

November 14, 2006

Re: Taxable benefits – two non-cash awards per year policy

We are replying to your letter dated October 31, 2006 in which you requested our views on the interpretation to be given to the two non-cash awards per year policy in your particular situation.

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I. Tax Aspects Overview:

a) Income Tax Act:

In accordance with paragraph 6(1)a) of the Income Tax Act (hereinafter “ITA”), the value of benefits of any kind whatever received or enjoyed by a taxpayer in a year in respect of, in the course of, or by virtue of an office or employment shall be included in the income of the taxpayer.

b) Technical News No. 22 dated January 11, 2002
CRA explains its new position in this document, as follows:

Response 4: (third paragraph) “Employers will be able to give employees two non-cash awards per year, on a tax-free basis, in recognition of special achievements such as reaching a set number of years of service, meeting or exceeding safety standards, or reaching similar milestones where the total cost of the awards to the employer is less than 500\$ per year. The employer will be able to deduct cost of the gifts and awards.

This new position was developed after extensive consultations, reflects current business practices and is in keeping with other reasonable positions that we have set out in our Interpretation Bulletin

IT-470 Employees’ Fringe Benefits. It makes it easier for employers to administer because it removes the burden of determining the fair market value of small gifts and



awards – something that is very subjective when the gift or award has a company logo”.

Response 6: “If the cost exceeds the 500\$ threshold, then the full fair market value of the gifts or awards will be included in the employee’s employment income.”

II. Assumptions:

The following hypothetical situation is divided into two sections:

a) Determination of taxable benefits

An employer gives an award to an employee, which is a pen. The cost to the employer is 600.00\$ (including sales taxes).

The fair market value of such an item determined by a competent person is 400.00\$ (including taxes). This fair market evaluation reflects the fact that such an award is engraved with the name of the employee and a corporate logo of the employer.

b) Various services rendered by the supplier

The supplier of the awards to the employer renders the following services to the employer:

- Creation and production of brochures;
- The services of professionals who created the program;
 - Tracking and evaluating results for the program;
- Managing the database of the employees and ongoing administration of the program for the employer;
 - Creating and managing websites strictly designed for the employer;
- Selling and wrapping the award selected by the employee, after applying appropriate logos and engraving names.

The first five elements indicated above form part of an administrative process. The last one represents the selling of an award, which includes the profit element of the vendor.

We assume that the supplier acting reasonably breaks down the charge to the employer between the following two elements in his monthly invoice:

- Cost of administration of the program for the employer;
- Charge for the award selected which includes an appropriate profit margin in such circumstances.



III. Tax Issues

Following the above tax aspects and your assumptions, specifically your interpretation requests are the following:

a) Determination of taxable benefits

What is the amount of taxable benefit that should be included in the employee's taxable income, would it be:

- 400\$ representing the full market value of the item?
- Or
- 0\$ because the value is below the threshold of 500\$?

b) Various services rendered by the supplier

Would CRA recognize that the cost of the award for the employer corresponds to the amount specified on the invoice, which is strictly related to the charge made for the award and excluding the cost of administration of the program?

IV. Your interpretation

a) Determination of taxable benefits

Your understanding of the CRA position is that an award is not considered as a taxable benefit for an employee when the total cost of such an award for the employer is less than 500\$ and the number of awards received by such an employee is not more than two per year.

If the cost of the award for the employer exceeds the amount of 500\$, the fair market value needs to be established in order to determine the amount to be included in the employee's income.

Such fair market may be lower than the cost to the employer because the award is engraved with the name of the employee and a corporate logo of the employer. The fair market value amount determined must then be included in the taxable income of the employee regardless of whether the fair market value amount exceeds 500\$ or not.



b) Various services rendered by the supplier

You are of the view that the administration of the program by the supplier is an independent service rendered by the employer that is not related to the cost of a particular award item distributed to an employee.

Consequently, the charge for the award indicated separately on the invoice (and independently from the other services rendered by the supplier) issued by the supplier to the employer would constitute the cost of the award to the employer for purposes of establishing the taxable benefit in accordance with section 6(1) a) of the ITA.

The cost of such an award could then be used in the application of CRA position regarding whether or not the policy related to two non-taxable awards with a cost lesser of 500\$ per year applied.

V. Comfort letter:

Finally, you would like to have our opinion regarding the tax issues described in section 111 above and whether or not your interpretation indicated in section IV above is correct.

VI. Our comments:

As mentioned in paragraph 22 of Information Circular 70-6R5 dated may 17, 2002, the Canada Revenue Agency (CRA) follows the practice of not issuing a written opinion regarding proposed transactions other than by way of an advance tax ruling. Otherwise, if the need is to determine if a completed transaction has received the adequate tax treatment, the first hand decision belongs to our tax district offices following the examination of all the facts and documents, which is generally done in the course of an audit mission.

However, we are prepared to offer the following general comments, which we hope may be of assistance.

The CRA's position is that an award is not considered as a taxable benefit for an employee when the total cost of such an award for the employer is less than 500\$ and the number of awards received by such an employee is not more than two per year.

If the cost of the award for the employer exceeds the amount of 500\$, the fair market value needs to be established in order to determine the amount to be included in the employee's income.



Such fair market may be lower than the cost to the employer because the award is engraved with the name of the employee and a corporate logo of the employer. The fair market value amount determined must then be included in the taxable income of the employee regardless of whether the fair market value amount exceeds 500\$ or not, in accordance with paragraph 6(1)a of the ITA.

As previously mentioned, the employer has chosen to delegate the administration of his reward program to a third party instead of administering its own program. We are of the view that the administration of this program by the supplier of the award is an independent service rendered to the employer that is not related to the cost of a particular award item distributed to an employee.

Consequently, the charge for the award indicated separately on the invoice (and independently from the other services rendered by the supplier) issued by the supplier to the employer would constitute the cost of the award to the employer for purposes of establishing the taxable benefit in accordance with section 6(1)a) of the ITA.

The cost of such an award could then be used in the application of the Canada Revenue Agency's position regarding whether or not the policy related to two non-taxable awards with a cost lesser of 500\$ per year applies.

We trust that these comments will be of assistance.