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CPA
Exam

INTEGRATED TAXMAP

2019 EDITION
(CPA EXAM)

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MENTION AU
CONCOURS PRIX DU MINISTRE



Prix d'excellence
en enseignement
(volet réalisation)



PRIX EXCELLENCE CPA
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CPA
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2019 EDITION
(CPA EXAM)

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Foreword

For the time being, the *Integrated TaxMap* consist of a vision that tax professors have regarding the preparation of tax students for the entrance exams to the Professional Accounting Orders, more precisely, the *Common Final Examination* (CFE) for students seeking to obtain the CPA designation. From this common vision arises an integration plan (which includes a prior review) of taxation in the academic career of graduate-level university students.



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Preparation for the Common Final Examination (CFE) - Introduction

Level of competency (A-B-C)

The contents of this volume covers all tax knowledge (related to the competency) required for new CPA candidates.

Specifically, the content covers and identifies all the required knowledge in the path of a CPA candidate who chooses the elective module "Taxation", as provided for in the CPA Professional Education Program.

CPA tags are used in the volume in order to inform the student of the master's level required for each of the topics. These tags make reference to the document *Related knowledge Guide to CPA Competency Map* issued by CPA Canada.

CPA
Core
Level A

CPA
Core
Level B

CPA
Core
Level C

CPA
Core
Not Required

Competency	Entry	Core		Core	Electives			
		C1	C2		E1 PM	E2 FIN	E3 AS	E4 TAX
TECHNICAL COMPETENCIES								
1. FINANCIAL REPORTING								
1.1 Financial Reporting Needs and Systems								
1.1.1	Evaluates financial reporting needs	B	A	A				
1.1.2	Evaluates the appropriateness of the basis of financial reporting	B	A	A				
1.1.3	Evaluates reporting processes to support reliable financial reporting	B	A	A				
1.1.4	Explains implications of current trends and emerging issues in financial reporting	C	C	C			B	
1.1.5	Identifies financial reporting needs for the public sector	C	C	C				
1.1.6	Identifies specialized financial reporting requirements for specified regulatory and other filing requirements	—	C	C				
1.2 Accounting Policies and Transactions								
1.2.1	Develops or evaluates appropriate accounting policies and procedures	B	A	A			A	
1.2.2	Evaluates treatment for routine transactions	A	A	A			A	

CPA
Elective
Level A

CPA
Elective
Level B

CPA
Elective
Level C

Tax structures and reflection methods

Compliance

- Tax – Who
- Tax – What
- Calculation of income (inclusions - deductions)
- Calculation of taxable income (deductions)
- Calculation of tax (rates, credits)
- Type of taxpayers (corporation, individual)

Tax planning

1- Tax exemption

- CGD (\$866,912 of capital gain (CG))
- Death benefit (\$10,000 of employment income)
- Reimbursement of the eligible housing loss by the employer (\$15,000 of employment income)

2- Reductions/Tax savings

- Taxable capital gain (TCG) (50% of the profit)
- Stock options (SO) (50% of the profit)
- Reimbursement of the eligible housing loss by the employer (excess of \$15,000: 50% of profit)

3- Income splitting

- Between related individuals (adult children specifically)
- Between the principal shareholder and his/her family (reasonable salary, dividend)
- Contribution to the spouse's RRSP (if lower income)
- Take heed of attribution rules
- Pension income splitting

4- Tax deferral

- Year-end bonus (declared and unpaid: deferral by one year)
- Contribute to the spouse's RRSP (if younger)
- Capital gains reserve (over 5 years)
- Tax-rollover transactions

Principles*Impossible to bypass the integration principle*

Receipt of \$866,912 exempt from capital gains without selling shares externally
(from the corporation's internal liquidities)

No double taxation

- Between 2 countries: Canadian tax paid vs. foreign tax paid (foreign tax credit)
- Between 2 taxpayers: corporate taxable income vs. individual taxable dividend
- Between 2 sub-sections of the Act: deemed dividend on share redemptions vs. proceeds of disposition upon disposition of shares

Very rare non-taxable amounts

- Life insurance payment (not treated as income)
- Lottery winnings
- Patrimony
- 50% capital gain

New knowledge (update)

The updated 2018 Integrated Taxmap takes into account the tax measures announced as of December 31, 2018 (in accordance with CPA Canada requirements).

Taxation of dividend :

	Non-Eligible dividend		Eligible dividend	
	Gross-up	Tax credit	Gross-up	Tax credit
2016 and 2017	17 %	10.5 %	38 %	15 %
2018	16 %	10 %	38 %	15 %
2019	15 %	9 %	38 %	15 %

Reducing the second personal income tax rate to 20.5 % from 22 %. This will take effect on January 1st, 2016 and for subsequent taxation years.

Introducing a 33 % personal income tax rate on individual taxable income in excess of \$210,371 in 2019, effective for the 2016 and subsequent taxation years :

- Impact on the calculation of the donation credit
- Impact on the tax of split income (kiddie tax)

Effective on January 1st, 2019, the small business tax rate is reduced to 9 %. (the small deduction is increased to 19 %)

Budget 2017 proposes to eliminate the ability for designated professionals to elect to use billed-basis accounting for taxation years that begin after March 22, 2017

Effective on January 1st, 2016, increase of the rate applicable to the investment income of private corporations:

- the refundable additional Part I tax on investment income of Canadian-controlled private corporations (CCPCs) will be increased by 4 percentage points (to 10.67 per cent from 6.67 per cent);
- the refundable portion of Part I tax on investment income of CCPCs will be increased by 4 percentage points (to 30.67 per cent from 26.67 per cent);
- the refundable Part IV tax on portfolio dividends received by private corporations will be increased by 5 percentage points (to 38.33 per cent from 33.33 per cent); and
- the rate at which refunds are made out of a private corporation's pool of refundable taxes previously paid (known as "Refundable Dividend Tax on Hand") when it pays dividends will be increased by 5 percentage points (to 38.33 per cent from 33.33 per cent of dividends paid).

Beginning January 2017, a new class (14.1) of depreciable property for CCA purposes is created and will replace the CEC deduction:

- CEC pool balances is calculated and transferred to the new CCA class. The depreciation rate for the amount transferred is 7 %.
- The existing CCA rules will generally apply, including rules relating to recapture, capital gains and depreciation (e.g., the "half-year rule")
- New capital expenses will be included at 100 % for depreciation
- New capital expenses have a 5 % annual depreciation rate

Elimination of personal tax credits since 2017 :

- Education and textook tax crédits
- Children's Fitness and Arts Tax credits
- Public transit Tax credit (effective as of July 1, 2017)

Beginning January 2018, the deduction in respect of eligible home relocation loans will be eliminated (25 000 \$ x prescribed rate)

Effective January 1, 2018, amendment to the rules on the tax on split income:

Before 2018: the split income tax (33%) apply if a minor child receives:

- A taxable dividend from a private company;
- Income from a partnership or trust in which a related person actively participates

After January 1, 2018: Extending the application to the rules on the tax on split income to individuals 18 years of age and over when the dividend is received from a corporation of which a family member is a shareholder or an officer.

Exceptions apply in certain circumstances:

- Some shares are excluded if:
 - Participation of more than 10% in votes and value;
 - The individual is 25 years of age or older;
 - less than 90% of revenues come from services
- Some businesses are excluded (the individual works an average of 20 hours per week)
- Some individuals are excluded (the spouse is 65 years old and over)
- The dividend does not come from a reasonable return related to an investment.

Related persons, Associated corporations, Affiliated persons, Connected persons

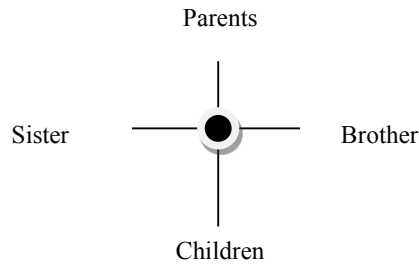
Related Persons

Applies everywhere in the Act...

Transfer at FMV between related persons, otherwise...double taxation

An individual is related to

- parents, brother/sister and children (PLUS all of the spouses, PLUS all of the corporations controlled by these individuals):
- parents, brother/sister and children of his/her spouse (PLUS all of the spouses, PLUS all of the corporations controlled by these individuals):



Associated Corporations

Allocation of the small business limit (i.e.: SBD) of \$500,000

Allocation of the R&D expense limit of \$3,000,000

Concept applicable only to corporations: controlled by the same person, group of persons, etc.

Connected Corporations

For the purposes of calculating Part IV Tax related to a dividend received from a taxable Canadian corporation (TCC)

- The corporation that receives the dividend holds the issued share capital of the payer corporation representing:
 - o More than 10 % of the voting shares AND
 - o More than 10 % of the FMV of all of the outstanding shares

OR

- The payer corporation is controlled by the receiving corporation

For the application of connected corporations: a corporation is controlled by another corporation if more than 50% of the voting shares is held by the receiving corporation and/or the people related to it



Affiliated Persons

Essentially to deny losses realized between affiliated persons

‘I am affiliated to myself, my spouse and to a company controlled by myself or my spouse’



No capital losses on:

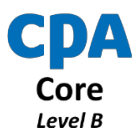
Superficial losses between affiliated persons (tax loss selling, concept of holding + 30 days and - 30 days).

As a summary:

Loss disposition between affiliated persons (type of property)	Effects if the vendor is an individual	Effects if the vendor is not an individual
Non-depreciable property	Disallowed capital loss The loss increases the property’s ACB for the purchaser	Disallowed capital loss The vendor keeps the loss. The loss can be used once the property is resold to a non-affiliated person.
Depreciable property	Disallowed terminal loss The vendor is deemed to have acquired a depreciable property for a value that is equal to the amount of the disallowed terminal loss	
Shares (upon redemption by a corporation)	Disallowed capital loss The ACB of the vendor’s remaining shares increase by the amount of the loss.	

Other situations where capital losses are denied:

- Disposition of depreciable assets and eligible capital assets
- Disposition of personal use property
- Disposition of accounts receivable in certain circumstances



Transfer of property between related parties



General rule: transfer always done at FMV between individuals dealing at non-arm's length

Otherwise: double taxation possible (except in the case of a donation)

Exceptions:

- Transfer to a spouse (deemed disposition and acquisition at the cost amount (mandatory rollover))
- Possible election at FMV
- Tax free rollover (85 ITA) to a corporation

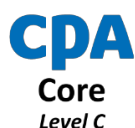
Attribution rules: applies to loans and transfers (including donations) between related persons whose goal is to reduce/avoid taxes

Effects: reattribution of property income

Transfer to a spouse	Transfer to a minor child (including nephews and nieces)
Reattribution of property income	Reattribution of property income
Reattribution of capital gain (CGD available)	NO capital gain reattribution
	Tax on split income (33 %) (Kiddie Tax): Maximum tax rate for children (to dividend income received by a minor child from a private corporation and business and rental income received from related partnership or trust) See new rules on Page 6 related to Tax on split income to individual 18 years of age and over
Loan or transfer to a corporation that does not qualify as a qualified small business corporation and where the spouse/minor child have over 10 % of the shares Benefit for the transferor: (FMV of the property x prescribed rate) – (interest and taxable dividends received)	

Non-applicable where:

- The property loaned/transferred generates business income
- Transfer done at FMV:
If the consideration includes a debt, it must bear interest at the prescribed rate and the interest must be paid
- Income from the spouse's TFSA
- Universal child care benefit (UCCB) deposited in the child's bank account
- Death or divorce triggers an end to attribution rules
- Income on income (2nd generation income)





Individual taxes



- 3a) Employment income, business income, property and other income
- 3b) TCG – ACL
- 3c) Other deductions for individuals (RRSP, childcare expenses, relocation expenses, pension supplement, etc.)
- 3d) Employment loss, business loss, property loss and business investment loss

Income

Deduction from taxable income:

Net capital losses, Non-capital losses

CGD

Stock option deduction, home relocation loan, etc.

Taxable income

Calculation of tax

Tax rate (15 %, 20.5 %, 26 %, 29 %, 33 %) x Taxable income =	XX
Application of personal tax credits	<u>(XX)</u>
- Spouse, equivalent, dependent, handicap, retirement, medical, adoption, donations, dividend, home buyer’s amount, employment	
- Education tax credits (tuition fees and interest)	
- Credit for EI, CPP or QPP	
- Etc.	
	<i>Basic federal tax</i> XX
Provincial tax abatement (if applicable) 16.5 % x Basic federal tax	(XX)
Application of other tax credits (foreign tax, political contributions)	<u>(XX)</u>
	<i>Taxes payable (refundable)</i> XX
Tax withheld	<u>(XX)</u>
	<u>Balance payable (receivable)</u> <u>XX</u>

2nd tax calculation possibly applicable:

Alternative Minimum tax

Important to know when to apply the AMT

When the CGD is claimed

Remuneration of an employee

Employment income: general rule, taxation on a cash basis.

Taxable benefits (compliance)

All benefits employees receive by virtue of their employment represent a taxable benefit, particularly:

What constitutes a taxable benefit:

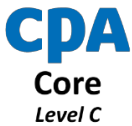
- Living expenses
- Director’s or other fees
- Use of an employer’s car
 - o Interest free or low interest loans
Capital of loan x (prescribed rate – interest paid)
 - o Home purchase loan: the prescribed rate is capped for 5 years
- Stock options:

Calculation of the benefit	Inclusion of the benefit	Possible deduction of 50% of the taxable benefit (in TI)
FMV of shares when exercised LESS: Price paid for shares LESS: Price paid for options	CCPC employees: when the shares are sold	CCPC employees: Shares held for at least 2 years OR No preferential price when option is granted
Taxable benefit increases the ACB of shares acquired	Other employees: when options are exercised	Other employees: No preferential price when option is granted

- Membership in a health club
- Lump-sum car allowance
- Donations of supplies manufactured by the employer (the taxable benefit represents the cost for the employer)

What does not represent a taxable benefit:

- Payment of professional dues (if primarily for the employer's benefit)
- Payment of tuition fees (if primarily for the employer's benefit)
- Payment for group insurance plan
- Reasonable car allowance if based on KM travelled by the employee
- Gifts and rewards (non-monetary, maximum of \$500)
- Employer's contribution to employee's RPP
- Retirement and mental health referral service

**Favourable remuneration for the employee (tax planning)**

Suggestions of preferential treatment for the employee:

Tax exemptions

- For death benefit of \$10,000 (non taxable for the estate)
- For a reasonable car allowance for travel expenses (based on KM)

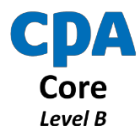
Reductions/Tax savings

- Loan to employee: very low prescribed rate; few taxable benefits
 - o Home purchase loan: the prescribed rate has a five-year ceiling
- Stock options: if eligible for the TI deduction, 50 % taxation on the gain

Tax deferral

- Employer's contribution to the RPP or DPSP for the employee's account
- Retirement allowance paid to the employee: possibility of transferring to the RRSP
 - o \$2,000 per year of employment prior to 1996
 - o (+) \$1,500 per year of employment year prior to 1989, if no RPP or RRSP to the benefit of the employee during these years
- Stock options: if a CCPC employee, deferral of the taxable benefit





Deductions for employees



Expenses incurred by an employee to earn employment income

The employer must confirm (Form T2200) that the employee is required to pay his/her employment expenses

The main deductions:

- Professional membership dues
- Union dues
- Registered pension plan contributions made by the employer
- Reasonable travel expenses (lodging, meals and transportation):
 - o Not reimbursed by the employer through a non-taxable allowance
 - o Meals: 50 % deductible if outside of the city for at least 12 hours
 - o Automobile expenses: all of the expenses related to the annual use of an automobile are deductible prorated based on the KMs travelled for employment purposes (over the total KMs travelled in the year)

TAKE HEED of the limits:

 - Lease: \$800/month
 - Purchase: \$30,000 (maximum CCA, passenger vehicle Class 10.1)
 - Interest on loan: \$300/month
- Home office:
 - o Principal place of employment OR
 - o Used exclusively for meeting clients/patients

All of the expenses related to the annual use of the residence² are deductible at the prorated percentage of the area occupied by the office space (over the total area of the residence)

The deduction is limited to employment income for the year (cannot result in an employment loss) – excess expenses may be carried forward to other years

Commission salespeople - **CHOICE** to:

- o Deduct expenses like other employees
LESS deductible expenses – NO limits on expenses
- OR**
- o Deduct expenses as if he/she were a self-employed worker
MORE deductible expenses – LIMITED to commission income

² Rent, repairs, heating and electricity. Property taxes and insurance are eligible for this calculation exclusively for a commission salesperson who elects to deduct his/her expenses by virtue of 8(1)f – limited to commission income

Automobiles

CPA
Core
Level B

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Elective
Level A

Tax impact for employees who use an automobile for employment purposes:

INCLUSION in employment income

An allowance is considered as a taxable benefit except when:

- A reasonable allowance is received by an employee for personal use of his/her automobile for employment purposes = NON TAXABLE – 6(1)b)(v), 6(1)b)(vii.1)

Reasonable:

- o \$0.58 for the first 5,000 KMs travelled by the employee
- o \$0.52 for each additional kilometre

Automobile made available to an employee by the employer = TAXABLE

- o Calculation of the standby charge – 6(1)e), 6(2)
- o Calculation of vehicle operating expenses – 6(1)k)

DEDUCTION from employment income

- The employee uses his personal automobile for employment purposes = DEDUCTIBLE – 8(1)h.1)
 - o Calculation of annual automobile expenses prorated based on the business-use portion of the distance travelled
 - o Maximum: lease expenses (\$800), CCA (\$30,000) and interest (\$300)

Tax impact of use an automobile in connection with its activities (business):

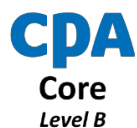
DEDUCTION against business income

- An entrepreneur uses his/her own automobile for business purposes = DEDUCTIBLE – 18(1)h)
 - o Calculation of annual automobile expenses prorated based on the business-use portion of the distance travelled
 - o Maximum: lease expenses (\$800), CCA (\$30,000) and interest (\$300)
- The corporation pays the employee a reasonable allowance so that the employee can use his/her own automobile for employment purposes = DEDUCTIBLE

Reasonable:

 - o \$0.58 for the first 5,000 KMs travelled by the employee
 - o \$0.52 for each additional kilometre
- Automobile made available to an employee by the employer = DEDUCTIBLE
 - o All of the expenses incurred to operate the automobiles made available to employees is deductible
 - o Maximum: lease expenses (\$800), CCA (\$30,000) and interest (\$300)

Automobile Supplied by an Employer		Automobile Supplied by the Employee															
Calculation of the taxable benefit		Calculation of the taxable allowance and the deduction for the employee															
<p><i>Employer is renting the automobile</i></p> <p><u>Automobile standby charge</u></p> <p>(i) Reasonable standby charge</p> <p><i>minus:</i></p> <p>(ii) any reimbursements by the employee</p> <p>Calculation of the standby charge</p> $\frac{*A}{B} \times \frac{2}{3} \times (\text{Annual leasing costs} (-) \text{insurance costs})$ <p>A= lesser of km for personal use or B B= 1 667 km x month</p> <p><u>Automobile operating cost benefit</u></p> <p>Formula A - B</p> <p>A=</p> <p>** 1/2 of the standby charge</p> <p>or</p> <p>0.28 \$ /km x km personal use</p> <p><i>minus:</i></p> <p>B= any reimbursements by the employee</p>		<p><i>Employer purchased the automobile</i></p> <p><u>Automobile standby charge</u></p> <p>(i) Reasonable standby charge</p> <p><i>minus:</i></p> <p>(ii) any reimbursements by the employee</p> <p>Calculation of the standby charge</p> $\frac{*A}{B} \times 2\% \times \text{Cost of the automobile} \times \text{number of months}$ <p>A= lesser of km for personal use or B B= 1 667 km x month</p> <p><u>Automobile operating cost benefit</u></p> <p>Formula A - B</p> <p>A=</p> <p>** 1/2 of the standby charge</p> <p>or</p> <p>0.28 \$ /km x km personal use</p> <p><i>minus:</i></p> <p>B= any reimbursements by the employee</p>				<p><i>Allowance received by the employee</i></p> <table border="1"> <tr> <td>Monthly fixed allowance</td> <td>Non-reasonable per-kilometre allowance</td> <td>No allowance</td> <td>Reasonable per-kilometre allowance ***</td> </tr> <tr> <td>Taxable</td> <td>Taxable</td> <td>Non-taxable</td> <td>Non-taxable</td> </tr> </table>				Monthly fixed allowance	Non-reasonable per-kilometre allowance	No allowance	Reasonable per-kilometre allowance ***	Taxable	Taxable	Non-taxable	Non-taxable
Monthly fixed allowance	Non-reasonable per-kilometre allowance	No allowance	Reasonable per-kilometre allowance ***														
Taxable	Taxable	Non-taxable	Non-taxable														
Calculation of the taxable benefit		<p><i>Deduction of automobile expenses paid by the employee</i></p> <p>Calculation of the expenses deductible:</p> <ul style="list-style-type: none"> - Fuel - license and registration fees - Maintenance and repairs - Assurance - Etc. - leasing costs (Max: 800 \$ per month) - CCA on automobile (Max : 30 000 \$) - Eligible interest (Max: 300 \$ per month) <p>X KM earning income / KM TOTAL</p> <p>- parking</p> <p>Expenses cannot be deducted</p> <p>(if the allowance is lower than the expenses deductible, the employee could deduct the expenses and be taxed on the allowance, for a net deduction)</p>															
<p>* $\frac{A}{B}$ = 1 when the automobile is not primarily used in the employee's duties</p> <p>** Can be considered only if the automobile is primarily used in the employee's duties</p>		<p>*** The allowance is deemed to be reasonable when:</p> <p>0.58 \$ for the 5 000 first km driven</p> <p>0.52 \$ for each additional kilometre</p>															



Other income



- Pension income (QPP, CPP, RPP, old age pension (OAP))
- RRSP withdrawal
- Employment insurance contributions
- Social assistance payment (deductible in calculating taxable income)
- Workplace accident compensation (deductible in calculating taxable income)
- Scholarships and fellowships:
 - o No taxation if the scholarship is related to a recognized study program
- Annuity received:
 - o Inclusion of the annuity amount (capital portion and interest)
 - o Deduction of capital portion
- Retirement allowance: amount paid by the former employer and:
 - o in recognition of long-standing service at retirement OR
 - o in connection with a job loss

Deduction for the portion of the allowance transferred to the RRSP or the RPP:

- o \$2,000 per year of employment before 1996
- o (+)\$1,500 per year of employment before 1989 if not RPP to benefit the employee for these years
- Death benefit: amounts paid out by former employer following the death of an employee.
 - \$10,000 exemption for the beneficiaries:
 - o It is mandatory to attribute the exemption to the spouse
 - o The other beneficiaries use the remaining balance of the exemption on a prorated basis, based on the amount of the benefit received by each beneficiary
- Reattribution of pension income split: a spouse may attribute pension income to the other spouse (max. = 50% of pension income):
 - o Before 65: eligible on income from an RPP
 - o After 65: eligible on income from an RPP and an RRSP
 - o Canadian Pension Plan and Old Age Security Pension: not eligible for income splitting



Deferred income plans



Think of deferred income plans as a tax planning strategy (tax deferral)

RRSP

Functioning

A = Unused RRSP contribution from previous years
 (+)
 B = lesser of:
 - 18% of the *earned income* in the previous year
 - RRSP ceiling for the year (\$26,500 in 2019)
 Less: the PA of the previous year attributed to the individual

Income splitting

Contribution to the spouse's RRSP: held for at least three consecutive December 31st (otherwise, contributor taxed on withdrawals)

If over 65, the RRSP withdrawal is considered as a defined pension income and is, therefore, eligible for pension income splitting

Possible income splitting between spouses since 2007

Spouses can pool all of their retirement income (eligible for the pension income tax credit) and split them, at their convenience (maximum 50%), between both tax returns.

Maturity of RRSP (at age 71)

- Purchase of a security
- Transfer into an RRIF: minimum withdrawal mandatory
- RRSP withdrawal: fully taxed

RPP (defined contribution vs. defined benefit)

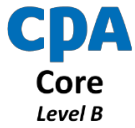
- Employee contribution: deductible
- Employer contribution: Not taxable
- Impact on the calculation of the pension adjustment (PA)

TFSA

- Maximum annual contribution of \$6,000 for 2019, if 18 and over
- No deduction or inclusion in income
- TFSA withdrawals become new contribution room the following year

RESP

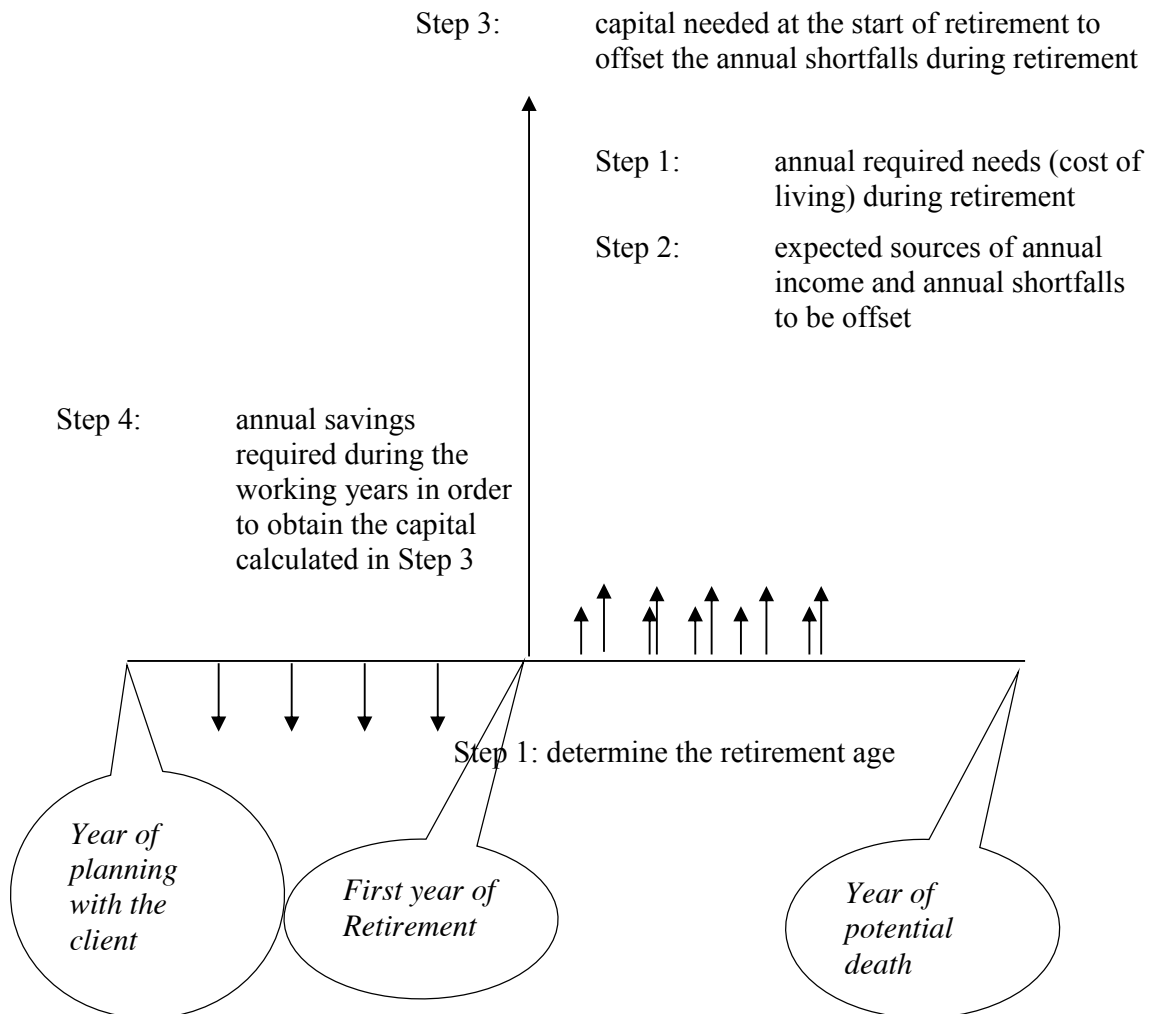
- Federal grant equal to 20 % of contributions, maximum of \$500/year
- Maximum \$50,000 contribution per beneficiary
- Income taxable (for the student) when funds are withdrawn



Personal financial planning



- 1. Determining annual needs (cost of living) during retirement**
 - Define the desired retirement age
 - Determine the desired quality of life during retirement
 - Index the desired quality of life until retirement age
- 2. Determine the annual sources of income available during retirement and determine the annual shortfall (if needed)**
- 3. Determine the retirement capital needed at the start of retirement in order to offset the annual shortfall**
- 4. Annual savings required before retirement in order to obtain the retirement capital needed at the start of retirement**



Corporate income tax

ITA Part I Tax (2018)

Taxable income	
Basic federal tax amount	38 %
Federal abatement	(10 %)
Sub-total	28 %

Active Business Income			Investment income ³	Dividend from Taxable Canadian Corporation (TCC)
SBD ⁴ (over \$500,000 shareable)	M&P income (N/A)	Other corporate income ⁵	Refundable tax on the Taxable Investment Income	
(19 %)	(13 %)	(13 %)	10.67 %	Deductible from TI
9 %	15 %	15 %	38.67 %	0 %

Less:

- Foreign tax credit
- Investment tax credit

To perform a general tax calculation, add the provincial component.

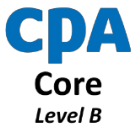
Part IV Tax (private corporation)

Calculation of Part IV tax	
Dividend received from non-connected corporation (TCC)	38.33 % of dividend received
Dividend received from connected corporation (TCC)	Dividend refund received by payer corporation X <u>Dividend received</u> Total dividend paid by the payer corporation

³ Includes in particular: interest, royalty, copyrights, revenue property, foreign dividend, taxable capital gain net of the capital loss deductible and net capital loss deducted during the year

⁴ CCPC only

⁵ The Personal Services Business income is not eligible for the general rate reduction of 13 %.

***RDTOH (private corporation)***

Beginning balance (RDTOH of at the end of the previous tax year)

(-) Dividend Refund of preceding year

(+) Refundable portion of Part I Tax⁶ of current year: 30.67 % of total investment income

(+) Part IV tax of the current year

RDTOH year-end balance

Dividend Refund (private corporation)

38.33 % of the dividend paid during the year

Max: RDTOH end of year balance

Capital dividend account (private corporation)

(+) Life insurance revenue received

(+) 50 % of CG (-) 50 % of CL

(+) Capital dividends received

(-) Capital dividends paid



⁶ *Ibid*



Scientific Research and Experimental Development (SR&ED)



Eligible SR&ED projects

- | | |
|----------------------------|------------------|
| - Experimental development | - Basic research |
| - Applied research | - Support work |

1- SR&ED expense account (T-661)

Account used to tally eligible SR&ED expenses so that they may be deducted against general business income when needed (no deadline)

Eligible expenses:

- Current expenses attributable to 90% or more of expenses related to performing SR&ED activities:
 - o Salary or wages incurred
 - o Cost of materials consumed and transformed
 - o Lease costs of equipment used
 - o Cost of third-party contracts
 - o Overhead

LESS: ITC claimed in the previous year

2- Investment tax credit (ITC)

15% rate ⁷	35% rate
CCPC: eligible expenses in excess of the expense limit attributable to a corporation (\$3,000,000)	CCPC: eligible expenses that do not exceed the limit of expenses attributable to the corporation (\$3,000,000)
Other corporations: all eligible expenses	

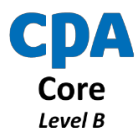
Expense limit: \$3,000,000 must be allocated between associated corporations
Reduction of the limit of expenses for a group of associated corporations:

Taxable income of the group of associated corporations for the previous year	\$500,000 and less	\$600,000	\$700,000	\$800,000 and more
Expense limit for the group	\$3,000,000	\$2,000,000	\$1,000,000	\$0

Mandatory use of ITC

1. Reduction of taxes payable under Part I
2. Refund of a portion of the remaining ITC (for CCPCs only)
3. Carryforward/Carryback of the remaining ITC against Part I taxes (-3, +20 years)

⁷ 20 % for the taxation year ending before 2014



GRIP/LRIP



For a CCPC

By default, a CCPC will pay a non-eligible *dividend*, unless where there is a GRIP balance

The GRIP includes:

- Business income taxed at the general rate (does not include the total investment income)
- Eligible dividend received from another corporation

The GRIP makes it possible to pay an eligible dividend:

- Grossed-up by **38 %** for the individual
- **15 %** dividend tax credit for the individual

Non-CCPC

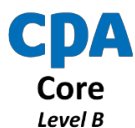
By default, a non-CCPC will pay an eligible dividend, except where there is a LRIP balance

The LRIP includes:

- Non-eligible dividend received from another corporation

A LRIP balance requires the corporation to pay non-eligible dividends equal to the LRIP:

- Grossed-up dividend of **15 %** for the individual
- **9 %** dividend tax credit for the individual



Employee or self-employed worker



Employee or self-employed worker?

1. Master/servant relationship: subordination in the performance of the work (location and work schedule, work responsibility)
2. The financial and economic criterion (risk of loss or profit)
3. Specific result of the work (worker carries out a specific assignment)
4. Integration of the tasks carried out by the worker (one or many clients)
5. Ownership of the tools

Risk: employee vs. self-employed worker status

For the employer: required to remit employer/employee source deductions (EI, QPP/CPP, QPIP)

For the employee: more deductible expenses if considered a self-employed worker

Personal Services Business (PSB)

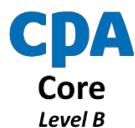
An incorporated employee

Consequence of being a corporation that is a PSB:

- Business income does not qualify as ABI, therefore, no SBD
- All expenses are non-deductible except for:
 - o Salary paid to the shareholder
 - o Operating expenses, if such expenses were deductible from a salary

Exception to the PSB qualification: if corporation has more than 5 full-time employees

The personal services business income is not eligible for the general rate reduction and an additional tax of 5 % is payable. Therefore, the federal tax rate equals to 33 %. (+ a provincial component)



Business income/property income



Active vs. passive business income

General rule to determine deductibility of an expense:

- Must be reasonable
- Must be incurred to earn business or property income:
 - o EXCEPT for a capital expense (non deductible)
 - o Excluding personal expenses (non deductible)

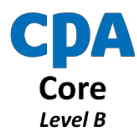
Accounting to tax income reconciliation

- Entertainment expenses (meals, drinks, entertainment): 50% non deductible (golf: 100% non deductible)
- Clubs dues are not deductible (fitness centre, golf club)
- Convention expenses: limit of 2 per year (\$50 per diem meal expense if included in convention price)
- Discretionary tax CCA vs. accounting depreciation
- Accounting gain/loss on disposal of asset vs. taxable capital gain (at 50%)/ recapture/terminal loss
- Incorporation and share capital reorganization expenses for corporations (Class 14.1 since January 2017)
- Accounting provisions (restructuring expenses, write-off, etc.): non deductible
- Deductible tax reserves:
 - o Bad debts: if account by account analysis
 - o Instalment sale (allowance where certain payments are required 2 years and more from the date of sale)
- Home office:
 - Principal place of business OR
 - Used exclusively to meet clients/patients

All of the expenses related to the annual use of the residence are deductible prorated based on the surface area occupied by the home office (over the total area of the residence)

The deduction is limited to the business income for the year (cannot give rise to a business loss) – carry forward of excess expenses to subsequent years

- Capital gain (CG): inclusion at 50% and capital gains reserve possible (minimum 20% taxation of CG/year)
- Declared but unpaid bonus: must be paid within 6 months following the end of the tax year in order to be deductible during the year (otherwise, deductible when paid)
- Withholdings on contracts (construction): not income earned for tax purposes
- Lease-breaking agreement fees by the owner: amortized over the remaining lease term (max. 40 years)
- Representation expenses, location search, public utility connections: deductible in business income
- Financing expenses for issuing debts or shares:
 - o Accounting: capitalize and amortize over the loan term
 - o Taxation: deductible on a straight-line basis over 5 years
- Capital Lease
 - o Accounting: capitalization and amortization
 - o Taxation: the lease payment is deductible on cash basis (legal reality)
- Interest in a partnership/business corporation
 - o Accounting:
 - Partnership: The taxpayer accounts for its pro-rata share of the accounting profit of the partnership
 - Corporation: The taxpayer accounts for its pro-rata share of the corporation profit when the equity accounting method is used
 - o Taxation:
 - Partnership: attribution of taxable income to partners based on ownership percentage (unit holders)
 - Corporation: is considered a separate taxpayer (income tax return and payment of taxes by the corporation)



Property income



Dividend income

Individual: Dividend gross-up and tax credit:

- Eligible dividend: 38 % + 15 % dividend tax credit
- Non-eligible dividend: 15 % + 9 % dividend tax credit

Corporation:

- Dividend received from a taxable Canadian corporation (TCC):
 - o taxable but fully deductible in the calculation of taxable income
 - o application of Part IV tax
- Dividend received from a foreign corporation :
 - o considered as investment income
 - o foreign tax credit available

Interest income

Individual:

- Interest must be included when received (cash basis)
- Investments whose interests are payable at intervals of more than one year: inclusion on the annual anniversary date of the investment

Company:

- Interest must be included when earned (accrual basis) – take heed of accrued interest (to be included)

Rental income

- Rental income must be included when earned (accrual basis) – take heed of prepaid rent collected (to be excluded)
- Deductible expenses: insurance, property tax, loan interest, repairs and maintenance, CCA, advertising, utilities that are the owner's responsibility, etc.
- Take heed: cannot create or increase a rental loss with the CCA

Attribution rules

Always verify the possible application of **attribution rules** where there is a property transfer (which generates investment income) between related persons



Core
Level B

Property income: deductions and restrictions



Elective
Level A

Interest deductible: interest paid or payable related to an amount that is borrowed and used to:

- acquire a revenue-producing property (purpose test)
- generate revenue from a property or business (purpose test)

Non-deductible interest:

- Interest paid or payable relating to a borrowed amount used to contribute to an RRSP, OAP, DPSP or a TFSA
- Interest paid relating to tax arrears (same treatment for a penalty paid)

Expenses related to loan and share issue expenses:

Deductible over 5 years, 20 % per year:

- Expenses of issuing shares
- Borrowing costs

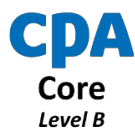
Interest and property taxes on real property:

If the land is not held primarily to generate revenue (vacant land), these expenses are deductible in part during the year:

- Up to the amount of revenue (net of other deductible expenses) generated by the land
- Portion of expense exceeding the revenue is added to the adjusted cost base (ACB) of the land

Foreign tax paid:

- Foreign tax credit paid (maximum tax credit of 15 % of foreign income for an individual)
- Any remaining foreign tax credit portion is deductible in the calculation of the income.



Capital assets



Current vs. Capital expenses (restoration vs. improvement)

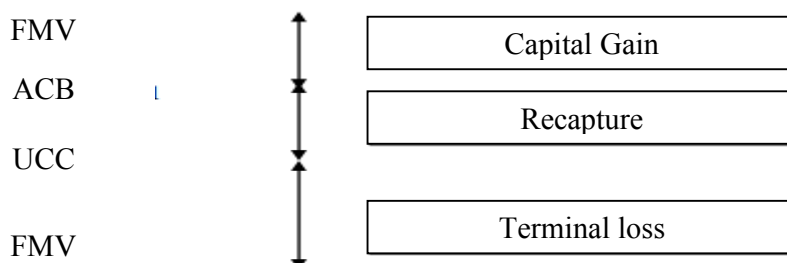
CCA: Always a discretionary expense

Available for use rule to claim the CCA

Half-year rule: on the net acquisitions for the year (except where acquired from a related party who was already subject to the half-year rule)

Taxation year of less than 12 months: CCA is prorated

Depreciable property



Rental property (particularities)

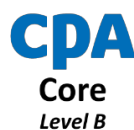
- Separate class if cost is over \$50,000
- Loss restrictions on the CCA (cannot create a loss with CCA)

Replacement property (involuntary disposal)

Deferral of the recapture and capital gain possible if a replacement property has been acquired before the end of the 2nd taxation year following the year of involuntary disposition

Eligible capital property (unlimited patent, goodwill acquired, organization and reorganization costs, etc.)

- Beginning January 2017, a new class (14.1) of depreciable property for CCA purposes will be introduced
- CEC pool balances will be calculated and transferred to the new CCA class. The depreciation rate for the amount transferred is 7 %.
- The existing CCA rules will generally apply, including rules relating to recapture, capital gains and depreciation (e.g., the “half-year rule”)
- New capital expenses will be included at 100 % for depreciation
- New capital expenses have a 5 % annual depreciation rate

Capital gain**Capital gain vs. Business income**

Intention at purchase time	Frequency of transaction	Type of property
Knowledge of taxpayer		Holding period

Individual:

- Capital gain is 50 % taxable
- Capital loss is 50 % deductible against the TCG. Otherwise, possible deferral -3, + carry forward indefinitely to offset the taxable capital gain



Corporation:

- Same as for an individual + Creation of a capital dividend account

Sales and acquisition related expenses (incurred over a capital expenditure) reduce the capital gain

Change of use

Deemed disposition and acquisition at FMV

- o Election available to avoid this rule only when there is a transition from personal use property to revenue-producing property.

Capital gain exemption on the sale of the principal residence

- Criteria relating to the principal residence:
 - o 1 per family per year
 - o Ordinarily inhabited
- Calculation of exemption (1 + number of years of designation/number of years of holding)
- Optimum designation (planning: designates the residence whose CG/year of detention is highest)

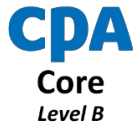
Property donation to a charitable organization: CG inclusion rate = 0%

Capital gains allowance

- Makes it possible to defer capital gain where a portion of the proceed of disposition (PD) is payable subsequent to year end
- Less:
 - o 4/5 of the capital gain (year 2 = 3/5, year 3 = 2/5, etc.)
 - o $\frac{\text{Balance of proceeds of disposition receivable} \times \text{capital gain}}{\text{Total proceeds of disposition}}$

Listed personal property and personal use property

- Rule of \$1,000 to determine the ACB and the proceeds of disposition



Alternative minimum tax (AMT)

- 2nd tax calculation (the individual pays the highest of the 2)
- Abuse of tax shelters (capital gains especially)
- The CGD is the key trigger
- Refundable over 7 years against tax payable
- Planning: allocate sale of shares over 2 years to minimize annual CG



Investment in the QSBC (90% CCPC):

1- Allowable business investment losses (ABIL)

Loss
selling

- Capital loss on investments in respect of debts or shares
- Is a QSBC at the time of disposition or at some point over the course of the 12 preceding months
- Limited by the CGD (100%) taken in the past
- 50% deductible from all sources of revenue
- Conditions:
 - o Shares are sold to an arm's-length person or;
 - o Can make an election (Sect. 50) and deemed have sold the shares for PD = 0 (under certain conditions)

2- Capital gain deduction

Profit realized on

- Individual only
- Taxable capital gain on QSBC shares (especially), qualified farm and fishing property
- QSBC shares:
 - o QSBC sale
 - o 2-year holding period
 - o 50 % during 2 years
- Limits:
 - o Lifetime ceiling of \$433,456 (\$866,912 x 50 %)
 - o Non-capital loss deducted in the year⁸
 - o Allowable capital loss for the year
 - o Cumulative Net Investment Losses (CNIL)⁹
 - o Cumulative Allowable Business Investment Losses (ABIL)¹⁰
- Planning:
 - o Crystallization when the conditions are met
 - o Freeze in favour of another person
 - o Eliminating the CNIL before year end (dividend payment)
 - o AMT of vendor – plan the sale over 2 years

Think purification otherwise...

If no prospective purchaser...

Divest one's participating shares for non-participating shares...
And why not crystallize at the same time...

3- Capital gain deferral (44.1 ITA)

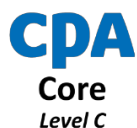
Profit realized on sale...
No CGD possible

- Individual only
- Capital gain on investments in shares
- Is a Small Business Corporation (SBC) at the time of disposition
- Shares held for at least 6 months before the disposition
- Must acquire new shares of an SBC in the year of disposition or in the 4 first months of the following year
- Planning:
 - o Deferral of capital gain when the new shares are resold
 - o Option to defer capital gain indefinitely by continually purchasing new shares of SBC
 - o End: end the investment in the SBC- taxation of total capital gain at such time

⁸ The non-capital loss deducted in the year should first be applied against taxable capital gains not eligible for the capital gain deduction.

⁹ Consider only the CNIL that were not used to reduce the capital gains deduction of a prior year.

¹⁰ Consider only the ABIL that did not reduce the capital gains deduction of a prior year. The ABIL deducted in the year should first taxable capital gains not eligible for the capital gain deduction.



Death



General rule: Deemed disposition (and re-acquisition) of all property at FMV

Exceptions: Donations in favour of a spouse (or a trust set up specifically for the spouse):

- Deemed disposition (and acquisition) at cost amount (automatic rollover)
- Possible elections at FMV to:
 - o Use the capital gains deduction
 - o Use capital losses from year of death and previous years
 - o Use remaining net-capital losses (less capital gains deductions already taken in the past) against all sources of revenue in the year of death and the year preceding death

Planning with regards to the decease of the principal shareholder:

PRE-death:

- Plan the donations of the property (to spouse vs. other people)
- Provide a clause for the payment of a death benefit payment (10 000\$)
- Declare a dividend to the shareholder (without paying it) – to qualify the dividend as *a rights or things* at the time of death

POST-death: consider not to apply automatic rollover for donations made to the spouse (if relevant to do so)

Separate returns (election):

- Rights or things (matured coupon and/or uncollected declared dividends)
- Revenue from a partnership/testamentary trust: the surplus of 12 months of revenue to be included at the time of death

Filing date (the later of):

- April 30
- or 6 months after the death

Special rules in the year of death:

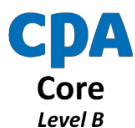
- Utilization of unused net capital losses against all sources of revenue (possible for the last 2 years)
- No reserve can be deducted in the year of death
- May claim medical expenses incurred over the past 24 months
- Alternative minimum tax: not applicable
- Donations: 75% limit on income is not applicable
- Non application of superficial loss
- Obtain clearance certificate for the estate

Post-death loss:

- Following the sale of a property by the estate: election to consider the loss in the deceased's tax return
- RRSP: decline in value between the death and distribution of the RRSP to the beneficiary: possible deduction of the decrease in value for the estate (or in the deceased's tax return) at the time of distribution

Donations to a minor child:

- RRSP:
 - o Taxable for the child
 - o Taxation deferred only for a child under age 18 who uses the amount to purchase an annuity until the child's 18th birthday or later
- Qualified farm property: deemed disposition and re-acquisition at the cost amount (automatic rollover)



Divorce



General rule:

- Property transfers between spouses in the divorce process: deemed disposition and acquisition at the cost amount (automatic rollover) for all properties
- Attribution rules not applicable on property transferred by way of a divorce

Support payment following divorce:

Distinction between capital payments (transfer of property between spouses in the process of divorcing) vs. periodic allowance (in order to maintain the spouse's and/or children's quality of life)

- Support payment EXCLUSIVE to the ex-spouse: taxable to the beneficiary and deductible for the payer
- Support payment IN PART to children: non-taxable and non-deductible

Generally, legal expenses incurred to establish a support payment arrangement are deductible for the pension's beneficiary (non deductible for the payer who is the defendant)

Moving expenses:

Deductible (except where reimbursed by the employer) up to the amount of the income earned in the year following the move (otherwise, deferral to subsequent years)

Eligible relocation:

- Be employed, operate a business or study in Canada
- New dwelling must be at least 40 KM closer to the new workplace/business/educational institution

Deductible expenses:

- Meal and temporary accommodation expenses near the previous/new residence (max. 15 days)
- Selling expense (broker) related to the former residence or lease termination fees
- Furniture transport and warehousing fees
- Maintenance fees for former unsold residence (max. \$5,000)
- Public utility connection/disconnection expenses

May create taxable benefit if:

- Employer reimburses an employee an amount in excess of actual relocation expenses
- Employer reimburses the loss related to the sale of a home:
 - o Housing Loss: taxable benefit = amount received by the employee
OR
 - o Eligible housing loss related to accommodation (requires being 40km closer to the workplace): taxable benefit = (amount received by the employee – \$15,000) X 50 %

Child care expenses:

Fees incurred for a child (16 years of age and under /or disabled) that lives with a parent

Annual limit:

Age of child	Annually	Vacation camp
From 7 to 16 years of age	\$5,000	\$125/week
Under 7 years of age	\$8,000	\$200/week
Disabled child	\$11,000	\$275/week

1st parent to deduct expenses is the parent with lower income:

Deduction equals the lesser of:

- Total child care expenses paid by parents
- Annual limit
- 2/3 of 1st parent's income earned

LESS:

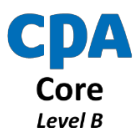
Portion of expenses deducted by the other parent, as the case may be

2nd parent to deduct expenses: parent with the highest income, only if the parent with the lower income is:

- *pursuing a post-secondary program of study or*
- *hospitalized*
- *imprisoned*

Deduction equals the lesser of:

- Total child care expenses paid by parents
- Annual limit
- 2/3 of 2nd parent's income earned
- Weekly (or monthly) limit during which the other spouse is in school/hospitalized/in prison



Recession



Loss carryforward:

- Net capital loss : -3 years, + indefinitely against TCG only
- Non-capital loss : -3 years, +20 years against all sources of income
- Farm loss : -3 years, +20 years against all sources of income
- Restricted farm loss : -3 years, +20 years against farm income only



Planning: consolidation of entities (merger or wind-up)

Makes it possible to use the losses of a company in a loss position to offset the income of another profitable company, subject to:

- Rules (constraints) of acquisition of control
- Expiry period of losses, which continues post-merger
- Carryback of losses (incurred post-merger) possible only if offset against taxable income (earned before the consolidation) of the parent company only (not possible for a subsidiary)



Bad debts and shares of bankrupt company (elect. of subsection 50(1) ITA):

Election to recognize a capital loss (deemed PD and ACB of 0 on this investment) if:

Bad debt	Shares of a company
Where the debt bears interest <i>(the taxpayer may be related with the person to whom the taxpayer is indebted)</i>	Where the company is bankrupt
Where the debt arises from the sale of property to an arm's-length person	Where the company is wound-up
	Where the company is in very poor financial condition: - Insolvent - Inactive - FMV of the share is nil - Wind-up reasonably expected <i>(the taxpayer may be related with the company in which the taxpayer holds shares)</i>

Allowable Business Investment Loss (ABIL):

Essentially, it is an allowable capital loss (ACL) which has to fulfill certain conditions:

The ACL on investment arises from the election of subsection 50(1) ITA	The ACL on an investment arises from the sale to an arm's length person
Type of investment sold: Share of a QSBC OR Debt from a CCPC (QSBC, in bankruptcy or being wound-up)	



Gain on settlement of debt (debt bearing interest):

Reduction of tax attributes (mandatory order) equivalent to the value of the gain on settlement of the debt:

1- Reduction of Non-capital losses, farming losses (FL) and restricted farming losses (RFL)
2- Reduction of Net capital losses
3- Reduction of UCC
4- Reduction of ACB of capital property
5- Reduction of current year's capital losses
6- Remaining gain, 50% inclusion



Unpaid remuneration:

Expenses deducted in calculating income (accrual method) and owing to an employee who has not included this amount in the calculation of his/her income (using the cash basis method)

In the event the amount remains unpaid 6 months after year-end of the payer:
Unpaid amount for the year of the expense is not deductible (retroactive impact)

Unpaid amounts (other than remuneration):

Expense deducted in calculating business income (accrual basis method) and owing to a related person who hasn't included the amount in the calculation of his/her income (using the cash basis method)

In the event the amount remains unpaid at the end of the 2nd taxation year following the year of the expense:

- Amount is included in the income in the 3rd taxation year of the person owing the amount (offsetting the deduction granted the 1st year)
OR
- Can elect to have the amount deemed paid by the payer and loaned to the other person (agreement between both parties)

Reserve for reorganization, closing or lay-off:

These expenses are deductible only when they are paid

Ceasing to carry on a business:

- Disposition of at least 90% of accounts receivable:
By default: CG or CL for the vendor (capital transaction)
(Section 22 ITA): Business income or loss for the vendor
- Disposition of inventories: business income or loss for the vendor
- Disposition of other capital property: usual rules apply



Core
Level C

Taxation of non-residents (individuals)



Elective
Level B

Resident (factual):

Individual who at some point during the year has a residential (legal) tie with Canada:

- Permanency and goal of the stay abroad
- Existence of residential ties with Canada
- Existence of residential ties elsewhere
- Frequency and duration of visits to Canada

Factual residents throughout the year:

Taxation in Canada of worldwide income for the entire year

Factual residents for part of the year:

Taxation in Canada of income from worldwide income for the period of the year in which the factual resident status applies

AND

Taxation in Canada from 3 income sources (employment, business and disposal of taxable Canadian property (TCP)) for the period of the year in which becomes non-resident

Non-resident:

Individual who has no residential (legal) tie with Canada at any point in the year

Deemed resident then?

Factual non-resident having stayed in Canada for 183 days (consecutive or not) or more in a taxation year:

IF YES: considered a Canadian resident for the entire year

Taxation in Canada on worldwide income for the entire year

IF NOT: considered a non-resident for the entire year

Taxed in Canada under ITA Part I for the entire year on:

- Income from employment earned in Canada
- Income from a business operated in Canada
- Gain on disposal of taxable Canadian property (TCP)

Departure from/Arrival in Canada

Deemed disposition at FMV of all properties at time of departure, except for TCPs

Deemed acquisition at FMV of all of the property at time of arrival, except for TCPs

Investment income paid to a non-resident taxable under Part XIII of the Act:

- Withholding by the Canadian payer (25% of investment income paid)
- The rate of tax withholding may be reduced under the Canada-U.S. tax treaty.
- The Canadian payer is responsible for the withholding

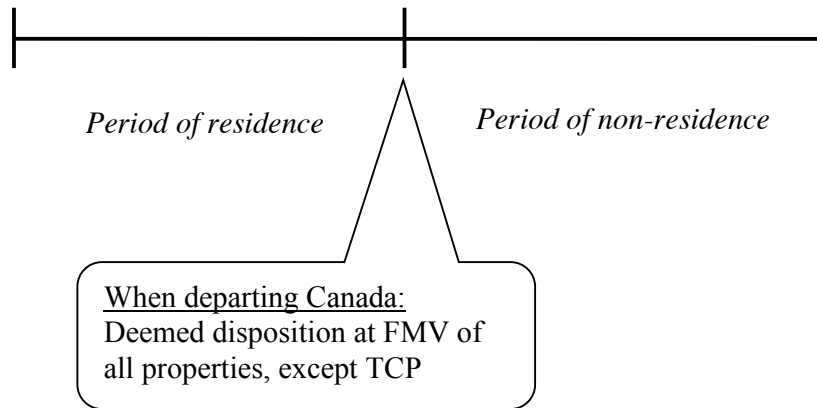
Exception:

Interest income paid to a non-related non-resident (Part XIII tax does not apply)

Summary:

Taxation in Canada:
Worldwide Income

Taxation in Canada:
- Income from employment earned in Canada
- Income from a business operated in Canada
- TCG on TCP





Goods and Services Tax (GST = 5 %)



Collection and application:

Taxable supplies	Exempt supplies	Zero-rated supplies
Collection of GST	Non taxable	Taxable at 0%
ITC application	No ITC application	ITC application

Registration:

Mandatory if operating a business in Canada, except if small supplier

Small supplier:

Total taxable sales are below \$30,000 (in total) for 4 consecutive quarters

Tax payable for the taxpayer – earliest of the following dates:

- Payment of supply
- Date when the supply becomes payable (invoice date)

Remittance of tax by the business that sells zero-rated supplies:

Must remit the tax collected according to the schedules: Annual, quarterly, monthly (based on sales)

Application for ITC by business that sells taxable supplies and zero-rate supplies:

Application of sales tax paid on purchases

Deadline: 4 years following the purchase period for claiming ITCs

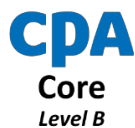
Penalty:

Levied on any late remittance

Interest:

Any unpaid balance bears interest after the remittance deadline

Interest accrues on late or insufficient tax instalments



Trust



Testamentary trust:

- Created following a death
- Taxed according to progressive tax rates for the first 36 months. Maximum tax rate will be applicable after.
- Year end: December 31 mandatory for taxation year end beginning after January 1st, 2016
- Income splitting possible subject to progressive tax rates

Inter-vivos trust:

- Taxation at the maximum rate: 33%
- Year end: December 31 mandatory
- Various uses: tax planning, safeguarding wealth, commonly used to split income between beneficiaries

Trust is taxed on income generated by trust and not distributed to beneficiaries during the year



Calculation of the trust's taxable income:

Income generated by trust

Less:

Amount paid or payable to the beneficiary (possible election: preferred beneficiary)





Partnership



Basic principle – taxation method:

Calculation of income and attribution to partners:

- Income maintains its characteristics for partners (business income, dividends, TCG, etc.)
- The CCA on depreciable assets is taken at the level of the partnership (different however for a property held in undivided co-ownership)

ACB of interest in partnership:

(The accounting capital will accumulate as per the accounting income)

The ACB allows the accurate calculation of the capital gain or loss upon the disposition of a partnership interest:

Additions according to 53(1)e(i) ITA:	Deductions according to 53(2)c ITA:
Contribution of the partner	Partner's fund withdrawals
Income of the partnership attributed to the partner	Losses of the partnership attributed to partners
Tax-free income earned by the partnership	Non-deductible expenses incurred by the Partnership
	Partial dispositions of the partnership interest

Retirement of a partner:

- Sale of partner's interest (to a third party): PD (-) ACB = capital gain or loss
- Redemption of interest (by the partnership) : PD (-) ACB = capital gain or loss
- Wind-up of Partnership (legal):
 - o With undivided interest in all of the property remitted to the partners (conflicts...):
Deemed disposition and acquisition at cost amount (rollover) for the partner and Partnership
 - o Without undivided interest in all of the property remitted to partners:
Deemed disposition and acquisition at FMV for the partner and partnership



Partner's death:

- Disposition at FMV upon death, except if bequeathed to spouse (automatic rollover)

Property rollover:

- A partner may rollover property into a partnership
- The partner may rollover property into a corporation

Limited partnership:

- General partner: partner who manages and assumes the risks (unlimited liability)
- Limited partner: partner investor, responsibility limited to partner's investment; no management involvement
- At-risk amount (limits the tax losses deductible on the amount invested in the general partnership)



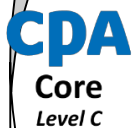
Business acquisition and sale



Personal acquisition vs. Acquisition by holding company:

- Personal acquisition:
 - o The price paid for the acquired shares becomes the ACB of such shares but does not in any way impact the PUC of these shares
 - o WITH USE OF FINANCING: the individual acquirer must pay income tax on income paid to him/her by the acquired company (salary/dividend) for the purpose of reimbursing the debt incurred to finance the acquisition
- Acquisition by holding company:
 - o The price paid for shares by a holding corporation will be the ACB and the PUC of the shares of the holding company. Then, the holding company acquires the shares of the target company
 - o WITH USE OF FINANCING: Makes it possible for the holding company to reimburse the debt incurred to finance the acquisition with a non-taxable dividend from the acquired company
Usually, this acquisition is quickly followed by a consolidation (merger or wind-up) of 2 companies (the holding company and the acquired operating company)¹¹

Take heed of section 84.1



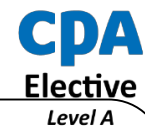
Business transfer in a family context:

DONATION: Deemed disposition AND deemed acquisition at FMV

- Purchaser will have a full ACB (= FMV)
- Possible CGD for vendor

Sale at FMV: Actual disposition AND actual acquisition at FMV

- Financing required by the purchaser (internal and/or external)
- Purchaser will have a full ACB (= FMV)
- Possible CGD for the vendor
- Take heed of 84.1 if selling to a non arm's-length corporation
 - o = possibility of a deemed dividend



Divesting participating shares in consideration for non-participating shares...

And why not crystallize at the same time...

FREEZE: ~~Practically no fund withdrawal~~ for new shareholders who issue new participating shares:

- Several possible tax deferral (rollover) strategies: share conversion, recapitalization, transfer to a holding company, etc.
- Crystallizing: voluntarily electing to make a TCG during a freeze in order to use the CGD
- Possibility of maintaining control (controlling shares)

¹¹ The holding company pays interest (that is deductible) with dividend income (which is not taxable). This situation, if it persists, will result in tax losses for the holding company. The combination makes it possible to use such losses to offset income from the operating company.



Share acquisition (sale) vs. asset purchase (sale):

(Support your client’s side – PURCHASER or VENDOR?)

PURCHASER

- ASSETS: bump up of the asset tax base to their FMV (good for the purchaser)
- ASSETS: favourable (reasonable) distribution of the purchase price between the various assets acquired (the excess represents goodwill acquired) – Inventory, depreciable assets (allocate to the classes starting with the highest CCA rates to the classes with the lowest rates), eligible capital property, non-depreciable assets
- SHARES: legally more straightforward
- SHARES: purchase the corporation’s legal history (liabilities)

VENDOR

- SHARES: available tax shelters for the vendor:
 - o Capital gains deduction (if there is a gain)
 - o Rollover to defer the capital gain (if there is a gain and no CGD available/applicable)
 - o Allowable business investment loss (ABIL- if there is a loss)
- ASSETS:
 - Disposition of at least 90 % of accounts receivable:*
By default: CG or CL for the vendor (capital transaction)
Joint election (ITA Section 22): business income or loss for the vendor
 - Disposition of inventories:* business income or loss for the vendor
 - Disposition of other assets:* usual rules apply

Change in status of company:

CCPC to public company	CCPC to private company (controlled by non-residents)
Loss of capital gains deduction for the shareholder	
Empty the CDA, since N/A for a public company	CDA still exists, however, the capital dividend paid to a non-resident shareholder is subject to Part XIII Tax
Empty the RDTOH, since N/A for a public company	RDTOH still exists
Loss of the SBD	



Acquisition of control



Step 1 – Complete the acquisition of control

- Acquisition: control takeover by a person who did not have control
- Control: more than 50% of voting shares

Take heed of transactions between non-arm's length parties, since no acquisition of control is considered to have taken place

Step 2 – Deemed year end – 249(4)

At the time of the acquisition of control

Step 3 – Net capital losses – 111(4)

No amount in respect of net capital loss is deductible in computing the corporation's taxable income for a taxation year ending after the acquisition of control

Step 4 – Automatic realization of unrecognized capital losses on non-depreciable property (ie: land, investments)– 111(4)c, d)

Step 5 – Automatic realization of unrecognized terminal losses on depreciable property – 111(5.1)

Step 6 – Election available to realize unrecognized capital gains and/or recaptures of depreciation (depreciable or non-depreciable property) – 111(4)e)

- Election to trigger capital gains and/or recapture the depreciation on the property held by the acquired company
- Deemed disposition (and acquisition) at the elected amount, ranging between the FMV of the property and its ACB

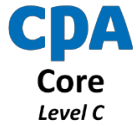
Step 7 – Non-capital losses – 111(5)

1 condition:

- Following an acquisition of control, the business (activity) of the acquired company is carried on by the corporation for profit or with a reasonable expectation of profit throughout the year.

1 limit (maximum):

- Up to the amount of income from the business (activity) that generated the business losses or from a business where substantially all of the income of which was derived from similar properties or the rendering of similar services.



Starting-up a company



Incorporation vs. personal business:

Personal business:

Start-up losses deductible against the entrepreneur's other personal sources of income

Incorporation:

- Incorporate when profits become significant
- When the personal liability risk becomes too high
- Consider company's expenses and administrative costs
- Tax deferral: corporate rate = 10 % and 15% vs. Individual tax = 33%
- Planning: start-up as a personal business (start-up loss) and incorporate when profits become significant (reduction of tax rate PLUS tax deferral on income kept in the company) OR where the personal liability risk becomes too high

Incorporation expenses: New Class 14.1

Start-up costs: deductible for tax purposes (often capitalized for accounting purposes)

Financing expenses (debt or shares): deductible over 5 years (20% per year)

Possible remuneration methods with a business corporation:

- Salary
- Dividend
- Income splitting with spouse and children (reasonable salary)
- Taxable and non-taxable benefits
- Etc.

Incorporation of an existing personal business:

- Asset rollover
- Unnecessary if all of the revenue is used annually
- If rollover of all of the company's assets, the 24-month holding period for the CGD is considered as automatically being met (if prompt subsequent resale of shares)

Shareholders' agreement

Company's year-end election (tax deferral)



Loans/shareholder benefits



15(1) ITA

Benefit conferred on shareholder (for example: personal expenses paid by the company)

- Shareholder's revenue
- Non-deductible for the company

DOUBLE TAXATION

15(2) ITA

Loan to shareholder by the company (or a person related to the shareholder)

LOAN CAPITAL

Loan (capital) to be included in the shareholder's income in the year in which the loan was received

Exceptions:

- Loan reimbursed before the subsequent year end of the company in which the loan was granted (two balance sheet rule)
- Shareholder owning less than 10% of the company's shares
- Loan used to purchase treasury shares
- Home purchase loan
- Loan for purchasing an automobile to use for employment purposes

If any of the above four conditions is met, must also indicate that:

- o The loan is received as an employee (loans also offered to other employees)
- AND
- o Loan shall be repaid in a reasonable amount of time

15(9) ITA

Loan to a shareholder by the company (or a person related thereto)

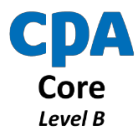
INTEREST-FREE LOAN

Applicable only on the capital portion of the loan, which is not included in the shareholder's income pursuant to ITA 15(2)

Capital of the loan in effect during the year (X) at the prescribed rate in effect
LESS: Interest paid in the year (or 30 days after)

Exceptions:

- Loan issued at market rate (may vary from prescribed rate)
- The capital portion of the loan is included in the shareholder's income pursuant to ITA 15(2)



Tax Administration



Individual (T1):

Filing: April 30 or June 15 (entrepreneur and spouse)

Payment of tax: April 30 for all

Business (T2):

Filing: 6 months after the taxation year-end

Payment of tax: 2 months after the year end (3 months for CCPC)

SR&ED expenditures claim (T-661):

18 months after year-end

Trusts (T3):

Filing: 3 months after the year-end

Payment of tax: 3 months after the year end

Interest:

- Payable from the tax balance due date
- Calculated based on outstanding tax balance

Penalties:

- Payable from the income tax return filing due date
- Calculated based on outstanding balance

Election on disposition of property under ITA subsection 85 (T2057):

Earliest of the 2 filing dates of the transferors

Election for a capital dividend form (T2054):

Filed the day the dividend is paid or becomes payable

Records:

A taxpayer must keep income tax returns for the past 6 years, independently of the minister's assessment power for a given year

Penalty for omission or false statements:

The penalty is equal to the highest of the following amounts:

- \$100;
- 50 % of the unpaid tax

Third-party PenaltiesPlanner penalty

When a false statement is made in the course of a planning activity or a valuation activity, the penalty amounts to the:

Greater of:

- \$1,000 or
 - the total of the person's gross entitlements for the planning or valuation activity
- Example: A tax shelter promoter holding seminars or presentations to provide information in respect of a specific tax shelter

Preparer penalty

A person who makes, or participates in, consents to, or would reasonably be expected to know that is a false statement, is liable to a penalty that amounts to the:

Greater of:

- \$1,000 or
- the penalty to which the other person would be liable (maximum \$100,000 + gross entitlements received)

Business combination¹²

Introduction

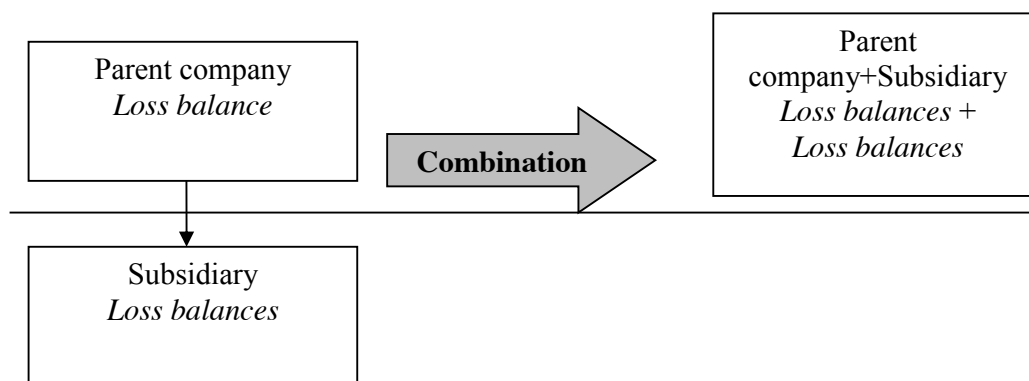
- Merger (87 ITA)
 - o Legal
 - o Tax
- Wind-up (88 ITA)
 - o Legal
 - o Tax
- LEGALLY: different
- TAX-WISE: treated similarly
 - o Addition of tax balances and attributes of 2 combined companies
 - o Perfect rollover for shareholders of 2 combined companies and for the 2 combined companies themselves

LEGAL DIFFERENCES:

- Merger:
 - o Dissolution of 2 existing companies and INCORPORATION of a new company
 - o Resulting year-end
- Wind-up:
 - o A subsidiary pays out a dividend in assets (and liabilities) to its parent company. No DISSOLUTION, no new INCORPORATION
 - o Potential DISSOLUTION of the subsidiary, which is empty

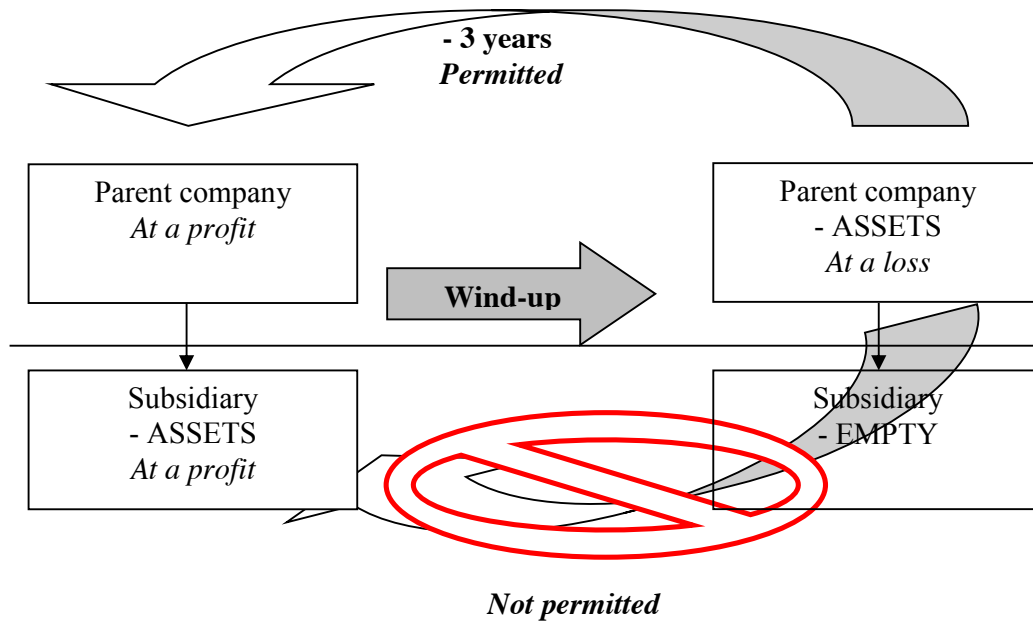
Use of losses – common rules:

- Losses incurred before the combination by each of the SURVIVING companies ARE APPLICABLE against income earned after the combination by the new company resulting from the combination
 - o By keeping their respective due dates
 - o Subject to rules governing acquisitions of control



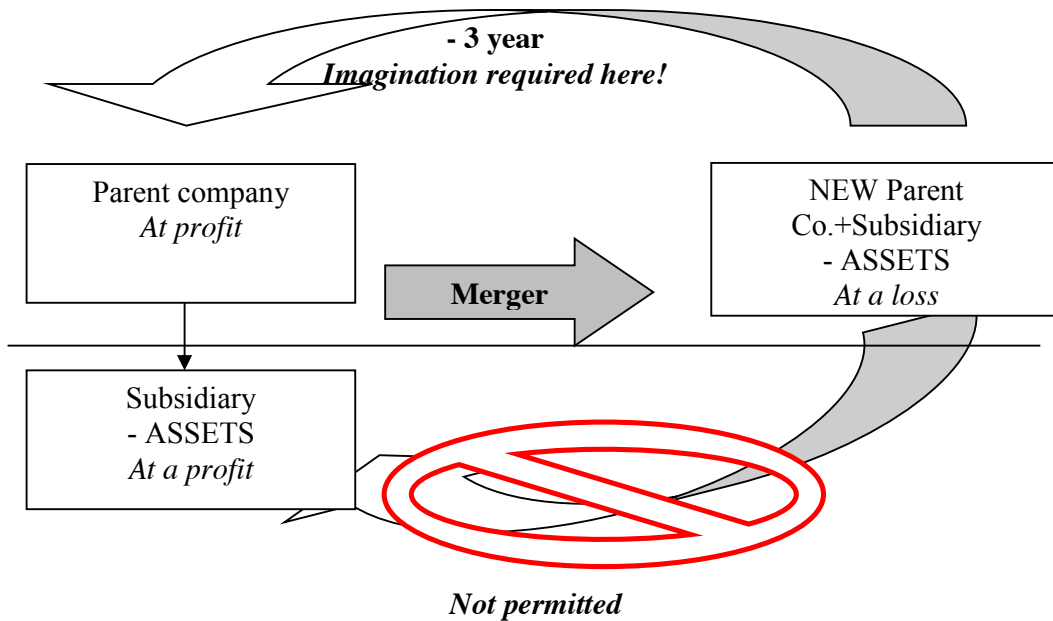
¹² Generic term that includes both mergers and wind-ups

- Losses incurred subsequent to the combination and creation of the new company, and incurred by the new company, ARE APPLICABLE against income earned before the combination EXCLUSIVELY by the PARENT COMPANY (bearing in mind their respective due dates)



- In the context of a MERGER BETWEEN A PARENT COMPANY AND A WHOLLY-OWNED SUBSIDIARY:
Losses incurred post-merger by the new company resulting from the merger ARE APPLICABLE against the income earned pre-merger by the PARENT COMPANY EXCLUSIVELY.

(2 different companies; imagination required here!)



- The losses realized post-combination by the new company resulting from the combination ARE NOT APPLICABLE against the income earned prior to the combination by a company THAT IS NOT THE PARENT COMPANY of the combination.

Planning:

- Offsetting of a business income and business loss (from several entities to 1 company)
- Synergy and economy of scale with regards to material, human, financial resources
- Administrative costs savings (one less company)



Transactions between shareholders and companies



Salaries vs. dividends:

- Basic rule = case by case
 - o Dividend: non deductible for the company, less tax for the individual (gross up + tax credit)
 - o Salary: deductible for the company, taxed at 100 % for the individual
 - o Unreasonable salary: not deductible for the company
- Other factors:
 - o Loss position business
 - o Business income over \$500,000
 - o RRSP contribution room
 - o CNIL to eliminate
 - o Consider payroll expenses in the analysis

Transactions on shares – Capital gain vs. Deemed dividend

Capital gain:

Sale of shares to another person

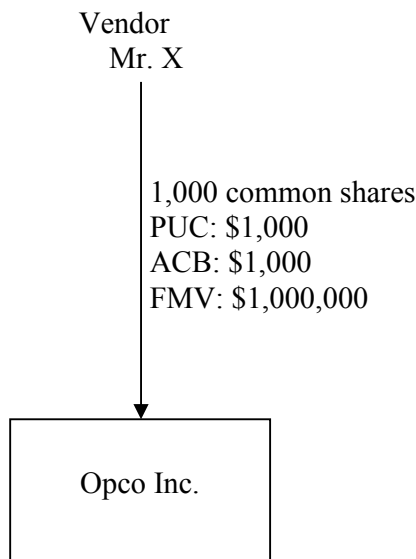
$CG = PD - ACB$

If selling shares to a company with whom the vendor does not deal at arm’s length: application of ITA 84.1 and potential deemed dividend

Deemed dividend:

The share redemption by the company may trigger a deemed dividend if the redemption amount paid by the company exceeds the Paid-up capital for the redeemed shares.

Deemed dividend (DD) = Amount paid (AP) upon redemption by the company – paid-up capital of redeemed shares



3 possible scenarios relating to the disposition of shares by Mr. X :	
1) Sale to another person	PD \$1,000,000 <u>ACB \$1,000</u> CG \$999,000 (possible CGD...)
2) Redemption by the company	AP \$1,000,000 PD-DD \$1,000 <u>PUC \$1,000</u> <u>ACB \$1,000</u> DD \$999,000 CG \$0
3) Sale to a company controlled by a non-arm’s length corporation (Mrs. X, for example) Application of 84.1 Deemed dividend of \$999,000	

Reorganization

Rollover: *Tax disposal that creates a transaction through a tax carry forward*

Contexts involving rollover items:

- Capital reorganization (shares): ITA section. 86
- Convertible property (shares): section. 51
- Transfer of Property to a partnership (shares and assets): Subsection. 97(2)
- Transfer of Property to a Corporation: (shares and assets): Section. 85

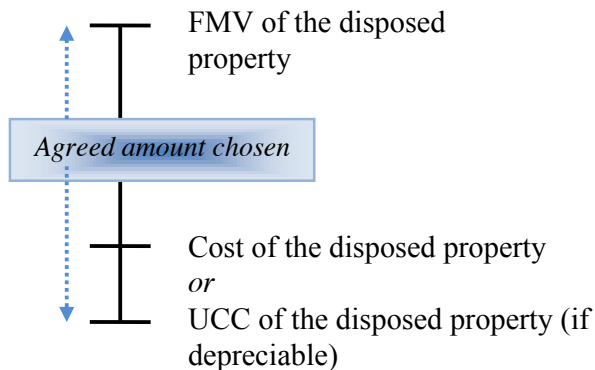
Subsection 97(2) and Section. 85:

Joint election made by the taxpayers (the vendor and the purchaser corporation) of the fictional transaction for tax purposes (referred to as the agreed amount (AA)):

- o AA becomes the PD of the vendor
- o AA becomes the acquisition cost of the purchaser's property
- o AA becomes the cost of the consideration received by the vendor

Limits of the agreed amount chosen:

(the agreed amount chosen must be within these limits)



Estate freeze

Freeze: *Divesting one’s participating shares in exchange for non-participating shares in order to equate the current value of non-participating (preferred shares) to the current value of the participating shares. This makes it possible to increase the future value of company’s new participating (common shares issued to new shareholders).*

Estate: *... in favour of a descendant (child, grandchild, etc.)*

Transactions that make it possible to achieve this objective and available rollover item:

- Capital reorganization (shares): Section. 86
- Convertible property (shares): Section. 51
- Transfer of Property to a Corporation: Section. 85

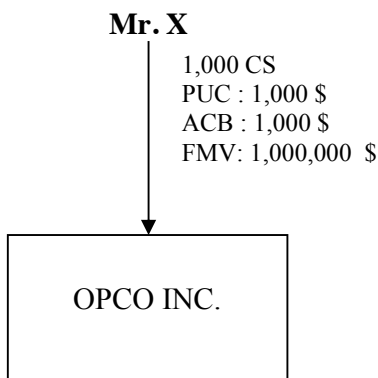
Advantages:

- Makes it possible to transfer a company to children or other new shareholders
- No immediate tax impact (tax deferral)
- No external financing needed for new shareholders (new common shares have no value at such time)

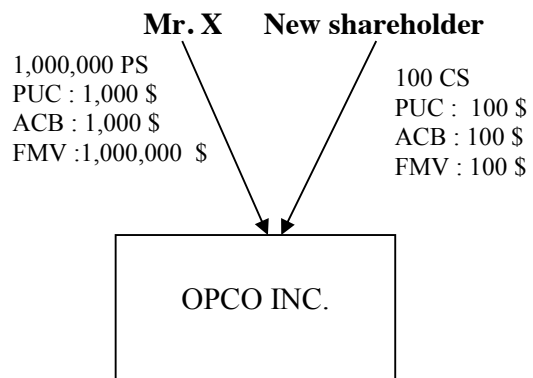
Steps:

- Exchange of common shares into preferred shares for the freezor
- Issue of new common shares to new shareholders desired

Before the transaction



After the transaction



Crystallization: *Increasing the ACB of a property (usually shares) by voluntarily triggering a capital gain (often cancelled out by using the capital gains deduction (CGD))*

Transaction that makes it possible to meet this objective and available rollover item:

- Transfer of Property to a Corporation: Section. 85

Advantages:

- Benefit from the CGD at the time the shares are considered QSBC (if no prospective purchaser)
- Increase (of \$848,252 in the example) of the ACB of new shares issued in consideration by the purchaser corporation and received by the vendor

Steps:

Vendor = individual

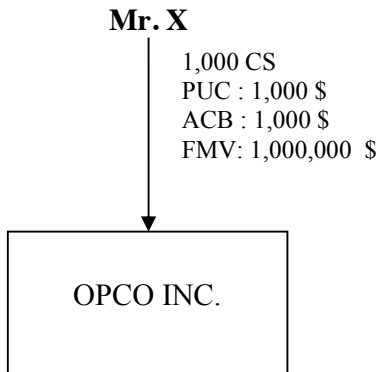
Purchaser = corporation

Transacted property = shares of a corporation

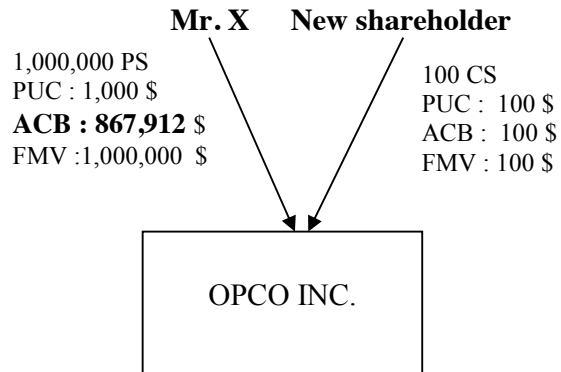
- o Sale of shares of a corporation
- o In consideration of new shares issued by the purchaser corporation
- o Choice of agreed amount (AA) to an amount in excess of the ACB of the shares sold (example: AA = ACB of shares sold + \$866,912)
 - AA becomes the PD of the vendor (CG= 866,912 x 50 % - CGD = 866,912 x 50 %)
 - AA becomes the acquisition cost of the shares acquired for the purchaser corporation
 - AA becomes the cost of the new shares issued in consideration by the purchaser corporation and received by the vendor

Alternative minimum tax may be applicable

Before the transaction



After the transaction



Financial statement tax analysis

When the board of evaluators gives you a complete set of financial statements in simulations, an analysis of these financial statements must be carried out, since items in these statements may give rise to tax issues that may have to be considered in your solution.

Work to be done:

- 1) Using the financial statements below, indicate those items likely to create a tax issue.
- 2) Refer to the solution to verify your answers.

TAX PLUS INC.
EARNINGS
Year ended December 31, 20XX

	20XX
	\$
Revenue	
Professional dues	826 500
Share of earnings in the corp. subsidiary	45 700
Share of earnings in the partnership	19 000
Dividends	13 490
Interest	1 290
	905 980
 Operating expenses	
Salaries and employee benefits and bonuses	222 164
Rent	37 200
Depreciation	18 900
Advertising	6 219
Supplies (maintenance)	5 360
Automotive allowance	3 678
Maintenance and repair	2 300
Travel and entertainment expenses	5 590
Convention expenses	5 845
Life insurance	5 029
Loss on disposal of assets	3 920
Computer purchases	5 700
Bank charges	1 889
Write-down of value in investment	1 000
Depreciation of financing expenses	1 849
Donation	537
Interest on long-term debt	16 848
Allowance for doubtful accounts	422
	344 450
Earnings before income taxes	561 530
Income tax provision	106 691
Net income	454 839

TAX PLUS INC.
RETAINED EARNINGS
December 31, 20XX

	<u>20XX</u>
	\$
Balance , beginning of year	366 493
Net income	<u>454 839</u>
	<u>821 332</u>
Dividends	<u>89 000</u>
Balance, end of year	<u><u>732 332</u></u>

TAX PLUS INC.
BALANCE SHEET
December 31, 20XX

	20XX
	\$
ASSETS	
Current assets	
Cash	32 500
Marketable Securities	325 000
Work in progress	8 434
Interest receivable	350
Advance to shareholder	29 000
	395 284
Property, plant and equipment (net carrying amount)	
Office furniture	38 900
Automobile (to the spouse of ...)	32 000
Computer equipment	12 800
Goodwill – client list	52 000
	135 700
Deferred financing expenses	15 500
Partnership investments	335 900
Investments in a corp. subsidiary	432 050
	919 150
	1 314 434
LIABILITIES	
Accounts payable	187 350
Salary and bonuses payable	7 913
Sales taxes payable	2 339
Income taxes	23 000
	220 602
Long-term debt	351 000
	571 602
SHAREHOLDERS' EQUITY	
Capital stock	10 500
Retained earnings	732 332
	742 832
	1 314 434

TAX PLUS INC. EARNINGS Year ended December 31, 20XX

	20XX	
	\$	
Revenue		
Professional dues	826 500	Non-taxable: the subsidiary files an income tax return
Share of earnings in a corp. subsidiary	45 700	Include the income (tax) and not the book profit
Share of earnings in partnership	19 000	
Dividends	13 490	Calculation of Part IV tax if taken from a TCC
Interest	1 290	
	<u>905 980</u>	A portion (generated by the working capital) may qualify as ABI
Operating expenses		Make sure that the portion receivable is recorded on the balance sheet (as the case may be)
Salaries and employee benefits and bo	222 164	
Rent	37 200	Deductible capital (capital cost allowance (CCA))
Depreciation	18 900	
Advertising	6 219	Publicity aimed at Canadians by a Canadian advertiser for deduction
Supplies (maintenance)	5 360	
Automotive allowance	3 678	Maximum 2 conventions deductible
Maintenance and repair	2 300	
Travel and entertainment expenses	5 590	Meals: 50% deductible Golf: non deductible
Convention expenses	5 845	
Life insurance	5 029	Separate tax calculation
Write-down of value in investme	3 920	
Computer purchases	5 700	Capitalizable and CCA deductible
Bank charges	1 889	
Investment write-off provision	1 000	Non-deductible
Amortization of financing expenses	1 849	Deductible 20% per year
Donation	537	
Interest on long-term	16 848	Deductible in the calculation of income taxable by the company
Allowance for doubtful accou	422	
	<u>344 450</u>	Deductible if taken from a specific account analysis
Earnings before income taxes	<u>561 530</u>	
Income tax provision	106 691	Non-deductible
Net income	<u><u>454 839</u></u>	

**TAX PLUS INC.
RETAINED EARNINGS
December 31, 20XX**

		<u>20XX</u>
Balance, beginning of year		\$ 366 493
Net income	Makes it possible to recover the RDTOH (as the case may be)	<u>454 839</u>
		<u>821 332</u>
Dividends	-Is it-possible to pay a capital dividend? (non taxable for the shareholder) -Is it-possible to reimburse PUC of shares? (non-taxable for the shareholder)	<u>89 000</u>
Balance, end of the year		<u><u>732 332</u></u>

**TAX PLUS INC.
BALANCE SHEET
December 31, 20XX**

		20XX	
ASSETS		\$	
Current assets			
Cash		32 500	
Marketable securities		325 000	
Work in progress		8 434	
Interest receivable		350	
Loan to shareholder		29 000	
		395 284	
Property, plant and equipment (net carrying amount)			
Office furniture	38 900		
Automobile (to the spouse ...)	32 000		
Computer equipment	12 800		
Goodwill – client list	52 000		
		135 700	
Deferred financing expenses		15 500	
Partnership investments		335 900	
Investments in a corp. subsidiary		432 050	
		919 150	
		1 314 434	
LIABILITIES			
Accounts payable		187 350	
Salary and bonus payable		7 913	
Sales taxes payable		2 339	
Income tax payable		23 000	
		220 602	
Long-term debt		351 000	
		571 602	
SHAREHOLDERS' EQUITY			
Capital stock		10 500	
Retained earnings		732 332	
		742 832	
		1 314 434	

Investment: is the company a qualified SBC?

Taxable (included in the professional dues)

Correctly apply the CCA, tax rules (class, rate, ½ year rule etc.)

Take heed of 15(1): Benefit to be included in the shareholder's income

15(2) - If on 2 consecutive balance sheets : loan to be included in shareholder's income

Class 14.1

20% deductible per year

Bonus must be paid within 6 months following the year end 20XX if not: non deductible in 20XX