

Canadian Tax Planners Newsletter

March April 2007

In this edition of the Canadian Tax Planners Newsletter, we shall review the tax implications of receiving money that cannot be classified as income from employment, self-employment, investments or various government programs. Our review shall include funds received from the following sources:

- gambling
- winnings at U.S. casinos
- proceeds from crime
- windfalls
- gifts and bequests
- life insurance
- disability insurance
- lotteries
- prizes won in contests
- strike pay
- damages
- barter transactions
- death benefits

Gambling

To best understand the tax rules related to gambling, let's review the facts of the Leblanc tax case that was recently heard in the Tax Court of Canada. The facts of the case were:

- the Leblanc brothers won just under a \$100,000 at a Toronto race track and decided to become full time gamblers focusing on Pro-Line. This lottery requires individuals to select the winners of multiple sporting events

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- the brothers were betting approximately \$300,000 per week on Pro-Line and three times they won prizes of just under \$2,000,000
- during the period 1996 to 1999, the brothers generated \$5.5 million of profit. Their total bets during the period was approximately \$52 million
- the brothers had a computer system and 15 assistants to run their operation

CRA assessed the brothers for the period 1996 to 1999 on the basis they were running a business and had a “system.” According to the trial judge, the brothers did not have a system, rather they had a pattern – they would bet massive amounts of money in a reckless manner on extreme long shots. In other words, they usually lost, but when they won, they won big. Bottom line – the amounts were not taxable and the Leblanc brothers won the case. For CRA to successfully assess a gambler, they must show the individual had a system that somehow minimized the chance element of the bet.

If an individual was running a gambling house or was a bookmaker, any profits would be taxable. If an individual is a gambler, CRA uses the following four criteria to determine if the amounts are taxable:

- the degree of organization that is present in the pursuit of the gambling activities
- the existence of special knowledge, or inside information that allows the individual to reduce the element of chance
- the individual’s intention to gamble for pleasure, as compared to attempting to earn a living from gambling activities
- the frequency of the bets

Since very few gamblers have a system that reduces the element of chance, it is rare that CRA will successfully reassess many gamblers. Most gamblers do not meet the CRA criteria. Although many taxpayers believe they have a system, most would not qualify as a legitimate system when examined using scientific criteria. In most cases, individuals do not report gambling income on their tax return. It is very difficult for CRA to become aware of the circumstances where an individual did profit by using a legitimate system. In those rare cases when CRA successfully reassess the individual and includes an amount in income; any gambling losses can be used to reduce the taxable income.

Winnings at U.S. Casinos

Although CRA is unable to tax most gambling profits, this is not the case in the United States. Casinos and other gambling establishments are required to apply a withholding tax of 30% on certain gambling winnings.

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