment. (2) He can be as creative as he wants. The I.M.F. is only interested in end results. (3) It would seem that he can choose his own employees (although in the last movie that choice was his undoing). (4) I don't think we ever did see how Phelps got paid but it would be a safe assumption that it was not on an hourly basis and (5) he seems to be responsible for other members of the espionage team. (6) Finally, it appears that he is free to manage his own scheduling so long as the job is complete in time for next week's episode.

All in all, the conclusion that I reach is that Mr. Phelps is not an employee but a contractor. He

must remit his own tax.

As cunning as he is, the only possibility for escape from the clutches of the Agency for Mr. Phelps is with the assistance of a tax professional. **“Your mission, should you choose to accept...”**

1. See http://shell3.ba.best.com/~gregwong/mi/sounds/mi_main_title.au
2. [1986] 3 F.C. 553 (F.C.A.)

NEXT MONTH'S TAX COUNSEL

More of : *The Queen v. Norway Insulation Inc et al* and the continuing consequences of C.C.R.A. violations of *The Charter of Rights and Freedoms*

and

The Hitchhiker's Guide to Tax Limitations.



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Donald P. Mallon, BSc LLB, a partner in Prowse & Chowne, is a seasoned litigator with over 20 years of experience. Focusing on administrative and tax litigation, he draws upon his courtroom and negotiation skills to effectively represent individual and business taxpayers in disputes with Revenue Canada.



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