

***Draft prepared for the IALS 2010 Conference in Milan, Italy. Please do not cite or quote without permission.**

Tax Law as Labour Regulation: The Case of Informal Family Workers

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This paper offers an illustration of how work is regulated not just by labour and employment laws as conventionally understood, but also by other fields of law that define which activities count as productive work and how different kinds of work are valued, measured, compensated and disciplined. I explore this idea specifically in the context of Canadian tax and employment insurance laws and their treatment of informal family workers, that is individuals who assist a spouse or other relative with employment duties or business activities.¹ I will briefly discuss the following questions:

- Who are informal family workers, and what is the evidence that they play a significant role in the economies of industrialized countries like Canada?
- How do tax and employment insurance laws regulate informal family workers?

1. Informal Family Workers in Canada: Definitions and Empirical Evidence

References to informal labour can mean many different things. This paper deals with one subgroup within the broad informal sector: individuals who contribute labour to a job or business of another family member. This work can be informal in several senses. It may be unpaid, or if paid the compensation may be undocumented, irregular, or delivered in some form other than traditional wages or profits. The working relationship may also be informal in the sense that responsibilities and rights of individual parties are never explicitly defined in a written or even verbal agreement, but rather negotiated on an ongoing basis within the context of household and family relations. Put differently, I am looking at market work that is legally associated with one individual as the dominant actor but is in substance carried out jointly with others who identify as their family members.

Documenting and quantifying the activities of informal workers presents obvious challenges in any country. In an industrialized country like Canada, however, the normal difficulties of obtaining reliable and complete information about informal family workers is compounded by an assumption that they are largely obsolete in

¹ This brief exploration draws in part on my previously published and forthcoming work. See in particular Lisa Philipps, "Helping Out in the Family Firm: The Legal Treatment of Unpaid Market Labour" (2008) 23:1 *Wisc. J. of Law, Gender & Society* 65; "Silent Partners: The Role of Unpaid Market Labour in Families" (2008) 14:2 *Feminist Economics* 37; and "Income Splitting and Gender Equality: The Case for Incentivizing Intra-Household Transfers", in *Challenging Gender Inequality in Tax Policy Making: Comparative Perspectives*, ed. Kim Brooks, Asa Gunnarson, Lisa Philipps and Maria Wersig (forthcoming, Hart Publishing).

developed economies. Household- or kin-based production is associated with earlier periods of Western history, before industrial capitalism split waged work in the market from unwaged work in the household.² In modern times, it has been studied mainly in the context of poorer countries with large informal and subsistence economies, for example in the gender and development literature.³ In the industrialized world such practices are often perceived as a relic that survives only in particular sectors such as agriculture, or in rarefied forms among elites (the corporate or political wife). As a result, little effort is made to gather systematic information about such workers or understand their circumstances.

Canadian labour force statistics do include data on “unpaid family workers” and elsewhere I have explained why these data probably capture only a very small slice of the total population of informal family workers (see note 1). Briefly, the statistics are limited by the fact that they cover only workers aged 15 and over; only those who provide unpaid services to a family owned business, as opposed to helping an employee, and then only if they reside with the business owner; and only those who identify unpaid family work as their ‘main job’.

Qualitative research tells a different story. Many studies of middle class corporate spouses and family owned businesses have detailed the pervasive and essential nature of family members’ participation in these livelihoods, especially by wives but also by children, husbands, and other relatives. The nature of the contributions covers the full range of operational and managerial tasks, but in the case of wives and other female relatives it often includes highly gendered activities that rely heavily on personal and emotional skills, such as social hosting, community outreach, customer relations and conflict mediation. Moreover, there is good reason to think that informal family work may be on the rise in industrialized countries with patterns of rising self-employment, more home-based work, and generally the deregulation and flexibilization of labour markets. Studies of the micro-businesses that have replaced standard employment for some workers have identified the crucial role that households play in the economic survival of such enterprises.⁴

Informal family workers may operate largely outside the scope of traditional labour and employment law. However this does not mean they are entirely unregulated. Rather, their choices, opportunities and working conditions may be shaped in important ways by other legal regimes including tax and social welfare laws. These regimes may apply to the informal worker directly, or indirectly via the business or employee who they are assisting. The following section provides some examples

² See ANTONELLA PICCHIO, *SOCIAL REPRODUCTION: THE POLITICAL ECONOMY OF THE LABOUR MARKET* (Cambridge University Press, 1992).

³ As discussed for example in Lourdes Beneria, *Accounting for women’s work*, in LOURDES BENERIA, ED., *WOMEN AND DEVELOPMENT: THE SEXUAL DIVISION OF LABOR IN RURAL SOCIETIES* (Praeger, 1982) 119, at 131-132; and LOURDES BENERIA, *GENDER, DEVELOPMENT, AND GLOBALIZATION: ECONOMICS AS IF ALL PEOPLE MATTERED* (Routledge, 2003), at 108-116; 134-136.

⁴ See for example studies by Susan Baines, Jane Wheelock and others cited in “Helping out in the Family Firm” and “Silent Partners”, note 1.

from tax and employment insurance law in Canada, both of which are administered by the Canada Revenue Agency.

2. The Tax and Employment Insurance Treatment of Paid Family Workers

Canadian tax law has historically approached paid family workers with an attitude of suspicion, constructing them as presumptive tax evaders or tax shelters.⁵ Until 1980, the federal Income Tax Act prohibited business owners outright from deducting any salary or wages paid to a spouse.⁶ In addition tax administrators had a discretionary power to ignore a legal partnership between spouses and attribute all the profits of a business to one member of the couple.⁷ The policy concern behind these rules was to prevent business owners from fraudulently reducing their tax liabilities by claiming as an employee or partner a spouse who was not in fact performing business related services or never obtained control over the alleged payments. However by assuming all such arrangements were illegitimate or at least suspect, and removing tax incentives for the business owner to pay wages or share profits, the rules disadvantaged relatives who participated in family enterprise. The probable effect of the tax system was therefore to deter the formalization of these working relationships and to shore up a model of family economic relations as personal and decommodified.

Tax law's resistance to the idea that family members could interact on genuinely commercial terms would in all likelihood have had a disproportionate impact on women's legal and economic status. For example in exercising their discretionary power to ignore spousal partnerships, both tax authorities and courts have often been skeptical about the value of women's labour and whether it is properly seen as market labour or merely an extension of their familial obligations.⁸ The current statutory regime takes a more neutral stance than the historical rules mentioned above, with family members being subject to the same rules as any other employee or partner. Nonetheless, gendered ideas about the nature and value of family labour can still exert influence when revenue officials or judges must determine whether related individuals intended to form a business partnership, or whether a salary paid to a relative is "reasonable" and therefore fully deductible.⁹ Moreover, Kathleen Lahey has noted that many wives suffer ongoing disadvantage because of the pre-1980 ban on deducting spousal wages, because an unpaid worker cannot make contributions to or accrue any rights to her own pension under either public or private pension savings regimes.¹⁰

Rather than paying wages or dividing profits, a transfer of corporate shares or other property may offer another means of compensating family members for their

⁵ In "Helping Out" and "Silent Partners" I considered how tax and other legal regimes treat *unpaid* family workers. Admittedly the distinction between paid and unpaid is blurry in this context, as the reasons for a transfer of income or property between individual family members are not always clear.

⁶ s.74(3),(4), repealed by S.C. 1980-81-82-83, c. 48. s.40(1).

⁷ S.74(5), repealed by S.C. 1980-81-82-83, c. 48. s.40(1).

⁸ The cases on partnership are discussed in "Helping Out", supra note 1.

⁹ s.67 limits the deduction of any expense to a "reasonable" amount.

¹⁰ K. Lahey, at *The Benefit/Penalty Unit in Income Tax Policy: Diversity and Reform* (Law Commission of Canada, September 18, 2000), at 97-98.

contributions to market production. This too can attract adverse tax consequences. Canada's income tax is based on individual filing and the statute includes several anti-avoidance rules designed to prevent taxpayers from shifting income to a spouse or child who is taxed in a lower rate bracket. I have argued elsewhere in favour of reforming these rules to incentivize genuine transfers of legal control over property to a spouse (defined in Canada to include common law and same sex partners).¹¹

The decision to pay an informal family worker also engages various payroll tax regimes, for example the requirement to pay Employment Insurance premiums and Canada or Quebec Pension Plan contributions. While these taxes might themselves operate as disincentives to formalizing the employment of a family member, they could also have the opposite effect. Making such contributions provides the worker with access to a safety net of public benefits, including parental leave, sick leave and compassionate care leave which in Canada are delivered through the Employment Insurance system. However like income tax law, the EI legislation regards family workers with suspicion. The statute deems a worker to be unqualified for benefits "if the employer and employee are not dealing with each other at arm's length", unless,

...the Minister of National Revenue is satisfied that, having regard to all the circumstances of the employment, including the remuneration paid, the terms and conditions, the duration and the nature and importance of the work performed, it is reasonable to conclude that they would have entered into a substantially similar contract of employment if they had been dealing with each other at arm's length.¹²

For these purposes "non-arm's length" is defined broadly to include both legally married and common law spouses (same sex or opposite sex), parents and children, siblings, and certain other relatives.

A preliminary review of cases which apply this provision indicates that tax authorities (who administer the EI regime) can be aggressive in denying coverage to family workers on the basis that their relationship with the employer is irregular, undocumented, or somehow different than what an arm's length employee would normally expect, for example because wages are paid into a joint account owned with the employer.¹³ Though there is some chance of having a denial of coverage overturned by a court, it must be assumed that some family workers do not bother to appeal. Moreover some judges maintain the same skeptical attitude toward family workers as do the tax authorities. Whether some families choose not to pay EI premiums at all because of the risk of such a challenge is harder to assess.

Concluding Thoughts and Future Research

¹¹ See "Income Splitting and Gender Equality", note 1.

¹² Employment Insurance Act, S.C. 1996, c. 23, ss.5(2)(i) and 5(3)(b).

¹³ See for example *Al-Haddadin v. Canada* [2000] TCJ No. 512 (Tax Court of Canada); *Yaskiw v. Canada* [2000] TCJ No.424; and *Yazdani v. Canada* [2000] TCJ No.538.

There is a consistent thread of suspicion toward informal family workers in both tax law and employment insurance law in Canada, with policy being oriented primarily towards prevention of fraud and abuse. This policy orientation may reflect a background assumption that legitimate informal family workers are only a tiny group that plays a marginal role in production, with virtually all market labour being provided outside the household. I have suggested here and elsewhere that this assumption reflects ideological and possibly outdated understandings of the nature of production in modern industrialized economies.

Discerning the regulatory effects of these legal presumptions is not a simple task. One method of tracking impacts is to analyze the outcomes of litigated disputes. Thus I hope to follow this draft with a more thorough analysis of the case law on when a family worker is considered to be in “insurable employment”. A clear pattern in the statutory law and decided cases might enable some inferences about the likely behaviour of others who are bargaining in the shadow of the law.