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## Solution to Assignment Problem Twenty - 2

**Note To Instructors** This problem is based on a Tax Court Of Canada case, Hamel Vs. The Queen (2012 DTC 1004).

### *Background*

The minister assessed Mr. Hamel on the basis of his not giving up Canadian residency on January 13, 2007 (the original date in the case). Mr. Hamel appealed to the Tax Court of Canada which resulted in Hamel Vs. The Queen (2012 DTC 1004).

The solution that follows is the judge's analysis and decision in the case (note that it was translated from French). The judge's conclusion also contained a long section of references to other cases which we have not included in this solution. The original dates in the case have been changed to correspond to the dates in the problem.

### *Judge's Analysis And Decision*

The respondent's main argument is that every person must have a residence. Presuming the appellant had not resided in Qatar, she found that he must necessarily have resided in Canada.

After arriving at this conclusion, she relied on the following facts:

- The appellant came to Canada a few times.
- The appellant had two bank accounts in Canada, which he used to make all his payments, in particular for his credit cards, which were also issued in Canada.
- The appellant had some money in an RRSP.
- The appellant had no postal address in Qatar.

As for the other elements, for example, not having a driver's licence, not having property such as furniture, clothing, accommodations or vehicles, and not having a health insurance card, the respondent claims that they have no impact one way or the other.

The evidence clearly showed that the appellant's decision came after a lengthy period of reflection. It also showed that the appellant did not have any deep roots and did not hesitate to leave when his son, who was ill, let him go with no regrets.

His relationship with his wife was so tense that they tolerated one another only because of their shared concern about their son who was ill.

The appellant had a very good position. He did not want to run away from his responsibilities. He gave all his property and agreed to pay generous support payments before leaving; he has always complied with these commitments. He did not apply for a new Canadian driver's licence when his was suspended, even though the evidence showed it was important for him to be able to use a car if he wanted an international driver's license or even a driver's licence from the country in which he was living.

He specifically gave up his health card in 2013.

Regarding the beginning of the relevant period of the appeal, the beginning of 2012, it must be considered that a reasonable person would be careful. The appellant stated he could only get a work permit if a medical exam showed he was in good health, otherwise he had to return to his country of origin. The same can be said for the position, the duration of which generally depends on the employer, not the employee. In other words, there is, normally, a reasonable delay before a permanent break. This explains the time between the beginning of the period in question and the time the appellant gave up his health insurance.

As for the argument that the appellant never had a residence in Qatar, I do not believe it is cogent, because the appellant was employed and had a residence. The appellant's strong interest in staying in Qatar was shown by the intensive courses he took to get a driver's licence, when he could have travelled with coworkers, even though he had cancelled his Canadian driver's licence. When his employment ended in Qatar, the appellant returned to the country to see the people with whom he had worked and the work he had done.



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In particular, in view of the following facts, I find that, on the preponderance of the evidence, the appellant's position must be accepted:

- The family context was special and conducive to a permanent departure.
- The appellant left after disposing of all his own property.
- The appellant waived his right to obtain a new driver's licence a few months before leaving Canada.
- The appellant returned to Canada a few times for very short stays that were for the purpose of visiting his two sons, his mother and friends.

After leaving Qatar upon the expiry of his work contract, the appellant returned to meet friends and business acquaintances, thereby showing he had been happy there.

The break came after a long period of thorough reflection.

The appellant has set out all the facts showing his intention to sever ties with this country permanently.

Although the relevance of prior facts is limited, they tend to confirm that the appellant severed his ties with Canada in mid-January 2012.

For these reasons, I conclude that the appellant ceased being a resident of Canada as of January 13, 2012. As a result, the appeal is allowed with costs in favour of the appellant.



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## Solution to Assignment Problem Twenty - 3

### *Case A*

John's 2 year tour would be considered a temporary absence from Canada. Given the facts, it appears his intent is not to permanently sever residential ties with Canada. This position is evidenced by the fact his tour is for a limited time and he will not be establishing residency in another country.

John's departure does not appear to be a true departure in that he has not severed any of the primary ties (dwelling, spouse and dependants) the CRA looks to. As a result, examining those ties would not be relevant since they are typically used when there is an intention to sever residential ties, but they are not all severed at the same time.

John will remain a Canadian resident during his tour and would be subject to Canadian tax on his worldwide income during 2013.

### *Case B*

Because she has an employment contract that requires her to return to Canada in three years, she will be viewed as having retained Canadian residence status. Although she has severed her ties with Canada, the requirement to return would show that she does not intend to permanently leave Canada. Jane will be subject to Canadian tax on her worldwide income during 2013.

### *Case C*

As she is exempt from taxation in Ghana because she is the spouse of a deemed Canadian resident, Laura would be a deemed resident of Canada for income tax purposes during 2013 [(ITA 250(1)(g)]. Laura would be subject to Canadian tax on her worldwide income during 2013.

### *Case D*

As noted in S5-F1-C1, commuting from the U.S. for employment purposes does not make an individual a deemed resident under the sojourner rules. Therefore, Martha would not be considered a Canadian resident for income tax purposes. However, under ITA 2(3) she would, unless exempted by the Canada/U.S. tax treaty, be subject to Canadian tax on her 2013 Canadian employment income. She would not be subject to Canadian tax on her U.S. savings account interest.

She would be exempted by the U.S. tax treaty if the amount of employment income was less than $10,000, or if she was physically present in Canada for less than 183 days. Her employment income was more than $10,000 and, because she was working 5 days a week, it appears that she was physically present in Canada for more than 183 days. Given these facts, she would not be exempted from Canadian taxation because of the Canada/U.S. tax treaty.

### *Case E*

Residency terminates at the latest of:

- the date the individual leaves Canada;
- the date the individual's family leaves Canada; and
- the date that individual establishes residency elsewhere.

As Barry's family did not leave Canada until July 1, 2013, Barry would be considered a Canadian resident until that date. Provided he has no intention of returning to Canada, he would be subject to Canadian taxes on his worldwide income for the period January 1, 2013 through July 1, 2013. In addition, he would be subject to Canadian tax on his rental income for the entire year (Part XIII tax).



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## Solution to Assignment Problem Twenty - 4

### *Case A*

While Bonix is no longer operating in Canada, it was incorporated here prior to April 27, 1965. If it had not carried on business in Canada after that date, it would not be a Canadian resident. However, it did carry on business in Canada after that date and, as a consequence, it is a deemed resident under ITA 250(4)(c).

### *Case B*

Dorad Inc. was not incorporated in Canada and its mind and management are not currently located here. Therefore, Dorad would not be considered a resident of Canada.

### *Case C*

Upton Inc. would be considered a resident of Canada. This conclusion is based on the fact that, while the Company was not incorporated in Canada, the mind and management of the Company appears to be resident in Canada.

### *Case D*

Carlin Inc. was incorporated in Canada after April 26, 1965. This means that, under ITA 250(4)(a), Carlin is a deemed resident of Canada. The fact that the mind and management of the company are located elsewhere is not relevant.



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## Solution to Assignment Problem Three - 2

### *Background*

The facts in this case reflect a Tax Court Of Canada case that was decided in June, 2010 (Vipan Bansal vs. Minister Of National Revenue).

At issue was whether the appellant worked as an employee or as an independent contractor during the period from January 1, 2008 to October 21, 2008 for the purposes of the Canada Pension Plan and the Employment Insurance Act. The appellant argued that he was an employee of the payor whereas the Minister determined that he was not.

### *Intent*

The most important factor in the employer/independent contractor decision is the intent of both parties. The court noted that, as there was a disagreement between the parties as to intent, it becomes necessary to look at all of the facts to determine the legal relationship that they reflect.

### *Factors Suggesting Independent Contractor Status*

**Tools** The Appellant provided his own car.

**Risk Of Loss**

- The Appellant had liability exposing him to a risk of loss.
- The Appellant incurred vehicle expenses, including insurance, maintenance and fuel.
- The Appellant incurred operating expenses such as liability insurance and a driver training endorsement.
- The Appellant paid for the installation and removal of the emergency brake provided by the Payor.

**Chance Of Profit** The more hours (over 20) the Appellant worked the greater were his chances of profit. Although not stated in the problem, this was not the case for the driving instructors having employee status since they were limited in the number of hours they could work.

**Control**

- The Appellant did not have a set schedule of hours or days of work.
- The Appellant could choose the routes for the lessons.
- The Appellant could work for anyone else (except as a driving instructor).

**Behaviour As An Entrepreneur** He behaved like an independent contractor in that he invoiced the Payor, charged the Payor GST, maintained his own books and records, and reported business income and business expenses on his 2006, 2007 and 2008 income tax returns.

### *Factors Suggesting Employee Status*

**Tools** The Payor provided vehicle signage, mirrors, traffic cones and an emergency brake.

**Control**

- The Payor provided the Appellant with a guide and the Appellant had to comply with all the instructions therein regarding the method of teaching.
- Although the Appellant could hire an assistant, he could not have someone replace him.

The conclusion of the Tax Court Of Canada was as follows:

> Here we have an Appellant who, if I accept his testimony, was an employee (even though he behaved for a number of years like an independent contractor), and yet he performed his services in his own vehicle, paid for the installation and removal of the emergency brake provided by the Payor, incurred operating expenses, including vehicle expenses (insurance, maintenance and fuel), paid for liability insurance and a driver training endorsement, effectively had exposure to all kinds of liability, did not



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have a set schedule of hours or days of work and could, in a way, set his own deadlines and priorities.

I cannot find in these circumstances that the existence of some degree of control by the Payor over the Appellant outweighs the overall view that the Appellant was in business on his own account (e.g., an independent contractor).



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## Solution to Assignment Problem Three - 4

### *Case A*

In this Case, the taxable benefit would be calculated as follows:

| | |
|---|---|
| Standby Charge [(2%)($28,500)(12)(18,000/20,004*)] | $6,155 |
| Operating Cost Benefit - Lesser Of: | |
| • [(18,000)($0.27)] = $4,860 | |
| • [(1/2)($6,155)] = $3,078 | 3,078 |
| Total Benefit | $9,233 |

*[(12)(1,667)]

As Ms. Smith's usage is more than 50 percent employment related, she can use the reduced standby charge calculation. In addition, she can use one-half the standby charge as her operating cost benefit.

### *Case B*

In this Case, the taxable benefit would be calculated as follows:

| | |
|---|---|
| Standby Charge [(2%)($28,500)(10)(11,000/16,667*)] | $3,762 |
| Operating Cost Benefit - Lesser Of: | |
| • [(11,000)($0.27)] = $2,970 | |
| • [(1/2)($3,762)] = $1,881 | 1,881 |
| Total Benefit | $5,643 |

*[(10)(1,667)]

As Ms. Smith's usage is more than 50 percent employment related, she can use the reduced standby charge calculation. In addition, she can use one-half the standby charge as her operating cost benefit.

### *Case C*

In this Case, the taxable benefit would be calculated as follows:

| | |
|---|---|
| Standby Charge [(2%)($28,500)(6)] | $ 3,420 |
| Operating Cost Benefit [(28,300)($0.27)] | 7,641 |
| Total Benefit | $11,061 |

As Ms. Smith's employment usage was less than 50 percent, there is no reduction in the basic standby charge. This also means that Ms. Smith cannot elect to use the alterative calculation of the operating costs benefit as one-half of the standby charge.



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## Solution to Assignment Problem Three - 8

### *Part A*

There would be no tax effects resulting from the granting of the options in 2011.

Since the option price was below the fair market value at the time the shares were issued, there is no deduction available under ITA 110(1)(d) in the calculation of Taxable Income. As Patricia's employer is a public company, the exercise of the options in 2012 will result in the following addition to Net Income For Tax Purposes and Taxable Income:

| | |
|---|---:|
| Fair Market Value At Exercise [(1,500)($50)] | $75,000 |
| Option Price [(1,500)($45)] | ( 67,500) |
| Employment Income | $ 7,500 |

In 2013, when the shares are sold, there is the following addition to Net Income For Tax Purposes and Taxable Income:

| | | |
|---|---:|---:|
| Proceeds Of Disposition [(1,500)($55)] | | $82,500 |
| Adjusted Cost Base [(1,500)($50)] | ($75,000) | |
| Commission [($82,500)(1%)] | ( 825) | ( 75,825) |
| Capital Gain | | $ 6,675 |
| Inclusion Rate | | 1/2 |
| Taxable Capital Gain | | $ 3,338 |

### *Part B*

There would be no tax effects resulting from the granting of the options in 2011.

If, the 2011 trading value for the shares had been $44, the option price would have been above fair market value and the ITA 110(1)(d) deduction would be available. On this basis, the 2012 results would be as follows:

| | |
|---|---:|
| Fair Market Value At Exercise [(1,500)($50)] | $75,000 |
| Option Price [(1,500)($45)] | ( 67,500) |
| Employment Income = Increase In Net Income For Tax Purposes | $ 7,500 |
| ITA 110(1)(d) Deduction [(1/2)($7,500)] | ( 3,750) |
| Increase In Taxable Income | $ 3,750 |

The results for 2013 would be unchanged from Part A.

### *Part C*

If Patricia's employer had been a Canadian controlled private company, there would be no tax effects in either 2011 or 2012.

There is no deduction available under either ITA 110(1)(d) or ITA 110(1)(d.1) when the shares are sold. The option price was below the fair market value when the options were issued. Further, Patricia did not hold the shares for the two years required for the ITA 110(1)(d.1) deduction. When the shares are sold in 2013, there is the following addition to Net Income For Tax Purposes and Taxable Income:

| | |
|---|---:|
| Fair Market Value At Exercise [(1,500)($50)] | $75,000 |
| Option Price [(1,500)($45)] | ( 67,500) |
| Taxable Capital Gain {[1/2][1,500)($55 - $50) - $825]} | 3,338 |
| Increase In Net Income For Tax Purposes And Taxable Income | $10,838 |



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## Solution to Assignment Problem Three - 10

Ms. Shirley Kantor's net employment income for the year ending December 31, 2013 would be calculated as follows:

| | |
|---|---|
| Salary | $142,000 |
| Federal And Provincial Income Tax | Nil |
| RPP Contributions | ( 3,200) |
| EI Premiums | Nil |
| CPP Contributions | Nil |
| United Way Donations | Nil |
| Professional Dues | ( 1,250) |
| Bonus - Item 2 | 25,000 |
| Car Benefit - Item 3 | 5,694 |
| Salary Advance - Item 4 | 50,000 |
| Allowance For Acquiring Business Clothing - Item 6 | 4,800 |
| Squash Club Membership - Item 6 | 2,800 |
| Financial Advisor Fees - Item 6 | 1,200 |
| Stock Option Benefit - Item 7 | 4,000 |
| Computer Related Supplies - Item 8 | ( 150) |
| Net Employment Income | $230,894 |

**Item 1** The reimbursement of moving expenses is not a taxable benefit. However, as the costs were reimbursed, Shirley cannot deduct them.

**Item 2** As employment income is determined on a cash basis, only the portion of the bonus that was received during 2013 will be included in income.

**Item 3** The taxable benefit on the car would be calculated as follows:

| | |
|---|---|
| Standby Charge [(2%)($39,550)(12)(8,000 ÷ 20,004*)] | $3,796 |
| Operating Cost Benefit - Lesser Of: | |
| [($0.27)(8,000)] = $2,160 | |
| [(1/2)($3,796)] = $1,898 | 1,898 |
| Total Benefit | $5,694 |

*[(12)(1,667)]

**Item 4** Even though the $50,000 is earned in 2014, it is paid in 2013 and, because employment income is on a cash basis, it must be included in income in that year.

**Item 5** The use of Aeroplan points earned on employment related travel does not create a taxable benefit.

**Item 6** While employer provided specialized clothing is not a taxable benefit, regular business clothing would not fit this description, resulting in the inclusion of this allowance in income. As the squash club membership is not used for employment related activity, it would be considered a taxable benefit. While mental or physical health counseling is not considered a taxable benefit, this is not the case with financial counseling.

**Item 7** While there would have been no employment inclusion resulting from the exercise of the stock options, there would be an inclusion of $4,000 [(500)($28 - $20)] when the shares are sold. This inclusion would be accompanied by a deduction of $2,000 [(1/2)($4,000)] in the calculation of Taxable Income. However, the deduction does not enter into the calculation of net employment income.

**Item 8** While Shirley cannot deduct CCA (tax depreciation) on the computer, she can deduct the cost of the supplies.



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## Solution to Assignment Problem Three - 12

Mr. Brooks' net employment income would be calculated as follows:

| | | |
|---|---|---|
| Gross Salary | | $53,000 |
| Additions: | | |
| Bonus (Amount Received Only) | $6,500 | |
| Disability Insurance Receipts (Note One) | 4,200 | |
| Personal Benefit On Car (Note Two) | 1,034 | |
| Stock Option Benefit [($28 - $23)(200)] (Note Three) | 1,000 | |
| Home Relocation Loan Benefit (Note Four) | 625 | 13,359 |
| | | $66,359 |
| Deductions: | | |
| RPP Contributions | ($2,800) | |
| Union Dues | ( 240) | ( 3,040) |
| Net Employment Income | | $63,319 |

**Note One** As all of the premiums were paid by the employer and were not considered to be a taxable benefit, benefits received under this coverage must be included in employment income.

**Note Two** The personal benefit on the company car, taking into consideration the two months he was in the hospital and unable to make use of the car, would be as follows:

| | |
|---|---|
| Standby Charge [(2/3)(12)($678)(10/12)(5,000/16,670)] | $1,356 |
| Operating Cost Benefit - Lesser Of: | |
| • [(5,000)($0.27)] = $1,350 | |
| • [(1/2)($1,356)] = $678 | 678 |
| Less: Payments Withheld By Employer | ( 1,000) |
| Taxable Benefit | $1,034 |

**Note Three** Although Mr. Brooks would qualify for the deduction of one-half of the stock option benefit under ITA 110(1)(d), it is a deduction from Taxable Income and would not affect the calculation of net employment income.

**Note Four** The taxable benefit associated with the home relocation loan would be calculated as follows:

[($125,000)(2% - Nil)(3/12)] = $625

There is a deduction available equal to the benefit associated with an interest free home relocation loan of up to $25,000. However, the deduction is applied in the calculation of Taxable Income. As a result, the usual ITA 80.4(1) imputed interest benefit is included in net employment income, a figure that is not changed by the deduction.

**Note Five** As it is reasonable to assume that the accounting course would primarily benefit his employer and is not for personal interest, the fees reimbursed by his employer would not create a taxable benefit.



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# CHAPTER FIVE SOLUTIONS

## Solution to Assignment Problem Five - 1

***Part A***

As the manufacturing and processing equipment was purchased after March 18, 2007 and before January 1, 2016, it would be allocated to Class 29. CCA for this Class is determined on a 50 percent straight line basis. This results in a 25%/50%/25% straight line write-off after consideration of the half-year rule.

The maximum CCA for 2011, 2012 and 2013 would be calculated as follows:

| | |
|---|---:|
| Capital Cost Of M&P Assets | $500,000 |
| 2011 CCA [(50%)(1/2)($500,000)] | ( 125,000) |
| UCC January 1, 2012 | $375,000 |
| 2012 CCA [(50%)($500,000 Original Cost)] | ( 250,000) |
| UCC January 1, 2013 | $125,000 |
| 2013 CCA (Balance In Class) | ( 125,000) |
| UCC January 1, 2014 | Nil |

***Part B***

If the new building is placed in the existing Class 1 and is not put into a separate Class 1, the applicable CCA rate will be 4 percent.

If the building is put into a separate Class 1, the applicable CCA rates will be as follows:

**Alternative 1** - 100 percent for manufacturing

Since the building will be used more than 90 percent for manufacturing, the CCA rate is 10 percent.

**Alternative 2** - 60 percent for manufacturing and 40 percent for office space

Since the building will not be used more than 90 percent for manufacturing, but will be used more than 90 percent for non-residential purposes, the CCA rate is 6 percent.

**Alternative 3** - 40 percent for manufacturing, 30 percent for office space and 30 percent for long-term residential rentals

Since the building will not be used more than 90 percent for non-residential purposes, the CCA rate is 4 percent. This is the same rate as would apply if the building was added to the existing Class 1.



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## Solution to Assignment Problem Five - 2

**Note To Instructor** Although the replacement property rules (covered in Chapter 8) might be considered relevant as a building was burned down and a new building was purchased, we have specified that a warehouse was disposed of, and an office building was purchased, to avoid that complication in this problem.

### *Class 1*

As it is a new building, is going to be used 100 percent for non-residential purposes, and it has been put in a separate Class, it is eligible for the enhanced CCA rate of 6 percent. Given this, the required information for this Class is as follows:

| | |
|---|---|
| January 1, 2013 UCC | Nil |
| Additions ($623,000 - $145,000) | $478,000 |
| One-Half Net Additions | ( 239,000) |
| Balance Subject To CCA | $239,000 |
| CCA [(6%)($239,000)] | ( 14,340) |
| One-Half Net Additions | 239,000 |
| January 1, 2014 UCC | $463,660 |

### *Class 3*

The required information for this Class is as follows:

| | |
|---|---|
| January 1, 2013 UCC | $798,000 |
| Dispositions - Lesser Of: | |
| Capital Cost - $150,000 | |
| Proceeds Of Disposition - $185,000 | ( 150,000) |
| Balance Subject To CCA | $648,000 |
| CCA [(5%)($648,000)] | ( 32,400) |
| January 1, 2014 UCC | $615,600 |

There would also be a taxable capital gain from the disposition of $17,500 [(1/2)($185,000 - $150,000)].

### *Class 8*

The required calculations for this class would be as follows:

| | | |
|---|---|---|
| January 1, 2013 UCC | | $346,000 |
| Additions | $105,000 | |
| Disposition - Lesser Of: | | |
| • Capital Cost = $83,000 | | |
| • Proceeds Of Disposition = $75,000 | ( 75,000) | 30,000 |
| One-Half Net Additions [(50%)($30,000)] | | ( 15,000) |
| Balance Subject To CCA | | $361,000 |
| CCA [(20%)($361,000)] | | ( 72,200) |
| One-Half Net Additions | | 15,000 |
| January 1, 2014 UCC Balance | | $303,800 |



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### *Class 10 - Vehicles*

The required information for this Class would be calculated as follows:

| | | |
|---|---|---|
| January 1, 2013 UCC | | $150,000 |
| Additions [(3)($25,000)] | $75,000 | |
| Disposition of Truck - Lesser Of: | | |
| • Capital Cost = $42,000 | | |
| • Proceeds Of Disposition = $18,000 | ( 18,000) | 57,000 |
| One-Half Net Additions [(50%)($57,000)] | | ( 28,500) |
| Balance Subject To CCA | | $178,500 |
| CCA [(30%)($178,500)] | | ( 53,550) |
| One-Half Net Additions | | 28,500 |
| January 1, 2014 UCC Balance | | $153,450 |

### *Class 10.1*

In the case of Class 10.1, recapture is not included in income and terminal losses cannot be deducted. However, in the year of disposition, one-half of the usual CCA can be deducted. This would $3,825 [(1/2)(30%)($25,500)]. The January 1, 2014 UCC balance would be nil.

### *Class 13*

The 2011 improvements are being written off over 10 years, the original term of the lease (8 years), plus the first renewal of two years. As the Company takes maximum CCA each year, the CCA taken in 2011 and 2012 must equal 15 percent [(10%)(1/2) + 10%] of the cost of the improvements. Given this, the January 1, 2013 UCC must equal 85 percent of the cost of the improvements. This indicates that the cost must have been $50,000 ($42,500 ÷ 85%).

Given this, the required information for this Class would be as follows:

| | | |
|---|---|---|
| January 1, 2013 Balance | | $42,500 |
| Additions | | 40,000 |
| Balance Subject To CCA | | $82,500 |
| CCA: | | |
| • First Improvements ($50,000 ÷ 10) | ($5,000) | |
| • Current Improvements [($40,000 ÷ 8)(1/2)] | ( 2,500) | ( 7,500) |
| January 1, 2014 UCC Balance | | $75,000 |

### *Class 29*

The required information for this Class would be calculated as follows:

| | |
|---|---|
| January 1, 2013 Balance | $63,000 |
| Disposition - Lesser Of: | |
| • Capital Cost = $252,000 | |
| • Proceeds Of Disposition = $51,000 | ( 51,000) |
| Balance Before Terminal Loss | $12,000 |
| Terminal Loss | ( 12,000) |
| January 1, 2014 UCC Balance | Nil |

After all of the assets in Class 29 have been retired there is still a $12,000 UCC balance. This results in a terminal loss that will be deducted in full from the Net Income of Fortin Aluminum. The terminal loss will also be deducted from the UCC balance.



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***Class 50***

The required information for this Class can be calculated as follows:

| | |
|---|---|
| January 1, 2013 Balance | $23,000 |
| Additions | 18,000 |
| One-Half Net Additions [(50%)($18,000)] | ( 9,000) |
| CCA Base | $32,000 |
| CCA [(55%)($32,000)] | ( 17,600) |
| One-Half Net Additions | 9,000 |
| January 1, 2014 UCC | $23,400 |

***Summary Of The Results (Not Required)***

The maximum CCA for the year ending December 31, 2013 and the January 1, 2014 UCC balances can be summarized as follows:

| | Maximum CCA | UCC |
|---|---|---|
| Class 1 | $14,340 | $463,660 |
| Class 3 | 32,400 | 615,600 |
| Class 8 | 72,200 | 303,800 |
| Class 10 | 53,550 | 153,450 |
| Class 10.1 | 3,825 | Nil |
| Class 13 | 7,500 | 75,000 |
| Class 29 | Nil | Nil |
| Class 50 | 17,600 | 23,400 |

In addition, the following income effects resulted from the information provided in the problem:

| | |
|---|---|
| Taxable Capital Gain On Class 3 Building | $17,500 |
| Terminal Loss On Class 29 Assets | ( 12,000) |
| Total Addition | $ 5,500 |



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## Solution to Assignment Problem Five - 5

The maximum CCA for 2011, 2012, and 2013, would be calculated as in the following schedules:

| 2011 | Class 1 | Class 10 | Class 8 |
|---|---|---|---|
| Opening Balance | Nil | Nil | Nil |
| Additions | | | |
| Class 1 ($326,000 - $53,000) | $273,000 | | |
| Class 10 [(12)($23,000)] | | $276,000 | |
| Class 8 | | | $85,000 |
| One-Half Net Additions | ( 136,500) | ( 138,000) | ( 42,500) |
| CCA Base | $136,500 | $138,000 | $42,500 |
| Maximum CCA | | | |
| Class 1 [(6%)($136,500)(245 ÷ 365)]* | ( 5,497) | | |
| Class 10 [(30%)($138,000)(245 ÷ 365)] | | ( 27,789) | |
| Class 8 [(20%)($42,500)(245 ÷ 365)] | | | ( 5,705) |
| One-Half Net Additions | 136,500 | 138,000 | 42,500 |
| January 1, 2012 UCC | $267,503 | $248,211 | $79,295 |

*As the Class 1 building is being used 100 percent for non-residential purposes and is allocated to a separate Class 1, it would qualify for the 6 percent CCA rate.

The total maximum CCA for 2011 would be $38,991 ($5,497 + $27,789 + $5,705).

| 2012 | Class 1 | Class 10 | Class 8 | Class 10.1 |
|---|---|---|---|---|
| Beginning UCC | $267,503 | $248,211 | $79,295 | Nil |
| Additions | | | | |
| Class 1 | Nil | | | |
| Class 10 [(5)($27,000)] | | 135,000 | | |
| Class 8 | | | Nil | |
| Class 10* | | | | $30,000 |
| Class 10 Disposition - Lesser Of: | | | | |
| Capital Cost = $115,000 | | | | |
| Proceeds = $80,000 | Nil | ( 80,000) | Nil | |
| One-Half Net Additions | Nil | ( 27,500) | Nil | ( 15,000) |
| CCA Base | $267,503 | $275,711 | $79,295 | $15,000 |
| Maximum CCA | | | | |
| Class 1 [(6%)($267,503)] | ( 16,050) | | | |
| Class 10 [(30%)($275,711)] | | ( 82,713) | | |
| Class 8 [(20%)($79,295)] | | | ( 15,859) | |
| Class 10.1 [(1/2)(30%)($30,000)] | | | | ( 4,500) |
| One-Half Net Additions | | 27,500 | Nil | 15,000 |
| January 1, 2013 UCC | $251,453 | $220,498 | $63,436 | $25,500 |

*The CCA base for the luxury car is limited to $30,000.

The total maximum CCA for 2012 would be $119,122 ($16,050 + $82,713 + $15,859 + $4,500).



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| 2013 | Class 1 | Class 10 | Class 8 |
|---|---|---|---|
| Beginning UCC | $251,453 | $220,498 | $63,436 |
| Additions | Nil | Nil | Nil |
| Proceeds Of Disposition - Lesser Of: | | | |
| $289,000 Vs. $273,000 | ( 273,000) | | |
| $296,000 Vs. $135,500 | | ( 135,500) | |
| $85,000 Vs. $12,300 | | | ( 12,300) |
| Balance With No Remaining Assets | ( $21,547) | $ 84,998 | $51,136 |
| Class 1 Recapture | 21,547 | | |
| Terminal Losses | | ( 84,998) | ( 51,136) |
| January 1, 2014 UCC | Nil | Nil | Nil |

With respect to the Class 10.1 vehicle, the *Income Tax Regulations* permit taking one-half of the regular CCA in the year of disposition. This amount would be $3,825 [(1/2)(30%)($25,500)].

No recapture of terminal loss can be recognized with respect to Class 10.1. However, the balance would be eliminated, leaving a January 1, 2014 UCC of nil.

The only CCA for 2013 would be the Class 10.1 CCA of $3,825 as Classes 1, 8 and 10 had no CCA for the year. There would be recapture of $21,547 for Class 1, a terminal loss of $84,998 for Class 10 and a $51,136 terminal loss for Class 8.

There would also be a taxable capital on the building of $8,000 [(1/2)($289,000 - $273,000)].



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## Solution to Assignment Problem Five - 6

### *Part A*

The required calculation of the maximum CCA and CEC for 2013 is as follows:

| Item | Amount |
|---|---|
| Class 8 (Note 1) | $ 46,600 |
| Class 10 [(30%)($152,000)] | 45,600 |
| Class 12 (Note 2) | 56,000 |
| Class 13 (Note 3) | 32,000 |
| CEC [(7%)($210,000)] | 14,700 |
| Maximum Total | $194,900 |

**Note 1** The Class 8 CCA would be calculated as follows:

| Item | Amount |
|---|---|
| Opening Balance | $220,000 |
| Additions | 42,000 |
| Proceeds Of Disposition (Less Than Cost) | ( 16,000) |
| One-Half Net Additions [(1/2)($42,000 - $16,000)] | ( 13,000) |
| CCA Base | $233,000 |
| CCA Rate | 20% |
| Maximum CCA | $ 46,600 |

**Note 2** The rate for Class 12 is 100 percent. However, some additions to this Class are subject to the half-year rules. The presence of an opening balance of $56,000 indicates that there must have been $112,000 of costs in 2012 that were subject to this rule. Given this, the entire balance could be deducted in 2013.

**Note 3** The $272,000 balance in Class 13 is equal to 85 percent of $320,000. This means that during the two years 2011 and 2012, 15 percent of their cost was deducted as CCA. As the half-year rules are applicable to this Class, this represents a half year for 2011 and a full year for 2012. Since Class 13 is a straight-line Class, this indicates that the CCA rate is 10 percent (15% ÷ 1.5). Based on this analysis, maximum CCA for 2013 would be $32,000 [(10%)($320,000)].

### *Part B*

Since the Company only has Net and Taxable Income before CCA and CEC of $51,000 and the problem states that loss carry overs should not be considered, maximum CCA and CEC would not be deducted. Only $51,000 in CCA and CEC should be taken in order to reduce the Taxable Income to nil.

As to which balances of CCA or CEC should be reduced, the usual procedure is to deduct the required amount from the balances with the lowest rates. By leaving the balances with higher rates untouched, larger amounts of CCA and CEC can be deducted in later periods as required.

Taking this approach, the recommended CCA and CEC deductions would be as follows:

| Item | Amount |
|---|---|
| CEC (Maximum Available) | $14,700 |
| Class 13 (Maximum Available) | 32,000 |
| Class 8 ($51,000 - $14,700 - $32,000) | 4,300 |
| Total CCA | $51,000 |

The deduction of this amount of CCA and CEC would serve to reduce Taxable Income to nil.



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## Solution to Assignment Problem Five - 8

**Note To Instructor**: The replacement property rules are covered in Chapter 8 and are not taken into consideration in this problem for the building.

### *Class 1*

The calculations related to the building that was replaced are as follows:

| | |
|---|---|
| Opening UCC Balance | $478,695 |
| Disposition - Lesser Of: | |
| Proceeds = $525,000 ($650,000 - $125,000) | |
| Capital Cost = $545,000 ($625,000 - $80,000) | ( 525,000) |
| Negative Ending Balance = Recapture Of CCA | ($ 46,305) |

There is also a capital gain resulting from the sale of the land. However, the requirements of the problem are limited to CCA, recapture, and terminal losses.

Since the replacement building is new, used 100 percent for non-residential purposes and allocated to a separate Class 1, it qualifies for an enhanced CCA rate. As it is not used for manufacturing and processing, the enhanced rate is 6 percent. Using this rate, the CCA on the new building would be as follows:

| | |
|---|---|
| Opening UCC Balance | Nil |
| Additions ($745,000 - $125,000) | $620,000 |
| One-Half Net Additions [(1/2)($620,000)] | ( 310,000) |
| CCA Base | $310,000 |
| Rate | 6% |
| Maximum 2013 CCA | $ 18,600 |

### *Class 8*

The required calculation here would be as follows:

| | |
|---|---|
| Opening Class 8 Balance | $243,000 |
| Additions | 74,000 |
| Disposals: Lesser Of: | |
| Capital Cost = $56,000 | |
| Proceeds = $17,000 | ( 17,000) |
| One-Half Net Additions [(1/2)($74,000 - $17,000)] | ( 28,500) |
| CCA Base | $271,500 |
| Rate | 20% |
| Maximum 2013 CCA | $ 54,300 |

### *Class 10*

The required calculations here would be as follows:

| | |
|---|---|
| Opening UCC Balance And CCA Base | $126,000 |
| Rate | 30% |
| Maximum 2013 CCA | $ 37,800 |

### *Class 10.1*

The Lexus would be allocated to a separate Class 10.1. The amount would be limited to $30,000, resulting in maximum 2013 CCA of $4,500 [(1/2)(30%)($30,000)]. The kilometers driven for personal purposes would affect the taxable benefit, but does not affect the CCA.



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### *Class 13*

Class 13 is a straight-line class. In this case, the term of the lease and one renewal totals ten years, resulting in a 10 year write off. The maximum CCA for 2013 would be $15,000 ($150,000 ÷ 10).

### *Class 14*

The limited life franchise would be allocated to Class 14 and amortized on a straight line basis over its legal life. Although this franchise was purchased on August 1, this would only affect the year of acquisition and the last year of its life. The maximum 2013 CCA would be for a complete year and would equal $7,750 ($62,000 ÷ 8).

### *CEC*

The maximum deduction from the cumulative eligible capital account is calculated as follows:

| | |
|---|---|
| 2011 Addition [(3/4)($84,000)] | $63,000 |
| CEC Amount At 7 Percent | ( 4,410) |
| January 1, 2012 Balance | $58,590 |
| CEC Amount At 7 Percent | ( 4,101) |
| January 1, 2013 Balance | $54,489 |
| Disposal [(3/4)($65,000)] | ( 48,750) |
| Balance After Disposal | $ 5,739 |
| CEC Amount At 7 Percent | ( 402) |
| January 1, 2014 Balance (Not Required) | $ 5,337 |

### *Summary (Required)*

The total maximum CCA and CEC write-off is calculated as follows:

| | |
|---|---|
| Class 1 | $ 18,600 |
| Class 8 | 54,300 |
| Class 10 | 37,800 |
| Class 10.1 | 4,500 |
| Class 13 | 15,000 |
| Class 14 | 7,750 |
| CEC Amount | 402 |
| Total CCA and CEC | $138,352 |

In addition, there is Class 1 recapture of $46,305.



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## Solution to Assignment Problem Six - 2

***Part A***

As the Honda Accord was sold during 2013, the Company would not be able to deduct CCA for that year. However, when the $25,000 proceeds of disposition is deducted from the $24,650 UCC balance, the result would be recapture of $350 ($24,650 - $25,000). Note that, because the BMW cost more than $30,000, it would have to be allocated to a separate Class 10.1. This means that its acquisition would not eliminate the recapture in Class 10.

The maximum CCA deduction on the BMW for the year ending December 31, 2013, would be calculated as follows:

| | |
|---|---:|
| Capital Cost (Limited To $30,000) | $30,000 |
| One-Half Net Additions | ( 15,000) |
| Balance For CCA Purposes | $15,000 |
| Rate | 30% |
| CCA For 2013 | $ 4,500 |

The operating costs for both vehicles totaling $12,300 would be deductible.

***Part B***

Because the Honda was used primarily (more than 50 percent) for employment purposes, it is eligible for the reduced standby charge and the alternative operating cost benefit calculation. This is not the case with the BMW sedan.

The minimum total benefit on the two vehicles would be calculated as follows:

| | | |
|---|---:|---:|
| Standby Charge: | | |
| Honda [(2%)($29,000)(6)(8,000 ÷ 10,002)] | | $ 2,783 |
| BMW - No Reduction [(2%)($105,000)(6)] | | 12,600 |
| Total Standby Charge | | $15,383 |
| Operating Cost Benefit: | | |
| Honda - Lesser Of: | | |
| [($2,783)(1/2)] = $1,392 | | |
| [(8,000)($0.27)] = $2,160 | $1,392 | |
| BMW [(19,000)($0.27)] | 5,130 | 6,522 |
| Minimum Total Benefit For 2013 | | $21,905 |



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## Solution to Assignment Problem Six - 8

### *Part A*

Under ITA 18(12), the following conditions must be satisfied in order for expenses related to work space in a self-contained domestic establishment to be deductible:

- the work space is either the individual's principal place of business; or
- the work space is used exclusively for the purpose of earning income from business and is used on a regular and continuous basis for meeting clients, customers, or patients of the individual in respect of the business.

With respect to Mr. Larson's mail order business, the allocated space in his home would appear to be his principal place of business. This means that he would be able to deduct work space in home costs in determining his net business income.

### *Part B*

The calculation of the minimum net business income to be reported in Mr. Larson's personal tax return is as follows:

| | | |
|---|---|---|
| Revenues | | $182,000 |
| Less: Expenses Other Than Home Work Space Costs: | | |
| Cost Of Merchandise Sold | ($98,000) | |
| Packaging Materials | ( 2,400) | |
| Shipping Costs | ( 4,600) | |
| Miscellaneous Office Supplies | ( 560) | |
| Telephone | ( 1,100) | |
| Printing Of Posters And Brochures | ( 420) | |
| CCA (Note 1) | ( 2,320) | ( 109,400) |
| Income Before Home Work Space Costs | | $ 72,600 |
| Less: Home Work Space Costs (Note 2) | | ( 4,332) |
| Net Business Income | | $ 68,268 |

**Note 1** Maximum CCA amounts on the assets of the business (not including CCA on the house) for the short fiscal year would be calculated as follows (alternative calculations shown in the two columns):

| | 100% | Short Fiscal Year (335/365) |
|---|---|---|
| Class 8 [($18,500)(1/2)(20%)] | $1,850 | $1,698 |
| Class 50 [($1,430)(1/2)(55%)] | 393 | 360 |
| Class 12 [($570)(1/2)(100%)] | 285 | 262 |
| Total | $2,528 | |
| Short Fiscal Year Factor | 335/365 | |
| Maximum 2013 CCA | $2,320 | $2,320 |



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**Note 2** The work space in home costs would be calculated as follows:

| | |
|---|---|
| Utilities For Home (Heat, Light, And Water) | $ 3,200 |
| Mortgage Interest Paid | 10,100 |
| House Insurance | 500 |
| Property Taxes | 4,300 |
| Repairs And Maintenance For Home | 2,600 |
| Total | $20,700 |
| Class 1 CCA [($426,000 - $150,000)(1/2)(4%)] | 5,520 |
| Total Costs For The Home | $26,220 |
| Percentage Of Floor Space | 18% |
| Subtotal | $ 4,720 |
| Short Fiscal Year Factor | 335/365 |
| Deductible Home Work Space Costs | $ 4,332 |

***Part C***

There are two issues that should be discussed with Mr. Larson.

- As this problem asks for "minimum" net business income, CCA must be deducted on Mr. Larson's home. The problem with this is that, if he takes CCA, it could jeopardize the principal residence exemption on this property, resulting in the payment of taxes on a portion of the taxable capital gain that might arise on any future sale of the property, assuming real estate prices are increasing. This is discussed in more detail in Chapter 8.
- Although it is not relevant for this year, Mr. Larson should be aware that the deduction of work space in home costs cannot be used to create a loss in the future. However, any amount not deductible because it is greater than his income can be deducted in any subsequent year provided there is sufficient income from the same business in that year. This provides for an unlimited carry forward of unused work space in home costs (see IT-514, *Work Space in Home Expenses*).



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## Solution to Assignment Problem Six - 9

The minimum Net Income For Tax Purposes would be calculated as follows (the related item number in the problem precedes the adjustment):

| Item | Description | | |
|---|---|---|---|
| | Accounting Income | | $691,183 |
| | Add: | | |
| I/S | Total Income Tax Expense | $217,000 | |
| I/S | Amortization Expense | 550,000 | |
| 1 | Accounting Bad Debt Expense (Note 1) | 16,750 | |
| 1 | 2012 Reserve For Bad Debts | 13,000 | |
| 2 | Charitable Donations | 27,000 | |
| 2 | Bonus Payments (Deductible In 2013) | Nil | |
| 2 | Golf Club Membership Dues ($12,000 + $2,400) | 14,400 | |
| 2 | Business Meals And Entertainment [(1/2)($32,000)] | 16,000 | |
| 2 | Personal Meal Costs | 5,000 | |
| 2 | Staff BBQ (Fully Deductible) | Nil | |
| 2 | Production Sponsorships (Deductible) | Nil | |
| 2 | Advertising To U.S. Market (Deductible) | Nil | |
| 2 | Software Purchases (Capital Costs - Class 12 and 50) | 38,000 | |
| 2 | Costs Related To Amending Articles Of Incorporation (Added To CEC - Note 4)) | 6,000 | |
| 2 | Thailand Convention Expenses (Note 2) | 17,000 | |
| 3 | Non-Deductible Penalty And Interest Expense | 2,000 | |
| 3 | Other Interest Expense (Deductible) | Nil | |
| 4 | Non-Deductible Travel Costs (Note 3) | 1,570 | |
| 6 | Income Inclusion On Sale Of Client List (CEC - Note 4) | 43,902 | |
| 9 | Taxable Capital Gain On Sale Of Shares (Note 5) | 76,354 | 1,043,976 |
| | Deduct: | | |
| 1 | Actual Bad Debt Write-Offs For 2013 (Note 1) | ($ 11,750) | |
| 1 | 2013 Reserve For Bad Debts (Note 1) | ( 15,000) | |
| 5 | Maximum CCA (Note 6) | ( 197,693) | |
| 5 | Terminal Loss (Note 6) | ( 5,000) | |
| 6 | Net Accounting Gain On Disposal Of Intangibles [($115,000 - Nil) - ($80,000 - $63,000)] | ( 98,000) | |
| 8 | Landscaping Costs Capitalized For Accounting Purposes | ( 35,000) | ( 362,443) |
| | Net Income For Tax Purposes | | $1,372,716 |

**Note 1** While this would be unusual in practice, the accounting figure for bad debt expense is different from the tax figure. Given this, we have added back the accounting deduction of $16,750, and included the appropriate amounts for tax purposes.

**Note 2** It is likely that the CRA would argue that a convention in Thailand is not consistent with the territorial scope of the corporation. However, an argument could be made that, given it deals with costume design and is an annual convention, it should be deductible.

**Note 3** Since the kilometre-based allowances were non-taxable, the deductible mileage is $0.54 for the first 5,000 kilometres per employee and $0.48 for additional kilometres. The non-deductible automobile expenses are calculated as follows:



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| | |
|---|---|
| Actual milage paid: | |
| [($0.58)(7 employees @ 4,000) + (1 @ 7,500)] | $20,590 |
| Deductible portion: | |
| {[($0.54)(7 @ 4,000 + 1 @ 5,000)] + [$0.48 @ 2,500]} | ( 19,020) |
| Non-deductible portion | $ 1,570 |

**Note 4** The addition to income from the cumulative eligible capital account is calculated as follows:

| | |
|---|---|
| January 1, 2013 Balance | $18,098 |
| Addition: Costs Of Amending Articles Of Incorporation [(3/4)($6,000)] | 4,500 |
| Disposal Of Client List [(3/4)($115,000)] | ( 86,250) |
| Balance After Disposal | ($63,652) |

The amount to be added to income is comprised of the following:

| | | |
|---|---|---|
| CEC Deductions Taken In Previous Years: | | |
| Incorporation Fees [(3/4)($30,000)] | | $22,500 |
| Less January 1, 2013 Balance | | ( 18,098) |
| CEC Deducted Previously | | $ 4,402 |
| Balance ($63,652 - $4,402) | $59,250 | |
| Conversion Factor [(3/4 ÷ 1/2) | 2/3 | 39,500* |
| Total Income Inclusion From Disposal Of Eligible Capital | | $43,902 |

*The $39,500 can also be calculated as [(1/2)($115,000 - $30,000 - $6,000)].

**Note 5** The capital gain was credited to retained earnings in error. It is necessary to add the taxable portion of $76,354 [(1/2)($152,708)] to income in order to calculate net income for tax purposes.

**Note 6** The CCA, and terminal loss for the year ending December 31, 2013, can be calculated as follows:

Class 1 - Existing Building

| | |
|---|---|
| Opening UCC | $650,000 |
| Rate (Class 1) | 4% |
| Class 1 CCA | $ 26,000 |

Class 1 - New Building - Separate Class

| | |
|---|---|
| Opening UCC | Nil |
| Addition | $475,000 |
| One-Half Net Additions | ( 237,500) |
| CCA Base | $237,500 |
| Rate (Class 1 > 90% used for manufacturing) | 10% |
| Class 1 CCA | $ 23,750 |



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Class 6 - Fence

| | |
|---|---:|
| Opening UCC | Nil |
| Addition | $52,000 |
| One-Half Net Additions | ( 26,000) |
| CCA Base | $ 26,000 |
| Rate (Class 6) | 10% |
| Class 6 CCA | $ 2,600 |

Class 8 - Office and other Equipment

| | |
|---|---:|
| Opening UCC | $95,000 |
| Addition | 1,200 |
| Disposition - Lesser Of: | |
| Capital Cost = $5,000 | |
| Proceeds Of Disposition = $3,500 | ( 3,500) |
| CCA Base | $92,700 |
| Rate (Class 8) | 20% |
| Class 8 CCA | $18,540 |

Class 10.1 - Existing Automobile

| | |
|---|---:|
| Opening UCC And CCA Base | $17,850 |
| Rate (Class 10.1) | 30% |
| Class 10.1 Full CCA | $ 5,355 |
| Claim (50 Percent In Year Of Disposition) | 50% |
| Class 10.1 CCA On Sold Automobile | $2,678 |

Class 10.1 - Replacement Automobile

| | |
|---|---:|
| Opening UCC | Nil |
| Addition, Limited To $30,000 | $30,000 |
| One-Half Net Additions | ( 15,000) |
| CCA Base | $15,000 |
| Rate (Class 10.1) | 30% |
| Class 10.1 CCA | $ 4,500 |

Class 12 - Applications Software

| | |
|---|---:|
| Opening UCC | Nil |
| Addition | $13,000 |
| One-Half Net Additions | ( 6,500) |
| CCA Base | $ 6,500 |
| Rate (Class 12) | 100% |
| Class 12 CCA | $ 6,500 |

Class 14 - Limited Life Intangibles

| | |
|---|---:|
| Opening UCC | $68,000 |
| Disposition - Lesser Of: | |
| Capital Cost = $95,000 | |
| Proceeds Of Disposition = $63,000 | ( 63,000) |
| Positive Ending Balance = Terminal Loss | $ 5,000 |



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Class 29 - Manufacturing and Processing Equipment

The 2010 addition to Class 29 was fully depreciated for tax purposes in 2012 (25% claim in 2010, 50% in 2011, and the final 25% in 2012). The 2012 addition of $180,000 will have resulted in a claim of $45,000 [(25%)($180,000)] for that year, leaving the opening balance of $135,000.

| | |
|---|---|
| Class 29 CCA [(50%)($180,000)] | $90,000 |

Class 44 - Limited Life Patent

| | |
|---|---|
| Opening UCC And CCA Base | $ 65,000 |
| Rate (Class 44) | 25% |
| Class 44 CCA | $ 16,250 |

Class 50 - Systems Software

| | |
|---|---|
| Opening UCC | Nil |
| Addition | $25,000 |
| One-Half Net Additions | ( 12,500) |
| CCA Base | $12,500 |
| Rate (Class 50) | 55% |
| Class 50 CCA | $ 6,875 |

### Summary of CCA

| | |
|---|---|
| Class 1 CCA - Existing Building | $ 26,000 |
| Class 1 CCA - New Building, separate class | 23,750 |
| Class 6 CCA | 2,600 |
| Class 8 CCA | 18,540 |
| Class 10.1 CCA ($2,678 + $4,500) | 7,178 |
| Class 12 CCA | 6,500 |
| Class 29 CCA | 90,000 |
| Class 44 - Limited Life Patent | 16,250 |
| Class 50 CCA | 6,875 |
| Total CCA | $197,693 |

| | |
|---|---|
| Terminal Loss - Class 14 | $ 5,000 |

### Factors Not Affecting Solution (Not Required)

- The bonuses paid June 15, 2014 are fully deductible as they were paid within 180 days of the end of the year in which they were accrued.
- The cost of the annual barbeque for all staff is fully deductible.
- Sponsorship of various themed theatre productions that use Angie's costumes is fully deductible as an advertising expense.
- Advertising in a U.S. theatre magazine to promote the business to U.S. customers is a deductible cost.
- The interest expense amounts related to operations and late payment of municipal property taxes are fully deductible.



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## Solution to Assignment Problem Six - 10

### *Part A - Justification For Deductibility*

In order to establish if any dog-related expenses are deductible, it must first be determined if the dog was acquired for the purpose of producing income from Lorna's practice. It appears quite clear from the problem that Sigmund was purchased in order to increase Lorna's revenues.

Since Sigmund was legitimately acquired in connection with a business, the expenses related to his maintenance and training (food, vet bills, etc.) would be deductible in full. It is possible that the CRA would claim that there is a personal benefit associated with the ownership of Sigmund. To the extent that this claim could be enforced, some part of the deductions for Sigmund would be lost.

However, since the original intent was to acquire a dog to be specially trained to be used as a therapy dog, there is a strong case for the full deduction of the costs associated with Sigmund.

There would be no requirement to show how much income was actually attributable to Sigmund's efforts, only that a connection is made to the income earning process. With that connection established, there would be no need to allocate expenses based on when Sigmund actually began to work.

### *Part B - Calculation Of Deductible Expenses*

For the year ending December 31, 2013, Lorna would be able to deduct the following expenditures:

| | |
|---|---:|
| Food, including puppy vitamins and supplements | $ 2,600 |
| Veterinary fees | 800 |
| Therapy dog training course fees | 1,400 |
| Dog walking fees paid to Alec (Note 1) | 3,280 |
| Car lease for SUV (Note 2) | 3,095 |
| Operating expenses for SUV | 2,950 |
| Purchase of paw protectors (Note 3) | 140 |
| Class 8 CCA (Note 3) | 122 |
| Total Deductions | $14,387 |

**Note 1** Since Alec is charging Lorna the fair market rate for the dog walking service, the fee would be deductible.

**Note 2** The amount that Lorna can deduct for the SUV lease payments is limited to $3,095, the least of:

- $5,700 [($950)(6)];
- $4,907 [($800)(184/30)]; and
- $3,095 {[$5,700][$30,000 ÷ (85%)($65,000)]}.

**Note 3** Any clothing that would normally be replaced within a year would be deductible. However, clothing expected to last for longer than a year would be included in Class 8 as would the dog crate. As a result, the Class 8 CCA would be equal to $122 [($820 + $400)(1/2)(20%)].

### *Part C - Sale Of Sigmund*

As stated in the problem, Sigmund's purchase cost is a capital asset that cannot be claimed as depreciable property. As a result, the gain on Sigmund's sale is capital in nature and the taxable capital gain is equal to $3,250 [(1/2)($8,700 -$200 - $2,000)].

Assuming Lorna has no other Class 8 assets, the UCC of Class 8 at January 1, 2015 would be equal to $878 [$1,220 - $122 - (20%)($1,220 - $122)]. Since she received $200 for these items, Lorna has a terminal loss of $678.



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The net increase in Lorna's Net Income For Tax Purposes for 2015 would equal $2,572 ($3,250 - $678).

### *Note To Instructor*

Since the question of whether a therapy dog is a depreciable asset is not answered specifically in the textbook, the fact that it is not depreciable was stated in the problem. If you are interested in how this conclusion was reached, we offer the following analysis.

The first thing we observe is that the nature of a dog is technically that of a capital expenditure meaning that ITA 18(1)(b) prevents any deduction except to the extent permitted by ITA 20. You then observe that there is no specific deduction under ITA 20 that would recognize such an expense though general rules that might apply are given.

The first is whether CCA could be claimed. ITR 1102(2) sets out a few ground rules as to what definitely cannot be claimed as CCA. ITR 1102(1)(c)) states that CCA cannot be deducted on a capital expenditure that was not incurred for the purpose of earning income. ITR 1102(1)(b) precludes CCA where the cost of a dog would be included in inventory. As a result, a person who breeds dogs as a business would be able to deduct the capital expenditures related to the dog breeding through a cost of goods sold inventory deduction.

So if a dog is acquired for the purpose of earning income and is not part of an inventory then a CCA deduction is not necessarily prohibited. What is needed next is a relevant CCA class.

When you search through the classes you quickly discover that there is no class that refers to animals at all. (There are special inventory rules for livestock such as cattle but as inventory only, not as deductible CCA.) This leads you to Class 8 which is commonly referred to as the catch-all class designed to pick up anything not included in some other class. When you look at the description of Class 8 you will see that paragraph (i) includes within Class 8 any tangible capital property not included in some other class, but then it lists a number of exclusions one of which is an "animal".

As a result, it must be concluded that the original cost of the therapy dog cannot be written off through CCA and is a non-depreciable property.



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## Solution to Assignment Problem Seven - 3

***2012***

The maximum CCA for 2012 would be calculated as follows:

| | Class 1 | Class 8 |
|---|---|---|
| Addition | $255,000 | $12,800 |
| One-Half Net Additions | ( 127,500) | ( 6,400) |
| CCA Base | $127,500 | $ 6,400 |
| Maximum CCA: | | |
| [(4%)($127,500)] | ( 5,100) | |
| [(20%)($6,400)] | | ( 1,280) |
| Add: One-Half Net Additions | 127,500 | 6,400 |
| January 1, 2013 UCC | $249,900 | $11,520 |

As the maximum 2012 CCA of $6,380 ($5,100 + $1,280) is less than the 2012 net rental income before CCA of $15,100 ($26,000 - $10,900), the full amount can be deducted.

Note that when an individual uses assets to produce property income (e.g., rental income), the full calendar year is considered to be the taxation year of the individual. This means that the short fiscal period rules are not applicable to Mr. Taylor.

***2013***

The terminal loss for Class 8 would be calculated as follows:

| | |
|---|---|
| January 1, 2013 UCC | $11,520 |
| Disposition - Lesser Of: | |
| • Cost = $12,800 | |
| • Proceeds Of Disposition = $10,400 | ( 10,400) |
| Balance Before Terminal Loss | $ 1,120 |
| Terminal Loss | ( 1,120) |
| January 1, 2014 UCC | Nil |

The terminal loss will be deducted from the Class 8 UCC leaving a January 1, 2014 balance of nil.

The 2013 net rental income before CCA is $9,100 ($28,400 - $18,180 - $1,120) and includes the Class 8 terminal loss. As a result, the Class 1 CCA for 2013 would be calculated as follows:

| | |
|---|---|
| January 1, 2013 UCC | $249,900 |
| CCA Deducted - Lesser Of: | |
| • Maximum Available = [(4%)($249,900)] = $9,996 | |
| • Net Rental Income = $9,100 | ( 9,100) |
| January 1, 2014 UCC | $240,800 |

While the maximum 2013 CCA on the building would be $9,996, the CCA deductible is limited to the net rental income before CCA of $9,100. This would leave a net rental income of nil.



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# CHAPTER EIGHT SOLUTIONS

## Solution to Assignment Problem Eight - 1

***Part A***

The total cost of the 96 shares remaining on December 31, 2013 would be $2,596. This is calculated in the following table:

| Acquisition Or Sale Date | Shares Purchased (Sold) | Cost Per Share | Total Cost | Average Cost/Share |
|---|---|---|---|---|
| February, 2009 | 60 | 24.00 | $ 1,440 | |
| November, 2010 | 90 | 28.00 | 2,520 | |
| April, 2011 | 45 | 30.00 | 1,350 | |
| Subtotal | 195 | | $5,310 | $27.23 |
| October, 2011 | ( 68) | 27.23 | ( 1,852) | |
| September, 2013 | 22 | 26.00 | 572 | |
| Subtotal | 149 | | $4,030 | $27.05 |
| November, 2013 | ( 53) | 27.05 | ( 1,434) | |
| December 31, 2013 Balances | 96 | | $2,596 | |

***Part B***

The average cost of the shares sold during July, 2013 would be calculated as follows:

| | |
|---|---|
| April, 2012 Purchase [(200)($24)] | $ 4,800 |
| December, 2012 Purchase [(160)($33)] | 5,280 |
| Total Cost | $10,080 |
| Average Cost ($10,080 ÷ 360) | $28.00 |

Given this average cost, the taxable capital gain on the July, 2013 sale of shares would be calculated as follows:

| | |
|---|---|
| Proceeds [(260)($36)] | $9,360 |
| Cost [(260)($28)] | ( 7,280) |
| Capital Gain | $2,080 |
| Inclusion Rate | 1/2 |
| Taxable Capital Gain | $1,040 |



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## Solution to Assignment Problem Eight - 4

### *Capital Gain And Reserve Limits*

The total amount of the taxable capital gain can be calculated as follows:

| | |
|---|---|
| Proceeds Of Disposition | $1,730,000 |
| Adjusted Cost Base | ( 430,000) |
| Total Capital Gain | $1,300,000 |
| Inclusion Rate | 1/2 |
| Total Taxable Capital Gain | $ 650,000 |

Under ITA 40(1)(a)(iii), the amount that can be deducted as a capital gains reserve is equal to the lesser of:

- [(Capital Gain)(Proceeds Not Yet Due ÷ Total Proceeds)]
- [(Capital Gain)(20%)(4 - Number Of Preceding Years Ending After Disposition)]

The first of the limiting factors is based, as would be expected, on the pattern of collections. In contrast, the second factor serves to require that at least 20 percent of any gain be recognized in the year of disposition and each subsequent year, regardless of the pattern of cash collections.

The payment schedule for the sale required a 30 percent down payment ($519,000/$1,730,000), followed by annual payments of 5 percent ($86,500/$1,730,000) in the following years. Given this, the reserve percentages under the two components of the ITA 40(1)(a)(iii) schedule are as follows:

| Year | Proceeds Not Yet Due | 20 Percent Formula |
|---|---|---|
| 2013 | 70% | 80% |
| 2014 | 65% | 60% |
| 2015 | 60% | 40% |
| 2016 | 55% | 20% |
| 2017 | 50% | Nil |

### *2013*

The maximum reserve for 2013 would be the lesser of:

- [($1,300,000)($1,211,000 ÷ $1,730,000)] = $910,000
- [($1,300,000)(20%)(4 - 0)] = $1,040,000

The lesser figure is $910,000, reflecting the fact that the down payment was greater than 20 percent. Given this, the taxable capital gain for 2013 would be calculated as follows:

| | |
|---|---|
| Total Capital Gain | $1,300,000 |
| New Reserve | ( 910,000) |
| Capital Gain | $ 390,000 |
| Inclusion Rate | 1/2 |
| Taxable Capital Gain For 2013 | $ 195,000 |

### *2014*

The maximum reserve for 2014 would be the lesser of:

- [($1,300,000)($1,124,500 ÷ $1,730,000)] = $845,000
- [($1,300,000)(20%)(4 - 1)] = $780,000

The lesser figure is $780,000. This reflects the fact that the required recognition of 40 percent exceeds the percentage of the proceeds collected (35%). Given this, the taxable capital gain for 2014 would be calculated as follows:



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| | |
|---|---|
| Previous Year's Reserve | $910,000 |
| New Reserve | ( 780,000) |
| Capital Gain | $130,000 |
| Inclusion Rate | 1/2 |
| Taxable Capital Gain For 2014 | $ 65,000 |

***2015, 2016 And 2017***

In these years, the 20 percent formula continues to provide the lower figure and the reserve would decline as follows:

- 2015 [($1,300,000)(20%)(4 Years - 2 Years)] = $520,000
- 2016 [($1,300,000)(20%)(4 Years - 3 Years)] = $260,000
- 2017 [($1,300,000)(20%)(4 Years - 4 Years)] = Nil

Based on this, taxable capital gain for these three years will be calculated as follows:

| | 2015 | 2016 | 2017 |
|---|---|---|---|
| Previous Year's Reserve | $780,000 | $520,000 | $260,000 |
| New Reserve | ( 520,000) | ( 260,000) | Nil |
| Capital Gain | $260,000 | $260,000 | $260,000 |
| Inclusion Rate | 1/2 | 1/2 | 1/2 |
| Taxable Capital Gain | $130,000 | $130,000 | $130,000 |

At the end of 2017, the entire taxable gain of $650,000 will have been recognized:

| | |
|---|---|
| 2013 | $195,000 |
| 2014 | 65,000 |
| 2015 | 130,000 |
| 2016 | 130,000 |
| 2017 | 130,000 |
| Total | $650,000 |



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## Solution to Assignment Problem Eight - 7

The gains on the two properties can be calculated as follows:

| | Country Home | Condominium |
|---|---|---|
| Proceeds Of Disposition | $1,200,000 | $900,000 |
| Adjusted Cost Base | ( 850,000) | ( 625,000) |
| Real Estate Commissions | | |
| [(5%)($1,200,000)] | ( 60,000) | |
| [(5%)($900,000)] | | ( 45,000) |
| Total Capital Gain | $ 290,000 | $230,000 |

The annual gain was $18,125 ($290,000 ÷ 16) on the country home and $28,750 ($230,000 ÷ 8) on the condominium. This would indicate that the maximum number of years should be allocated to the condominium. However, because of the plus 1 in the reduction formula, one year can be left off.

Based on this analysis, the seven years 2007 through 2013 should allocated to the condominium, with the nine years 1998 through 2006 being allocated to the country home. The required calculations would be as follows:

| | Country Home | Condominium |
|---|---|---|
| Total Capital Gain | $ 290,000 | $230,000 |
| Exemption: | | |
| Country Home | | |
| [$290,000][(9 + 1) ÷ 16] | ( 181,250) | |
| Condominium | | |
| [$230,000][(7 + 1) ÷ 8] | | ( 230,000) |
| Capital Gain | $108,750 | Nil |
| Inclusion Rate | 1/2 | N/A |
| Taxable Capital Gain | $ 54,375 | Nil |

This gives a total taxable capital gain on the two properties of $54,375.



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## Solution to Assignment Problem Eight - 8

Listed personal property consists of these specified items as listed in ITA 54:

(i) print, etching, drawing, painting, sculpture, or other similar work of art,
(ii) jewelry,
(iii) rare folio, rare manuscript, or rare book,
(iv) stamp, or
(v) coin.

The tax consequences of the dispositions can be described as follows:

1. **Oil Painting** She will have a listed personal property capital gain on this disposition of $4,000 ($780,000 - $78,000 - $698,000).

2. **Miniature Vehicles** She will have a personal use property capital gain of $11,000 ($23,000 - $12,000).

3. **Antique Doll House** She will have a personal use property capital gain of $3,050 ($4,500 - $450 - $1,000 Floor).

4. **Sailboat** She will have a personal use property loss on the sailboat of $13,000 ($48,000 - $23,000 - $38,000). As the sailboat is not listed personal use property, the loss cannot be deducted against any source of income

5. **Jewelry Collection** She will have a listed personal property capital loss on this disposition of $18,000 ($43,000 - $61,000). As jewelry is included in the definition of listed personal property, this loss can be deducted to the extent that Rita has gains on listed personal property.

6. **First Edition** She will have a listed personal property capital gain on this disposition of $1,300 ($14,200 - $400 - $12,500).

The overall amount to be included in Net Income For Tax Purposes can be calculated as follows:

| | | |
|---|---|---|
| **Personal Use Property** | | |
| Gain On Miniature Vehicles | $11,000 | |
| Gain On Antique Doll House | 3,050 | |
| Loss On Sail Boat | Nil | $14,050 |
| **Listed Personal Property** | | |
| Gain On Oil Painting | $4,000 | |
| Gain On First Edition | 1,300 | |
| Total Listed Personal Property Gains | $5,300 | |
| Loss On Jewelry (See Note) | ( 5,300) | Nil |
| Net Capital Gains | | $14,050 |
| Inclusion Rate | | 1/2 |
| Addition To Net Income For Tax Purposes | | $ 7,025 |

**Note** The deduction for the jewelry loss is limited to the amount of gains on listed personal property. This will leave an allowable listed personal property loss carry over of $6,350 [(1/2)($18,000 - $5,300)]. As covered in Chapter 11, this unused amount can be carried back 3 years and forward 7 years.


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## Solution to Assignment Problem Eight - 12

### *Case A*

The capital gain on the disposition is $800,000 ($2,200,000 - $1,400,000). As the cost of the replacement shares is only $1,800,000, the permitted deferral would be $654,545 [($1,800,000 ÷ $2,200,000)($800,000)].

The adjusted cost base of the replacement shares would be $1,145,455 ($1,800,000 - $654,545).

### *Case B*

The capital gain on the disposition is $700,000 ($1,900,000 - $1,200,000). As the cost of the replacement shares is only $1,400,000 ($500,000 + $900,000), the permitted deferral would be $515,789 [($1,400,000 ÷ $1,900,000)($700,000)].

The cost base of the two investments would be calculated as follows:

| | A Shares | B Shares |
|---|---|---|
| Purchase Price | $500,000 | $900,000 |
| Deferral: | | |
| [($515,789)($500,000 ÷ $1,400,000)] | ( 184,210) | |
| [($515,789)($900,000 ÷ $1,400,000)] | | ( 331,579) |
| Adjusted Cost Base | $315,790 | $568,421 |



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## Solution to Assignment Problem Eight - 13

***Part A***

The 2013 tax consequences would be as follows:

**Land** The Company would have a taxable capital gain on the Land calculated as follows:

| | |
|---|---:|
| Proceeds Of Disposition | $1,100,000 |
| Adjusted Cost Base | ( 350,000) |
| Capital Gain | $ 750,000 |
| Inclusion Rate | 1/2 |
| Taxable Capital Gain | $ 375,000 |

**Building** The Company would have a taxable capital gain and recapture calculated as follows:

| | |
|---|---:|
| Proceeds Of Disposition | $2,300,000 |
| Capital Cost | ( 2,100,000) |
| Capital Gain | $ 200,000 |
| Inclusion Rate | 1/2 |
| Taxable Capital Gain | $ 100,000 |

| | |
|---|---:|
| Opening UCC | $ 850,000 |
| Deduct Disposition - Lesser Of: | |
| Capital Cost = $2,100,000 | |
| Proceeds Of Disposition = $2,300,000 | ( 2,100,000) |
| Negative Closing UCC Balance = Recapture | ($1,250,000) |
| Recapture (Included In Income) | 1,250,000 |
| UCC - January 1, 2014 | Nil |

**Equipment** The Company would have recapture calculated as follows:

| | |
|---|---:|
| Opening UCC | $165,000 |
| Deduct Disposition - Lesser Of: | |
| Capital Cost = $450,000 | |
| Proceeds Of Disposition = $320,000 | ( 320,000) |
| Negative Closing UCC Balance = Recapture | ($155,000) |
| Recapture (Included In Income) | 155,000 |
| UCC - January 1, 2014 | Nil |

***Part B***

**Land** With respect to the Land, the capital gain resulting from the use of the ITA 44(1) election would be the lesser of:

- $750,000 (regular capital gain); and
- $500,000 (the excess of the $1,100,000 proceeds of disposition for the old land over the $600,000 cost of the replacement land).

The taxable amount would be $250,000 [(1/2)($500,000)] and this would be included in the revised 2013 Net Income For Tax Purposes.

If the ITA 44(1) election is used in 2014, the deemed adjusted cost base of the replacement land would be calculated as follows:



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| | |
|---|---|
| Cost | $600,000 |
| Capital Gain Reversed By Election ($750,000 - $500,000) | ( 250,000) |
| Deemed Adjusted Cost Base Of Replacement Land | $350,000 |

Note that the deemed adjusted cost base of the replacement land has been reduced to the actual adjusted cost base of the old land.

**Building** If the ITA 44(1) election is used in 2014, the amended 2013 capital gain would be nil, the lesser of:

- $200,000 (regular capital gain); and
- Nil (reflecting the fact that there was no excess of the $2,300,000 proceeds of disposition for the old building over the $2,500,000 cost of the replacement building).

If the ITA 13(4) election is used in 2014, the amended 2013 recapture would be calculated as follows:

| | | |
|---|---|---|
| January 1, 2013 UCC Balance | | $850,000 |
| Deduction: | | |
| Lesser Of: | | |
| • Proceeds Of Disposition = $2,300,000 | | |
| • Capital Cost = $2,100,000 | $2,100,000 | |
| Reduced By The Lesser Of: | | |
| • Normal Recapture = $1,250,000 | | |
| • Replacement Cost = $2,500,000 | ( 1,250,000) | ( 850,000) |
| Recapture Of 2013 CCA (Amended) | | Nil |

If both elections are used in 2014, the UCC of the replacement building is calculated as follows:

| | |
|---|---|
| Cost | $2,500,000 |
| Capital Gain Reversed By Election | ( 200,000) |
| Deemed Capital Cost | $2,300,000 |
| Recapture Reversed By Election | ( 1,250,000) |
| UCC - Replacement Building | $1,050,000 |

Note that the $1,050,000 UCC for the new building is equal to the UCC of the old building ($850,000), plus the additional $200,000 ($2,500,000 - $2,300,000) in funds required for its acquisition.

**Equipment** As this is a voluntary disposition, the ITA 13(4) and 44(1) elections can only be used on real property (land and buildings). They cannot be used on the equipment and, as a consequence, the $155,000 in recapture will not be altered in the amended return. As the elections cannot be used, both the capital cost and the UCC of the new equipment will be $520,000.

### *Part C*

After the application of the ITA 44(1) election, there was a $500,000 capital gain on the land and no gain on the building. Some reduction of Net Income For Tax Purposes can be achieved under the ITA 44(6) election. However, the reduction is limited to the $200,000 difference between the $2,300,000 proceeds resulting from the sale of the old building, and the $2,500,000 cost of the replacement building. This would reduce the capital gain on the land by $200,000. The adjusted cost base of the replacement land would remain at $350,000.



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This would still leave the capital gain on the building at nil. This can be shown as follows:

| | |
|---|---|
| Deemed Proceeds Of Disposition ($2,300,000 + $200,000) | $2,500,000 |
| Less: Cost Of Replacement Building | 2,500,000 |
| Capital Gain | Nil |

Using this election, the amended 2013 Net Income For Tax Purposes would be reduced by $100,000 [(1/2)($200,000)]. It would be possible to further reduce the gain on the land by transferring more of the proceeds to the building. The result, however, would be a new gain on the building that would be equal to the gain reduction on the land.

With the use of this election, the deemed cost of the new building would be $2,100,000 [$2,500,000 - ($2,300,000 + $200,000 - $2,100,000)] and the UCC would be reduced to $850,000 ($2,100,000 - $1,250,000).

Also note that there is a cost involved with this election. While the Company has reduced its 2013 Net Income For Tax Purposes by one-half of the $200,000 capital gain, it has forgone future CCA for the full amount of $200,000. Under normal circumstances, this would not be advisable as the trade-off for the tax deferral is a substantial increase in future taxes.


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## Solution to Assignment Problem Nine - 2

As both the general moving allowance and the compensation for the housing loss were paid for by the Ottawa office, these would likely be considered income at the new location. Given this view, Lawrence's employment income at the new location can be calculated as follows:

| | |
|---|---|
| General Moving Allowance | $18,000 |
| Compensation For Loss On Kelowna Residence (Note 1) | 7,500 |
| Salary At New Location (1 Month At $8,000) | 8,000 |
| Total Employment Income At New Location | $33,500 |

**Note 1** Under ITA 6(20), one-half of any housing loss reimbursement in excess of $15,000 must be included in income. As the total reimbursement was $30,000, the inclusion would be $7,500 [(1/2)($30,000 - $15,000)].

| Deductible Moving Expenses | |
|---|---|
| Cost Of House Hunting Trip (Note 2) | Nil |
| Real Estate Commission - Kelowna Home | $21,000 |
| Legal Fees - Kelowna Home | 800 |
| Other Kelowna Home Costs (Not Deductible) | Nil |
| Moving Company Costs ($3,500 + $1,200) | 3,700 |
| Costs Of Travel To Ottawa | 1,800 |
| Costs Of Food And Lodging In Ottawa (Note 3) | 3,375 |
| Moving Expense Deductions Available (Note 4) | $30,675 |

**Note 2** As the new condominium residence does not become available during the house hunting trip, the food and lodging costs cannot be deducted as being incurred "near the new residence".

**Note 3** Costs of food and lodging at or near the old or new residence are limited to $3,375 [(15 Days)($225)].

**Note 4** As the deductible costs are less than the income at the new location, they are fully deductible in Lawrence's 2013 tax return. There would be no carry forward of moving costs.



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**Note 1** Under ITA 6(20), one-half of any housing loss reimbursement in excess of $15,000 must be included in income. As the total reimbursement was $30,000, the inclusion would be $7,500 [(1/2)($30,000 - $15,000)].

| Deductible Moving Expenses | |
|---|---|
| Cost Of House Hunting Trip (Note 2) | Nil |
| Real Estate Commission - Kelowna Home | $21,000 |
| Legal Fees - Kelowna Home | 800 |
| Other Kelowna Home Costs (Not Deductible) | Nil |
| Moving Company Costs ($3,500 + $1,200) | 3,700 |
| Costs Of Travel To Ottawa | 1,800 |
| Costs Of Food And Lodging In Ottawa (Note 3) | 3,375 |
| Moving Expense Deductions Available (Note 4) | $30,675 |

**Note 2** As the new condominium residence does not become available during the house hunting trip, the food and lodging costs cannot be deducted as being incurred "near the new residence".

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## Solution to Assignment Problem Nine - 3

***Mrs. Holmes***

Generally, the spouse with the lower income must claim the deduction for child care expenses. However, under certain circumstances, for example if this spouse is a full time student, the spouse with the higher income can claim the deduction for the period the spouse is a student. Under this provision, Mrs. Holmes can claim the least of the following:

| | Case A | Case B |
|---|---|---|
| Actual Payments [($250)(50)] | $12,500 | $12,500 |
| 2/3 Of Earned Income* [(2/3)($81,000)] | $54,000 | $54,000 |
| Annual Expense Limit: | | |
| Case A [(2)($7,000)] | $14,000 | |
| Case B [(2)($7,000) + (1)($4,000)] | | $18,000 |
| Periodic Expense Limit: | | |
| Case A [(2)($175)(6 weeks)] | $ 2,100 | |
| Case B {[(2)($175)(6 weeks)] + [(1)($100)(6 weeks)]} | | $ 2,700 |

*The employment income figure used for this purpose is gross and not net employment income.

In Case A, the least of these figures is $2,100, the Periodic Expense Limit. In Case B, the least of the figures is $2,700, also the Periodic Expense Limit.

***Mr. Holmes***

The calculations for Mr. Holmes are as follows:

| | Case A | Case B |
|---|---|---|
| Actual Payments | $12,500 | $12,500 |
| 2/3 Of Earned Income [(2/3)($18,000)]* | $12,000 | $12,000 |
| Annual Expense Limit: | | |
| Case A [(2)($7,000)] | $14,000 | |
| Case B [(2)($7,000) + (1)($4,000)] | | $18,000 |

*The universal child care benefit payments are not included in Mr. Holmes' earned income for this purpose.

The lowest figure in both cases is $12,000, two-thirds of Mr. Holmes' earned income. Mr. Holmes' deduction is reduced by the amount claimed by Mrs. Holmes.

Given this, Mr. Holmes' deduction is $9,900 ($12,000 - $2,100) in Case A, and $9,300 ($12,000 - $2,700) in Case B.



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## Solution to Assignment Problem Nine - 5

### *Part A - Net Income For Tax Purposes*

The minimum Net Income For Tax Purposes that can be reported by Ms. Watts is calculated as follows:

| | | |
|---|---|---|
| Wages From Cold Lake Employment | | $ 9,600 |
| Moving Costs To Cold Lake (Note 1) | | ( 685) |
| Scholarship Received | $4,000 | |
| Exempt Portion Of Scholarship (100%) | ( 4,000) | Nil |
| Child Care Costs (Note 2) | | ( 1,500) |
| Employment Income In Calgary | | 600 |
| Moving Costs To Calgary (Note 1) | | ( 600) |
| Eligible Dividends Received | | 3,500 |
| Gross Up Of Dividends [(38%)($3,500)] | | 1,330 |
| Child Support Received (Note 3) | | Nil |
| Inheritance (Not Taxable) | | Nil |
| TFSA Contributions (Note 4) | | Nil |
| TFSA Withdrawal (Note 4) | | Nil |
| RESP Contributions (Note 5) | | Nil |
| Net Income For Tax Purposes | | $12,245 |

**Note 1** The cost of the move to Cold Lake is deductible against the income that was earned there as it is more than 40 km from Calgary. The moving costs related to the move back to Calgary can be deducted to the extent of her employment income at that location. The remaining $226 ($826 - $600) can be carried forward to apply against any eligible income that is earned in Calgary during 2014.

**Note 2** As she is the lower income spouse, Ms. Watts will deduct the child care payments. The deduction is the least of the following amounts:

- The amount paid = $1,500 [(12)($125)].
- The annual child care expense amount = $8,000 [(2)($4,000)].
- Two-thirds of Earned Income = $6,800 [(2/3)($9,600 + $600)].

**Note 3** Since 1997, child support payments are not deductible to the payor and are not taxed in the hands of the recipient.

**Note 4** TFSA contributions and withdrawals have no tax consequences. There is also no income attribution as a result of the TFSA contribution by Ms. Watts' husband.

**Note 5** Contributions to RESPs are not deductible.

### *Part B - Registered Education Savings Plan*

While contributions to RESPs are not deductible, earnings within the plan accumulate on a tax free basis. Further, when the earnings are withdrawn, they are likely to be taxed in the hands of the plan beneficiaries. As they will be full or part time students at this time, they will either be in a low tax bracket or, in many cases, have income that is below the basic personal tax credit. This arrangement can involve a considerable savings in taxes.

In addition, for contributions of up to $2,500 per year, the federal government will make additional contributions under the Canada Education Savings Grants (CESG) program. These contributions will add a minimum of $500 to the first $2,500 of annual contributions. Note, however, that given her husband's level of income, the family will not be eligible for the Canada Learning Bonds program.

Given the potential tax savings, as well as the federal government contributions under the CESG program, Ms. Watts and her husband should consider contributing at least $2,500 per year to each of the children's RESPs.



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Since her children have not had RESPs before, they have CESG contribution room carried forward. Ms. Watts should determine the contribution schedule required to maximize the CESGs for both children so that she can plan to take advantage of the CESG contribution room if there are sufficient funds available.



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## Solution to Assignment Problem Ten - 2

### *Part A - Maximum RRSP Deduction*

Mark's maximum 2013 RRSP deduction would be calculated as follows:

| | |
|---|---|
| Unused Deduction Room - January 1, 2012 | $25,000 |
| 2012 Addition | Nil |
| 2013 Addition (Based On 2012 Earned Income Of Nil) | Nil |
| Maximum 2013 RRSP Deduction | $25,000 |

### *Part B - Excess RRSP Contributions*

At the beginning of 2012, Mark's undeducted contributions of $27,000 are equal to his $25,000 unused deduction room, plus the permitted $2,000 cushion. As there are no further contributions during 2012, there are no excess contributions during the 2012 taxation year.

The excess contributions for 2013 would be calculated as follows:

| | |
|---|---|
| Undeducted Contributions | |
| January 1, 2013 ($25,000 - $15,000) | $10,000 |
| Additional Contribution On March 1, 2013 | 50,000 |
| Total Undeducted Contributions | $60,000 |
| Unused Deduction Room | ( 25,000) |
| Permitted Cushion | ( 2,000) |
| Excess Contributions | $33,000 |
| Penalty Rate | 1% |
| Monthly Penalty | $ 330 |
| Months (March To December) | 10 |
| Total Penalty | $ 3,300 |



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## Solution to Assignment Problem Ten - 3

***Part A***

Mr. Detwiller's Net Income For Tax Purposes would be calculated as follows:

| | | |
|---|---|---|
| Income Under ITA 3(a): | | |
| Net Employment Income | $56,000 | |
| Eligible Dividends | 7,800 | |
| Gross Up | 2,964 | $66,764 |
| Income Under ITA 3(b): | | |
| Taxable Capital Gains | $ 5,400 | |
| Allowable Capital Losses | ( 8,200) | Nil |
| Balance From ITA 3(a) And (b) | | $66,764 |
| Subdivision e Deductions | | ( 2,500) |
| Balance From ITA 3(c) | | $64,264 |
| Deductions Under ITA 3(d): | | |
| Net Rental Loss | | ( 9,000) |
| Net Income For Tax Purposes | | $55,264 |

Mr. Detwiller's Net Income For Tax Purposes is $55,264 and he has a net capital loss carry over of $2,800 ($5,400 - $8,200).

***Part B - Case 1***

Mr. Detwiller's 2012 Earned Income would be calculated as follows:

| | |
|---|---|
| Net Employment Income | $56,000 |
| Add Back RPP Contributions | 1,500 |
| Net Rental Loss | ( 9,000) |
| Earned Income | $48,500 |

Given this, his maximum 2013 contribution would be calculated as follows:

| | |
|---|---|
| Unused Deduction Room - End Of 2012 | $10,000 |
| Annual Addition - Lesser Of: | |
| • 2012 RRSP Dollar Limit = $23,820 | |
| • 18% of 2012 Earned Income Of $48,500 = $8,730 | 8,730 |
| Less 2012 PA ($1,500 + $3,000 + $1,000) | ( 5,500) |
| 2013 RRSP Deduction Limit | $13,230 |
| Allowable Excess Amount | 2,000 |
| Non-Penalty Contribution Limit | $15,230 |
| Undeducted Contributions From Previous Years | ( 4,500) |
| Maximum RRSP Contribution | $10,730 |

If Mr. Detwiller contributes this amount of $10,730, his deduction will be equal to $13,230 and he will carry forward RRSP contributions of $2,000 ($4,500 + $10,730 - $13,230).



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***Part B - Case 2***

Mr. Detwiller's 2012 Earned Income would be calculated as follows:

| | |
|---|---|
| Net Employment Income | $56,000 |
| Net Rental Loss | ( 9,000) |
| Earned Income | $47,000 |

Given this, his maximum 2013 contribution would be calculated as follows:

| | |
|---|---|
| Unused Deduction Room - End Of 2012 | $10,000 |
| Annual Addition - Lesser Of: | |
| • 2013 RRSP Dollar Limit = $23,820 | |
| • 18% of 2012 Earned Income Of $47,000 = $8,460 | 8,460 |
| Less 2012 PA | ( 4,500) |
| 2013 RRSP Deduction Limit | $13,960 |
| Allowable Excess Amount | 2,000 |
| Non-Penalty Contribution Limit | $15,960 |
| Undeducted Contributions From Previous Years | ( 4,500) |
| Maximum RRSP Contribution | $11,460 |

If Mr. Detwiller contributes this amount of $11,460, his deduction will be equal to $13,960 and he will carry forward RRSP contributions of $2,000 ($4,500 + $11,460 - $13,960).

***Part B - Case 3***

Mr. Detwiller's 2012 Earned Income would be calculated as follows:

| | |
|---|---|
| Net Employment Income | $ 56,000 |
| Net Rental Loss | ( 9,000) |
| Business Income | 220,000 |
| Earned Income | $267,000 |

Given this, his maximum 2013 contribution would be calculated as follows:

| | |
|---|---|
| Unused Deduction Room - End of 2012 | $10,000 |
| Annual Addition - Lesser Of: | |
| • 2013 RRSP Dollar Limit = $23,820 | |
| • 18% of 2012 Earned Income Of $267,000 = $48,060 | 23,820 |
| Less 2012 PA | Nil |
| 2013 RRSP Deduction Limit | $33,820 |
| Allowable Excess Amount | 2,000 |
| Non-Penalty Contribution Limit | $35,820 |
| Undeducted Contributions From Previous Years | ( 4,500) |
| Maximum RRSP Contribution | $31,320 |

If Mr. Detwiller contributes this amount of $31,320, his deduction will be equal to $33,820 and he will carry forward RRSP contributions of $2,000 ($4,500 + $31,320 - $33,820).



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## Solution to Assignment Problem Ten - 5

**_Part A_**

For purposes of determining her maximum 2013 RRSP contribution, 2012 Earned Income would be calculated as follows:

| | | |
|---|---|---|
| Net Employment Income* | | |
| Salary | $120,000 | |
| Employee Stock Option Benefit | 5,000 | |
| Benefit On Interest Free Loan | 5,000 | |
| Deductible Employment Expenses | ( 4,000) | $126,000 |
| Business Income | | 35,000 |
| Royalty Income (Own Invention) | | 5,000 |
| Rental Loss | | ( 10,000) |
| Spousal Support Payments | | ( 12,000) |
| Earned Income | | $144,000 |

*Note that, in calculating Earned Income for RRSP purposes, no deduction is made from net employment income for contributions made to an RPP.

A listing of the items that are not included in the calculation of Earned Income is as follows:

- Registered Pension Plan Contributions
- Interest Income
- Taxable Capital Gains
- Non-Eligible Dividends

**_Part B_**

The calculation of Ms. Goodman's maximum deductible RRSP contribution for 2013 is as follows:

| | |
|---|---|
| 2011 RRSP Dollar Limit | $22,450 |
| 2012 RRSP Dollar Limit | 22,970 |
| Opening Unused RRSP Deduction Room | $45,420 |
| Annual Addition - Lesser Of: | |
| • 2013 RRSP Dollar Limit = $23,820 | |
| • 18 Percent Of 2012 Earned Income [(18%)($144,000)] = $25,920 | 23,820 |
| 2012 PA | ( 9,000) |
| Maximum Deductible RRSP Contribution For 2013 | $60,240 |

The calculation begins with the determination of her unused deduction room at the end of 2012. As she has made no contributions to either an RRSP or an RPP in years prior to 2012 and no contribution to an RRSP in 2012, her unused deduction room at the end of 2012 would be the RRSP Dollar Limit for the years 2011 and 2012.

To this amount we add $23,820, the lesser of the 2013 RRSP Dollar Limit of $23,820 and $25,920 (18 percent of Ms. Goodman's 2012 Earned Income of $144,000).

From this total we subtract Ms. Goodman's 2012 PA of $9,000.



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## Solution to Assignment Problem Ten - 6

***Part A***

Minimum Net Income For Tax Purposes would be calculated as follows:

| | |
|---|---|
| Business Income | |
| Accounting Net Income | $183,000 |
| Additions: | |
| Accounting Amortization | 23,000 |
| Recapture (Note 1) | 12,000 |
| Meals And Entertainment (Note 2) | 7,000 |
| Deductions: | |
| Maximum CCA (Given) | ( 31,000) |
| Accounting Gain On Asset Sale ($34,500 - $24,000) | ( 10,500) |
| Net Business Income | $183,500 |
| Property Income | |
| Interest | 1,200 |
| Royalties | 8,400 |
| Taxable Capital Gains | |
| Taxable Capital Gain On Depreciable Assets (Note 3) | 2,250 |
| Taxable Capital Gain On Personal Assets | 18,000 |
| Allowable Capital Loss On Sale Of Shares | ( 1,000) |
| Other Deductions | |
| Spousal Support Paid | ( 3,600) |
| 2013 Net Income Before RRSP Deduction | $208,750 |

**Note 1** Recapture of CCA would be calculated as follows:

| | |
|---|---|
| UCC - January 1, 2013 | $18,000 |
| Lesser Of: | |
| Capital Cost = $30,000 | |
| Proceeds Of Disposition = $34,500 | ( 30,000) |
| Negative Ending UCC Balance = Recapture Of CCA | ($12,000) |

**Note 2** As only one-half of the $14,000 in deducted business meals and entertainment that were deducted in determining accounting Net Income can be deducted for tax purposes, $7,000 [(1/2)($14,000)] must be added back to accounting Net Income to arrive at Net Business Income.

**Note 3** The taxable capital gain would be calculated as follows:

| | |
|---|---|
| Depreciable Assets - Proceeds Of Disposition | $34,500 |
| Capital Cost | 30,000 |
| Capital Gain On Depreciable Assets | $ 4,500 |
| Inclusion Rate | 1/2 |
| Taxable Capital Gain | $ 2,250 |



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***Part B***

Given that we are asked to assume the Alicia's 2012 Earned Income is equal to her 2013 Earned Income, we will need to calculate the 2013 figure. The calculations are as follows:

| | |
|---|---|
| Net Business Income | $183,500 |
| Royalties (Taxpayer Was Author) | 8,400 |
| Spousal Support Paid | ( 3,600) |
| Earned Income For RRSP Purposes | $188,300 |

Using this information, the maximum RRSP deduction for 2013 would be calculated as follows:

| | |
|---|---|
| Unused Deduction Room - January 1, 2013 | $ 6,500 |
| Lesser Of: | |
| 2013 RRSP Limit = $23,820 | |
| [(18%)($188,300)] = $33,894 | 23,820 |
| PA | N/A |
| Maximum RRSP Deduction For 2013 | $30,320 |

At the beginning of 2013, Alicia had $4,500 of undeducted contributions. In order to make the maximum 2013 deduction of $30,320, she will have to make an additional contribution of $25,820 ($30,320 - $4,500).



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## Solution to Assignment Problem Ten - 7

### *Retiring Allowance Rollover*

If Mr. White accepts his employer's offer of cash, he has two alternative courses of action. First, he can do nothing, in which case the full $68,000 will be an addition to his Net Income For Tax Purposes for the current year. His second alternative will be to transfer some part of the payment to a Registered Retirement Savings Plan (RRSP) on a tax free basis. While he will still have to include the full $68,000 in his income, he will be eligible for a deduction equal to a specified amount of such transfers.

The rules prior to 1989 permit tax free transfers of up to $2,000 per year of service with the employer who is making the payments, plus an additional $1,500 per year of service for each year during which the employer was not making vested contributions to either a Registered Pension Plan or a Deferred Profit Sharing Plan. For 1989 through 1995, the amount of this transfer is limited to $2,000 per year of post-1988 service. For service after 1995, the transfer is no longer available.

In 2013, Mr. White's limit would be $31,500 [(12 years)($2,000) + (5 years)($1,500)]. The excess of $36,500 ($68,000 - $31,500) will be taxed in the year in which it is received.

### *Alternatives Available*

As to the appropriate course of action, it depends on Mr. White's circumstances. If he anticipates finding another job within a short period of time and has no immediate need for the additional cash, the tax free transfer to an RRSP is probably the most appropriate course of action. He could use the excess retiring allowance to make his maximum regular RRSP contribution.

Although he could make a non-deductible RRSP contribution of up to $2,000 without being assessed any penalty, there are other alternative savings plans available to him. If he has available funds, he should consider contributions to an RESP for the triplets and TFSAs for himself and his wife.

On the other hand, if he wishes to take some time off, or is uncertain as to his future job prospects, he may wish to retain all of the cash on a personal basis. Note, however, if the offer is accepted late in the year after Mr. White has received most of his annual income, the retention of the additional $68,000 would likely push Mr. White into the highest tax bracket. This could be avoided by putting the maximum of $31,500 into an RRSP, with funds withdrawn as needed in the following year.

Another possibility is that Mr. White is at or near retirement age. If this is the case, he will probably wish to transfer the maximum of $31,500 to an RRSP in order to gain flexibility in terms of when the income will be taxed during his retirement years.

If the funds are subsequently transferred to a RRIF or withdrawn from the RRSP in the form of an annuity, the payments will be eligible for the pension income tax credit after Mr. White reaches age 65. The RRIF and annuity payments will also be eligible for the pension income splitting provisions (see Chapter 9).

As a final note, if Mr. White chooses to make a tax free transfer to an RRSP, the transaction does not change his RRSP Deduction Limit for the year. That is, the maximum deductible RRSP contribution for 2013 will be the same, whether or not he transfers part of the retiring allowance into his plan.



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# CHAPTER ELEVEN SOLUTIONS

## Solution to Assignment Problem Eleven - 1

***2010 Analysis***

The required information can be calculated as follows:

| | | |
|---|---|---|
| ITA 3(a) | | |
| Property Income | $27,600 | |
| Dividends Received | 3,120 | |
| Gross Up | 780 | $31,500 |
| ITA 3(b) | | |
| Taxable Capital Gains [(1/2)($1,800)] | $ 900 | |
| Allowable Capital Losses [(1/2)($9,200)] | ( 4,600) | Nil |
| ITA 3(c) | | $31,500 |
| ITA 3(d) | | |
| Farm Loss (See Note) | | ( 7,350) |
| Net Income For Tax Purposes And Taxable Income | | $24,150 |

**Note** Mr. Barkin's farm losses are restricted as follows:

| | | |
|---|---|---|
| Total Farm Loss | | $12,200 |
| Deductible Amount: | | |
| First $2,500 | ($2,500) | |
| One-Half Of $9,700 ($12,200 - $2,500) | ( 4,850) | ( 7,350) |
| Restricted Farm Loss Carry Forward | | $4,850 |

As noted in the problem, none of the losses can be carried back before 2010. This would leave the following carry forward balances at the end of 2010:

- Restricted Farm Loss Carry Forward $4,850
- Net Capital Loss Carry Forward ($4,600 - $900) $3,700

***2011 Analysis***

The required information can be calculated as follows:

| | | |
|---|---|---|
| ITA 3(a) | | |
| Farm Income | $ 2,320 | |
| Non-Eligible Dividends Received | 4,120 | |
| Gross Up | 1,030 | $ 7,470 |
| ITA 3(b) | | |
| Taxable Capital Gains [(1/2)($3,000)] | $ 1,500 | |
| Allowable Capital Losses | Nil | 1,500 |
| ITA 3(c) | | $ 8,970 |
| ITA 3(d) | | |
| Property Loss | | ( 22,250) |
| Net Income For Tax Purposes | | Nil |
| 2010 Net Capital Loss Carry Forward | | ($ 1,500) |
| Taxable Income (Loss) | | Nil |

Since there are taxable capital gains this year, and the problem states that Mr. Barkin would like to deduct the maximum amount of his net capital loss carry forwards, the net capital loss carry forward of $1,500 is added to the balance of the non-capital loss.



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The non-capital loss carry over is calculated as follows:

| | |
|---|---|
| Property Loss | $22,250 |
| 2010 Net Capital Loss Deducted | 1,500 |
| ITA 3(c) Income | ( 8,970) |
| Non-Capital Loss Carry Over For 2011 | $14,780 |

The entire non-capital loss carry over could be carried back to 2010, but since Mr. Barkin requires $18,500 in Taxable Income to fully utilize his tax credits, the maximum carry back to 2010 is $5,650, calculated as follows:

| | |
|---|---|
| 2010 Taxable Income (As Reported) | $24,150 |
| Required 2010 Income For Tax Credits | ( 18,500) |
| Maximum Carry Back | $ 5,650 |

This carry back leaves Mr. Barkin with his required $18,500 in 2010 amended Taxable Income.

There would be the following carry forward balances at the end of 2011:

- Restricted Farm Loss Carry Forward (Unchanged) $4,850
- Net Capital Loss Carry Forward ($3,700 - $1,500)] $2,200
- Non-Capital Loss Carry Forward ($14,780 - $5,650) $9,130

***2012 Analysis***

The required information can be calculated as follows:

| | | |
|---|---|---|
| ITA 3(a) | | |
| Property Income | $44,100 | |
| Farm Income | 3,840 | |
| Non-Eligible Dividends Received | 5,980 | |
| Gross Up | 1,495 | $55,415 |
| ITA 3(b) | | |
| Taxable Capital Gains [(1/2)($6,000)] | $3,000 | |
| Allowable Capital Losses | Nil | 3,000 |
| Net Income For Tax Purposes | | $58,415 |
| Restricted Farm Loss Carry Forward (Equal To Farm Income) | | ( 3,840) |
| Net Capital Loss Carry Forward (Less Than $3,000) | | ( 2,200) |
| Non-Capital Loss Carry Forward (All) | | ( 9,130) |
| Taxable Income | | $43,245 |

There would be the following carry forward balances at the end of 2012:

- Restricted Farm Loss Carry Forward ($4,850 - $3,840) $1,010



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### *2013 Analysis*

The required information can be calculated as follows:

| | | |
|---|---|---|
| ITA 3(a) | | |
| Non-Eligible Dividends Received | $ 8,720 | |
| Gross Up | 2,180 | $10,900 |
| ITA 3(b) | | |
| Taxable Capital Gains [(1/2)($6,700)] | $ 3,350 | |
| Allowable Capital Losses [(1/2)($21,300)] | ( 10,650) | Nil |
| ITA 3(c) | | $10,900 |
| ITA 3(d) | | |
| Property Loss | ($30,800) | |
| Farm Loss | ( 2,400) | ( 33,200) |
| Net Income For Tax Purposes And Taxable Income | | Nil |

The available non-capital loss can be calculated as follows:

| | |
|---|---|
| Property Loss | $30,800 |
| ITA 3(c) Income | ( 10,900) |
| Non-Capital Loss Carry Over | $19,900 |
| Farm Loss (Unrestricted) | 2,400 |
| Total Loss Carry Over For 2013 | $22,300 |

Although technically, the farm loss is accounted for separately from the non-capital loss, since the farm loss is less than $2,500 it is treated as an unrestricted farm loss and can be applied against all types of income. Given the carry over rules are the same, we have treated this farm loss as part of the non-capital loss carry over. The preceding loss carry over of $22,300 is available for carry back to 2012.

With respect to the net capital loss of $7,300 ($10,650 - $3,350), there are $800 ($3,000 - $2,200) in taxable capital gains left in 2012 as the basis for a carry back. This means that $800 of this year's allowable capital loss can be carried back, leaving $6,500 ($7,300 - $800) to be carried forward as a net capital loss balance.

If both the $22,300 available farm and non-capital loss, as well as the $800 net capital loss were carried back, the amended 2012 Taxable Income would be as follows:

| | |
|---|---|
| 2012 Taxable Income (As Reported) | $43,245 |
| Non-Capital Loss Carry Back From 2013 | ( 22,300) |
| Net Capital Loss Carry Back From 2013 | ( 800) |
| 2012 Amended Taxable Income | $20,145 |

This is more than the $18,500 of Taxable Income required to use the 2012 tax credits.

Given these carry backs, the remaining loss carry forwards would be as follows:

- Restricted Farm Loss Carry Forward (Unchanged) $1,010
- Net Capital Loss Carry Forward ($7,300 - $800) $6,500



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## Solution to Assignment Problem Eleven - 2

Before consideration of any carry backs, Dotty would have 2012 Taxable Income as follows:

| | |
|---|---|
| Net Taxable Capital Gains | $ 5,000 |
| Net Rental Income | 16,000 |
| Interest Income | 36,000 |
| Net Income For Tax Purposes And Taxable Income | $57,000 |

The loss on Spec Inc. is a Business Investment Loss (BIL) of $300,000 ($425,000 - $125,000). However, because of her use of the lifetime capital gains deduction in 2011, $25,000 of this amount would be disallowed. Given this, the available Allowable Business Investment Loss (ABIL) would be calculated as follows:

| | |
|---|---|
| Total Loss | $300,000 |
| Disallowed By Lifetime Capital Gains Deduction Use | ( 25,000) |
| Balance | $275,000 |
| Inclusion Rate | 1/2 |
| Allowable Business Investment Loss (ABIL) | $137,500 |

Given this, Dotty's 2013 Taxable Income is calculated as follows:

| | | |
|---|---|---|
| **Income Under ITA 3(a)** | | |
| Net Rental Income | $14,000 | |
| Interest Income | 24,000 | $ 38,000 |
| **Income Under ITA 3(b)** | | |
| Taxable Capital Gains | $6,000 | |
| Allowable Capital Loss (Disallowed ABIL) [(1/2)($25,000)] (Note 1) | ( 12,500) | Nil |
| Balance Under ITA 3(c) | | $ 38,000 |
| **Deduction Under ITA 3(d)** | | |
| ABIL (Note 2) | | ( 137,500) |
| Net Income For Tax Purposes And Taxable Income | | Nil |

**Note 1** As the $25,000 disallowed BIL becomes an ordinary capital gain, it must be deducted against the 2013 taxable capital gain. This leaves a net capital loss carry over of $6,500 ($12,500 - $6,000) of which $5,000 can be carried back to 2012.

**Note 2** As the ABIL was realized in 2013, it must be used to reduce that year's income to Nil. Note that, because of this rule, Dotty cannot deduct a smaller amount in order to have sufficient income to absorb her basic personal tax credit. After this deduction, a carry over of $99,500 ($137,500 - $38,000) remains. For the next 10 years, this amount will be treated as a non-capital loss carry forward that can be deducted against other sources of income. If it has not been utilized within the 10 years, it then becomes a net capital loss carry forward, deductible for an unlimited number of future periods, but only against net taxable capital gains.

Using the carry over amounts, the 2012 tax return would be amended as follows:

| | |
|---|---|
| Net Income For Tax Purposes (As Originally Calculated) | $57,000 |
| Net Capital Loss Carried Back | ( 5,000) |
| Optimum Taxable Income = Basic Personal Amount | ( 10,822) |
| Non-Capital Loss Carried Back | ($41,178) |



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As planned, these deductions leave a Taxable Income of $10,822. The taxes on this amount will be eliminated by Dotty's basic personal credit. Since 2011 Taxable Income was less than the basic personal amount, there would be no carry back to that year. The following carry forwards remain after these carry back amounts are deducted:

| | |
|---|---|
| Net Capital Loss Carry Forward ($6,500 - $5,000) | $1,500 |
| Non-Capital Loss Carry Forward ($99,500 - $41,178) | $58,322 |



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## Solution to Assignment Problem Eleven - 4

***Part A***

Mr. and Mrs. Baxter's Taxable Income would be calculated as follows:

| | Mrs. Baxter | Mr. Baxter |
|---|---|---|
| Registered Pension Plan Receipts | Nil | $48,000 |
| RRIF Withdrawals | Nil | 28,000 |
| Interest On Government Bonds | $1,100 | 3,400 |
| Non-Eligible Dividends Received | 3,000 | Nil |
| Gross Up On Dividends (25 Percent) | 750 | Nil |
| Old Age Security Benefits | 6,550 | 6,550 |
| Net Income Before Clawback | $11,400 | $85,950 |
| Social Benefits Repayment (Note 1) | Nil | ( 2,249) |
| Net Income For Tax Purposes And Taxable Income Before Any Transfer Of Dividends | $11,400 | $83,701 |

**Note 1** Mrs. Baxter would not have to repay any of her OAS benefits as her Net Income is well below the threshold income of $70,954. Mr. Baxter's social benefits repayment would be $2,249, the lesser of:

- $6,550, and
- [(15%)($85,950 - $70,954)] = $2,249.

Mrs. Baxter's Tax Payable would be calculated as follows:

| | | |
|---|---|---|
| Federal Tax Before Credits [(15%)($11,400)] | | $1,710 |
| Tax Credits | | |
| Basic Personal | $11,038 | |
| Other (Transferred To Mr. Baxter) | Nil | |
| Total Base | $11,038 | |
| Rate | 15% | ( 1,656) |
| Dividend Tax Credit [(2/3)($750)] | | ( 500) |
| Federal Tax Payable | | Nil |

The transfer to Mr. Baxter would be calculated as follows:

| | | |
|---|---|---|
| Credits Available For Transfer: | | |
| Age | | $ 6,854 |
| Disability | | 7,697 |
| Total Available | | $14,551 |
| Reduced By Excess Of: | | |
| Mrs. Baxter's Net Income | ($11,400) | |
| Over Basic Personal Credit Amount | 11,038 | ( 362) |
| Available For Transfer | | $14,189 |



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The amount owing for Mr. Baxter would be calculated as follows:

| | | |
|---|---|---|
| Tax On First $43,561 | $ 6,534 | |
| Tax On Next $40,140 ($83,701 - $43,561) At 22 Percent | 8,831 | $15,365 |
| Tax Credits | | |
| Basic Personal | ($11,038) | |
| Spousal Including FCA ($13,078 - $11,400) | ( 1,678) | |
| Age {$6,854 - [(15%)($83,701 - $34,562)]} | Nil | |
| Pension | ( 2,000) | |
| Transfer From Spouse (Preceding Calculation) | ( 14,189) | |
| Credit Base | ($28,905) | |
| Rate | 15% | ( 4,336) |
| Charitable Donations [(15%)($200) + (29%)($560 + $450 - $200)] (Note 2) | | ( 265) |
| Federal Tax Payable | | $10,764 |
| OAS Clawback | | 2,249 |
| Amount Owing | | $13,013 |

**Note 2** Charitable donations can be claimed by either spouse, as long as the total donations are less than 75 percent of the claiming spouse's Net Income For Tax Purposes. As Mrs. Baxter has no Tax Payable, Mr. Baxter will claim her charitable donations. It is usually advantageous for one spouse to claim all the charitable donations if they total more than $200, as the low rate of credit is only applied once.

### *Part B - Eligibility For Transfer*

Mr. Baxter's current spousal credit is $1,678. If Mrs. Baxter's dividends are transferred, she would be left with Net Income For Tax Purposes of $7,650 ($11,400 - $3,000 - $750). This would leave a spousal credit of $5,428 ($13,078 - $7,650). As this is an increase from the previous amount, the transfer is permitted.

### *Part C*

If Mrs. Baxter's dividends are transferred to Mr. Baxter, their new Taxable Income figures would be calculated as follows:

| | Mrs. Baxter | Mr. Baxter |
|---|---|---|
| Net Income Before Clawback As Per Part A | $11,400 | $85,950 |
| Dividend Transfer | ( 3,000) | 3,000 |
| Gross Up Transfer | ( 750) | 750 |
| Net Income After Dividend Transfer Before Clawback | $ 7,650 | $89,700 |
| Social Benefits Repayment (Note 3) | Nil | ( 2,812) |
| Net Income For Tax Purposes And Taxable Income | $ 7,650 | $86,888 |

**Note 3** Mrs. Baxter would not have to repay any of her OAS benefits as her Net Income is well below the threshold income of $70,954. Mr. Baxter's social benefits repayment would be $2,812, the lesser of:

- $6,550, and
- [(15%)($89,700 - $70,954)] = $2,812.



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As Mrs. Baxter's revised income figure is below the basic personal credit of $11,038, her Tax Payable would continue to be nil. The transfer to Mr. Baxter would be calculated as follows:

| | | |
|---|---|---|
| Credits Available For Transfer: | | |
| Age | | $ 6,854 |
| Disability | | 7,697 |
| Total Available | | $14,551 |
| Reduced By Excess Of: | | |
| Mrs. Baxter's Net Income | ($ 7,650) | |
| Over Basic Personal Credit Amount | 11,038 | ( Nil) |
| Available For Transfer | | $14,551 |

With respect to Mr. Baxter, his amount owing would be calculated as follows:

| | | |
|---|---|---|
| Tax On First $43,561 | $6,534 | |
| Tax On Next $43,327 ($86,888 - $43,561) At 22 Percent | 9,532 | $16,066 |
| Tax Credits | | |
| Basic Personal | ($11,038) | |
| Spousal Including FCA ($13,078 - $7,650) | ( 5,428) | |
| Age {$6,854 - [(15%)($86,888 - $34,562)]} | Nil | |
| Pension | ( 2,000) | |
| Transfer From Spouse (Preceding Calculation) | ( 14,551) | |
| Credit Base | ($33,017) | |
| Rate | 15% | ( 4,953) |
| Charitable Donations [(15%)($200) + (29%)($560 + $450 - $200)] | | ( 265) |
| Dividend Tax Credit [(2/3)($750)] | | ( 500) |
| Federal Tax Payable | | $10,348 |
| OAS Clawback | | 2,812 |
| Amount Owing | | $13,160 |

The use of the ITA 82(3) dividend transfer has decreased Mr. Baxter's federal Tax Payable from $10,764 to $10,348. However, it has increased the OAS clawback from $2,249 to $2,812. Overall, the net effect is an increase in the amount owing of $147. Clearly, the transfer of dividends is not a desirable alternative.



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# Solution to Assignment Problem Eleven - 6

### *Net Income For Tax Purposes And Taxable Income*

Ms. Klaus' minimum Net Income For Tax Purposes and Taxable Income would be calculated as follows:

| | | |
|---|---|---|
| **Net Employment Income** | | |
| Gross Salary - Ottawa | $62,000 | |
| RPP Contributions - Ottawa | ( 2,500) | |
| Stock Option Benefit (Note One) | 10,000 | |
| Gross Salary - Toronto | 13,000 | |
| RPP Contributions - Toronto | ( 650) | |
| Moving Allowance (Note Two) | 7,500 | $ 89,350 |
| **Business And Property Income** | | |
| Non-Eligible Dividends On Lintz Shares | $ 7,500 | |
| Gross Up [(25%)($7,500)] | 1,875 | |
| Mail Order Business (Note Three) | 22,500 | 31,875 |
| **Net Taxable Capital Gains** | | |
| Lintz Shares [(1/2)($105,000 - $95,000 - $1,050)] | $ 4,475 | |
| Employer's Shares (Note Four) | ( 175) | 4,300 |
| **Other Sources Of Income (Subdivision d)** | | |
| Child Support (Note Five) | $ -0- | |
| Retiring Allowance (Note Six) | 30,000 | 30,000 |
| **Other Deductions From Income (Subdivision e)** | | |
| Moving Expenses (Note Two) | ($ 5,160) | |
| Child Care Costs (Note Seven) | ( 7,560) | |
| RRSP Contributions (Note Eight) | ( 36,498) | ( 49,218) |
| Net Income For Tax Purposes | | $106,307 |
| Stock Option Deduction (Note One) | | ( 5,000) |
| Taxable Income | | $101,307 |

**Note One** The required inclusion would be calculated as follows:

| | |
|---|---|
| Fair Market Value At Exercise [($20)(2,000 Shares)] | $40,000 |
| Cost Of Shares [($15)(2,000 Shares)] | ( 30,000) |
| Stock Option Benefit | $10,000 |

As the option price at the time the options were issued was greater than the fair market value of the shares at that time, Ms. Klaus is entitled to a deduction under ITA 110(1)(d), equal to one-half of the $10,000 employment income benefit.

**Note Two** All allowances received from an employer, except for those that are specifically exempted, must be included in employment income. As there is no exemption for a moving expense allowance, the $7,500 received by Ms. Klaus must be added to income. However, she can then deduct the following moving expenses in the calculation of Net Income For Tax Purposes:



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| | |
|---|---|
| Moving Company Charges | $3,800 |
| Airfare For Toronto Trip (Not Deductible) | Nil |
| Meals And Lodging On Toronto Trip (Not Deductible) | Nil |
| Gas For October 31 Move To Toronto | 65 |
| Lodging In Ottawa On October 30 | 110 |
| Meals On October 30 And October 31 | 250 |
| Lease Cancellation Charges | 935 |
| Legal Fees On Acquisition Of Toronto Home (Not Deductible) | Nil |
| Total | $5,160 |

You should note that this situation should have been structured differently. By giving an allowance not based on actual expenses, the employer placed Ms. Klaus in the position of having to list her expenses. As a consequence, she was limited to those deductions specified in ITA 62(3). The result is a net inclusion in income of $2,340 ($7,500 - $5,160). As an alternative, the employer could have reimbursed her for all of the expenses listed in the problem, without creating a taxable benefit for Ms. Klaus. This would have cost the employer less than $7,500 and, in addition, Ms. Klaus would have avoided the additional taxes on the $2,340. The legal fees on the new home are not deductible because she did own a home in the old location.

**Note Three** The interest on the demand loan is deductible and does not require adjustment. The $27,000 withdrawal would have no effect on business income.

**Note Four** For shares acquired through the exercise of stock options, the adjusted cost base is the fair market value of the shares at the time of exercise. As a consequence, the allowable capital loss arising on the disposition of the employer's shares would be calculated as follows:

| | | |
|---|---|---|
| Proceeds Of Disposition [($20)(2,000 Shares)] | | $40,000 |
| Less: | | |
| Adjusted Cost Base [($20)(2,000)] | ($40,000) | |
| Selling Costs | ( 350) | ( 40,350) |
| Capital Gain (Loss) | | ($ 350) |
| Inclusion Rate | | 1/2 |
| Taxable Capital Gain (Allowable Capital Loss) | | ($ 175) |

**Note Five** Ms. Klaus cannot deduct the $2,500 in legal fees paid in connection with her separation agreement. However, as her husband will not be able to deduct the $25,000 lump sum payment, it does not have to be included in her income. The $48,000 [($4,000)(12 Months)] in child support will not be deductible to her husband and will be excluded from her Net Income For Tax Purposes.

**Note Six** All of the retiring allowance must be included in income under ITA 56(1)(a)(ii). Subject to a limit of $2,000 per year of service prior to 1996, amounts transferred to an RRSP can be deducted under ITA 60(j.1). Ms. Klaus had 20 years of service prior to 1996. As a result, her maximum transfer would be $40,000 [(20)($2,000)]. Given this, she can transfer to her RRSP, and deduct, the entire $30,000 retiring allowance.

**Note Seven** The deductible child care costs of $7,560 would be the least of:

| | |
|---|---|
| • Actual Child Care Expense Plus Deductible Camp Fees [$7,160 + ($100 Limit)(4 Weeks)] | $ 7,560 |
| • Annual Limit ($10,000 For Louise + $4,000 For Martin) | 14,000 |
| • Two-Thirds Of Earned Income [(2/3)($89,350 + $2,500 + $650 + $22,500)] | 76,667 |

**Note Eight** Ms. Klaus' maximum deductible RRSP contribution of $36,498, which includes her retiring allowance, is calculated as follows:



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| | | |
|---|---|---|
| Unused Deduction Room - End Of 2012 | | Nil |
| Lesser Of: | | |
| • 2013 RRSP Dollar Limit = $23820 | | |
| • 18% Of 2012 Earned Income Of $61,100 = $10,998 | | $10,998 |
| Less 2012 PA | | ( 4,500) |
| RRSP Deduction Limit | | $ 6,498 |
| Retiring Allowance | | 30,000 |
| Maximum Deductible RRSP Contribution For 2013 | | $36,498 |

***Tax Payable***

The Tax Payable would be calculated as follows:

| | | |
|---|---|---|
| Tax on First $87,123 | | $16,118 |
| Tax on Next $14,184 ($101,307 - $87,123) At 26 Percent | | 3,688 |
| Total Before Credits | | $19,806 |
| Basic Personal Amount | ($11,038) | |
| Eligible Dependant - Martin (Note 9) | ( 11,038) | |
| Caregiver Including FCA - Louise (Note 9) | ( 6,530) | |
| Child | ( 2,234) | |
| CPP | ( 2,356) | |
| EI | ( 891) | |
| Canada Employment | ( 1,117) | |
| Transfer Of Louise's Disability | ( 7,697) | |
| Medical Expenses (Note Ten) | ( 15,518) | |
| First Time Home Buyer's | ( 5,000) | |
| Credit Base | ($63,419) | |
| Rate | 15% | ( 9,513) |
| Non-Eligible Dividend Tax Credit [(2/3)($1,875)] | | ( 1,250) |
| Charitable Donations [(15%)($200) + (29%)($1,500 - $200)] | | ( 407) |
| Political Contributions Tax Credit [(3/4)($400) + (1/2)($350) + (1/3)($150)] | | ( 525) |
| Net Federal Tax | | $ 8,111 |
| CPP Overpayment ($2,307 + $500 - $2,307) | | ( 500) |
| EI Overpayment ($840 + $390 - $840) | | ( 390) |
| Amount Owing To The CRA | | $ 7,221 |

**Note Nine** As the eligible dependant credit can only be claimed for one individual, claiming it for Martin means that Louise does not qualify for this credit. As she does not qualify for this credit, she would be eligible for both the infirm dependant over 17 and the caregiver tax credits. In these circumstances, ITA 118(4)(d) deems Louise not to be a dependant, in effect requiring the caregiver credit to be claimed. Because Louise is disabled, and her income is below the threshold for the caregiver credit, Ms. Klaus can claim the full amount of the caregiver credit, as well as the family caregiver amount.

**Note Ten**

| | | |
|---|---|---|
| Marcia And Martin's Medical Expenses ($9,700 + $900) | | $10,600 |
| Threshold - Lesser Of: [(3%)($106,307)] and $2,152 | | ( 2,152) |
| Subtotal | | $ 8,448 |
| Louise's Medical Expense | $7,250 | |
| Reduced By The Lesser Of: | | |
| • [(3%)($6,000)] = $180 | | |
| • 2013 Limit = $2,152 | ( 180) | 7,070 |
| Allowable Medical Expenses | | $15,518 |



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# Solution to Assignment Problem Eleven - 8

## Part A - Jihoon's Results

### *Net Income For Tax Purposes*

Note, because Jihoon's income is subject to the tax on split income, the income attribution rules are not applicable. Given this, Jihoon Son's Net Income For Tax Purposes would be calculated as follows:

| | |
|---|---:|
| Dividends Received | $20,000 |
| Gross Up [(25%)($20,000)] | 5,000 |
| ITA 20(1)(ww) Deduction For Split Income | ( 25,000) |
| Net Income For Tax Purposes | Nil |

### *Taxable Income*

As his Net Income For Tax Purposes is nil, Jihoon Son's Taxable Income would also be nil.

### *Tax Payable*

As his Taxable Income is nil, Jihoon Son's regular federal Tax Payable would also be nil. However, he would have a tax on his split income, calculated as follows:

| | |
|---|---:|
| Split Income | $25,000 |
| Rate | 29% |
| Tax Before Credit | $ 7,250 |
| Dividend Tax Credit [(2/3)(25%)($20,000)] | ( 3,333) |
| Tax Payable On Split Income | $3,917 |

As his regular Tax Payable is nil, his total Tax Payable would be $3,917.

## Part B - Jimon's Results

### *Net Income For Tax Purposes*

Ms. Son's Net Income For Tax Purposes would be calculated as follows:

| | |
|---|---:|
| Net Employment Income (Salary - Musical Notes Inc.) | $150,000 |
| Property Income (Note 1) | 115,500 |
| Net Taxable Capital Gains (Note 2) | 386,900 |
| Child Care Expenses (Note 6) | ( 3,500) |
| RRSP Deduction (Given) | ( 9,500) |
| Net Income For Tax Purposes | $639,400 |

**Note 1** Ms. Son's property income would be calculated as follows:

| | |
|---|---:|
| Non-Eligible Dividend On Son Enterprises Shares | $ 60,000 |
| Gross Up [(25%)($60,000)] | 15,000 |
| Interest Income From South Korean Bank Account (100%) | 500 |
| Royalties | 40,000 |
| Property Income | $115,500 |



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**Note 2** Ms. Son's net taxable capital gains would be calculated as follows:

| | |
|---|---|
| Gain On Musical Notes Inc. Shares ($575,000 - $100) | $574,900 |
| Listed Personal Property Gain On Painting ($50,000 Minus The Lesser Of $200 And $1,000 Floor) | 49,000 |
| Listed Personal Property Loss Carry Forward (Note 3) | ( 500) |
| Sale Of Vacant Land (Note 4) | 150,000 |
| Net Foreign Currency Gain ($700 - $100) | 600 |
| Foreign Currency Exemption For Individuals | ( 200) |
| Loss On Music Collection (Note 5) | Nil |
| Net Capital Gains | $773,800 |
| Inclusion Rate | 1/2 |
| Net Taxable Capital Gain | $386,900 |

**Note 3** Under ITA 41(2) the net gain on listed personal property is defined as the gains for the current year, reduced by the carry over amounts from the seven preceding years or the three subsequent years. Ms. Son had a listed personal property loss carry forward of $500, which is deducted against her listed personal property gain on the painting that was sold in 2013. Note that the listed property loss carry forward is deducted in the calculation of net taxable capital gains for inclusion in Net Income For Tax Purposes.

**Note 4** Since Jimin had made a small profit annually on renting the land, the property taxes must have been deducted each year and would have no effect on the calculation of the capital gain. The gain would be $150,000 ($175,000 - $25,000).

**Note 5** The fair market value of the music collection donated to the university is less than Jimin's adjusted cost base. However, since this is personal use property, the loss is not deductible.

**Note 6** Child care expenses cannot be deducted for a child with net income in excess of the basic personal credit ($11,038 for 2013). However, since split income is deducted in the determination of Net Income For Tax Purposes and Jihoon has no income other than split income, his Net Income For Tax Purposes is nil.

### *Taxable Income*

Ms. Son's Taxable Income would be calculated as follows:

| | |
|---|---|
| Net Income For Tax Purposes | $639,400 |
| Less: Lifetime Capital Gains Deduction (Note 7) | ( 267,450) |
| Less: Net Capital Loss Carry Forward | ( 2,000) |
| Taxable Income | $369,950 |

**Note 7** The maximum lifetime capital gains deduction would be $267,450 calculated as the least of the following amounts:

**Capital Gains Deduction Available = $275,000**

| | |
|---|---|
| Maximum lifetime limit [(1/2)($750,000)] | $375,000 |
| Less: used in previous year [(1/2)($200,000)] | ( 100,000) |
| Capital Gains Deduction available | $275,000 |



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**Annual Gains Limit = $287,450**

This limit is equal to A - B, where

A = $287,450

The lesser of the net taxable capital gains (see Note 2) on:

- All Capital Assets = $386,900
- Qualifying Property [(1/2)($574,900)] = $287,450

B = Nil

The total of:

- The amount, if any, by which net capital loss carry overs deducted for the year under ITA 111(1)(b), exceeds the excess of net taxable capital gains for the year [ITA 3(b)] over the amount determined in Part A of this formula. This amount is nil [$2,000 – ($386,900 - $287,450)]; and
- Allowable Business Investment Losses realized during the current year. This amount is also nil.

This provides an annual gains limit of $287,450 ($287,450 - Nil).

**Cumulative Gains Limit = $267,450**

| | |
|---|---|
| Annual Gains Limit From Previous Years | $100,000 |
| Current Year Annual Gains Limit | 287,450 |
| Less: Previous Lifetime Capital Gains Deduction | ( 100,000) |
| Less: CNIL (Given - See Note 8) | ( 20,000) |
| Cumulative Gains Limit | $ 267,450 |

**Note 8** Note that if Ms. Son had paid herself sufficient dividends, rather than salary, she could have eliminated her CNIL and increased her lifetime capital gains deduction by $20,000.

***Tax Payable***

Ms. Son's regular Tax Payable would be determined as follows:

| | | |
|---|---|---|
| Tax On First $135,054 | | $28,580 |
| Tax on Next $234,896 ($369,950 - $135,054) at 29% | | 68,120 |
| Tax Before Credits | | $96,700 |
| Tax Credits: | | |
| Basic Personal | ($11,038) | |
| Eligible Dependant | ( 11,038) | |
| Child Credit | ( 2,234) | |
| CPP | ( 2,356) | |
| Canada Employment Credit | ( 1,117) | |
| Children's Arts Credit ($500 Maximum) | ( 500) | |
| Child Fitness Credit | ( 200) | |
| Medical Expenses (Note 9) | ( 17,848) | |
| Total Credit Base | ($46,331) | |
| Rate | 15% | ( 6,950) |
| Charitable Donation Credit (Note 10) | | ( 5,047) |
| Foreign Tax Credit (Note 11) | | ( 50) |
| Dividend Tax Credit [(2/3)($15,000)] | | ( 10,000) |
| Federal Tax Payable | | $74,653 |



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**Note 9** The base for Ms. Son's medical expense credit can be calculated as follows:

| | |
|---|---|
| Eligible Medical Expenses – Jihoon Son | $20,000 |
| Reduced By The Lesser Of: | |
| • [(3%)($639,400)] = $19,182 | |
| • 2013 Threshold Amount = $2,152 | ( 2,152) |
| Total Credit Base | $17,848 |

**Note 10** The maximum charitable donation receipt she can receive is for $17,500, the fair market value of the collection donated to the university as it is less than Jimin's adjusted cost base. The credit is $5,047 [(15%)($200) + (29%)($17,500 - $200)].

**Note 11** Ms. Son's Adjusted Division B Income would be calculated as follows:

| | |
|---|---|
| Net Income For Tax Purposes | $639,400 |
| Lifetime Capital Gains Deduction Taken | ( 267,450) |
| Capital Loss Carry Forward Deducted | ( 2,000) |
| Adjusted Division B Income (= Taxable Income) | $369,950 |

Her Tax Otherwise Payable would be calculated as follows:

| | |
|---|---|
| Tax Before Credits | $96,700 |
| Basic Personal Credits | ( 6,950) |
| Charitable Donation Credit | ( 5,047) |
| Tax Otherwise Payable | $84,703 |

Since the foreign non-business tax withheld is less than 15 percent of the foreign income, Ms. Son's credit for foreign tax paid would be the lesser of the foreign tax withheld of $50 and an amount determined by the following formula:

[(Foreign Non-Business Income ÷ Adjusted Division B Income)(Tax Otherwise Payable)]

= [($500 ÷ $369,950)($84,703)] = $114

As the amount withheld is the lesser of the two figures, her foreign tax credit is $50.

### *Alternative Minimum Tax Payable*

Ms. Son's Adjusted Taxable Income for alternative minimum tax purposes would be calculated as follows:

| | |
|---|---|
| Regular Taxable Income | $369,950 |
| 30 Percent Of Net Capital Gains [(30%)(2)($386,900)] | 232,140 |
| Dividend Gross Up [(25%)($60,000)] | ( 15,000) |
| Adjusted Taxable Income (For AMT) | $587,090 |

The calculation of the alternative minimum tax would be as follows:

| | |
|---|---|
| Adjusted Taxable Income | $587,090 |
| Basic Exemption | ( 40,000) |
| Amount Subject To Tax | $547,090 |
| Rate | 15% |
| Minimum Tax Before Credits | $ 82,064 |
| Basic Personal Tax Credits | ( 6,950) |
| Charitable Donation Credit | ( 5,047) |
| Alternative Minimum Tax Payable | $ 70,067 |

As the alternative minimum tax payable is less than the regular tax payable, the regular amount would be paid.



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## Part C

### *Ms. Son – RRSP, TFSA and cash flow considerations*

Ms. Son has asked you to consider whether she should use her TFSA or her RRSP funds if she needs cash in the next few years as her jazz quartet develops a following and becomes a significant source of income for her.

If the condo Ms. Son is planning to buy will be her principal residence, she will be eligible to withdraw funds from her RRSP under the Home Buyers' Plan. Since the maximum withdrawal available under this Plan is $25,000, that may not prove adequate for all her cash needs.

It would be best for her to use her TFSA funds next should she need access to additional cash or if she does not qualify for the Home Buyers' Plan. Withdrawing money from her TFSA will not result in any additional tax cost to Jimin. In addition, she will be able to return funds to her TFSA in the future, which will not be possible if funds are withdrawn from her RRSP other than through the Home Buyers' Plan.

With respect to withdrawing money from her RRSP other than through the Home Buyers' Plan, it is possible to do so, but not recommended. These withdrawals from an RRSP account will be taxed in the year of withdrawal. Also, this type of RRSP withdrawal does not result in an increase in the ability to make future contributions, so it would result in a permanent reduction in the amount of money that Ms. Son could save for her retirement in a tax deferred savings arrangement.



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## Solution to Assignment Problem Four - 4

Mr. Brooks' net employment income would be calculated as follows:

| | | |
|---|---|---|
| Gross Salary | | $53,000 |
| Additions: | | |
| Bonus (Amount Received Only) | $6,500 | |
| Disability Insurance Receipts (Note One) | 4,200 | |
| Personal Benefit On Car (Note Two) | 1,034 | |
| Stock Option Benefit [($28 - $23)(200)] (Note Three) | 1,000 | |
| Home Relocation Loan Benefit (Note Four) | 625 | 13,359 |
| | | $66,359 |
| Deductions: | | |
| RPP Contributions | ($2,800) | |
| Union Dues | ( 240) | ( 3,040) |
| Net Employment Income | | $63,319 |

**Note One** As all of the premiums were paid by the employer and were not considered to be a taxable benefit, benefits received under this coverage must be included in employment income.

**Note Two** The personal benefit on the company car, taking into consideration the two months he was in the hospital and unable to make use of the car, would be as follows:

| | |
|---|---|
| Standby Charge [(2/3)(12)($678)(10/12)(5,000/16,670)] | $1,356 |
| Operating Cost Benefit - Lesser Of: | |
| • [(5,000)($0.27)] = $1,350 | |
| • [(1/2)($1,356)] = $678 | 678 |
| Less: Payments Withheld By Employer | ( 1,000) |
| Taxable Benefit | $1,034 |

**Note Three** Although Mr. Brooks would qualify for the deduction of one-half of the stock option benefit under ITA 110(1)(d), it is a deduction from Taxable Income and would not affect the calculation of net employment income.

**Note Four** The taxable benefit associated with the home relocation loan would be calculated as follows:

[($125,000)(2% - Nil)(3/12)] = $625

### *Taxable Income*

Mr. Brooks' Taxable Income would be calculated as follows:

| | |
|---|---|
| Net Income For Tax Purposes (Net Employment Income) | $63,319 |
| Stock Option Deduction [(1/2)($1,000)] | ( 500) |
| Home Relocation Loan Deduction - Lesser Of: | |
| • Benefit Included In Income = $625 | |
| • [($25,000)(2% - Nil)(3/12)] = $125 | ( 125) |
| Taxable Income | $62,694 |



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***Tax Payable***

Mr. Brooks' federal Tax Payable (Refund) would be calculated as follows:

| | | |
|---|---|---|
| Tax On First $43,561 | | $ 6,534 |
| Tax On Next $19,133 ($62,694 - $43,561) At 22 Percent | | 4,209 |
| Federal Tax Before Credits | | $10,743 |
| Basic Personal Amount | ($11,038) | |
| Eligible Dependant - Harold | ( 11,038) | |
| Child Including FCA - Harold (Note Five) | ( 4,274) | |
| Transfer Of Harold's Disability | ( 7,697) | |
| Transfer Of Harold's Disability Supplement | ( 4,490) | |
| Caregiver - Mother (Note Six) | ( 4,490) | |
| EI Premiums | ( 891) | |
| CPP Contributions | ( 2,356) | |
| Canada Employment | ( 1,117) | |
| Public Transit Passes (Note Seven) | ( 860) | |
| Medical Expenses (Note Eight) | ( 10,890) | |
| Tuition Fee - Unreimbursed Music Course (Note Nine) | ( 600) | |
| First Time Home Buyer's | ( 5,000) | |
| Credit Base | ($64,741) | |
| Rate | 15% | ( 9,711) |
| Charitable Donations [(15%)($200) + (29%)($480 - $200)] | | ( 111) |
| Net Federal Tax | | $ 921 |
| Federal Income Tax Withheld | | ( 3,000) |
| Federal Tax Payable (Refund) | | ($ 2,079) |

**Note Five** Harold qualifies for the family caregiver amount. While this amount can be added to both the eligible dependant and the child tax credits, when one child qualifies for both of these credits, it is only added to the child tax credit.

**Note Six** Mr. Brooks is eligible for the caregiver credit for his mother as she is over 64 years of age and her income is below the threshold for the caregiver credit. This means that Mr. Brooks can claim the full amount of the caregiver credit. As she is not infirm, the family caregiver amount is not available for her.

**Note Seven** Mr. Brooks cannot claim the cost of the transit passes for his mother. As a result, the base for the public transit pass credit is $860 [(10)($26 + $60)].

**Note Eight** Allowable medical expenses are as follows:

| | | |
|---|---|---|
| Mr. Brooks' And Minor Child (Harold) Medical Expenses ($9,300 + $2,450) | | $11,750 |
| Reduced By The Lesser Of: | | |
| • [(3%)($63,319)] = $1,900 | | |
| • 2013 Threshold Amount = $2,152 | | ( 1,900) |
| Grace's Medical Expenses | $1,265 | |
| Reduced By The Lesser Of: | | |
| • $2,152 | | |
| • [(3%)($7,500)] = $225 | ( 225) | 1,040 |
| Allowable Medical Expenses | | $10,890 |

**Note Nine** Since the music course was less than three consecutive weeks in duration, Mr. Brooks cannot claim the education or textbook credit for that course. As the accounting course tuition fees were reimbursed by his employer, no education or textbook credits are available for that course either.



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## Solution to Assignment Problem Four - 5

### *Part 1 - Net Income For Tax Purposes*

As Mr. Cousteau's only income is from employment, his Net Income For Tax Purposes is equal to Net Employment Income. The required amount would be calculated as follows:

| | |
|---|---|
| Salary | $70,000 |
| Additions | |
| Bonus ($5,000 ÷ 5) | 1,000 |
| Salary Deferral Benefit (Bonus Past 2016) | 1,000 |
| Performance Award (Briefcase) | 800 |
| Christmas Basket ($600 - $500) | 100 |
| Loan Benefit (Note 1) | 6,250 |
| Automobile Benefit (Note 2) | 10,899 |
| Employer Paid Premium On Life Insurance | 600 |
| Deductions | |
| RPP Contributions | ( 1,200) |
| CMA Dues | ( 900) |
| Net Income For Tax Purposes | $88,549 |

**Note 1** The home loan benefit would be calculated as follows:

| | |
|---|---|
| Taxable Benefit Under ITA 80.4(1)(a) - Lesser Of: | |
| • [(3%)(2/4)($500,000) + (2%)(1/4)($500,000)] = $10,000 | |
| • [(3%)(3/4)($500,000)] = $11,250 | $10,000 |
| Reduction For Payments Under ITA 80.4(1)(c) [(1%)($500,000)(3/4)] | ( 3,750) |
| Total ITA 80.4(1) Benefit = Addition To Net Income For Tax Purposes | $ 6,250 |

**Note 2** The automobile benefit would be calculated as follows:

| | |
|---|---|
| Toronto Standby Charge [(2/3)($875 - $50)(3)(3,000/5,001)] | $ 990 |
| Toronto Operating Cost Benefit - Lesser Of: | |
| • [($0.27)(3,000)] = $810 | |
| • [(1/2)($990)] = $495 | 495 |
| Vancouver Standby Charge [(2%)($31,300)(9)] | 5,634 |
| Vancouver Operating Cost Benefit [($0.27)(14,000)] | 3,780 |
| Total | $10,899 |

On the Vancouver vehicle, employment usage was less than 50 percent. This means that the alternative operating cost benefit calculation is not available.

**Other Notes:**

- A bonus that is payable more than 3 years after the end of the year in which an employee provides services is a salary deferral arrangement and must be included in income.
- Performance awards are fully taxable.
- The exempt portion of non-cash gifts is limited to $500.
- As the housing loan was related to a re-location, there will be an offsetting deduction in the calculation of Taxable Income.
- While employer payments for life insurance premiums are a taxable benefit, employer contributions to RPPs are not a benefit.



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***Part 2 - Taxable Income***

Mr. Cousteau's Taxable Income would be calculated as follows:

| | |
|---|---|
| Net Income For Tax Purposes | $88,549 |
| Home Relocation Loan Deduction - Lesser Of: | |
| • ITA 80.4(1) Benefit = $6,250 | |
| • [(3%)(2/4)($25,000) + (2%)(1/4)($25,000)] = $500 | ( 500) |
| Taxable Income | $88,049 |

Despite the fact that the prescribed rate has increased, Mr. Couteau can continue to use the rate in effect at the time the loan was made to calculate the taxable benefit. This can continue for a period of five years. Note that the deduction is calculated as if the loan had been for $25,000 rather than $500,000.

***Part 3 - Federal Tax Payable***

Mr. Cousteau's federal Tax Payable would be calculated as follows:

| | | |
|---|---|---|
| Tax On First $87,123 | | $ 16,118 |
| Tax On Next $926 ($88,049 - $87,123) At 26 Percent | | 241 |
| Tax Before Credits | | $16,359 |
| Credits: | | |
| Basic Personal Amount | ($11,038) | |
| Spousal Including FCA ($11,038 + $2,040 - $9,000) | ( 4,078) | |
| Disability Transfer From Spouse | ( 7,697) | |
| Child - Haley | ( 2,234) | |
| Caregiver Including FCA - Manny (Note 3) | ( 6,530) | |
| Infirm Dependant Over 17 - Jay (Note 4) | ( 4,578) | |
| Child Fitness (Dance Lessons) - Maximum | ( 500) | |
| First Time Home Buyer | ( 5,000) | |
| CPP | ( 2,356) | |
| EI | ( 891) | |
| Canada Employment | ( 1,117) | |
| Medical Expenses (Note 5) | ( 3,223) | |
| | ($49,242) | |
| Rate | 15% | ( 7,386) |
| Charitable Donations [(15%)($200) + (29%)($1,500 + $500 - $200)] | | ( 552) |
| Federal Tax Payable Before Withholding | | $ 8,421 |
| Amounts Withheld | | ( 8,500) |
| Balance Owing (Refund) | | ($ 79) |

**Note 3** Manny qualifies for both the caregiver credit and the infirm dependant over 17 credit. In these circumstances, ITA 118(4)(d) effectively requires the use of the caregiver credit. Because Manny is infirm, and his income is below the threshold for the caregiver credit, Mr. Cousteau can claim the full amount of the caregiver credit, as well as the family caregiver amount.

**Note 4** Jay does not qualify for the caregiver credit as he does not reside with Phil. He would, however, qualify for the infirm dependant over 17 credit which includes the family caregiver amount. This results in a credit of $4,578 [($6,530 - ($8,500 - $6,548)]. Note there is no provision for the transfer of a parent's age or pension credit.

**Note 5** The base for the medical expense tax credit can be calculated as follows:



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| | | |
|---|---|---|
| Phil, Claire, And Haley ($650 + $1,940 + $860) | | $3,450 |
| Reduced By The Lesser Of: | | |
| • [(3%)($88,549)] = $2,656 | | |
| • 2013 Threshold Amount = $2,152 | | ( 2,152) |
| Manny | $1,250 | |
| Reduced By The Lesser Of: | | |
| • [(3%)($15,000)] = $450 | | |
| • $2,152 | ( 450) | 800 |
| Cameron | $480 | |
| Reduced By The Lesser Of: | | |
| • [(3%)($3,000)] = $90 | | |
| • $2,152 | ( 90) | 390 |
| Jay | $990 | |
| Reduced By The Lesser Of: | | |
| • [(3%)($8,500)] = $255 | | |
| • $2,152 | ( 255) | 735 |
| Total | | $3,223 |

**Note 6** Although Mr. Cousteau can claim Cameron's allowable medical expenses, he cannot claim a credit for Cameron as he is not infirm.



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## Solution to Assignment Problem Four - 6

***Part A***

Martin's minimum Net Income For Tax Purposes would be calculated as follows:

| | |
|---|---|
| Salary | $ 98,500 |
| Additions: | |
| Bonus (2013 Receipt) | 3,000 |
| Bonus (Amounts After 2016 - Salary Deferral) | 3,000 |
| Client Meals And Entertainment (Note 1) | Nil |
| Stock Options (Note 2) | 12,500 |
| Interest Free Loan Benefit (Note 3) | 1,400 |
| Automobile Benefit (Note 4) | 8,935 |
| Gifts (Note 5) | 550 |
| Deductions: | |
| RPP Contributions | ( 4,300) |
| Union Dues | ( 450) |
| Net Income For Tax Purposes | $123,135 |

**Note 1** Martin's meal and entertainment costs exceed his employer's reimbursement by $5,000 ($12,300 - $7,300). However, as he has no commission income, he cannot deduct these out-of-pocket costs.

**Note 2** The stock option benefit would be calculated as follows:

[(500)($70 - $45)] = $12,500

Note that, because the option price was less than the fair market value of the shares at the time the options were granted, no ITA 110(1)(d) deduction is available in the determination of Taxable Income (Part B).

**Note 3** The loan does not qualify as a home relocation loan. The taxable benefit on the loan is calculated as follows:

[(1%)($280,000)(6/12)] = $1,400

**Note 4** The automobile benefit would be calculated as follows:

| | |
|---|---|
| Standby Charge [(2%)(11)($45,200)(11,000 ÷ 18,337)] | $5,965 |
| Operating Cost Benefit - Lesser Of: | |
| • [(1/2)($5,965)] = $2,983 | |
| • [($0.27)(11,000)] = $2,970 | 2,970 |
| Total Benefits | $8,935 |

As Martin's employment related use was more than 50 percent, the reduced standby charge is available. In addition, he could use the alternative calculation of the operating cost benefit. However, it does not provide the lower figure in this case.

**Note 5** The gift certificate for $250 is taxable because it is a near-cash gift. The first $500 of the long-service award will not be a taxable benefit. However, the excess of $300 ($800 - $500) will be a taxable benefit. As the value of the Christmas gift basket is under $500, it will not create a taxable benefit. The total taxable benefit for gifts is $550 ($250 + $300).

***Part B***

Martin's Taxable Income would be equal to his Net Income For Tax Purposes as there is no stock option deduction or home relocation loan deduction available.



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***Part C***

Based on the Taxable Income calculated in Part B, Martin's Tax Payable would be calculated as follows:

| | | |
|---|---|---|
| Tax On First $87,123 | | $16,118 |
| Tax On Next $36,012 ($123,135 - $87,123) At 26 Percent | | 9,363 |
| Tax Before Credits | | $25,481 |
| Credits: | | |
| Basic Personal Amount | ($11,038) | |
| Spousal Including FCA ($11,038 + $2,040 - $9,400) | ( 3,678) | |
| Caregiver Including FCA - Devon (Note 6) | ( 6,530) | |
| Child - David | ( 2,234) | |
| Transfer Of Brian's Disability | ( 7,697) | |
| Transfer Of Derek's Education Related Credits (Note 7) | ( 3,388) | |
| First Time Home Buyers (Maximum) | ( 5,000) | |
| Transit Passes [($85)(1)(10)] (Note 8) | ( 850) | |
| EI Premiums | ( 891) | |
| CPP Contributions | ( 2,356) | |
| Canada Employment | ( 1,117) | |
| Medical Expenses (Note 9) | ( 16,288) | |
| Credit Base | ($61,067) | |
| Rate | 15% | ( 9,160) |
| Charitable Donations [(15%)($200) + (29%)($2,000 - $200)] | | ( 552) |
| Federal Tax Payable | | $15,769 |
| Federal Tax Withheld | | ( 18,000) |
| Amount Owing (Refund) | | ($ 2,231) |

**Note 6** Devon is eligible for both the infirm dependant over 17 and the caregiver tax credits. In these circumstances, ITA 118(4)(d), in effect, requires the use of the caregiver credit. Because Devon is infirm, and his income is below the threshold for the caregiver credit, Martin can claim the full amount of the caregiver credit, as well as the family caregiver amount.

**Note 7** Derek's total education related amounts are calculated as follows:

| | |
|---|---|
| Tuition | $10,300 |
| Education [(8)($400)] | 3,200 |
| Textbook [(8)($65)] | 520 |
| Total | $14,020 |

Derek will have to reduce his own Tax Payable to nil before transferring any credits. He will require $1,612 [$13,500 - $11,038 - ($85)(1)(10)] of this amount. This means that his transfer will be limited to $3,388 ($5,000 - $1,612). This will leave Derek with a carry forward of $9,020 ($14,020 - $5,000).

The reason for the assumption of no CPP contributions is that business income is not covered until Chapter 6. Derek's self-employed income would be reduced by half of the CPP paid and his tax payable would be reduced by the other half.



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**Note 8** The transit pass credit can only be claimed for children who have not attained the age of 19 during the year. Although he has paid for them, Martin cannot claim Derek's transit passes. Derek has claimed them in the Note 7 calculation.

**Note 9** The base for Martin's medical expense credit can be calculated as follows:

| | | |
|---|---|---|
| Martin, Brian, And David | | |
| ($2,200 + $1,700) | | $ 3,900 |
| Reduced By The Lesser Of: | | |
| • [(3%)($123,135)] = $3,694 | | |
| • 2013 Threshold Amount = $2,152 | | ( 2,152) |
| Devon's Medical Expenses | $10,600 | |
| Reduced By The Lesser Of: | | |
| • $2,152 | | |
| • [(3%)($5,150)] = $155 | ( 155) | 10,445 |
| Derek's Medical Expenses | $4,500 | |
| Reduced By The Lesser Of: | | |
| • $2,152 | | |
| • [(3%)($13,500)] = $405 | ( 405) | 4,095 |
| Allowable Medical Costs | | $16,288 |



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## Solution to Assignment Problem Twenty-One - 4

The sales are fully taxable. GST paid on the cost of balloons purchased and Operating Costs can be claimed as an input tax credit. All other items are GST exempt. The net GST remittance for the month is calculated as follows:

| | |
|---|---|
| GST On Sales [(5%)($69,000)] | $3,450 |
| Input Tax Credits: | |
| Balloons Purchased [(5%)($12,000 - $3,000 + $4,000)] | ( 650) |
| Salaries And Wages | Nil |
| Operating Costs [(5%)($14,500)] | ( 725) |
| Amortization Expense | Nil |
| Net GST Remittance For The Month | $2,075 |



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## Solution to Assignment Problem Twenty-One - 7

***Part A(i) - Regular GST Method***

Using this method, the GST payable would be calculated as follows:

| | |
|---|---|
| Sales [(5%)($350,000)] | $17,500 |
| Purchases [(5%)($200,000)] | ( 10,000) |
| Capital Expenditures [(5%)($20,000)] | ( 1,000) |
| GST Payable - Regular Method | $ 6,500 |

***Part A(ii) - Quick Method***

In order to determine the Quick Method remittance rate, the following amounts are required:

| | |
|---|---|
| 2012 GST Inclusive Purchases Of Goods For Resale [($160,000)(105%)] | $168,000 |
| 2012 GST Inclusive Sales Of Taxable Supplies [($275,000)(105%) + $28,000] | $316,750 |

Since $168,000 ÷ $316,750 equals 53 percent and this is greater than 40 percent, Brown Retailer would use the reseller's remittance rate of 1.8 percent.

The alternative figure under the quick method would be calculated as follows:

| | |
|---|---|
| Basic Tax [(1.8%)(105%)($350,000)] | $6,615 |
| Credit On First $30,000 [(1%)(30,000)] | ( 300) |
| Subtotal | $6,315 |
| Capital Expenditures [(5%)($20,000)] | ( 1,000) |
| GST Payable - Quick Method | $5,315 |

***Part B***

If the exempt sales were zero-rated instead, Brown Retail could not use the Quick Method as the GST included sales of taxable supplies would be over $400,000. They would total $467,500 [$80,000 + ($350,000)(105%) + $20,000].



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