TEST ITEM FILE - PROBLEMS

Byrd & Chen's Canadian Tax Principles
2010 - 2011 Edition

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- Updates and corrections to the supplements package
- PowerPoint slide presentations for all chapters
- Online posting policy for assignment problem solutions and permission form
- Solutions to Tax Software Problems, updated for the 2010 version of ProFile (January, 2011)

Bookmarks In PDF File

To assist you in navigating through the electronic version of this Test Item File, (available on the Instructor's CD-ROM) there are bookmarks on the first page of each Test Item problem and solution

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Chapter One Test Item File Problems

TIF PROBLEM ONE - 1
Introduction - Essay Questions

Provide brief answers to each of the following questions:

1. Indicate three disadvantages of a tax system that uses progressive rates.

2. A regressive tax is one that taxes high income individuals at lower effective rates. Explain why a sales tax levied at a flat rate of 8 percent can be regressive.

3. The Canadian income tax system is often used to achieve various economic objectives. Give three examples that illustrate this point.

4. Distinguish between horizontal equity and vertical equity as these terms are used in describing tax systems.

5. The government pays a "child tax benefit" to the parents of children who are under 18 years of age. The payments are reduced by a percentage of income in excess of a specified level. What objectives are achieved by this benefit system?

6. What is the meaning of "taxation year" as the phrase is used in the *Income Tax Act*.

7. Under what circumstances will a person who is not resident in Canada be required to pay Canadian income taxes?

8. What are the components of Net Income For Tax Purposes?

9. ITA 3(b) states that a taxpayer should "determine the amount, if any", by which taxable capital gains exceeds allowable capital losses. In this context, what is the meaning of the phrase "the amount, if any".

10. What is the difference between tax avoidance and tax deferral?

11. What is income splitting? Under what circumstances will it provide tax benefits to an individual?

12. Contributions to a Registered Retirement Savings Plan can be deducted to reduce the taxes of an individual in the year that they are made. However, these contributions will be subject to tax when they are withdrawn from the plan. What type of tax planning is involved in this arrangement?

TIF PROBLEM ONE - 2
Introduction - True Or False

1. A value added tax is a tax levied on the increase in value of a commodity or service that has been created by the taxpayer's stage of the production or distribution cycle.

   True or False?

2. A partnership can be a taxable entity for income tax purposes.

   True or False?

3. A partnership can be a taxable entity for GST purposes.

   True or False?

4. In general, provincial income taxes are based on a specified percentage of federal tax payable.

   True or False?

5. The federal government does not collect personal or corporate taxes for Ontario or Quebec.

   True or False?

6. A sales tax is a regressive tax even when it is applied at a single rate on all transactions.

   True or False?

7. A major advantage of progressive tax rates is that their use encourages economic growth.

   True or False?

8. Tax expenditures are less costly to administer than direct funding programs.

   True or False?

9. Part I of the *Income Tax Act* is the largest and most important part.

   True or False?

10. The citation ITA 61(4)(b)(ii) would be read Paragraph 61, Subparagraph 4, Section b, Subsection ii.

    True or False?

11. An income tax is payable for each taxation year on the Taxable Income of every person resident in Canada at any time in the year.

    True or False?

12. Any taxpayer can choose the calendar year as their taxation year.

    True or False?

TIF PROBLEM ONE - 3
Introduction - Multiple Choice

Canadian Tax System

1. Which of the following is not a taxable entity for Canadian income tax purposes?

   A. Darklyn Ltd., a Canadian resident corporation.
   B. Ms. Sarah Bright, a Canadian resident.
   C. Walters and Walters, a group of CMAs operating as a partnership.
   D. The Martin family trust.

2. With respect to provincial income taxes, other than those assessed in Quebec, which of the following statements is not correct?

   A. Each province can apply different rates to as many brackets for individuals as it wishes.
   B. The federal government collects the provincial income tax for individuals for every province except Quebec.
   C. Each province can establish its own tax credits to apply against Tax Payable for individuals.
   D. Each province can establish rules for determining the Taxable Income of individuals.

Tax Policy Concepts

3. Which of the following can be considered an advantage of an income tax system based on progressive rates?

   A. A progressive rate system is simpler to administer.
   B. A progressive rate system provides greater stability in the context of changing economic conditions.
   C. A progressive system discourages tax evasion.
   D. A progressive system encourages greater effort on the part of individuals.

4. Which of the following statements with respect to using tax expenditures rather than program spending is not correct?

   A. It is more costly to administer tax expenditures as opposed to program spending.
   B. Tax expenditures reduce the visibility of government actions.
   C. Tax expenditures leave fewer decisions in the hands of the private sector, thereby providing for more efficient allocation of resources.
   D. Tax expenditures reduce the impact of progressive rates on higher income taxpayers.

5. Which of the following would not be considered a desirable characteristic of a tax system?

   A. Balance between sectors.
   B. Inelasticity.
   C. Neutrality.
   D. Flexibility.

6. Which of the following would be considered a desirable characteristic of an effective tax system?

   A. Inelasticity.
   B. Lack of international competitiveness.
   C. Simplicity.
   D. Ambiguity.

7. We should not have a tax system which encourages investment in particular assets or in particular areas of the county. This statement reflects which of the following qualitative characteristics of an effective tax system?

   A. Neutrality.
   B. Horizontal equity.
   C. Simplicity.
   D. Elasticity.

8. Taxpayers who earn $100,000 in dividends should pay the same amount of tax as taxpayers who earn $100,000 in capital gains. This statement reflects which of the following qualitative characteristics of an effective tax system?

   A. Vertical equity.
   B. Neutrality.
   C. Elasticity.
   D. Horizontal equity.

Income Tax Reference Materials

9. With respect to the structure of the *Income Tax Act*, which of the following statements is correct?

   A. The major components of the *Income Tax Act* are called Divisions.
   B. The current *Income Tax Act* has Sections numbers 1 through 260, reflecting the fact that there are 260 Sections in the *Act*.
   C. All Parts of the *Income Tax Act* have Divisions.
   D. All Parts of the *Income Tax Act* contain at least one Section.

10. Of the following publications, indicate the one that is not a legislative source.

   A. *Income Tax Act*.
   B. Interpretation Bulletins.
   C. Income Tax Application Rules.
   D. International Tax Treaties.
   E. Income Tax Regulations.

11. Of the following publications, indicate the one that is not published by the CRA.

   A. Interpretation Bulletins.
   B. Information Circulars.
   C. Dominion Tax Cases.
   D. Income Tax Technical News.

12. There are a number of common areas of litigation involving the CRA. Indicate which type of transaction is least likely to be in dispute.

   A. Arm's length versus non-arm's length transactions.
   B. Capital versus income transactions.
   C. Unreported revenues from business transactions.
   D. Establishment of fair market value.
   E. The deductibility of farm losses against other sources of income.

13. Where would an individual find the formula for determining the prescribed rate?

   A. The Income Tax Act.
   B. The Income Tax Regulations.
   C. A CRA Interpretation Bulletin.
   D. A CRA Information Circular.

14. Which of the following statements is not correct?

A. Most major income tax changes are introduced in the annual Federal Budget.
B. A federal election can prevent passage of draft legislation.
C. Proposed changes in tax law are usually introduced to parliament in the form of a Notice of Ways and Means Motion.
D. When there is a conflict between the Canadian *Income Tax Act* and an international agreement, the terms of the Canadian *Income Tax Act* prevail.

Liability For Tax

15. With respect to the calculation of Net Income For Tax Purposes, which of the following statements is not correct?

A. Subdivision e deductions are subtracted from the total of all positive sources of income.
B. Allowable capital losses for the year can only be deducted to the extent of taxable capital gains for the year.
C. Business losses can be netted against employment income in determining the positive amounts to be included under ITA 3(a) and 3(b).
D. Property losses can only be deducted after the subtraction of Subdivision e deductions.

Tax Planning

16. Providing employees with private health care benefits involves what type of tax planning?

A. Tax evasion.
B. Tax deferral.
C. Income splitting.
D. Tax avoidance.

17. Making contributions to an RRSP always involves what type of tax planning?

A. Tax avoidance and tax deferral.
B. Tax deferral.
C. Tax avoidance.
D. Income splitting.

TIF PROBLEM ONE - 4
Introduction - Exam Exercises

Exam Exercise One - 1 (Non-Resident Liability For Tax)

Ms. Michelle Walker, a U.S. citizen, has Canadian employment income of $22,000 and U.S. employment income of $40,000 Canadian. She lives in Seattle, Washington and is a resident of the United States for the entire year. Ms. Walker does not believe that she is subject to taxation in Canada. Is she correct? Explain your conclusion.

Exam Exercise One - 2 (Net Income For Tax Purposes)

Ms. Sonia Nexus is a computer specialist with net employment income of $66,000. During the current year she has:

- a taxable capital gain on the sale of land of $13,500,
- an allowable capital loss on the sale of shares of $24,000,
- interest income of $10,250,
- net rental losses of $6,750, and
- a loss from her unincorporated business of $28,000.

In addition, she makes spousal support payments of $14,000 and makes a deductible contribution to her RRSP of $3,000 (these are Subdivision e deductions). Determine her minimum Net Income For Tax Purposes for the current year and indicate the amount and type of any loss carry overs that are available at the end of the year. Show all of your calculations.

Exam Exercise One - 3 (Tax Planning)

Mr. Jack Bronson makes a $5,000 contribution to his Registered Retirement Savings Plan. What type of tax planning is involved in this transaction? Explain your conclusion.

Exam Exercise One - 4 (Tax Planning)

Mr. John Lenonovitz is an unemployed poet. As Mr. Lenonovitz has no known sources of income, his wife Natasha has decided to make contributions to an RRSP in his name, rather than making contributions to her own plan. What type of tax planning is involved in this decision? Explain your conclusion.

Exam Exercise One - 5 (Tax Planning)

Mrs. Janice Theil gives $50,000 in Canada Savings Bonds to her 27 year old, unemployed daughter. What type of tax planning is involved in this transaction? Explain your conclusion.

TIF PROBLEM ONE - 5
Introduction - Key Term Matching

The following three key terms are listed at the end of Chapter 1, "Introduction To Federal Taxation In Canada":

A. Fiscal Period

B. Taxable Canadian Property

C. Person

The following list contains 6 potential definitions for the preceding key terms.
NOTE There is only **ONE** correct definition for each key term.

1. An individual human being.

2. A taxation year that is longer or shorter than 52 weeks.

3. A term used in the *Income Tax Act* to refer to taxable entities. For income tax purposes, the three taxable entities are individuals, corporations, and trusts.

4. Any property that is physically situated in Canada.

5. A taxation year that does not exceed 53 weeks.

6. A group of assets that are listed under the definition of Taxable Canadian Property in ITA 248(1). These assets are distinguished by the fact that gains on their disposition are taxable without regard to the residence of the selling taxpayer.

Required: For each of the three key terms listed, indicate the number of the item that provides the **BEST** definition of that term. As only one definition is completely correct, please indicate only one number for each key term. No marks will be awarded if you indicate more than one number for any key term.

TIF PROBLEM ONE - 6
Net Income For Tax Purposes

The following two Cases make different assumptions with respect to the amounts of income and deductions of Ms. Leslie Burke for the current taxation year:

Case A Ms. Burke had employment income of $17,000 and net rental income of $8,500. Her unincorporated business lost $12,300 during this period. As the result of dispositions of capital property, she had taxable capital gains of $17,400 and allowable capital losses of $19,200. Her Subdivision e deductions for the year totalled $6,300. Fortunately for Ms. Burke, she won $1,000,000 in a lottery on March 3.

Case B Ms. Burke had employment income of $42,100, interest income of $8,200, and a loss from her unincorporated business of $51,000. As the result of dispositions of capital property, she had taxable capital gains of $22,400 and allowable capital losses of $19,200. Her Subdivision e deductions for the year amounted to $4,200.

Required: For both Cases, calculate Ms. Burke's Net Income For Tax Purposes (Division B income). Indicate the amount and type of any loss carry overs that would be available at the end of the current year.

TIF PROBLEM ONE - 7
Net Income For Tax Purposes

The following two Cases make different assumptions with respect to the amounts of income and deductions of Mr. Morris Dorne for the current taxation year:

Case A Mr. Dorne had employment income of $50,000 and interest income of $12,000. His unincorporated business lost $23,000 during this period. As the result of dispositions of capital property, he had taxable capital gains of $95,000 and allowable capital losses of $73,000. His Subdivision e deductions for the year totalled $8,000. He also experienced a loss of $5,000 on a rental property that he has owned for several years.

Case B Mr. Dorne had employment income of $45,000, net rental income of $23,000, and a loss from his unincorporated business of $51,000. As the result of dispositions of capital property, he had taxable capital gains of $25,000 and allowable capital losses of $46,000. His Subdivision e deductions for the year amounted to $10,500. Fortunately for Mr. Dorne, he won $560,000 in a lottery on February 24.

Required: For both Cases, calculate Mr. Dorne's Net Income For Tax Purposes (Division B income). Indicate the amount and type of any loss carry overs that would be available at the end of the current year.

Chapter Two Test Item File Problems

TIF PROBLEM TWO - 1
Procedures And Administration - Essay Questions

1. An individual can request that an employer reduce the amounts withheld for income taxes. What conditions must be met for this request to be granted? Provide an example of a situation where this request would be granted.

2. Briefly describe the due dates applicable to the remittance of source deductions by the various classes of employers.

3. Under what circumstances must an individual make income tax instalment payments during the current year?

4. If an individual is required to make quarterly instalment payments on their income taxes, how is the required amount of the instalments determined?

5. On April 30 of the current year, her filing due date, Nicole Houde finds that she has a significant net tax owing. She will not be able to pay this until the beginning of July. She doesn't want to file her return until she has the funds available to pay the balance. What advice would you give Ms. Houde in this regard?

6. Under what circumstances must a corporation make income tax instalment payments during its current taxation year?

7. If a corporation that is not a small CCPC is required to make instalment payments on their income taxes, how are the required amounts determined?

8. If a corporation that is a small CCPC is required to make quarterly instalment payments on their income taxes, how are the required amounts determined?

9. Cases can be heard by the Tax Court of Canada using either the general or the informal procedures. How do these two procedures differ?

10. One of your clients has received his instalment notice and has asked your advice as to whether he should make the payments. Provide the requested advice.

TIF PROBLEM TWO - 2
Procedures And Administration - True Or False

1. If an individual believes that the amount of income taxes withheld by his employer is greater than the amount that he will have to pay in a particular year, he can make a request to the CRA to have his source deductions reduced.

   True or False?

2. Because the taxation year of an individual must be based on the calendar year, all individuals will have the same filing due date.

   True or False?

3. If an individual dies after October in a particular taxation year, his legal representatives must file his tax return by the later of his normal filing due date and six months after the date of his death.

   True or False?

4. If quarterly instalments must be paid by an individual, they can be calculated as one-quarter of the net tax owing for the preceding year.

   True or False?

5. If an individual is required to make income tax instalment payments, one acceptable pattern of payments is to base each payment on one-quarter of the estimated Tax Payable for the current taxation year.

   True or False?

6. The interest rate applicable on refunds to individuals is 4 percentage points less than the interest rate applicable on amounts owing to the CRA.

   True or False?

7. The penalty for an individual making insufficient instalment payments is 5 percent of the total unpaid tax at the filing date, plus 1 percent per month.

   True or False?

8. Without regard to whether an individual's filing due date is April 30 or June 15, any balance of tax owing must be paid by April 30.

   True or False?

9. All corporations must file their tax returns no later than six months after the end of their fiscal year, and pay any balance of tax owing no later than three months after the end of their fiscal year.

   True or False?

10. The notice of objection for a corporation must be filed within 90 days from the date of mailing of the notice of assessment.

    True or False?

TIF PROBLEM TWO - 3
Procedures And Administration - Multiple Choice

Individual Filing Requirements

1. With respect to the filing of an individual income tax return, which of the following statements is correct?

   A. An individual is required to file an income tax return if their only source of income is business income, even if no tax is payable.
   B. An individual is required to file an income tax return if they have reached the age of 18 by the end of the year.
   C. If an individual has disposed of a capital property during the year, they are required to file an income tax return, even if no tax is payable.
   D. An individual is not required to file an income tax return if no tax is payable for the year.

2. For the 2010 taxation year, John Bookman had a taxable capital gain of $45,000 and a net business loss of $45,000, resulting in a Taxable Income of nil. Which of the following statements is correct?

   A. John is not required to file a tax return for 2010.
   B. John must file a tax return on or before June 15, 2011.
   C. John must file a tax return on or before December 31, 2011.
   D. John must file a tax return on or before April 30, 2011.

3. John Barron is self-employed and plans to file his 2010 tax return on June 15, 2011. His balance-due day is:

   A. April 30, 2010.
   B. April 30, 2011.
   C. June 15, 2011.
   D. June 15, 2010.

4. Ms. Loren dies on February 1, 2011. All of her income is from employment activities and she does not have a spouse or common-law partner. What is the latest date for filing her 2010 income tax return?

   A. April 30, 2011.
   B. June 15, 2011.
   C. August 1, 2011.
   D. June 30, 2011.

5. Mr. Finlay, a retired individual whose only source of income was pension receipts, dies on August 15, 2010. By what date must Mr. Finlay's final tax return be filed?

   A. April 30, 2011.
   B. February 28, 2011.
   C. February 15, 2011.
   D. December 31, 2010.
   E. None of the above.

6. Ms. Deveco's 2010 income tax return is due on April 30, 2011 While she is too busy to file her tax return on that date, she remits a check to the government for $10,000, her estimated amount of net tax owing on that date. She has never filed a late return before. She prepares and files her tax return on May 31, 2011. At this time, the return shows that her actual net tax owing was $9,800. Assuming that the interest rate applicable to late payment of taxes is one-half percent per month without daily compounding, how much will she owe in penalties and interest on the late filing?

   A. $ 49.
   B. $490.
   C. $588.
   D. $637.
   E. Nil.

Individual Instalments

7. Ms. Marston has net tax owing for 2008 of $4,500, net tax owing for 2009 of $8,000, and net tax owing for 2010 of $7,500. If she wishes to pay the minimum total amount of instalments for the 2010 taxation year, her first payment on March 15 will be for what amount?

   A. Nil.
   B. $1,125.
   C. $1,875.
   D. $2,000.

8. Jason Marks has to pay his tax by instalments as a result of his significant investment income. His net tax owing in 2008 was $13,600. In 2009, it was $15,000. His estimate for 2010 is $17,000. If he decides to pay his 2010 tax instalments according to the prior year option, how much should he pay on September 15, 2010?

   A. $3,400.
   B. $3,750.
   C. $4,250.
   D. $6,500.

9. All of the following people will have to pay tax by instalments this year, except:

   A. Jane White, who received a one-time bonus of $60,000 last year and, because her employer had not deducted enough tax, found herself with net tax owing of $8,200.
   B. Karen Phillips, who has started to earn investment income, which resulted in net tax owing of $3,000 last year. Her investment income is expected to be even greater this year.
   C. Blake Fortin, who established a sole proprietorship two years ago. Blake had a very successful first year and, as result, he had net tax owing that year of $85,000. Business dropped in his second year, resulting in net tax owing of only $1,500. This year, business has picked up again and he expects to have net tax owing of $53,000.
   D. Terri Jones, who has had net taxable capital gains on real estate in excess of $40,000 in each of the last two years, and who expects to have similar gains this year.

10. Larry Short has self-employment income of $62,000 in 2010. Prior to this year, he was employed full-time and his employer's withholdings more than covered his tax liability for the year. Larry estimates that, based on his self-employment income, his net tax owing for 2010 will be $8,000. Which of the following statements is true?

   A. Larry must file his return for 2010 by April 30, 2011.
   B. Larry should pay instalments in 2010.
   C. Larry must pay his income tax for 2010 by June 15, 2011.
   D. If Larry has as much income in 2011 as he had in 2010, he will have to pay instalments during 2011.

Corporate Filing Requirements

11. For corporations, the filing deadline for tax returns is:

    A. April 30.
    B. the fiscal year end.
    C. three months after the fiscal year end.
    D. three months after the fiscal year end if the small business deduction is claimed, otherwise two months after the fiscal year end.
    E. six months after the fiscal year end.

12. PS Swim Inc. has a year end of November 30. For its 2010 taxation year, its income tax return is due on:

    A. January 31, 2011.
    B. February 28, 2011.
    C. April 30, 2011.
    D. May 31, 2011.
    E. None of the above.

13. For its 2010 taxation year, its first year of operation, PS Swim Inc. filed its return three months late. The unpaid tax at the due date for the return was $2,500. This amount was not paid until the return was filed. What would its penalty be?

    A. Nil.
    B. $75.
    C. $125.
    D. $200.
    E. $500.

Corporate Instalments

14. PP Ltd., a client of your firm, has a November 30th year end and has requested you to advise them on what its monthly instalments for the 2010 tax year will be. Its taxes payable for its November 30, 2008 and November 30, 2009 years were $13,800 and $13,200, respectively. Its estimated taxes payable for the November 30, 2010 year are $14,400. PP Ltd. wants to pay the lowest amount possible, without incurring interest penalties. What would its instalments be?

    A. Twelve payments at $1,200 per month.
    B. Twelve payments at $1,100 per month.
    C. Twelve payments at $1,150 per month.
    D. Two monthly payments at $1,200 each, followed by ten monthly payments at $1,140 each.
    E. None of the above.

15. A Canadian public corporation had federal taxes payable in 2008 and 2009 exceeding $3,000. One correct option it has with respect to its 2010 instalments is to pay:

    A. equal instalments, on a quarterly basis, based on its 2009 federal taxes payable.
    B. on a monthly basis, instalments equal to 1/12th of its estimated 2010 federal taxes payable.
    C. one lump-sum payment, within three months of its 2010 year end.
    D. on a monthly basis, instalments equal to 1/12th of its 2008 federal taxes payable.

16. If a Canadian public corporation is experiencing a year-to-year decrease in taxes payable, the most advantageous calculation of instalments that would be allowed is:

    A. monthly, based on the estimated tax for the current year.
    B. quarterly, based on the estimated tax for the current year.
    C. monthly, based on the estimated tax for the immediately preceding year.
    D. quarterly, based on the estimated tax for the immediately preceding year.
    E. monthly, based on the estimated tax for the second preceding year and the immediately preceding year.
    F. quarterly, based on the estimated tax for the second preceding year and the immediately preceding year.

Assessments And Appeals

17. Tom Arnold filed his 2010 tax return on March 1, 2011. The CRA mailed a notice of assessment to Tom dated May 15, 2011, and Tom received it on May 30, 2011. If Tom disagrees with the notice of assessment, he has until which one of the following dates to file a notice of objection?

    A. 90 days from March 1, 2011.
    B. 90 days from April 30, 2011.
    C. 90 days from May 15, 2011.
    D. 90 days from May 30, 2011.
    E. None of the above.

18. Minnie Belanger is retired. She mailed her 2010 tax return on March 5, 2011. She received a portion of the tax refund claimed and an assessment notice, dated April 19, 2011, which set out the difference between the amount claimed and the amount of the refund. As Minnie disagrees with the notice of assessment, she wishes to file a notice of objection. By which of the following dates must she file her notice of objection?

    A. March 5, 2012.
    B. April 19, 2012.
    C. April 30, 2012.
    D. July 18, 2011.
    E. June 15, 2012.

19. For a public corporation, which of the following statements is true with respect to filing a notice of objection?

    A. It must be filed no later than 180 days from the date the notice of assessment was mailed.
    B. It must be filed the later of 90 days after the date the notice of assessment was filed and one year from the filing date for the return under assessment.
    C. It must be filed the later of 180 days after the date the notice of assessment was filed and one year from the filing date for the return under assessment.
    D. It must be filed no later than 90 days after the notice of assessment was mailed.

TIF PROBLEM TWO - 4
Procedures And Administration - Exam Exercises

Exam Exercise Two - 1 (Individual Due Dates)

Mark Brown's 2010 Net Income includes business income. When is his 2010 tax return due? By what date must his 2010 tax liability be paid in order to avoid the assessment of interest on amounts due?

Exam Exercise Two - 2 (Deceased Taxpayer Due Date)

George Klause dies on March 1, 2011. All of his income during 2010 was earned through his unincorporated accounting practice. By what date must his representatives file his 2010 income tax return? Explain your answer.

Exam Exercise Two - 3 (Individual Instalments)

At the beginning of 2010, the following information relates to Sarah Elmsley:

Year	Net Tax Owing
2008	$1,800
2009	6,400
2010 (estimated)	3,600

Indicate whether Ms. Elmsley is required to make instalment payments during 2010. Explain your conclusion and, if your answer is positive, indicate the minimum instalments that will be required and when they are due.

Exam Exercise Two - 4 (Individual Instalments)

Horace Greesom filed his 2009 return on time. At the beginning of 2010, the following information relates to Mr. Greesom:

Year	Taxes Payable	Amounts Withheld
2008	$56,000	$45,000
2009	49,000	46,000
2010 (estimated)	65,000	45,000

What amounts will be shown on the Instalment Reminder notices for 2010 and when will the amounts be due? Should he pay those amounts? Explain your conclusion.

Exam Exercise Two - 5 (Penalties And Interest For Individuals)

Despite the fact that her net tax owing has been between $7,000 and $8,000 in the two previous years, and is expected to be a similar amount during 2010, Marsha Fields has made no instalment payments for 2010. While her normal filing date would be April 30, 2011, she does not file her 2010 return or pay the balance owing until August 24, 2011. What penalties and interest will be assessed for the 2010 taxation year?

Exam Exercise Two - 6 (Corporate Instalments - Regular And Small CCPC)

Lemar Ltd. has a December 31 year end. It is not a small CCPC. For 2008, its taxes payable were $71,500, while for 2009, the amount was $93,600. For 2010, its estimated taxes payable are $114,700. What would be the minimum instalment payments for the 2010 taxation year and when would they be due? How would your answer differ if Lemar Ltd. qualified as a small CCPC?

Exam Exercise Two - 7 (Corporate Instalments - Regular And Small CCPC)

Chemco Inc. has a December 31 year end and is not a small CCPC. For 2008, its taxes payable were $146,300, while for 2009, the amount was $94,650. For 2010, its estimated taxes payable are $52,300. What would be the minimum instalment payments for the 2010 taxation year and when would they be due? How would your answer differ if Chemco Inc. qualified as a small CCPC?

Exam Exercise Two - 8 (Corporate Due Dates)

The taxation year end for Grange Inc. is March 31, 2010. It is a Canadian controlled private corporation that claims the small business deduction and had Taxable Income for the year ending March 31, 2009 of $165,000. Indicate the date on which the corporate tax return must be filed, as well as the date on which any final payment of taxes is due.

Exam Exercise Two - 9 (Corporate Due Dates)

The taxation year end for Lawnco Inc. is January 31, 2010. Indicate the date on which the corporate tax return must be filed, as well as the date on which any final payment of taxes is due.

Exam Exercise Two - 10 (Notice of Objection)

Ms. Nancy Forth filed her 2010 tax return as was required on April 30, 2011. She receives an initial assessment notice during May, 2011. However, on July 12, 2012, she receives a reassessment indicating that she owes additional taxes, as well as interest on the unpaid amounts. The reassessment was mailed on July 2, 2012. What is the latest date for filing a notice of objection for this reassessment? Explain your answer.

TIF PROBLEM TWO - 5
Procedures And Administration - Key Term Matching

The following five key terms were listed at the end of Chapter 14, "Procedures And Administration".

A. NETFILE

B. Net Tax Owing

C. Source Deductions

D. Tax Evasion

E. Instalment Threshold

The following list contains 10 potential definitions for the preceding key terms.
NOTE There is only **ONE** correct definition for each key term.

1. An electronic system for filing individual tax returns. While the system can be used by anyone, the return must be transmitted by a registered EFILE service provider using approved software.

2. An amount, currently $3,000, of net tax owing that is used to determine the need for individuals to make instalment payments (i.e., individuals are required to make instalment payments if their net tax owing in the current year and one of the two preceding years exceeds the instalment threshold of $3,000).

3. This typically involves deliberately ignoring a specific part of the law or willfully refusing to comply with legislated reporting requirements. Tax evasion, unlike tax avoidance, has criminal consequences.

4. An electronic filing system that requires the use of an approved software program. The individual uses the Internet to transmit their return directly to the CRA, without the use of a third party.

5. A term, applicable to individual taxpayers, used to describe the sum of federal and provincial taxes owing for the year.

6. Amounts that are withheld by an employer from the income of employees. The amounts withheld are based on the expected income tax liability of the employee for the current year.

7. A term, applicable to individual taxpayers, used to describe the sum of federal and provincial taxes owing for the year, less amounts withheld for the year.

8. An amount, currently $3,000, of total tax owing that is used to determine the need for individuals to make instalment payments (i.e., individuals are required to make instalment payments if their total tax owing in the current year and one of the two preceding years exceeds the instalment threshold of $3,000).

9. Amounts that are withheld by an employer from the income of employees. The withholdings for income taxes, Canada Pension Plan contributions, and Employment Insurance premiums must be remitted to the government.

10. The undertaking of transactions or arrangements with a view to avoiding or minimizing the payment of taxes. As the term is generally used, it refers to legitimate procedures that could also be described as tax planning.

Required: For each of the five key terms listed, indicate the number of the item that provides the **BEST** definition of that term. As only one definition is completely correct, please indicate only one number for each key term. No marks will be awarded if you indicate more than one number for any key term.

TIF PROBLEM TWO - 6
Instalment Payments For Individuals

The following information relates to Ms. Shannon Birch for tax years ending December 31:

	Federal And Provincial Income Taxes Payable	Income Taxes Withheld By Employer
2008	$23,000	$21,500
2009	$27,000	$15,000
2010 (Estimated)	$21,200	$18,000

Required:

A. Indicate whether Ms. Birch has an obligation to make instalment payments during the 2010 taxation year. Explain your conclusion.

B. If Ms. Birch is required to make instalment payments, indicate the amounts that should be paid and the dates on which the amounts are payable. Your answer should include the alternatives that are available to Ms. Birch, as well as an indication as to which alternative is preferable.

C. Ms. Birch would like your advice as to whether or not she should make the recommended instalment payments. Explain your conclusion.

TIF PROBLEM TWO - 7
Instalment Payments For Individuals And Corporations

For the year ending December 31, 2008, the taxpayer's combined federal and provincial taxes payable amounted to $93,000, while for the year ending December 31, 2009, the amount payable was $108,000. It is estimated that federal and provincial taxes payable for the year ending December 31, 2010 will be $82,500.

Case A
The taxpayer is an individual whose employer withholds combined federal and provincial taxes of $86,700 in 2008, $109,500 in 2009, and $79,200 in 2010.

Case B
The taxpayer is an individual whose employer withholds combined federal and provincial taxes of $91,500 in 2008, $98,700 in 2009, and $78,300 in 2010.

Case C
The taxpayer is a small CCPC with a December 31 year end.

Case D
The taxpayer is a corporation with a December 31 year end. It is not a small CCPC. Assume that its combined federal and provincial taxes payable for the year ending December 31, 2008 are estimated to be $78,100, instead of the $93,000 given in the problem.

Required: For each of the preceding independent Cases, provide the following information:

1. Indicate whether instalments are required during the year ending December 31, 2010.
2. Calculate the amount of instalments that would be required under each of the acceptable methods available.
3. Indicate which of the acceptable methods would best serve to minimize instalment payments during 2010. If instalments must be paid, indicate the date on which they are due.

Chapter Three Test Item File Problems

TIF PROBLEM THREE - 1
Employment Income - Essay Questions

1. Explain how a bonus arrangement can be used to defer the taxes paid by an employee.

2. List and briefly describe the major factors that will be considered in determining whether an individual is working as an employee or as an independent contractor.

3. The tax consequences of being classified as an employee rather than as an independent contractor can be significant. As a result, it is not uncommon to find controversy and, in some cases, litigation resulting from the need to make this distinction. Explain the importance, from the point of view of an employee, of the distinction between being classified as an employee versus being classified as a self-employed independent contractor.

4. Tax planning considerations are very significant in deciding the kinds of benefits that will be provided to employees. Explain why salary payments are considered the basic benchmark with which other types of employee compensation will be compared.

5. List two types of employee benefits that involve tax deferral and two types of benefits that involve tax avoidance.

6. London Wholesalers employs over 50 full time salespeople, all of whom are provided with a company car. While the cars are used primarily for business purposes, all of the sales staff drive them at least 20,000 kilometers per year for personal reasons. As controller of the Company you are aware that there is tax legislation in effect which can create substantial taxable benefits that could accrue to these salespeople because they have the use of a company car.

   Required: Indicate some of the ways in which the Company and the sales staff might legitimately reduce the amount of the taxable benefit associated with having the use of a company car.

7. An employee may be paid a monthly amount for using his own automobile in employment related activities. Alternatively, he may be paid a reasonable amount based on the number of kilometers driven. From the point of view of both the employer and the employee, explain the tax treatment that will be given to these two alternatives.

8. Briefly describe the calculation of the taxable benefits that may be assessed on loans to employees that are not considered to be housing loans related to relocations.

9. For tax purposes, an employee who receives an option on his employer's stock that is not in-the-money will not have an employment income inclusion at the time the option is received. Do you agree with this treatment? Explain your conclusion.

10. Under what circumstances is an individual entitled to a deduction equal to one-half of the employment income inclusion resulting from exercising or selling stock options?

    (continued)

TIF Problem Three - 1

Employment Income - Essay Questions

11. The number of deductions that can be made in computing employment income is fairly limited. Further, certain types of expenses must meet specified conditions in order to be eligible for deduction.

    Required:

    A. Indicate the conditions that must be met in order for a salesperson to deduct expenses in computing employment income.

    B. Indicate the conditions that must be met in order for travel costs to be deducted in computing employment income.

TIF PROBLEM THREE - 2
Employment Income - True Or False

1. Employment income is the salary, wages, and other remuneration, including gratuities, that are receivable by an individual during the year.

True or False?

2. If properly constructed, bonus arrangements can result in tax deferral for employees.

True or False?

3. One of the advantages of being an independent contractor rather than an employee is that you do not have to make CPP contributions.

True or False?

4. Employers generally prefer contracting out as it avoids the cost of CPP and EI contributions.

True or False?

5. Payments by employers of premiums on life insurance for employees are not taxable benefits.

True or False?

6. When an employee pays all of the premiums for disability insurance coverage, the payments are not deductible and the benefits received are tax free.

True or False?

7. Payments by employers to private health care plans are not taxable benefits and any benefits received under such plans are tax free.

True or False?

Questions 8, 9, and 10 relate to the following facts:

An employee is given a $10,000 interest free loan from her employer on January 1 to buy a car to be used for business trips. Due to a serious illness, she used the car for only nine months of the year. Assume that the prescribed rate is 2 percent for the entire year.

8. Her taxable benefit from the loan is $200 for the year.

True or False?

9. She pays her employer $1,000 on September 30 to decrease the loan. Her taxable benefit from the loan is $180 for the year.

True or False?

10. In calculating her minimum standby charge, the imputed interest from the loan is part of her operating costs.

True or False?

TIF PROBLEM THREE - 3
Employment Income - Multiple Choice

Employee vs. Self-Employed

1. Veronica mows lawns during the summer. In 2010 she was paid directly by homeowners for her work, in some case on the basis of the completed job, in other cases at an hourly rate. Her friend Jonathon does the same work. However, he is paid at an hourly rate by a lawn maintenance company.

    A. Veronica earns business income and Jonathon earns employment income. Veronica will be able to deduct more expenses than Jonathon.
    B. Veronica and Jonathon both earn employment income.
    C. Veronica earns business income and Jonathon earns employment income. Their deductible expenses will be the same.
    D. Veronica and Jonathon both earn business income.

Employee Benefits

2. Indicate which of the following benefits provided by an employer is not considered part of employment income.

    A. Reimbursement of moving expenses.
    B. Travel expenses of the employee's spouse.
    C. Payments resulting from wage loss replacement plans.
    D. Premiums paid by an employer on life insurance policies.
    E. Individual premiums under provincial hospitalization plans.

3. Indicate which of the following benefits provided by an employer is considered part of employment income.

    A. Subsidized meals provided in employer facilities.
    B. Low rent housing.
    C. Transportation to the job in employer vehicles.
    D. Premiums under private health services plans.
    E. Uniforms and special clothing.

4. Which of the following is not a taxable benefit?

    A. A cash Christmas gift to an employee from the employer. All the employees received a cash bonus of $150.
    B. Payment of the tuition for an employee completing a general interest degree on a part-time basis.
    C. A 20 percent discount on the employer's merchandise, available to all employees. The employer's mark-up is 50 percent.
    D. Low rent housing provided by the employer.

5. Which one of the following benefits received from an employer may not result in a taxable benefit to the employee?

    A. A reasonable allowance of 45 cents per kilometer for driving on employer business.
    B. An interest free loan used to acquire shares of the employer.
    C. Employer paid life insurance premiums for $20,000 of employee coverage.
    D. Use of the employer's vehicle which is used 95% for employment purposes.

6. In which one of the following lists are **all** items relevant when computing net employment income?

   A. Employee contributions to a registered pension plan; signing bonus on accepting employment; availability of an employer-owned automobile.
   B. Monthly automobile allowance; group disability insurance paid by the employer; promotional cost incurred in selling the employer's products.
   C. Subsidized meals in employer's facilities; life insurance paid by the employer; legal fees incurred to collect unpaid salary.
   D. Tips and gratuities; dental insurance paid by the employer; exercise of options to purchase shares of the employer.

7. An employee has been offered a choice of an increase in salary of $100,000 or a combination of salary and other benefits with a cost to the employer of $100,000. Assuming that the employee would buy the listed benefits with his own funds if they were not provided in the benefits package, which of the following packages would be the most advantageous from a tax perspective?

   A. A dental plan plus a leased automobile that would be used only for personal travel by the employee.
   B. Life insurance plus a leased automobile that would be used only for personal travel by the employee.
   C. Salary plus life insurance.
   D. Salary only.

Automobile Benefits

Questions 8 Through 11 Questions 8 through 11 are based on the following information:

The cost of the car is $20,000 including GST and PST. If the car is leased, the monthly lease payment is $500 including GST and PST. The car is driven for a total of 26,000 km during 2010 and its operating costs for the year are $4,000. For each of the **independent** questions 8 through 11, choose one of the following answers. Each answer can be used more than once.

A. $1,150.	F. $2,455.
B. $1,650.	G. $3,240.
C. $1,800.	H. $3,300.
D. $1,964.	I. $3,959.
E. $2,250.	J. $4,752.

8. Assume the car is purchased. It is available to an employee for the whole year. He drives it for personal purposes for a total of 9,000 km. The minimum taxable benefit is:

9. Assume the car is leased. It is available to an employee for 11 months of the year. He drives it for personal purposes for a total of 6,000 km. The minimum taxable benefit is:

10. Assume the car is purchased. It is available to an employee for 10 months of the year. He drives it for personal purposes for a total of 11,000 km. The minimum taxable benefit is:

11. Assume the car is leased. It is available to an employee for 11 months of the year. He drives it for personal purposes for a total of 7,500 km and reimburses the employer $1,100 ($100 per month) for the use of the car. The minimum taxable benefit is:

12. Mr. Brown's employer provides him with an automobile for his personal use, and pays all operating costs for that vehicle. The vehicle, used by Mr. Brown throughout 2010, cost his employer $31,500, including GST of $1,500 (no provincial sales tax was charged on the vehicle purchase). Mr. Brown drove the vehicle 45,000 km during the year, of which 9,000 km were for personal purposes. His employer paid $7,750 in operating costs for the year. Mr. Brown paid nothing to his employer for the use of the vehicle. Which one of the following amounts represents the **minimum** taxable benefit that Mr. Brown must include in his employment income for the use of this vehicle in 2010?

    A. $2,268.
    B. $4,859.
    C. $5,102.
    D. $5,561.

13. The following facts relate to an employer provided automobile.

Original cost of automobile, including HST of $4,602	$40,000
Replacement value of car at time of providing it to employee	$30,000
Capital cost allowance claimed by employer	$ 3,000
Personal use kilometers driven by employee during the year	2,000 km
Total kilometers driven by employee during the year	30,000 km
Number of months automobile was made available to employee	12

    Which one of the following amounts represents the employee's minimum standby charge in 2010?

    A. $720.
    B. $960.
    C. $640.
    D. $9,600.

Allowances

14. With respect to the determination of net employment income, which of the following statements is correct?

    A. All allowances must be included in income.
    B. All reimbursements are taxable.
    C. Some allowances are taxable, but reimbursements are never taxable.
    D. All allowances must be included in income, but reimbursements are never taxable.

Loans To Employees

15. T. Adams commenced employment at Moana Sales Ltd. on February 1, 2010. He had lived in an apartment until May 2010, at which time he purchased a new house. Under the terms of his employment, he received a housing loan on May 1, 2010 of $80,000 at a rate of 2 percent. He pays the interest on the loan on a monthly basis. Assume the 2010 prescribed interest rates applicable to employee loans are as follows:

First quarter	5%
Second quarter	4%
Third quarter	3%
Fourth quarter	3%

    What is T. Adams' taxable benefit on the above loan for 2010?

    A. Nil.
    B. $267.40.
    C. $670.68.
    D. $1,073.97.
    E. $2,147.95.

Employee Stock Options

16. Ms. Joan Hanson is an employee of a Canadian controlled private corporation. During 2009, she receives options to purchase 500 shares of her employer's common stock at a price of $22 per share. At this time, the estimated per share value of the stock is $20.50. During 2010, she exercises all of these options. At this time, the estimated market value of the stock is $31.50 per share. On December 1, 2010, she sells the stock for $38.75 per share. The net effect of the 2010 transactions on her Taxable Income would be:

    A. An increase of $1,812.50.
    B. An increase of $2,375.00.
    C. An increase of $4,187.50.
    D. An increase of $4,750.00.
    E. An increase of $6,562.50.

17. An employee of a public Canadian corporation receives an option to purchase 1,000 of her employer's common shares at $20 per share in July, 2009. At this time, the fair market value of the stock is $19 per share. In March, 2010, when the fair market value is $26 per share, she exercises the option and immediately sells the shares. By what amount do these transactions increase her Taxable Income?

    A. $1,000 in 2009.
    B. $3,000 in 2010.
    C. $3,500 in 2010.
    D. $6,000 in 2010.

Questions 18 And 19 Questions 18 and 19 are based on the following information:

Scott Bicycle Manufacturing Ltd. (SBM) is a Canadian controlled private corporation. Brian Mills, one of SBM's employees, was granted stock options on October 11, 2006 for 10,000 shares at $3 per share. Brian exercised the stock options on September 30, 2007, when the market price was $6 per share. In June 2010, Brian purchased a new home and sold the shares for $7 each. The fair market value on October 11, 2006 was $4 per share.

18. What is the effect of these facts on Brian's Taxable Income?

    A. $15,000 in 2007.
    B. $15,000 in 2010.
    C. $30,000 in 2007.
    D. $20,000 in 2010.
    E. None of the above.

19. What is the adjusted cost base to Brian of the SBM shares at the time of sale in June, 2010?

    A. $30,000.
    B. $45,000.
    C. $60,000.
    D. $70,000.
    E. None of the above.

Questions 20 And 21 Questions 20 and 21 are based on the following information:

Mr. Morra commenced employment with Peoples Bank Ltd., a public corporation, on September 1, 2005. On June 30, 2008, he was granted options to purchase 500 shares of Peoples Bank Ltd. stock for $15 per share. The market value on June 30, 2008 was $16 per share.

Mr. Morra exercised his options on May 31, 2010, purchasing 500 shares for $15 per share when the market value was $17 per share. On September 1, 2011, Mr. Morra sold the shares for $24 each.

20. What is the effect of the above transactions on Mr. Morra's Taxable Income in 2010?

A. Nil.
B. An increase of $250.
C. An increase of $500.
D. An increase of $1,000.

21. What is the effect of the above transactions on Mr. Morra's Taxable Income in 2011?

A. Nil.
B. An increase of $1,750.
C. An increase of $2,750.
D. An increase of $3,500.

Employment Deductions

22. John secured employment as a commissioned salesman in July, 2010. In 2010, he received a base salary of $60,000, and $5,000 of commissions. A further $4,000 of commissions earned in December was paid to him in January, 2011. John worked away from the office negotiating sales contracts, and he is required to pay his own traveling expenses. His employer has signed a Form T2200 certifying that requirement, and certifying that no reimbursements are paid for any expenses John incurs to earn commissions. John incurred the following costs from July through December 2010:

Meals and entertainment for potential customers	$14,000
Driving costs (90% of driving was for employment purposes):	
Fuel	4,000
Insurance	750
Repairs	2,250
Leasing costs ($500 per month)	3,000

What is the maximum deduction John may claim for employment expenses in 2010?

A. $5,000.
B. $9,000.
C. $15,000.
D. $16,000.

23. Which of the following criteria is not necessary in order for a salesperson to deduct office costs?

A. Must pay own expenses.
B. Must carry on duties away from the employer's place of business.
C. Must not receive an expense allowance which has not been included in income.
D. Must receive all remuneration in commissions.

TIF PROBLEM THREE - 4
Employment Income - Exam Exercises

Exam Exercise Three - 1 (Bonus)
Connely Ltd. has an August 31 year end. On August 31, 2009, it declares a bonus of $250,000 payable to Ms. Sara Connely, the founder of the Company. The bonus is payable on April 1, 2010. Describe the tax consequences of this bonus to both Connely Ltd. and Ms. Sara Connely.

Exam Exercise Three - 2 (GST On Taxable Benefits)
Mr. John Lamarche, as the result of an outstanding sales achievement within his organization, is awarded two airline tickets to Bali. His employer pays a travel agent $5,275, plus $264 in GST for the tickets. What is the amount of Mr. Lamarche's taxable benefit?

Exam Exercise Three - 3 (Taxable Benefits - Purchased Automobile)
Ms. Robin Nestor is provided with an automobile that is owned by her employer. The employer purchased the car in 2010 for $54,000, plus $7,020 in HST. During 2010, she drives the car a total of 72,000 kilometers, of which 67,000 kilometers were employment related. The automobile was available to Ms. Nestor for 268 days during 2010. Calculate Ms. Nestor's minimum taxable benefit for the use of the automobile.

Exam Exercise Three - 4 (Taxable Benefits - Leased Automobile)
During 2010, Mr. Sam Warren is provided with an automobile that is leased by his employer. The monthly lease payment is $791 per month. This figure includes $35 in GST and $56 in PST. During the year, the car is available to Mr. Warren for a total of 310 days. During this period, he drives the car a total of 40,000 kilometers, 22,000 of which are employment related. Calculate Mr. Warren's minimum taxable benefit for the use of the automobile.

Exam Exercise Three - 5 (Deductible Automobile Costs)
Mr. Rudy Jackson is required by his employer to use his own automobile in the course of his employment. To compensate him, he is paid an annual allowance of $4,200. During 2010, he drove his automobile a total of 26,720 kilometers, of which 8,150 were employment related. His total automobile costs for the year, including lease costs, are $8,623. What amounts will Mr. Jackson include and deduct from his 2010 employment income related to the use of his automobile?

Exam Exercise Three - 6 (Disability Insurance Benefits)
Ms. Jessica Tremblay is a member of a group disability plan sponsored by her employer. During 2010, her employer's share of the annual premium was $2,175. Beginning in 2009, Ms. Tremblay was required to contribute $324 per year to this plan. The 2009 and 2010 contributions were withheld from her wages by her employer. During 2010, Ms. Tremblay was hospitalized for a period of six weeks and received $6,940 in benefits under the plan. What amount will Ms. Tremblay include in her 2010 employment income?

Exam Exercise Three - 7 (Employee Housing Loan Benefits)

On January 1, 2010, Mr. Packard receives a $135,000 loan from his employer to assist him in purchasing a home. The loan requires annual interest at a rate of 3.1 percent, which he pays on December 31, 2010. Assume that the relevant prescribed rate is 5 percent during the first quarter of 2010, 6 percent during the second quarter, and 4 percent during the remainder of the year. What is the amount of Mr. Packard's taxable benefit on this loan for the year?

Exam Exercise Three - 8 (Tax Planning - Loan Benefits)

In 2010, a senior executive asks her employer for a $240,000 interest free housing loan that does not qualify as a home relocation loan. At this time, the employer has investment opportunities involving a rate of return of 8.2 percent before taxes. Assume the relevant prescribed rate for the period is 3 percent, while the market rate for home mortgages is 5 percent. The employee is subject to a marginal tax rate of 44 percent, while the employer pays corporate taxes at a marginal rate of 33.7 percent. Should the employer grant the loan or, alternatively, provide sufficient salary to carry an equivalent loan from a commercial lender? Explain your conclusion.

Exam Exercise Three - 9 (Stock Options - Public Company)

Ms. Mary Mason is employed by a large public company. In 2008, she was granted options to acquire 1,000 shares of her employer's common stock at a price of $23 per share. At the time the options were granted, the shares were trading at $20 per share. In May, 2010, when the shares are trading at $45 per share, she exercises her options and acquires 1,000 shares. What is the effect of the exercise of the options on Ms. Mason's 2010 net employment income?

Exam Exercise Three - 10 (Stock Options - CCPC)

How would your answer to Exam Exercise Three - 9 differ if Ms. Mason's employer was a Canadian controlled private corporation?

Exam Exercise Three - 11 (Stock Options - Public Company)

Several years ago, Mr. Kerry Johnson's employer gave him options to purchase 1,000 shares of the employer's stock at a price of $13.25 per share. At that time, the shares were trading at $13.25 per share. The employer is a publicly traded company. During June, 2010, Mr. Johnson exercises the options. At this time, the shares are trading at $18.50 per share. Prior to the end of the year, Mr. Johnson sells the shares for $19.75 per share. Determine the effect of these transactions on Mr. Johnson's Net Income For Tax Purposes and Taxable Income.

Exam Exercise Three - 12 (Stock Options - Public Company)

Mr. John Savage has been employed for several years by a Canadian public company. In 2008, Mr. Savage was granted options to acquire 4,000 shares of his employer's stock for $54 per share. At this time, the shares have a fair market value of $50 per share. On July 15, 2010, Mr. Savage exercises all of these options. At this time, the fair market value of the shares is $82 per share. In February 2011, he sells all of the shares for $97 per share. Calculate the tax consequences of the transactions that took place during 2010 and 2011 on Mr. Savage's Net Income For Tax Purposes and Taxable Income.

Exam Exercise Three - 13 (Stock Options - Private Company)

Note this is the same as Exam Exercise Three-12 except that the employer is a CCPC.

Mr. John Savage has been employed for several years by a Canadian controlled private corporation. In 2008, Mr. Savage was granted options to acquire 4,000 shares of his employer's stock for $54 per share. At this time, the shares have a fair market value of $50 per share. On July 15, 2010, Mr. Savage exercises all of these options. At this time, the fair market value of the shares is $82 per share. In February 2011, he sells all of the shares for $97 per share. Calculate the tax consequences of the transactions that took place during 2010 and 2011 on Mr. Savage's Net Income For Tax Purposes and Taxable Income.

Exam Exercise Three - 14 (Commission Salesperson Expenses)

Mrs. Joan Conway is a commission salesperson. During the current year, her gross salary was $46,700. In addition, she earned $9,200 in commissions. Her employment related costs during the year were advertising costs of $6,150, client entertainment of $8,850, and travel costs of $9,325. She is required to pay her own expenses and does not receive any allowance from her employer. What is Mrs. Conway's maximum expense deduction for the current year? Show your calculations.

Exam Exercise Three - 15 (Employment Income Expenses)

Doug Evans works for a company that sells video equipment. His records for the current year contain the following information:

Salary Received	$61,250
Commissions Received	6,250
Total Employment Inclusions	$67,500

Advertising And Promotion	$ 1,250
Traveling Expenses	7,500
Capital Cost Allowance On Van*	1,875
Interest On Van Loan*	625
Total Employment Deductions	$11,250

*The van is used exclusively for employment related activities.

Mr. Evans meets the conditions for deducting employment income expenses. Given the preceding information, determine Mr. Evans' minimum net employment income for the current year. Explain your conclusions.

TIF PROBLEM THREE - 5
Employment Income - Key Term Matching

The following five key terms are listed at the end of Chapter 3, “Employment Income”.

A. Allowance

B. Taxable Benefit

C. Self-Employed Individual

D. Operating Cost Benefit

E. Stock Option

The following list contains 10 potential definitions for the preceding key terms.
NOTE There is only **ONE** correct definition for each key term.

1. An allowance provided by an employer to an employee that must be included in the employee’s Employment Income. The amount is included on the employee’s T4.

2. An amount of money, or the value of goods or services, that an employer pays or provides in addition to salary.

3. A contractual arrangement which gives the holder the right to require the issuing corporation to redeem the shares that he is holding.

4. Non-cash benefits provided to employees by an employer (e.g., subsidized meals in an employer’s facilities).

5. A benefit, based on a pro rata share of automobile operating costs, assessed to an employee whose employer pays these costs for an automobile provided to the employee.

6. An individual who is employed by a corporation in which he is a specified shareholder.

7. A contractual arrangement which gives the holder the right to purchase a specified number of shares for a specified period of time at a specified acquisition price.

8. An amount paid by an employer to an employee to provide for certain types of costs incurred by the employee, usually travel costs or automobile costs.

9. A taxable benefit assessed to employees whose employers pay the operating costs of an automobile provided to the employee. It is designed to reflect, on a notional basis, the value of these operating costs.

10. An individual who has a business relationship with a taxpayer. Whether or not an individual is working as an employee or a self-employed individual is dependent on factors such as control, ownership of tools, chance of profit or risk of loss, and the ability to subcontract or hire an assistant.

Required: For each of the five key terms listed, indicate the number of the item that provides the **BEST** definition of that term. As only one definition is completely correct, please indicate only one number for each key term. No marks will be awarded if you indicate more than one number for any key term.

TIF PROBLEM THREE - 6
Employee Stock Options

Ms. Merian Bytech, is an employee of Merlin Industries Ltd. During 2008, Ms. Bytech was granted options to acquire 200,000 of her employer's shares at a price of $15 per share. All of the options are vested at the time they are granted.

On August 1, 2009, all of the options are exercised. On this date, the Merlin Industries shares have a fair market value of $22 per share.

On November 1, 2010, Ms. Bytech sells all of her Merlin Industries shares at $28 per share.

Required: Indicate the tax effect on Ms. Bytech with respect to the granting of the options, their exercise, and the sale of the shares under each of the following independent assumptions. Your answer should include the effect on both Net Income For Tax Purposes and Taxable Income. Ignore the election to defer employment income resulting from the exercise of stock options that is available in 2009.

A. Merlin Industries Ltd. is a Canadian controlled private corporation. At the time the options were granted, the Company's shares had a fair market value of $14 per share.

B. Merlin Industries Ltd. is a Canadian controlled private corporation. At the time the options were granted, the Company's shares had a fair market value of $18 per share.

C. Merlin Industries Ltd. is a Canadian public company. At the time the options were granted, the shares were trading at $15 per share.

D. Merlin Industries Ltd. is a Canadian public company. At the time the options were granted, the shares were trading at $18 per share.

TIF PROBLEM THREE - 7
Employment Income

Note To Instructor This problem is extended in TIF Problem Four - 7.

Mr. Samuel Kern is an administrator for a publicly traded Canadian manufacturing company. His gross salary for the year ending December 31, 2010 is $67,600. For the 2010 taxation year, Mr. Kern's employer withheld the following amounts from his income:

Federal Income Tax	$11,200
Employment Insurance Premiums	747
Canada Pension Plan Contributions	2,163
Registered Pension Plan Contributions	1,800
Contributions To Group Disability Plan	175

Mr. Kern's employer made a matching contribution of $1,800 to his registered pension plan and a $175 matching contribution for the group disability insurance.

Other Information:

1. During 2010, Mr. Kern is provided with an automobile that has been leased by his employer. The lease payments are $815 per month, an amount which includes all taxes and an $89 monthly payment for insurance. The total operating costs of the car were $4,600 for the year and they were paid by the employer. The car is available to him for nine months of the year and he drives it a total of 32,000 kilometers. Of this total, 29,000 kilometers were for travel required in pursuing the business of his employer and the remainder was for personal use. He reimbursed his employer $50 per month of use for his personal use of the automobile.

2. During 2010, Mr. Kern was hospitalized for a period of three weeks. The disability plan provided him with benefits of $1,650 during this period. Mr. Kern began making contributions to this plan in 2009 at the rate of $175 per year.

3. Mr. Kern was required to pay 2010 dues to his professional association in the amount of $1,233.

4. In 2007, Mr. Kern was given options to buy 200 shares of his employer's stock at a price of $75 per share. At the time the options were issued, the shares were trading at $70 per share. On June 1, 2010 Mr. Kern exercises the options. At the time of exercise, the shares are trading at $83 per share. He is still holding the shares on December 31, 2010.

Required: Calculate Mr. Kern's minimum net employment income for the year ending December 31, 2010. Provide reasons for omitting items that you have not included in your calculations. Ignore all GST considerations.

TIF PROBLEM THREE - 8
Employment Income

Mrs. Vera Smiles is a sales representative for a Canadian controlled private corporation that manufactures office furniture. Her gross salary for the year ending December 31, 2010 is $53,000 and, in addition, she earned commissions of $34,500. For the 2010 taxation year, Mrs. Smiles' employer withheld the following amounts from her income:

Federal And Provincial Income Taxes	$22,400
Registered Pension Plan Contributions	3,200
Contributions To Group Disability Plan	236

Mrs. Smiles' employer made a $3,200 matching contribution to her registered pension plan and a $236 matching contribution to her group disability insurance.

Other Information:

1. During 2010, Mrs. Smiles is provided with an automobile that has been leased by her employer. The lease payments are $1,220 per month, an amount which includes a $127 per month payment for insurance. The car is available to her for ten months of the year, and she drives it a total of 67,000 kilometers. Of this total, 63,000 kilometers were for travel required in pursuing the business of her employer, and the remainder was for personal use. She reimbursed her employer $1,400 for her personal use of the automobile.

2. During 2010, Mrs. Smiles was hospitalized for a period of four weeks. The disability plan provided her with benefits of $2,650 during this period. Mrs. Smiles began making contributions to this plan in 2009, at the rate of $236 per year.

3. On July 1, 2010, Mrs. Smiles received a $50,000 loan from her employer. The loan requires annual interest payments at a rate of 1 percent and Mrs. Smiles pays the interest for 2010 on January 18, 2011. Assume that at the time the loan was granted and for the remainder of the year, the prescribed rate was 2 percent. The loan is still outstanding at the end of the year.

4. In 2007, Mrs. Smiles was given options to buy 200 shares of her employer's stock at a price of $32 per share. At the time the options were issued, the shares had a fair market value of $30 per share. On June 1, 2010, Mrs. Smiles exercises the options. At the time of exercise, the shares had a fair market value of $45 per share. She does not plan to sell the shares for at least two years.

5. During the year, Mrs. Smiles traveled extensively on business. She had travel costs of $3,365 in air fares, $4,880 in travel lodging, and $2,450 in meals while on the road. She also spent $2,720 to entertain clients. Her employer reimbursed her fully for these costs on presentation of the receipts.

Required: Calculate Mrs. Smiles' minimum net employment income for the year ending December 31, 2010. Provide reasons for omitting items that you have not included in your calculations. Ignore all GST and PST considerations.

TIF PROBLEM THREE - 9
Employment Income With Commissions

Mr. Jones is a salesman handling a line of computer software throughout Western Canada. During 2010, he is paid a salary of $25,800 and receives sales commissions of $47,700. He does not receive an allowance from his employer for any of his expenses. During the year, Mr. Jones made the following employment related expenditures:

Airline Tickets	$ 2,350
Office Supplies And Postage	415
Purchase Of Laptop Computer	2,075
Client Entertainment	1,750
Cost Of New Car	24,000
Operating Costs Of Car	7,200

The new car was purchased on January 5, 2010, and replaced a car which Mr. Jones had leased for several years. During 2010, Mr. Jones drove the car a total of 50,000 kilometers, of which 35,000 kilometers were for employment related purposes. The capital cost allowance for the car (100 percent) is $3,600.

In addition to expenditures to earn employment income, Mr. Jones has the following additional disbursements:

Alberta Blue Cross Medical Insurance Premiums	$435
Group Life Insurance Premiums	665

Mr. Jones indicates that he regularly receives discounts on his employer's merchandise and, during the current year, he estimates that the value of these discounts was $1,300.

One of the suppliers of his employer paid $2,450 to provide Mr. Jones with a one week vacation at a northern fishing lodge.

Required: Determine Mr. Jones' net employment income for the 2010 taxation year. Ignore all GST and PST implications.

Chapter Four Test Item File Problems

TIF PROBLEM FOUR - 1

Tax Payable For Individuals - Essay Questions

1. Under what circumstances is an individual entitled to a home relocation loan deduction? How is the amount of the deduction calculated?

2. Explain briefly the rules for determining which province will assess an individual for income taxes. From the point of view of tax planning, is the province in which an individual is taxed an important issue?

3. ITA 118(1)(a) provides a tax credit for an individual's "spouse or common-law partner". Briefly describe the types of relationships that are eligible for this tax credit.

4. Under what circumstances can a taxpayer deduct the ITA 118(1)(b) credit for an eligible dependant?

5. The same relative of an individual may be eligible for either the ITA 118(1)(d) tax credit for an infirm dependant over 17 or the ITA 118(1)(c.1) caregiver credit. As the value of the two credits is the same, what determines which credit should be used?

6. The charitable donations tax credit is the only credit which is partially calculated at the maximum federal rate of 29 percent. What is the likely reason for this unique feature?

7. A medical expense tax credit, based on the total medical expenses for a family, can be claimed by either spouse. Does it make any difference which spouse makes the claim?

8. Certain credits against Tax Payable can be transferred to a spouse or common-law partner. Indicate which credits are eligible for this transfer. Include only credits that can be transferred, not credits that can be taken by either spouse or common-law partner.

9. Some tax credits are referred to as "refundable". What does this mean?

10. Some analysts contend that the OAS clawback is effectively an increase in an individual's tax rate. Explain this view.

TIF PROBLEM FOUR - 2
Tax Payable For Individuals - True Or False

1. Worker's compensation payments are not included in an individual's Net Income For Tax Purposes.

   True Or False?

2. The home relocation loan deduction is only available when the taxpayer has moved to a new work location and his new dwelling is at least 40 kilometers closer to this new location.

   True Or False?

3. Provincial income taxes are calculated as a percent of federal Tax Payable.

   True Or False?

4. All federal tax credits are calculated by multiplying the lowest federal income tax bracket rate by an indexed base figure.

   True Or False?

5. A person claiming the ITA 118(1)(b) tax credit that is available to an eligible individual supporting a related dependant in a self-contained domestic establishment can claim the credit for their child, even if the child is not a resident of Canada.

   True Or False?

6. An individual cannot claim the pension income credit if their only income is from the Canada Pension Plan.

   True Or False?

7. If both spouses have medical expenses, it will usually be to their advantage for one of the spouses to claim the credit on the basis of their combined medical expenses.

   True Or False?

8. There is no limit on the amount of tuition, education and textbook credits that can be transferred to a spouse.

   True Or False?

9. Sharon Jarvis contributed $500 to the Federal Liberal Party. She is eligible for a federal political contributions tax credit of $500.

   True Or False?

10. The federal political contributions tax credit is deductible in computing Taxable Income, but cannot create a Taxable Loss.

    True Or False?

TIF PROBLEM FOUR - 3
Tax Payable For Individuals - Multiple Choice

Taxable Income

1. On July 1, 2010, Sam Confrey received a five year, $50,000 loan from his employer. The loan was intended to assist Sam with the purchase of a home in his new employment location. The new home is 47 kilometers closer to Sam's new work location. The interest rate on the loan was 3 percent. Assume that during the third and fourth quarters of 2010, the relevant prescribed rate of interest is 4 percent. The effect of this transaction on his Taxable Income would be:

    A. An increase of $250.
    B. An increase of $500.
    C. An increase of $750.
    D. An increase of $2,000.
    E. No change.

2. In December 2007, Arcor Co. advanced funds of $200,000 to Mr. Jones, a new employee of the corporation, to assist him in acquiring a residence when he moved from Newfoundland to commence employment in British Columbia. The loan bears no interest and is to be repaid in full on December 31, 2012. The prescribed interest rate at the time of this advance was 5 percent. Assuming that the prescribed interest rate throughout 2010 was 6 percent, which one of the following represents the increase in Mr. Jones's Taxable Income in 2010 due to this loan?

    A. $ 8,750.
    B. $10,000.
    C. $10,500.
    D. $12,000.

Tax Credits

3. Which of the following tax credit bases is not subject to full indexation?

    A. Amount for an eligible dependant.
    B. Age amount.
    C. Disability amount.
    D. Pension income amount.

4. Of the following statements about tax credits, which one is correct?

    A. They are deducted from total income and are effectively not subject to tax.
    B. They reduce tax by the same amount regardless of a taxpayer's marginal tax rate.
    C. They are deducted from Net Income For Tax Purposes and are effectively not subject to tax.
    D. Their impact is greater for taxpayers with a higher marginal tax rate.

5. Jean Marchand is a single parent with a child. Which of the following conditions is not required for Jean to claim the ITA 118(1)(b) credit for an eligible dependant?

    A. Jean must maintain a self-contained domestic establishment.
    B. The child must be under 18 years of age, or mentally or physically infirm.
    C. The child must be a resident of Canada.
    D. The child must be wholly dependent for support on Jean.

6. Jake Baxter donated $100,000 to a Canadian registered charity. His Net Income For Tax Purposes for the year is $120,000. Calculate Jake's maximum federal tax credit for charitable gifts.

   A. $13,500.
   B. $15,000.
   C. $26,072.
   D. $28,974.

7. Of the following statements about medical expenses, which one is correct?

   A. A taxpayer can only claim his own medical expenses.
   B. The claim must be made in the calendar year the expense was incurred.
   C. Only expenses in excess of a specified amount are eligible for a tax credit.
   D. The amount of the tax credit is dependent on the taxpayer's marginal tax rate.

8. For an individual who is over 65 years of age, which of the following types of pension income does not qualify for the ITA 118(3) pension income tax credit?

   A. Payments from the Canada Pension Plan.
   B. Old Age Security payments.
   C. Payments from a provincial pension plan.
   D. All of the above.

9. Which of the following tax credits cannot be transferred to a spouse?

   A. The age credit.
   B. The disability credit.
   C. The education credit.
   D. The EI and CPP credits.
   E. The pension income credit.

10. With respect to the federal political contributions tax credit, which of the following statements is correct?

    A. Contributions made to any registered political party are eligible for the credit.
    B. Contributions made to a candidate at the time of a federal general election are eligible.
    C. The credit is equal to 29 percent of the eligible contributions made.
    D. There is no upper limit to the amount of the credit that can be claimed, as long as the contributions are made within the legal limits governing campaign contributions.

11. During the year, Ted Knight received worker's compensation payments totaling $10,000 as a result of an injury he suffered at work. His only other source of income for the year was his wages of $25,000. Which one of the following represents Ted's Net and Taxable Incomes for the year?

    A. Net Income $25,000, Taxable Income $25,000.
    B. Net Income $30,000, Taxable Income $30,000.
    C. Net Income $35,000, Taxable Income $25,000.
    D. Net Income $35,000, Taxable Income $35,000.

TIF PROBLEM FOUR - 4
Tax Payable For Individuals - Exam Exercises

Exam Exercise Four - 1 (Home Relocation Loan)

On January 1, 2010, Ms. Anna Rossi's employer asks her to relocate to one of the company's offices in a different city. In order to facilitate the move, the employer provides her with a $78,000, five year home relocation loan. Annual interest of 1 percent must be paid on the loan. Assume that throughout 2010, the relevant prescribed rate is 5 percent. Determine the effect of this loan on Ms. Rossi's 2010 Taxable Income.

Exam Exercise Four - 2 (Calculation Of Tax Payable Before Credits)

During 2010, Mark Forbes is a resident of Ontario and has calculated his Taxable Income to be $53,175. Calculate his 2010 federal Tax Payable before consideration of credits.

Exam Exercise Four - 3 (Personal Tax Credits)

Mr. Don Deloran has 2010 Net Income For Tax Purposes of $26,100. The corresponding figure for his spouse is $5,800. Mr. Deloran has no tax credits other than the basic personal credits for his spouse and himself. Determine Mr. Deloran's federal tax credits for 2010.

Exam Exercise Four - 4 (Caregiver Tax Credit)

Gerrard Bensen lives with his wife and their two children. Two years ago, his mother who is 72 years old and extremely healthy, moved in with him. Her Net Income For Tax Purposes for 2010 is $15,100. Determine the amount of Gerrard's caregiver tax credit, if any, for 2010.

Exam Exercise Four - 5 (Infirm Dependent Over 17 Tax Credit)

Margo Riche is married and has a 27 year old son who lives in a group home. The son is dependent on Margo because of a physical infirmity. His Net Income For Tax Purposes for 2010 is $6,550. Determine the amount of Margo's caregiver and infirm dependant over 17 tax credit for 2010.

Exam Exercise Four - 6 (Eligible Dependent Vs. Caregiver Tax Credits)

Sheila Cox is a single individual with an 83 year old father. While her father is not mentally or physically infirm, he lives with Sheila. He has Net Income For Tax Purposes for 2010 of $7,675. Calculate the tax credits that will be available to Sheila as a result of her father living with her.

Exam Exercise Four - 7 (Caregiver Vs. Infirm Dependent Over 17 Tax Credits)

Toshiro Mifune is married and has a 28 year old daughter. She lives with him and is dependant because of a physical infirmity. For 2010, she has investment income of $9,315. Toshiro would like to know whether he should take the caregiver tax credit for his daughter or, alternatively, the infirm dependant over 17 tax credit. Calculate the amount of the credit that you have selected.

Exam Exercise Four - 8 (Multiple Credits For Dependants)

Mr. John Foret is 42 years old and divorced from his wife. His Net Income For Tax Purposes for 2010 is $56,000. He has retained the family home and both of the children of the marriage live with him. His daughter is 23 years old and suffers from Down Syndrome. She does not qualify for the disability tax credit. His son is 14 years old and in good health. His daughter has no income during 2010, while his son has Net Income For Tax Purposes of $2,100. Determine Mr. Foret's maximum federal tax credits for 2010.

Exam Exercise Four - 9 (Age Tax Credit)

Ms. Marlene Burns is 69 years old and has 2010 Net Income For Tax Purposes of $46,642. Determine Ms. Burns' age credit for 2010.

Exam Exercise Four - 10 (Adoption Expenses Tax Credit)

Claude Lafleur and his spouse have adopted an infant French orphan. The adoption process began in October, 2009 when they traveled to France to discuss the adoption and view available children. The cost of this trip was $3,850. Their provincial government opens the adoption file on March 15, 2010, and the adoption order is issued on September 29, 2010. In October, the couple returns to France to pick up their new daughter. The happy family returns to Canada on October 20, 2010. The cost of this trip is $6,280.

Additional expenses paid during the first week of October, 2010 were $1,759 paid to the French orphanage and $5,600 paid to a Canadian adoption agency. Legal fees incurred during the adoption period were $3,250. After arrival in Canada, an additional $3,200 in medical expenses were incurred for the child prior to the end of 2010. Mr. Lafleur's employer has a policy of providing reimbursement for up to $4,500 in adoption expenses eligible for the adoption expenses tax credit. This amount is received in October, 2010 and will be considered a taxable benefit to Mr. Lafleur. What is the maximum adoption expenses tax credit that can be claimed by Mr. Lafleur or his spouse?

Exam Exercise Four - 11 (Charitable Donations Tax Credit)

Leon Fiero has 2010 Net Income For Tax Purposes of $70,400. Each week, without fail, he plays a nation-wide lottery. While over the years he has not had any winnings of consequence, his fortunes have changed and, in 2010, he wins over $320,000. As he had hoped to do for many years, he donates $120,000 of these winnings to the Canadian Cancer Society in 2010.

He chooses to claim $15,000 of his donations in 2010. In 2011, his income remains at $70,400 and he makes no further donations. Determine Mr. Fiero's charitable donations tax credit for 2010, as well as the base for the maximum allowable charitable donations tax credit for 2011. Until what year can he claim any unused portions of his 2010 donation?

Exam Exercise Four - 12 (Medical Expense Tax Credit)

Mr. Samuel Silverstein has a spouse and a 19 year old dependent son. Mr. Silverstein's 2010 Net Income For Tax Purposes is $125,000. For 2010, Mr. Silverstein's spouse has no income and his son has Net Income For Tax Purposes of $8,675. During 2010, Mr. Silverstein and his spouse have medical expenses of $2,842. His son has medical expenses of $7,780 which Mr. Silverstein paid. Determine Mr. Silverstein's medical expense credit for 2010.

Exam Exercise Four - 13 (Refundable Medical Expense Supplement)

During 2010, Mr. Chris Mackey has Net Income For Tax Purposes of $28,248. Mr. Mackey and his common-law partner, Emily, have total medical expenses of $10,325. Emily has no income of her own. Determine Mr. Mackey's minimum Tax Payable for 2010.

Exam Exercise Four - 14 (Disability Tax Credit)

Lorraine Tramer lives with her husband and 20 year old paraplegic daughter, Marie, who qualifies for the disability tax credit. Lorraine has medical expenses of her own of $2,500. During 2010, Lorraine paid medical expenses of $9,850 for Marie, none of which involved attendant care expenses. Marie has no income of her own. Lorraine's Taxable Income for 2010 was $108,600. Determine the total amount of tax credits related to Marie that will be available to Lorraine.

Exam Exercise Four - 15 (Education Related Tax Credits)

During 2010, Frank Balmer attends university for five months of full time study and three months of part time study. His total tuition for the year, including all ancillary fees, is $4,100, of which he prepaid $1,400 in 2009. The amount paid in 2010 includes $415 in fees that are only charged to students in his biology program. Interest for the year on his student loan was $417. Determine the total amount of education related tax credits that would be available for Mr. Balmer for 2010.

Exam Exercise Four - 16 (Carry Forward Of Education Related Tax Credits)

At the beginning of 2010, Karl Schmidt has a carry forward of education related credits from 2009 of $525 [(15%)($3,500)]. During 2010, he is in full time attendance at a Canadian university for 10 months of the year. His tuition fees total $5,650 for the year. His Taxable Income for 2010 is $34,650. Other than education related tax credits, his only tax credit is his basic personal credit. Determine Karl's total education related tax credits and any available carry forwards.

Exam Exercise Four - 17 (Transfer Of Education Related Tax Credits)

Betty Masters has 2010 Taxable Income of $11,785. She attends university in London, England on a full time basis for 9 months of the year, paying a total amount for tuition of $26,800 (Canadian dollars). Her only tax credit, other than education related credits, is her basic personal credit. Determine Betty's education related credits and indicate how much of this total could be transferred to a supporting parent and how much would be carried forward.

Exam Exercise Four - 18 (Transfer Of Credits From A Spouse)

Mrs. Rhonda Lee is 65 years old and has Net Income For Tax Purposes of $53,500. Of this total, $30,600 was from a life annuity that she purchased with RRSP funds. Her spouse is 68 years old, has no income of his own (he is ineligible for OAS), and is attending university on a full time basis. His tuition fees for the year were $3,450 and he was in full time attendance for 3 months of the year. Determine Mrs. Lee's maximum federal tax credits for 2010. Ignore the possibility of splitting her pension income with her spouse.

Exam Exercise Four - 19 (Political Contributions Tax Credit)

Mr. Allen Dion contributes $826 to the Canadian Political Alliance, a registered federal political party. Determine the amount of his federal political contributions tax credit.

Exam Exercise Four - 20 (Labour Sponsored Funds Credit)

On June 30, 2010, Ms. Monica Neville purchases newly issued shares in a prescribed labour sponsored venture capital corporation at a cost of $4,600. The province in which Ms. Neville lives provides a provincial tax credit for this investment. Determine the amount of the federal tax credit that will result from this purchase.

Exam Exercise Four - 21 (EI And OAS Clawbacks)

For 2010, Mr. Oliver Clemens has net employment income of $57,200, receives EI payments of $9,460, and receives $6,200 in Old Age Security (OAS) payments. No amount was withheld from the OAS payments because he had very low income in the previous two years due to large business losses. Determine Mr. Clemens' Net Income For Tax Purposes for 2010.

TIF PROBLEM FOUR - 5
Tax Payable For Individuals - Key Term Matching

The following five key terms were listed at the end of Chapter 4, "Taxable Income and Tax Payable for Individuals".

A. Spouse

B. OAS Clawback

C. Dependant

D. Indexation

E. Eligible Dependant Tax Credit

The following list contains 10 potential definitions for the preceding key terms.
NOTE There is only **ONE** correct definition for each key term.

1. A taxing back, or reduction, in the payment of Old Age Security benefits. The federal government taxes back, or retains, an amount of these payments equal to 15 percent of the individual's income.

2. The process of adjusting tax brackets and all tax credits to reflect changes in the Consumer Price Index.

3. As defined in ITA 118(6), an individual who, at any time during the year, is dependent on the taxpayer for support and is the child or grandchild of the individual or of the individual's spouse or common-law partner, the parent, grandparent, brother, sister, uncle, aunt, niece, or nephew, if resident in Canada at any time in the year, of the individual or of the individual's spouse or common-law partner.

4. A credit against Tax Payable that is available to an individual supporting a dependant in a self-contained domestic establishment.

5. A taxing back, or reduction, in the payment of Old Age Security benefits. The federal government taxes back, or retains, an amount of these payments equal to 15 percent of the individual's income in excess of an indexed threshold amount.

6. As defined in ITA 118(6), an individual who, at any time during the year, is dependent on the taxpayer for support and is the child or grandchild of the individual or of the individual's spouse or common-law partner, the parent, grandparent, brother, sister, uncle, aunt, niece, or nephew of the individual or of the individual's spouse or common-law partner.

7. A person of the opposite sex to whom a taxpayer is legally married.

8. A credit against Tax Payable that is available to a single individual supporting a dependant in a self-contained domestic establishment.

9. A person to whom a taxpayer is legally married.

10. The process of adjusting tax brackets and some tax credits to reflect changes in the Consumer Price Index.

Required: For each of the five key terms listed, indicate the number of the item that provides the **BEST** definition of that term. As only one definition is completely correct, please indicate only one number for each key term. No marks will be awarded if you indicate more than one number for any key term.

TIF PROBLEM FOUR - 6
Tax Payable For Individuals - Personal Tax Credits

In each of the following independent Cases, determine the maximum amount of 2010 personal tax credits, including transfers from a spouse or dependant, that can be applied against federal Tax Payable by the taxpayer.

1. Mr. Hanson has Net Income For Tax Purposes of $40,000, none of which is employment income. He is single and provides support for his mother. His mother is a widow who resides in England, and has income of $700 per year.

2. Mr. Johnson has Net Income For Tax Purposes of $250,000, all of which is employment income. His employer has withheld and remitted the required EI and CPP amounts. Mr. Johnson was married on December 1, 2010. His wife, an accounting student, had salary of $27,500 for the period from January 1 to November 30, 2010 and $2,500 for the month of December, 2010.

3. Mr. Massey has Net Income For Tax Purposes of $60,000, none of which is employment income. He lives with his common-law wife and her two children from a previous marriage. The two children are eight and ten years of age and neither his wife nor the children have any source of income.

4. Mr. Jones is married and has Net Income For Tax Purposes of $70,000, none of which is employment income. His 19 year old dependent son attends university. His wife has Net Income For Tax Purposes of $1,200, and his son has Net Income For Tax Purposes of $2,900. His son does not wish to transfer his tuition, education or textbook credits.

5. Ms. Morrison is divorced, maintains a residence far from her former spouse, and receives $1,000 per month in child support payments. She has custody of the two children from the marriage. They are aged seven and ten and have no income of their own. Her Net Income For Tax Purposes is $50,000, none of which is employment income.

6. Mr. Bagley is 68 years old and has Net Income For Tax Purposes of $27,000, which is comprised of OAS benefits of $6,200 and $20,800 of pension income. His wife is 52 years old and is blind. She has no income of her own.

TIF PROBLEM FOUR - 7
Tax Payable For Individuals - Calculation

Note To Instructor This problem is an extension of Test Item File Problem Three - 7.

Mr. Samuel Kern is an administrator for a publicly traded Canadian manufacturing company. His gross salary for the year ending December 31, 2010 is $67,600. For the 2010 taxation year, Mr. Kern's employer withheld the following amounts from his income:

Federal Income Tax	$11,200
Employment Insurance Premiums	747
Canada Pension Plan Contributions	2,163
Registered Pension Plan Contributions	1,800
Contributions To Group Disability Plan	175

Mr. Kern's employer made a matching contribution of $1,800 to his registered pension plan and a $175 matching contribution for the group disability insurance.

Other Information:

1. During 2010, Mr. Kern is provided with an automobile that has been leased by his employer. The lease payments are $815 per month, an amount which includes all taxes and an $89 monthly payment for insurance. The total operating costs of the car were $4,600 for the year and they were paid by the employer. The car is available to him for nine months of the year and he drives it a total of 32,000 kilometers. Of this total, 29,000 kilometers were for travel required in pursuing the business of his employer and the remainder was for personal use. He reimbursed his employer $50 per month of use for his personal use of the automobile.
2. During 2010, Mr. Kern was hospitalized for a period of three weeks. The disability plan provided him with benefits of $1,650 during this period. Mr. Kern began making contributions to this plan in 2009 at the rate of $175 per year.
3. Mr. Kern was required to pay 2010 dues to his professional association in the amount of $1,233.
4. In 2008, Mr. Kern was given options to buy 200 shares of his employer's stock at a price of $75 per share. At the time the options were issued, the shares were trading at $70 per share. On June 1, 2010 Mr. Kern exercises the options. At the time of exercise, the shares are trading at $83 per share. He is still holding the shares on December 31, 2010.
5. Mr. Kern donated $500 to the Canadian Cancer Society in 2009, but forgot to claim the donation in 2009. He has found the donation receipt in his files.
6. Mr. Kern lives with his wife and 23 year old son, David. His wife has Net Income For Tax Purposes of $3,660. David is a full time student at university for 8 months of the year and has Net Income For Tax Purposes of $5,780. Mr. Kern has paid David's tuition for 2010 of $6,700, and in return, David has agreed to transfer the maximum credit possible to his father.
7. Mr. Kern paid the following medical costs:

For Himself	$2,100
For His Wife	770
For David	3,260
Total	$6,130

Required: Calculate, for the 2010 taxation year, Mr. Kern's minimum Taxable Income and federal Tax Payable (Refund). Indicate any carry forwards available to him and his dependants and the carry forward provisions. Ignore all GST considerations.

TIF PROBLEM FOUR - 8
Comprehensive Tax Payable With Employment Income

Ms. Marcy Van Horne is employed by a large public corporation and her 2010 salary is $126,000. In addition to her annual salary, she received a performance bonus of $25,000, one-half of which will be paid in 2010, with the remaining one-half not due until July 1, 2011. In addition to her salary, she earns commissions of $32,000 during 2010.

During 2010, Ms. Van Horne's employer withheld the following amounts from her compensation:

EI Premiums	$ 747
CPP Contributions	2,163
RPP Contributions	7,400
Life Insurance Premiums (Employer Makes A Matching Contribution)	550

Ms. Van Horne is divorced and has custody of her two children. They are aged 12 and 17. The 12 year son has 2010 income of $2,500. The 17 year old daughter is in full time attendance at a university during 8 months of the year. Ms. Van Horne pays her annual tuition of $7,000. The daughter has summer income of $4,500 and has agreed to transfer her education related credits to her mother. Also living with Ms. Van Horne is her 68 year old father who helps with maintenance of the house. Although his Net Income For Tax Purposes for 2010 totals only $8,000, he has supplemented his income for years with his casino winnings.

Other Information:

1. Ms. Van Horne is provided with an automobile by her employer. During 2010, it is driven 48,000 kilometres, of which 42,500 are employment related. The automobile is leased by the employer at a monthly rate of $728, including GST of $30 and PST of $48. The monthly rate also includes a payment for insurance of $50 per month. The automobile is available to Ms. Van Horne for 11 months during 2010.

2. Ms. Van Horne incurred the following employment related expenses during 2010:

Advertising	$5,600
Entertainment	9,000
Meals	2,400
Hotels	8,400
Airline Tickets	3,400
Total Expenses	$28,800

   Ms. Van Horne's employer reimburses all of her meal costs and one-half of her hotel bills. No other expenses were reimbursed.

3. During 2009, Ms. Van Horne was granted options to acquire 5,000 shares of her employer's common shares at an option price of $25 per share. This was also the market value of the shares at this time.

   During July, 2010, Ms. Van Horne exercises all of the options at a point in time when the shares were trading at $31 per share. She is still holding the shares at the end of the year.

4. Ms. Van Horne buys monthly transit passes for both of her children during the school year. The cost is $45 per month per child. Passes were purchased for 9 months during 2010.

5. During 2010, Ms. Van Horne gives total cash of $1,800 to a variety of registered charities.

6. Also during 2010, Ms. Van Horne donates $300 to each of the three federal political parties.

7. During 2010, Ms. Van Horne pays for the following eligible medical costs:

For Herself	$ 850
For Her Two Children	1,480
For Her Father	3,940
Total Medical Costs	$6,270

Required:

A. Determine Ms. Van Horne's minimum Net Income For Tax Purposes for the 2010 taxation year.

B. Determine Ms. Van Horne's minimum Taxable Income for the 2010 taxation year.

C. Based on your answer in Part B, determine Ms. Van Horne's federal Tax Payable for the 2010 taxation year. Indicate any carry forwards available to her and her dependants and the carry forward provisions. Ignore any amounts that might have been withheld by her employer or paid in instalments.

Chapter Five Test Item File Problems

TIF PROBLEM FIVE - 1
CCA - Essay Questions

1. For accounting purposes, assets are generally recorded at their acquisition cost. This amount would include the basic invoice cost, delivery and installation costs, and other expenditures required to make the asset available for use by the enterprise. Indicate some of the reasons why the capital cost of an asset for tax purposes may differ from the asset cost that will be recorded for accounting purposes.

2. The calculation of amortization expense under generally accepted accounting principles and the determination of CCA to be deducted for tax purposes can be viewed as somewhat similar procedures. However, there are some differences that arise in the application of these procedures. Describe the similarities and differences between the procedures used to calculate amortization expense for accounting records and those procedures used to establish the amount of CCA to be deducted in tax returns.

3. Briefly explain why it is important to take care in allocating assets to the appropriate CCA class.

4. If the government wishes to increase or decrease the rate applicable to a particular type of asset, this can be accomplished using two different approaches. Describe these approaches, indicate which you think is preferable, and explain the reason for your preference.

5. If a taxpayer has decided, in a particular taxation year, to deduct less than the maximum available CCA, he will need to decide from which classes the amount that will be deducted should be taken. How will he make this decision? Explain your conclusion.

6. When a depreciable asset is sold or retired, the procedures used for tax purposes are usually very different than those used for accounting purposes. Describe the differences between the procedures used for tax purposes and those that would be required under generally accepted accounting principles for dispositions of depreciable assets.

7. When a taxpayer acquires a photocopier to be used in producing business income, he can either allocate its cost to his general Class 8 or, alternatively, elect to allocate it to a separate Class 8. What is the potential advantage of allocating the cost of a photocopier to a separate Class 8?

8. What is the definition of eligible capital property? Provide three examples of such property.

TIF PROBLEM FIVE - 2
CCA - True Or False

1. Capital cost allowance is analogous to the accounting term amortization and allocates the cost of the capital asset to current and subsequent taxation years.

   True or False?

2. Undepreciated capital cost is decreased by government assistance received to acquire assets and increased by acquisitions of depreciable assets.

   True or False?

3. Capital cost allowance for each class can be calculated using the declining balance method or the straight line method, as long as it is the same method used to calculate amortization for the financial statements.

   True or False?

4. A corporation with a June 30 year end begins its operations on January 1, 2010. It has acquired $50,000 of Class 8 assets on January 1. The maximum CCA for its fiscal year ending June 30, 2010 is $5,000.

   True or False?

5. If a patent is acquired near the end of its legal life, it will usually be a good idea to elect to include its cost in Class 14.

   True or False?

6. The separate class election for photocopiers should be used only if the assets are retained and used for long periods of time.

   True or False?

7. Recapture of CCA occurs when there is a negative balance in the class at the end of the year.

   True or False?

8. Cumulative eligible capital is amortized at a maximum rate of 7 percent, calculated on a straight line basis.

   True or False?

9. Goodwill is purchased for $60,000 during the year. The maximum CEC amount that can be deducted for tax purposes for the year is $1,575.

   True or False?

TIF PROBLEM FIVE - 3
CCA And CEC - Multiple Choice

CCA Questions

1. The Nelson Company has a taxation year end of December 31. On January 1 of the current year, the UCC of Class 8 was $80,000. The Nelson Company has a policy of always deducting maximum CCA. Each of the **independent** Parts of this question deal with transactions during the current year which involved Class 8 assets. Choose one of the following answers for each Part (individual answers can be used more than once).

A. $10,000	I. $52,000	P. $10,000 Recapture
B. $10,800	J. $60,800	Q. $25,000 Recapture
C. $13,000	K. $67,000	R. $10,000 Terminal Loss
D. $17,000	L. $72,000	S. $25,000 Terminal Loss
E. $18,000	M. $73,000	T. $10,000 Capital Loss
F. $19,000	N. $90,000	U. $25,000 Capital Loss
G. $20,000	O. $91,000	V. $10,000 Capital Gain
H. $22,000		W. $25,000 Capital Gain

Part A An asset was purchased for $20,000 on April 1. Maximum CCA for Class 8 is:

Part B An asset with a capital cost of $15,000 was sold for $4,000 on June 30. Minimum UCC on January 1 of the following year is:

Part C An asset with a capital cost of $15,000 was sold for $26,000 on September 1. Maximum CCA for Class 8 is:

Part D An asset with a capital cost of $15,000 was sold for $26,000 on September 1. Minimum UCC on January 1 of the following year is:

Part E An asset with a capital cost of $100,000 was sold on June 30 for $90,000. Also during the year, an asset was purchased for $60,000. Maximum CCA for Class 8 is:

Part F The last asset in the class, with a capital cost of $105,000, was sold on July 15 for $90,000. This would give rise to:

Part G The last asset in the class, with a capital cost of $105,000, was sold on August 1 for $70,000. This would give rise to:

Part H An asset with a capital cost of $40,000 was sold for $50,000 on September 1. This would give rise to:

Part I An asset with a capital cost of $70,000 was sold on October 1 for $90,000. An asset was purchased on November 1 for $100,000. Maximum CCA for Class 8 is:

Part J An asset with a capital cost of $70,000 was sold on May 1 for $90,000. An asset was purchased on May 15 for $100,000. Minimum UCC on January 1 of the following year is:

2. The capital cost of an asset includes a number of costs. Indicate which cost would not be considered part of the capital cost.

   A. Legal fees incurred to acquire the asset.
   B. Duties paid on the asset.
   C. Fire and theft insurance paid on the asset.
   D. Non-refundable provincial sales taxes paid on the asset.
   E. An appropriate allocation of overhead.

3. A business has $5,000 in Taxable Income before CCA in the current year. The management anticipates a high income for the subsequent year. The maximum CCA deductible for the year in Class 8 is $5,000 and the maximum CCA deductible for the year in Class 12 is $5,000. To minimize the subsequent year's taxes, the business should:

   A. Claim maximum CCA on Class 8 only.
   B. Claim maximum CCA on Class 12 only.
   C. Claim maximum CCA on Class 8 and Class 12.
   D. Claim no CCA for the year.
   E. Claim $2,500 CCA on Class 8 and $2,500 CCA on Class 12.

4. During the current year, Denos Corporation incurred costs of $45,000 for leasehold improvements to its newly rented building. The lease was signed in the current year for an initial term of three years plus four successive options to renew the lease, each for an additional one year term. Which one of the following amounts represents the **maximum** capital cost allowance claim in the current year?

   A. $ 4,500.
   B. $ 5,625.
   C. $ 9 ,000.
   D. $11,250.

5. On December 1 of the current year, Plen Limited purchased a franchise for $70,000. The franchise has a limited life of 15 years. Which one of the following amounts represents the **maximum** amount of capital cost allowance Plen Limited can deduct for its current year ending on December 31?

   A. $ 198.
   B. $ 396.
   C. $1,837.
   D. $3,675.

6. In the current fiscal year, a corporation acquired a rental property from its sole shareholder. The building was transferred at its fair market value of $125,000, but was not allocated to a separate Class 1. The shareholder originally paid $150,000 for it. The property was included in Class 1 (4%) on the shareholder's tax return. The shareholder has earned rental income on the property since its acquisition in 1979. The undepreciated capital cost of the building at the time of the transfer was $120,000.

   Which one of the following amounts represents the **maximum** allowable capital cost allowance that the corporation may claim for this building in the current fiscal year?

   A. $2,400.
   B. $2,500.
   C. $4,800.
   D. $5,000.

7. ABC Enterprises began operations on September 1 of the current year. It has chosen December 31 as its year end. On October 1 of the current year, the proprietorship purchased furniture and fixtures for $40,000. The maximum capital cost allowance on the furniture and fixtures for the current year ending December 31 will be:

   A. $1,088.22.
   B. $1,336.99.
   C. $4,000.00.
   D. $8,000.00.

8. Robert bought a rental property ten years ago for $320,000, with $80,000 of the purchase price allocated to the land. Over the ten years, he claimed CCA such that his UCC at the beginning of this year for the building was $196,000. Robert sold the property this year for $520,000, with $180,000 of the sale price allocated to the land. Which of the following statements is correct?

   A. Robert has recapture of $44,000.
   B. Robert has recapture of $124,000.
   C. Robert has recapture of $144,000.
   D. Robert has a capital gain of $100,000.

9. Sherry owned a rental property. She originally acquired the property for $260,000 with $200,000 of the cost attributed to the building. Over the years, Sherry has claimed CCA of $32,000, such that her UCC at the beginning of the year was $168,000. The rental property is the only asset in the class. This year, she sold the property for $214,000, with $160,000 of the sale price attributed to the building. Which of the following statements is correct?

   A. Sherry has a terminal loss of $8,000.
   B. Sherry has a capital loss of $36,000.
   C. Sherry has an allowable capital loss of $4,000.
   D. Sherry has recapture of $32,000.

CEC Question

10. Indicate which of the following could not be an eligible capital expenditure.

   A. Cost of fines and penalties.
   B. Cost of government rights with an unlimited life.
   C. Appraisal costs associated with capital costs.
   D. Costs of incorporating a new company.
   E. Cost of customer lists.

TIF PROBLEM FIVE - 4
CCA - Exam Exercises

Exam Exercise Five - 1 (CCA Error)

During 2010, your company acquired a depreciable asset for $437,000 and your accountant included this asset in Class 1 at the end of the year (it was not allocated to a separate Class 1). Early in 2011, you discover that the asset should have been allocated to Class 8. What was the impact of this error on your 2010 deductions from business income?

Exam Exercise Five - 2 (Class 10 And Half-Year Rules)

Lambda Ventures, an unincorporated business, has a Class 10 UCC balance on January 1, 2010 of $453,000. During 2010, it acquires additional Class 10 assets at a cost of $63,200. Also during 2010, it deducts $36,700 from the Class 10 UCC for dispositions. Determine the maximum CCA for 2010 and the January 1, 2011 UCC balance.

Exam Exercise Five - 3 (Short Fiscal Periods)

Fielding Inc. is incorporated on August 1, 2010. On September 15, 2010, the Company acquires $150,000 in Class 10 assets. The Company has a December 31 year end and no other depreciable assets are acquired before December 31, 2010. Determine the maximum CCA for the year ending December 31, 2010.

Exam Exercise Five - 4 (CCA And Tax Planning)

Pointer Ltd. has determined that, for the current year, it has Taxable Income before the deduction of CCA of $40,000. It is the policy of the Company to limit CCA deductions to an amount that would reduce Taxable Income to nil. At the end of the year, before the deduction of CCA, the following UCC balances are present:

Class 1 (Buildings Acquired In 2005)	$475,000
Class 8	95,000
Class 10	102,000
Class 10.1	26,000

There have been no additions to these classes during the year. Which class(es) should be charged for the $40,000 of CCA that will be required to reduce Taxable Income to nil? Explain your conclusion.

Exam Exercise Five - 5 (Recapture)

At the beginning of 2010, Marquee Inc. has two assets in Class 10. The balance in this class is $7,423. The cost of each asset in the class was $7,500. On June 30, 2010, one of the assets is sold for $7,950. There are no other additions or dispositions prior to the Company's December 31, 2010 year end. What is the effect of the disposition on the Company's 2010 net business income? In addition, determine the January 1, 2011 UCC balance.

Exam Exercise Five - 6 (Terminal Loss)

At the beginning of 2010, Quest Inc. has two assets in Class 43. The cost of each asset was $72,000 and the Class 43 UCC balance was $56,472. On June 30, 2010, both of these assets are sold for a total of $41,500. There are no other additions or dispositions prior to the Company's December 31, 2010 year end. What is the effect of the disposition on the Company's 2010 net business income? In addition, determine the January 1, 2011 UCC balance.

Exam Exercise Five - 7 (Separate Class Election)

In January, 2010, Multilink Inc. acquires 5 photocopiers at a cost of $5,500 each. In December, 2010, two of these photocopiers are upgraded for newer models. The new photocopiers cost $6,000 each, and the Company receives an upgrade allowance for each old photocopier of $2,000. Indicate the amount(s) that would be deducted from 2010 business income if no election is made to put each photocopier in a separate class. Contrast this with the deduction(s) that would be available if the separate class election is used.

Exam Exercise Five - 8 (CEC With Disposition)

During 2008, Korngold Inc. purchases another business and pays $123,000 for its goodwill. Prior to this acquisition, the cumulative eligible capital balance of Korngold Inc. is nil. There are no additions to this balance in 2009 or 2010. On December 1, 2010, the business acquired in 2008 was sold, and the sale price included a payment for goodwill of $118,200. Korngold Inc. takes the maximum deduction for cumulative eligible capital in both 2008 and 2009. What amount, if any, will be included in the Company's 2010 income as a result of this sale?

TIF PROBLEM FIVE - 5
CCA - Key Term Matching

The following five key terms were listed at the end of Chapter 5, “Capital Cost Allowances And Cumulative Eligible Capital”.

A. Terminal Loss

B. Half-Year Rules

C. Undepreciated Capital Cost

D. Recapture Of CCA

E. Cumulative Eligible Capital

The following list contains 10 potential definitions for the preceding key terms.
NOTE There is only **ONE** correct definition for each key term.

1. An amount expended to acquire an intangible asset that is not eligible for either write-off through CCA deductions or as a deduction in the period in which it is acquired.

2. The capital cost of a depreciable asset class, less the cumulative CCA that has been taken to date. The tax equivalent of book value in accounting.

3. This term is used to refer to the amortized balance of eligible capital expenditures. The amortization of this amount that is deducted under ITA 20(1)(b) is usually referred to as the cumulative eligible capital amount.

4. A group of rules which require, for most CCA classes, the subtraction of one-half of the year's net additions (additions, less the amount subtracted from the class because of disposals) from the UCC balance that is carried over to the next taxation year.

5. An addition in the calculation of business and property income which arises when the last asset in a CCA class is retired and a positive balance is left in the class.

6. An inclusion in business and property income that arises when deductions from a CCA class, engendered by disposals, leave a negative balance in that class at the end of the taxation year.

7. A group of rules which require, for most CCA classes, the subtraction of one-half of the year's net additions (additions, less the amount subtracted from the class because of disposals) from the class, prior to calculating the CCA for the year.

8. A deduction in the calculation of business and property income which arises when the last asset in a CCA class is retired and a positive balance is left in the class.

9. An inclusion in business and property income that arises when a depreciable asset is sold for proceeds that exceed the balance in its UCC class.

10. The capital cost of a depreciable asset class, less the cumulative CCA that has been taken to date. The tax equivalent of net book value in accounting.

Required: For each of the five key terms listed, indicate the number of the item that provides the **BEST** definition of that term. As only one definition is completely correct, please indicate only one number for each key term. No marks will be awarded if you indicate more than one number for any key term.

TIF PROBLEM FIVE - 6
CCA Calculations

All Night Service Ltd. was incorporated on April 1, 2008 to supply computer service 24 hours per day. At the time of incorporation, the Company establishes December 31 as its year end for both tax and accounting purposes. On April 1, 2008, the Company acquired a new building to be used as an office and communications centre at a cost of $250,000. This total cost is allocated $180,000 to the building and $70,000 to the land. As the building is being used 100 percent for non-residential purposes, it is allocated to a separate Class 1. Also on this date, the Company purchased six cars to be used by the service technicians at a cost of $25,000 per vehicle.

On May 1, 2008, the Company purchased a variety of computer repair and maintenance equipment at a cost of $48,000. The Company owns no computers as it leases all of its computer hardware and software.

During 2009, the Company trades in three of its old cars on three new minivans. The list price of the new minivans is $24,000 per vehicle, and the Company receives a trade-in allowance towards this list price of $14,000 per old vehicle.

On September 20, 2010, a convertible is acquired at a cost of $98,000 for use by the president of the Company. In addition, several unusual events occur during 2010. They are as follows:

- Equipment that had a value of $12,000 was stolen by one of the service technicians.
- One of the original six cars was involved in a severe accident, resulting in repair costs of $8,270. Because the Company's insurance has a deductibility clause, the insurance proceeds covered only $7,770 of these repair costs.
- Because he had never received a speeding ticket (despite numerous violations) while driving the car allocated to him, a departing service technician offers the Company $27,000 for one of its original six cars. The Company accepts the offer.

Required:

A. Determine the maximum CCA that can be taken in each of the years 2008 through 2010. In your calculations, include and identify the January 1, 2009, January 1, 2010, and January 1, 2011 UCC balances. Ignore GST/HST/PST considerations.

B. Explain the tax effects of the unusual events that occurred during 2010.

TIF PROBLEM FIVE - 7
CCA And Tax Planning

For its taxation year ending December 31, 2010, Northcote Inc. has determined that its Net Income For Tax Purposes, before any deduction for CCA amounts, is equal to $328,000. The Company does not have any Division C deductions, so whatever amount is determined as Net Income For Tax Purposes will also be the amount of Taxable Income for the taxation year.

On January 1, 2010, the Company has the following UCC balances:

Class 1 (Building Acquired In 2005)	$2,597,000
Class 8	718,000
Class 10	524,000

During 2010, the cost of additions to Class 10 amounted to $374,000, while the proceeds from dispositions in this class totalled $234,000. In no case did the proceeds of disposition exceed the capital cost of the assets retired and there were still assets in Class 10 on December 31, 2010.

There were no acquisitions or dispositions in either Class 1 or Class 8 during 2010.

Required:

A. Calculate the maximum CCA that could be taken by Northcote Ltd. for the taxation year ending December 31, 2010.

B. As Northcote's tax advisor, indicate how much CCA you would advise the Company to take for the 2010 taxation year, and the specific classes from which it should be deducted. Provide a brief explanation of the reasons for your recommendation. In providing this advice, do not take into consideration the possibility that losses can be carried either forward or back.

TIF PROBLEM FIVE - 8
CCA, Recapture, And Terminal Losses

On January 1, 2010, the beginning of its taxation year, Bard Ltd. has the following information on depreciable assets in its records:

Type Of Asset	Undepreciated Capital Cost	Original Capital Cost
Class 8 Furniture	$ 24,000	$147,000
Class 1 Buildings (Acquired In 2005)	562,000	846,000
Class 10 Automobiles	220,000	315,000

During the 2010 taxation year, the following transactions occur:

Sale Of Furniture Furniture with an original cost of $52,000 was sold for $36,000.

Purchase And Sale Of Buildings A new building was acquired on February 1, 2010 at a cost of $325,000. Of this total, $75,000 was the estimated value of the land on which the building was situated. The building will be used 100 percent for non-residential purposes and, in order to access the extra 2 percent CCA rate, it has been placed in a separate Class 1.

Also during the year, a building with an original cost of $335,000 was sold for $352,000. Of the $352,000 received, $200,000 is for the land on which the building is situated. The adjusted cost base of the land was equal to the $200,000 proceeds of disposition.

Sale Of Automobiles An extensive analysis of capital and operating costs indicated that the Company would be better off leasing automobiles, rather than continuing to purchase and retain ownership of these assets. As a consequence, all of the Company's automobiles were sold on December 28, 2010 for $185,000. The leased vehicles were delivered on January 2, 2011.

Required: For the taxation year ending December 31, 2010 calculate the maximum CCA that can be deducted by Bard Ltd. In addition, calculate the January 1, 2011 UCC balances and indicate any other tax consequences that would result from the described transactions.

TIF PROBLEM FIVE - 9
Depreciable Asset Retirements And CEC Sale

Vance Enterprises closes its books on December 31 of each year. On January 1, 2010, the following information on depreciable assets was contained in its records:

Type Of Asset	Undepreciated Capital Cost	Original Capital Cost	Date Of Acquisition
Equipment	$ 2,100	$ 26,000	January, 2003
Buildings	205,000	250,000	January, 1998
Automobile	10,200	20,500	June, 2006

There was no balance in the Cumulative Eligible Capital account at this time.

During the 2010 fiscal year, the following transactions occur:

> **Sale Of Equipment** - As the result of an extensive analysis, it is decided that it would be better to sell the existing equipment and to replace it with improved equipment that will be leased. The equipment is sold for $21,000.
>
> **Sale Of Buildings** - A similar decision is made with respect to the buildings. They are sold for $342,000 and replaced with leased premises. Of the $342,000 received, $80,000 is for the land on which the buildings are situated. The adjusted cost base of the land was equal to the $80,000 proceeds of disposition. The lease term is for four years with no options for renewal. However, a total of $39,000 is spent on leasehold improvements to make the buildings more suitable for the business.
>
> **Sale Of Automobile** - The automobile is used by Ms. Vance for both business and personal matters. It is sold during the current year and replaced with a leased vehicle. The sale proceeds are $8,900.
>
> **Sale Of Goodwill** - In order to further streamline her operations, Ms. Vance sells off a portion of her operations to another individual. No depreciable or capital assets were disposed of. However, an amount of $110,000 was received for the goodwill of this portion of the business.

Required: For the taxation year ending December 31, 2010 calculate the maximum CCA that can be deducted by Vance Enterprises. In addition, calculate the January 1, 2011 UCC balances and indicate any other tax consequences that would result from the described transactions.

TIF PROBLEM FIVE - 10
Cumulative Eligible Capital

The retail division of Moxy Distributors Inc. (MDI) was established through the acquisition of three unincorporated operations. These acquisitions were made during the taxation year ending December 31, 2008, with the following amounts being paid for goodwill:

Operation	Goodwill Acquired
A	$150,000
B	225,000
C	180,000

Operation A proved to be unprofitable and was sold during the taxation year ending December 31, 2009. The sales proceeds included a payment for goodwill of $82,000.

As MDI continued to have difficulties with lack of profits in its retail division, Operations B and C were sold during the year ending December 31, 2010. The proceeds from the sale of Operation B included a $210,000 payment for goodwill, while the proceeds from the sale of Operation C included a payment for goodwill of $283,000.

On January 1, 2008, MDI had a cumulative eligible capital balance of nil. MDI made the maximum CEC deduction in both 2008 and 2009.

Required: Determine the tax consequences resulting from the preceding transactions for each of the years 2008 through 2010.

Chapter Six Test Item File Problems

TIF PROBLEM SIX - 1
Business Income - Essay Questions

1. Assets can be acquired for use in a business, for resale by a business, or as investments. For each of these classifications, indicate (1) how the income earned will be classified, and (2) how the income resulting from the sale of the asset would be classified.

2. For tax purposes, the sale of inventories is treated differently than the sale of non-depreciable capital assets. Briefly describe the different treatments given to these two types of sales.

3. While there are many similarities between business income (for tax purposes) and accounting income as determined under GAAP, there are a number of differences. Indicate four such differences.

4. While business income and property income are covered in the same subdivision of the *Income Tax Act*, there are differences in the tax treatment of these two types of income. Briefly describe two of these differences.

5. What is a reserve? Explain briefly the reserve system that is used in determining net business income.

6. List three reserves that can be deducted in the determination of net business income.

7. Compare the procedures used to determine bad debt expense under GAAP, with those used to determine the annual deduction for bad debts under the *Income Tax Act*.

8. Section 18 of the *Income Tax Act* lists a number of general limitations on the deductions that can be made in the determination of net business income. Briefly describe four of these limitations.

9. Both employees and self-employed individuals can deduct the costs associated with maintaining a home office. Compare the items that can be deducted by an employee with those that can be deducted by a self-employed individual.

10. ITA 67 indicates that no deduction is available for an outlay or expense, except to the extent that the outlay or expense was reasonable in the circumstances. Provide an example of an outlay or expense that would be disallowed by this provision.

11. List and briefly describe three of the exceptions to the rule that only 50 percent of the cost of business meals and entertainment can be deducted in the determination of Net Income For Tax Purposes.

12. The *Income Tax Act* limits the deductions associated with the ownership of company cars. Describe these limitations.

13. Describe the alternative methods of inventory valuation that can be used for tax purposes.

14. In determining whether an individual can deduct farm losses against other sources of income, taxation authorities divide farmers into three categories. Describe these categories and indicate how the farm losses for each category are treated in the year they occur.

15. In situations where a business ceases to operate and its assets are being sold,, it is important that the parties to the transaction make the ITA 22 election with respect to the accounts receivable that are being transferred. Explain this importance.

TIF PROBLEM SIX - 2
Business Income - True Or False

1. The tax rules for determining business income are identical to those used for determining property income.

   True or False?

2. When property acquired for personal use is sold for more than its cost, there will be a taxable capital gain.

   True or False?

3. The deduction of CCA cannot be used to create or increase a net business loss.

   True or False?

4. If an asset has been held for a considerable period of time, any gain on its disposition will be treated as business income.

   True or False?

5. Differences between business income for tax purposes and business income as determined under GAAP can be either permanent or temporary.

   True or False?

6. When a business makes payments that are unreasonable in the circumstances, they cannot be deducted in the calculation of either accounting Net Income or net business income.

   True or False?

7. If a reserve is deducted for accounting purposes, it can also be deducted for tax purposes.

   True or False?

8. The amounts charged to income for bad debts on accounts receivable will generally be the same for both tax and accounting purposes.

   True or False?

9. A self-employed individual cannot deduct CCA on a home office in his principal residence unless it is used exclusively for income producing purposes.

   True or False?

10. Landscaping costs can be deducted in the determination of net business income, even if they involve items that would normally be considered capital assets.

    True or False?

11. For the hobby farmer, deductible farming losses for a year are restricted to $2,500, plus one-half of the next $12,500.

    True or False?

12. Inventories can be valued at aggregate market, which can mean replacement cost or net realizable value.

    True or False?

13. When a business ceases to operate and its inventories are disposed of, a gain on the inventories will be treated as a capital gain unless an election is made by the selling taxpayer.

True or False?

14. When a business ceases to operate and its accounts receivable are disposed of with the other business assets, any loss on the receivables will be treated as a capital loss unless a joint election is made by the purchaser and seller.

True or False?

TIF PROBLEM SIX - 3
Business Income - Multiple Choice

Business Vs. Property

1. Which of the following statements is not correct?

   A. In determining property income, the deduction of CCA cannot be used to create or increase a loss.
   B. Both business and property income are subject to the income attribution rules.
   C. Property income is not included in the earned income calculation that limits RRSP deductions.
   D. Travel expenses cannot be deducted against property income.

Business Vs. Capital Gains

2. In determining whether a gain resulting from a disposition of an asset is capital or business, various criteria have been used. Which of the following considerations would be least likely to affect the decision?

   A. The length of time the asset is held.
   B. Whether the transaction is related to the taxpayer's business.
   C. The number and frequency of similar asset dispositions.
   D. Whether the taxpayer knew the investment could be sold for a profit if the investment return was inadequate.
   E. Whether the transaction resulted in a gain or loss.

3. Jerry collects baseball cards as a hobby. During the current year, he acquired twenty-five different items at a total cost of $29,550. During the year, he sold each of those items and received total proceeds of $55,900. What is the effect of these transactions on Jerry's Net Income For Tax Purposes?

   A. Jerry has a taxable capital gain of $26,350.
   B. Jerry has a taxable capital gain of 13,175.
   C. Jerry has business income of $26,350.
   D. Because the collection was a hobby, the gain does not have to be included in Net Income For Tax Purposes.

4. Which of the following is correct?

   A. In determining whether a disposition is capital or business in nature, the number and frequency of transactions is taken into account.
   B. A taxpayer must include 50 percent of both business income and capital gains in their Taxable Income.
   C. Amounts collected under an insurance policy are considered capital gains.
   D. The sale of a depreciable asset can result in a capital gain or capital loss.

Inclusions And Reserves

5. A business may sometimes receive amounts of cash for goods or services to be delivered in a future taxation year. Under the requirements of the *Income Tax Act*, these amounts should be:

   A. included in income when the goods or services are delivered.
   B. included in income no later than 180 days after the end of the taxation year.
   C. allocated to income over the period between the time the cash is received and the time the goods and services are delivered.
   D. included in income when the cash is received.

6. In 2009, Marg's Antiques deducted a reserve for doubtful debts of $12,000. During 2010, she had actual write-offs of $12,500 and recoveries of previously written off debts of $1,500. At the end of 2010, she deducted a reserve for doubtful debts of $14,000. Marg's 2010 net deduction for bad debts would be:

   A. $12,500.
   B. $11,000.
   C. $13,000.
   D. $14,000.

7. Ed's Appliances Ltd (Ed's) sold a furnace to a customer in October, 2010 for $10,000. The mark-up on the cost of the furnace was 100 percent. The customer paid 20 percent of the purchase price on delivery, with the remainder of the purchase price due in March 2011. What is the maximum reserve Ed's can claim for tax purposes for its November 30, 2010 year end?

   A. $2,000.
   B. $4,000.
   C. $6,000.
   D. $8,000.
   E. None of the above.

Limitations On Deductions

8. For income tax purposes, X Co. can deduct life insurance premiums paid providing:

   A. The life insurance policy is required as security on a loan from a financial institution.
   B. The interest payable on the loan for which the life insurance is required is deductible by X Co. for tax purposes.
   C. The premium paid is for the president of X Co.
   D. Both A and B.
   E. All of A, B, and C.

9. Maxine is the proprietor of a home based business. She paid $25,000 to her editorial assistant, $8,000 to her son as her computer technician, and $32,000 to herself as salary. How much can she deduct as a business expense on her income tax return?

   A. Nil.
   B. $25,000.
   C. $33,000.
   D. $65,000.

10. Jon Bogen operates a consulting business out of a dedicated space in his home. It is his principal place of business. With respect to the items that he can deduct, which of the following statements is correct?

   A. Jon can only deduct a pro rata share of operating costs and utilities.
   B. Jon can only deduct a pro rata share of operating costs, utilities, and property taxes.
   C. Jon can only deduct a pro rata share of operating costs, utilities, property taxes, and mortgage interest.
   D. Jon can deduct a pro rata share of operating costs, utilities, property taxes, mortgage interest and CCA.

11. Jean Brochet uses an automobile in his unincorporated business. It cost $53,000 in 2009, with maximum CCA being deducted in that year. The purchase was financed with a bank loan of $37,000. For 2010, the interest on this loan was $4,440. The automobile is used exclusively for business purposes, with the 2010 operating costs totaling $7,500. In determining his 2010 business income, his maximum automobile related deduction will be:

    A. $18,800.
    B. $19,590.
    C. $24,665
    D. $20,150

Specific Deductions

12. For tax purposes, the cost of the end of period inventory can be determined in a variety of ways. Which of the following approaches cannot be used?

    A. Last-In, First-Out.
    B. First-In, First-Out.
    C. Specific Identification.
    D. Average Cost.

13. Which of the following items is not deductible in calculating net business income for the current taxation year?

    A. An $11,000 legal fee paid for services rendered in conjunction with a new issue of the company's common stock.
    B. A $125,000 management bonus paid 125 days after the end of the corporation's current taxation year.
    C. An amount of $25,000 paid for planting large maple trees in various locations on the grounds of the company's facilities.
    D. A $10,000 contribution to a company pension fund.

14. Widget Production Ltd. has a fiscal year end of June 30. In February 2008, the Company borrowed $750,000 to fund an expansion. The Company paid $21,000 to obtain this financing. In January 2009, the Company repaid $250,000 of the principal and in June 2010, it repaid the remaining $500,000. All repayments were made from cash flow from operations. For tax purposes, which one of the following schedule of claims represents the **most** rapid method of claiming the costs of obtaining this financing.

    A. $4,200 in each of fiscal 2008 through 2012.
    B. $4,200 in each of 2008 and 2009, and the remaining $12,600 in 2010.
    C. $4,200 in 2008, $8,400 in 2009, and $8,400 in 2010.
    D. $7,000 in 2009 and $14,000 in 2010.

15. In fiscal year 2009, ABC Ltd. acquired raw land for $150,000. The shareholders had been advised that this land would soon be approved for commercial development, causing it to increase in value significantly, and they had hoped to sell it within the next 12 months for a large profit. The Company rented the land for the whole of 2009 to a farmer as pasture, for an annual rent of $1,000. It also paid $300 in property taxes and $4,000 in interest on funds borrowed to purchase the land. In 2009, it also incurred $800 in legal fees defending itself against a lawsuit brought by its tenant. Unfortunately for the Company, the efforts of an environmental group lobbying against the development plans were successful. ABC sold the property for $125,000 in early 2010, when it became clear that development would not be permitted.

    Calculate the Net Income (Loss) For Tax Purposes to be reported for each of 2009 and 2010 resulting from the transactions described above.

	2009	2010
A.	$0 income	$29,100 loss
B.	$200 income	$29,300 loss
C.	$800 loss	$28,300 loss
D.	$4,100 loss	$25,000 loss

16. Quality Homes Ltd. (Quality) has a December 31, 2010 year end. The controller has calculated the Company's 2010 income as $50,000. However, in arriving at this amount, the controller deducted $30,000 of salary to an employee who is the sole shareholder of the Company and $5,000 of salary to an arm's length employee. Both of these amounts were paid on June 30, 2011. Which one of the following represents Quality's 2010 Net Income For Tax Purposes?

    A. $50,000.
    B. $55,000.
    C. $80,000.
    D. $85,000.

TIF PROBLEM SIX - 4
Business Income - Exam Exercises

Exam Exercise Six - 1 (Capital Gains Identification)
During 2010, William Lemay acquired a six unit apartment building for $315,000 with the intention of operating it as a rental property. Three weeks after his purchase, he received an unexpected offer to purchase the building for $387,000. He accepts the offer. Should the $72,000 be treated as a capital gain or as business income? Justify your conclusion.

Exam Exercise Six - 2 (Bad Debts)
At the end of 2009, Barton's Books has ending accounts receivable of $87,500. Of this amount, it is estimated that $3,400 would prove uncollectible. A reserve for tax purposes is deducted for this amount. During 2010, $3,600 of accounts receivable are written off. At the end of 2010, accounts receivable total $103,200, with $4,100 of this amount expected to be uncollectible. By what amount will the 2010 net business income of Barton's Books be increased or decreased by the preceding information with respect to bad debts?

Exam Exercise Six - 3 (Bad Debts And Undelivered Services)
Frank's Auto Body, an unincorporated business, keeps its records on a cash basis. During 2010, its first year of operation, the business has cash sales of $71,200. At the end of the year, an additional $22,450 of revenues was receivable. Of the amounts received, $7,100 was for services to be delivered during 2011. Frank estimates that $650 of the end of year receivable amounts will be uncollectible. By what amount will the 2010 net business income of Frank's Auto Body be increased by the preceding information?

Exam Exercise Six - 4 (Reserve For Unpaid Amounts)
During February, 2010, Jacob's Jewels sells a broach for $428,000. The cost to the business of this necklace was $212,000, resulting in a gross profit of $216,000. The $428,000 sales price is to be paid in four equal annual instalments on December 31 in each of the years 2011 through 2014. Jacob's Jewels has a December 31 year end. Indicate the amount of the reserve that can be deducted, and the net business income, for each of the years 2010 through 2014.

Exam Exercise Six - 5 (Interest In Thin Capitalizations)
On January 1, 2009, a new Canadian corporation is created by issuing $9,100,000 in debt securities and $2,100,000 in common shares. The debt securities pay interest at 7 percent. The new corporation will use December 31 as its year end. At the time the corporation is formed, Mr. Phillip Roundtree, who is a resident of England, acquires $5,250,000 of the debt securities and 29 percent of the common shares. On January 1, 2010 the Retained Earnings balance of the corporation is $750,000. How much, if any, of the interest paid in 2010 on Mr. Roundtree's holding of debt securities would be disallowed under the thin capitalization rules in ITA 18(4)?

Exam Exercise Six - 6 (Home Office Costs)

During 2010, Janice Teason has the following costs related to her principal residence:

Utilities	$3,200
Maintenance And Repairs	3,800
Telephone:	
Monthly Charge	480
Personal Long Distance Charges	275
Employment/Business Related Long Distance Charges	780
Supplies	675
Property Taxes	6,400
House Insurance	1,800
Interest On Mortgage	6,200

Ms. Teason estimates that she uses 30 percent of the residence for employment/business related purposes. Maximum CCA on 100 percent of the house would be $15,000. Determine the maximum deduction that would be available to Ms. Teason assuming:

A. She is an employee with $80,000 in income (no commissions).
B. She is an employee with $80,000 in commission income
C. She is self-employed and earning $80,000 in business income.

Exam Exercise Six - 7 (Automobile Ownership Costs)

Mr. Alex Roddle acquires an automobile to be used 100 percent of the time in his unincorporated business. This business has been in operation for several years. The purchase occurs on October 1, 2010 at a cost of $83,000. He finances $70,000 of the car purchase through his bank at an annual rate of 9 percent. Interest charges for the period October 1, 2010 through December 31, 2010 amount to $1,575. What amounts can Mr. Roddle deduct in his 2010 tax return with respect to this acquisition? Ignore GST and PST considerations.

Exam Exercise Six - 8 (Automobile Leasing Costs)

On November 1, 2010, Ms. Sherry Boland leases an automobile to be used 100 percent of the time in her unincorporated business. The lease cost is $862 per month, and a total of $1,724 was paid for the year. The manufacturer's suggested list price for the automobile is $53,000. Ms. Boland makes no down payment and no refundable deposits. Determine the maximum lease payment that she can deduct for 2010. Ignore GST and PST considerations.

Exam Exercise Six - 9 (Leases: Tax Vs. GAAP)

Sharp Ltd. signs an 8 year lease for an asset with an economic life of 9 years. The lease payments are $32,500 per year. Compare the tax treatment of the lease with its treatment under GAAP.

Exam Exercise Six - 10 (Farm Losses)

Ms. Janine Futon teaches ethics at a Canadian university on a full time basis. Because of her firm belief in the medical benefits of marijuana, she has owned and managed an operation which farms this product in a rural location near her home. While she is aware that her farming operation is of questionable legality, her background in ethics compels her to report her income from this operation in her tax return. While in most years the operation has reported a profit, her current year operations show a loss of $13,250. How much of this loss is deductible in calculating her current year's Net Income For Tax Purposes? Explain your conclusion.

Exam Exercise Six - 11 (Professional Income)

Ms. Joan Vickers is an accountant and, at the beginning of the current year, she had unbilled work in process of $41,400, as well as uncollected billings of $48,700. During the year, she bills the remaining work in process and collects all of these new receivables, as well as the uncollected amounts that were present at the beginning of the year. Her work during the year totals potential billings of $206,350. Of this amount, $171,300 has been billed and $152,100 of these billings have been collected. Calculate her inclusion in net business income for the year using:

- the cash basis;
- the billed basis; and
- accrual accounting.

Exam Exercise Six - 12 (ITA 22 Election)

Mr. Brian Brock is selling his unincorporated business during 2010. Included in his assets are accounts receivable with a face value of $87,560. He and the purchaser of the business have agreed that the net realizable value of these receivables is $82,150. In 2009, he deducted a reserve for bad debts of $4,800. Determine the tax effect of selling these receivables for Mr. Brock, provided that he and the purchaser jointly elect under ITA 22.

TIF PROBLEM SIX - 5
Business Income - Key Term Matching

The following five key terms were listed at the end of Chapter 6, "Income Or Loss From A Business".

A. Hobby Farmer

B. Reserve

C. Billed Basis

D. Thin Capitalization

E. Business Income

The following list contains 10 potential definitions for the preceding key terms.
NOTE There is only **ONE** correct definition for each key term.

1. A reference to situations where a non-resident specified shareholder is receiving interest on an amount of debt that exceeds two times the sum of his share of contributed capital plus 100 percent of Retained Earnings.

2. Income that is earned through active business activity. This would include amounts earned by producing goods, selling goods or services, or selling capital assets.

3. A method of determining net business income based on recording inclusions when the relevant amounts are billed. Can be used by all individuals reporting professional income.

4. A deduction in the calculation of net business income or net taxable capital gains.

5. An amount of resources set aside to provide for future obligations.

6. A part-time farmer who does not have a reasonable expectation of profit.

7. A corporate capital structure in which the amount of owners' capital is "thin" when compared to the amount of debt.

8. A method of determining net business income based on recording inclusions when the relevant amounts are billed. Can only be used by certain specified types of professionals.

9. Income that is earned through active business activity. This would include amounts earned by producing goods, selling goods or services, or delivering services.

10. A farmer who operates a farm as a hobby, but has a reasonable expectation of making a profit.

Required: For each of the five key terms listed, indicate the number of the item that provides the **BEST** definition of that term. As only one definition is completely correct, please indicate only one number for each key term. No marks will be awarded if you indicate more than one number for any key term.

TIF PROBLEM SIX - 6
Computation Of Business Income

The condensed before tax Income Statement for Swindex Incorporated for the year ending December 31, 2010, prepared from information included in its financial statements, is as follows:

Sales	$3,000,000
Cost Of Sales	(1,570,000)
Gross Margin	$1,430,000
Other Expenses (Not Including Taxes)	(755,000)
Operating Income Before Taxes	$ 675,000
Other Income And Losses	275,000
Income Before Taxes	$ 950,000

Other Information:

1. During the year, the Company spent $5,200 for landscaping its head office grounds. For accounting purposes this was treated as a capital expenditure, but was not amortized during the current year.

2. The Other Expenses (Not Including Taxes) account included the following amounts:

Bond discount amortization	$ 500
Interest on deficient corporate tax instalments	1,700
Reserve for inventory declines	96,300
Interest paid on bonds issued	22,000
Amortization expense	36,500
Cost of advertising in magazine distributed only in Jamaica	22,000
Charitable donations	19,100
Cost of sponsoring local hockey teams	3,200
Cost of advertising circulars (One-half have been distributed)	15,000

3. The Other Income And Losses account contains the following items:

Damages paid for breach of contract	$18,000
Loss from theft	2,800
Cost of appraisal of property to be sold	3,800

Required: Using the preceding information, calculate Swindex Incorporated's Net Income For Tax Purposes for the year ending December 31, 2010. In preparing your solution, ignore any deductions associated with depreciable assets or eligible capital property. In addition, provide reasons for any items that were excluded from your calculations.

TIF PROBLEM SIX - 7
Computation Of Business Income

Astrolab Industries has a taxation year that ends on December 31. For the year ending December 31, 2010, the Company's accounting statements prepared in accordance with generally accepted accounting principles showed a Net Income of $278,000. The accountant has provided the following other information that was used in the preparation of this Net Income figure:

1. A total of $123,000 was deducted as income tax expense. This amount included $16,000 in future income taxes.
2. As the Company was late in making its required income tax instalments, it was required to pay interest of $400.
3. For the year ending December 31, 2010, the Company recorded $83,000 in amortization expense. Maximum available CCA deductions for this period were $97,000.
4. The Company's accounting expenses included a payment of dues in a local golf club of $2,500. The cost of entertaining clients at this club during the year ending December 31, 2010 was $9,600.
5. For accounting purposes, no allowance for bad debts was established at either the beginning or the end of 2010. The $5,200 bad debt expense that was included in the accounting records reflected only the amounts that were written off during the year. For tax purposes, the Company deducted a reserve of $3,400 for the taxation year ending December 31, 2009. An appropriate reserve for the year ending December 31, 2010 would be $4,200.
6. The 2010 accounting expenses include $1,500 for the premiums on a life insurance policy on the life of the Company's president. The Company is the beneficiary of this policy. One of the Company's major creditors requires that this policy be in force during all periods in which there are loan balances outstanding.
7. The 2010 accounting expenses included $37,000 in bonuses that were declared in favour of Company executives. Only $12,000 of these bonuses were paid in 2010, with the balance being payable in February, 2011.
8. The bond interest expense that is included in the accounting records includes $3,200 in discount amortization.
9. On December 31, 2010, the Company paid landscaping costs of $27,000. These costs were treated as capital expenditures for accounting purposes and, as the expenditure was made at the end of the year, no amortization was recorded in the 2010 financial statements.

Required: For each of the preceding items, indicate the appropriate treatment in the tax records of Astrolab Industries Ltd. for the year ending December 31, 2010. For those items that require adjustments of accounting Net Income in order to arrive at Net Income For Tax Purposes, indicate the specific adjustment that would be required. The calculation of Net Income For Tax Purposes is not required.

TIF PROBLEM SIX - 8
Computation Of Business Income With CCA and CEC

For the year ending December 31, 2010, the Income Statement of Markham Ltd., prepared in accordance with generally accepted accounting principles, is as follows:

Revenues		$973,000
Expenses:		
Cost Of Goods Sold	$272,000	
Selling And Administrative Costs	132,000	
Amortization Expense	156,000	
Other Expenses	137,000	(697,000)
Income Before Tax Expense		$276,000
Income Tax Expense:		
Current	($ 97,000)	
Future	(32,000)	(129,000)
Net Income		$147,000

Other Information:

1. The Company spent $6,000 during the year on landscaping for its new building. For accounting purposes this was treated as an asset. The Company will not amortize this balance as it believes the work has an unlimited life.
2. Selling And Administrative Costs include $15,000 in business meals and entertainment.
3. Other Expenses include contributions to registered charities of $3,700.
4. As the Company expects to issue more shares during 2011, it made a number of amendments to its articles of incorporation and included the legal costs in Other Expenses. These costs totalled $6,000.
5. During 2009, Markham Ltd. acquired a competing business at a price that included goodwill of $70,000. For accounting purposes, there is no impairment or write-down of the goodwill purchased in either year.
6. Other Expenses includes bond discount amortization of $2,500.
7. Selling And Administrative Costs include membership fees for several employees in a local golf and country club. These fees total $3,400.
8. On January 1, 2010, the Company had the following UCC balances:

Class 1	$400,000
Class 8	575,000
Class 10	45,000
Class 13	68,000

The Class 1 balance relates to a single building acquired in 2000 at a cost of $550,000. It is estimated that the value of the land at this time was $50,000. On February 1, 2010, this building is sold for $612,000. It is estimated that the value of the land is unchanged at $50,000. In the accounting records, this real property was carried at $507,000, $457,000 for the building and $50,000 for the land. The resulting gain on the building is included in the accounting revenues.

The old building is replaced on February 15, 2010 with a new building acquired at a cost of $683,000 of which $60,000 is allocated to land. The Company chose not to put the new building into a separate Class 1 so it does not qualify for the 6 percent CCA rate. No elections are made with respect to the replacement of the building.

There are no dispositions of Class 8 assets during the year. However, there are acquisitions in the total amount of $126,000.

As the Company has decided to lease all of its vehicles in the future, all of the assets in Class 10 are sold during the year. The capital cost of these assets was $93,000 and the proceeds of disposition amounted to $37,000. The net book value of these assets was $52,000 and the resulting accounting loss of $15,000 was included in Other Expenses.

The Class 13 balance relates to a single lease that commenced on January 1, 2008. The lease has an initial term of seven years, with two successive options to renew for three years each. Expenditures on this leasehold were $50,000 in 2008 and $27,000 in 2009. There were no further expenditures in 2010. The write-off of these expenditures for accounting purposes is included in Amortization Expense.

9. Other Expenses includes interest on late income tax instalments of $500 and on late municipal tax payments of $275.
10. Markham Ltd. deducts maximum CCA.

Required: Determine Markham Ltd.'s 2010 minimum Net Income For Tax Purposes. In addition, calculate the January 1, 2011 UCC for each CCA class. Indicate why you have excluded some items from your calculations.

TIF PROBLEM SIX - 9
Computation Of Business Income With CCA and CEC

For the taxation year ending December 31, 2010, Voxit Inc. recorded Net Income of $565,000. This amount was determined under generally accepted accounting principles.

Other Information:

1. The following items were deducted (added) during the year:

Current Income Tax Expense	$210,000
Future Income Tax Benefit	(23,000)
Interest Expense (Includes $3,500 In Discount Amortization)	22,000
Interest On Deficient Corporate Tax Instalments	1,250
Reserve For Inventory Declines	12,600
Amortization Expense	51,500
Charitable Donations	14,500
Cost Of Sponsoring Local Soccer Team	4,600
Loss From Employee Theft	5,200
Loss On The Sale Of Vehicles	36,200
Cost Of Appraisal Of Property To Be Sold	2,600

2. On January 1, 2010, the Company has the following UCC balances:

Class 1 (All Assets Acquired in 2005)	$325,236
Class 8	226,964
Class 10	87,468
Class 13	29,322

During the year ending December 31, 2010, the Company acquired furniture and fixtures at a cost of $262,000. Furniture and fixtures with a cost of $275,000 and a fair market value of $189,000 were traded in on the new assets.

The balance in Class 10 reflects the Company's fleet of delivery vehicles. In the accounting records, their net book value was $92,700. During the year ending December 31, 2010, all of these vehicles were sold and replaced with leased vehicles. The sale proceeds amounted to $56,500, with the amount received for each vehicle being less than its cost.

The Class 13 assets relate to a lease that was signed on January 1, 2006. At that time, the cost of the improvements on the leased property was $36,400. The basic term of the lease is 10 years and there are two 4 year renewal options.

Until July, 2010, all the computer equipment was leased. During July, 2010, computer equipment and systems software was purchased for $20,000.

3. On January 1, 2010, the Company had no CEC balance. On that date, the Company sold one of its divisions. The sale proceeds included a payment for internally generated goodwill of $43,000.

On December 31, 2010, the Company acquired an unincorporated business. The purchase price included a $55,000 payment for goodwill. As the acquisition was late in the year, none of the acquired assets were amortized for accounting purposes.

Required: Using the preceding information, calculate Voxit Inc.'s minimum Net Income For Tax Purposes for the year ending December 31, 2010.

Chapter Seven Test Item File Problems

TIF PROBLEM SEVEN - 1
Property Income - Essay Questions

1. The tax rules for recognizing interest inclusions are different for individuals than they are for corporations. Briefly describe these differences.

2. GAAP requires that any premium that is received on the issuance of debt securities be amortized as an adjustment of interest expense over the life of the debt. Explain briefly the tax treatment of premium that is received on the issuance of debt securities.

3. Briefly explain the tax treatment of corporate bonds that are issued at a discount.

4. One of your friends has acquired a zero coupon bond at a cost of $9,016. While no interest will be paid on the bond, he will receive $12,000 at the end of three years. He is particularly pleased with this investment as he believes that the entire difference between its cost and its maturity value will be taxed as a capital gain when he receives the maturity value of $12,000. Is he correct? If not, explain how you believe this bond will be taxed.

5. Briefly describe the disappearing source rules.

6. Each rental property that is owned by an individual that has a cost in excess of $50,000 must be placed in a separate CCA class. What is the objective of this requirement?

7. When an investor receives a payment, what characteristics determine whether it is an interest payment or a dividend payment?

8. Briefly explain the concept of integration.

9. Briefly describe the application of the 2010 federal gross up and tax credit procedures for (1) eligible dividends and (2) non-eligible dividends.

10. How is the adjusted cost base of units in an income trust determined?

TIF PROBLEM SEVEN - 2
Property Income - True Or False

1. Corporations must use the full accrual approach to recognize interest inclusions.

   True or False?

2. For tax purposes, neither premium nor discount on long-term debt is ever amortized by the issuer as an adjustment of interest expense.

   True or False?

3. In considering whether interest will be deductible, the direct use of the borrowed money is the relevant consideration.

   True or False?

4. Interest on debt incurred to acquire equity securities is only deductible if the securities have a history of paying regular dividends.

   True or False?

5. An individual purchased a warehouse as an investment property two years ago. During the current year, he received rents of $8,000 and paid the following expenses; interest of $6,000, property taxes of $2,000, heat, light and power of $500, and maintenance of $300. The UCC of this Class 1 asset was $60,000 on January 1 of the current year. He cannot claim a rental loss in the current year.

   True or False?

6. The federal dividend tax credit for eligible dividends can be expressed as 10/17 of the gross up, 25.88 percent of dividends received, or 17.97 percent of grossed up dividends.

   True or False?

7. When the holder of income trust units receives a distribution that contains a return of capital, the amount of the return of capital must be added to the adjusted cost base of the units.

   True or False?

8. Mutual funds can be organized as either corporations or trusts.

   True or False?

9. For tax purposes, stock dividends must be treated in exactly the same manner as cash dividends.

   True or False?

10. When foreign tax authorities withhold taxes on the foreign source income of a Canadian resident, only the net amount received will be included in the Net Income For Tax Purposes of the Canadian resident.

    True or False?

TIF PROBLEM SEVEN - 3
Property Income - Multiple Choice

Interest

1. A taxpayer loaned $20,000 for one year to his mother-in-law on October 1, 2008. Interest at 6 percent per year was payable on September 30, 2009, but was not paid until February 1, 2010. There are several ways in which the interest can be allocated to the years involved. For the following parts of the question, indicate which method corresponds to the interest allocation if it is a method that is permitted by the ITA. If it is not a permitted method, indicate the answer E.

   A. Accrual Method
   B. Cash Method
   C. Compound Interest Method
   D. Receivable Method
   E. Not Allowed Method

   i. Income for 2008 is $300, 2009 income is $900, and 2010 income is nil.

   ii. Income for 2008 is nil, 2009 income is $1,200, and 2010 income is nil.

   iii. Income for 2008 is nil, 2009 income is $900, and 2010 income is $300.

   iv. Income for 2008 is nil, 2009 income is nil, and 2010 income is $1,200.

2. A corporation issues debt with a maturity value of $1,000,000 for proceeds of $900,000. The debt matures in 10 years and pays annual interest at a rate of 10 percent. Which of the following statements is correct?

   A. The corporation will be able to deduct interest of $110,000 in each of the years 1 through 10.
   B. The corporation will be able to deduct interest of $100,000 in each of the years 1 through 10 and will have a fully deductible loss of $100,000 in year 10.
   C. The corporation will be able to deduct interest of $100,000 in each of the years 1 through 10 and will have a capital loss in year 10 of $100,000, only one-half of which will be deductible.
   D. The corporation will be able to deduct interest of $90,000 in each of the years 1 through 10.

3. A corporation issues debt with a maturity value of $1,000,000 for proceeds of $1,100,000. The debt matures in 10 years and pays annual interest at a rate of 10 percent. The issuer is not a money lender and there is no evidence that there was a deliberate creation of a premium. Which of the following statements is correct?

   A. The corporation will be able to deduct interest of $90,000 in each of the years 1 through 10.
   B. The corporation will be able to deduct interest of $100,000 in each of the years 1 through 10 and will have a fully taxable gain of $100,000 in year 10.
   C. The corporation will be able to deduct interest of $100,000 in each of the years 1 through 10 and will have a capital gain in year 10 of $100,000, only one-half of which will be taxable.
   D. The corporation will be able to deduct interest of $100,000 in each of the years 1 through 10 and there will be no tax consequences at maturity.

TIF Problem Seven - 3

Property Income - Multiple Choice

4. Which of the following is not a characteristic of interest?

   A. It must represent compensation for use of a principal amount.
   B. It must accrue continuously over time.
   C. It must be paid on a regular, periodic basis.
   D. It must be calculated with reference to a principal amount.

5. On July 1, 2010, Jon Laxtor acquires an investment contract with a maturity value of $100,000. It matures on June 30, 2015, with interest accruing at 8 percent per annum. Interest is paid for the first one and one-half years on December 31, 2011. The remaining interest will be paid at maturity. With respect to the minimum amount of interest that Jon must recognize for tax purposes, which of the following statements is correct?

   A. Jon will have to recognize $4,000 in 2010 and $8,000 in 2011.
   B. Jon will have to recognize nil in 2010 and $8,000 in 2011.
   C. Jon will have to recognize nil in 2010 and nil in 2011.
   D. Jon will have to recognize nil in 2010 and $12,000 in 2011.

Rental Income

6. Saul has two residential rental properties that are mortgaged. Both properties are in Class 1 with a maximum CCA rate of 4 percent. At the beginning of the year, Property A has a UCC of $500,000 and Property B has a UCC of $1,100,000. Before consideration of CCA, Property A earned net rental income of $43,000, and Property B had a net rental loss of $27,000. What is the maximum amount of CCA Saul will be able to claim this year?

   A. Nil.
   B. $16,000.
   C. $20,000.
   D. $44,000.

Dividends

7. Sherry is in the top federal tax bracket of 29 percent. She lives in a province where her provincial marginal tax rate is 17.5 percent and the provincial dividend tax credit is 31 percent of the dividend gross up. If Sherry receives an eligible dividend of $16,000 from a Canadian public corporation in 2010, how much will she have left after tax?

   A. $ 4,390.
   B. $10,607.
   C. $11,610.
   D. $12,326.

8. Martin held 2 percent of the outstanding shares of a Canadian public corporation. The corporation issued an eligible stock dividend in 2010 and capitalized $800,000 of its retained earnings. By how much will Martin's Taxable Income increase as a result of the dividend?

   A. $ 8,000.
   B. $16,000.
   C. $20,000.
   D. $23,040.

Income Trusts

9. On January 1, 2010, John Traverse acquires 12,000 units of the RV Income Trust at a cost of $720,000. During 2010, the trust makes a distribution of $5.00 per unit. Of this total $1.50 is a return of capital while the remaining $3.50 is ordinary income. John reinvests the total distribution in RV units at a cost of $55 per unit. What is the adjusted cost base of John's units on December 31, 2010?

   A. $58.21 per unit.
   B. $53.62 per unit.
   C. $59.58 per unit.
   D. $60.00 per unit.

Foreign Source Income

10. Ravinder, an individual whose other income places him in the maximum 29 percent federal tax bracket, has a foreign investment that earns $50,000 (Canadian) of non-business income. The government of the foreign country withholds $10,000 of this amount, with the remaining $40,000 being remitted to Ravinder during 2010. By what amount will Ravinder's 2010 Federal Tax Payable increase as a result of this transaction?

   A. $ 4,500.
   B. $ 6,275.
   C. $11,600.
   C. $14,500.

TIF PROBLEM SEVEN - 4
Property Income - Exam Exercises

Exam Exercise Seven - 1 (Discount Bonds)

On January 1, 2010, Latkin Inc. issues bonds with a maturity value of $1,250,000 and a maturity date of December 31, 2015. The bonds pay interest on December 31 of each year at an annual coupon rate of 2 percent. They are sold for proceeds of $1,150,000 for an effective yield of 3.5 percent. The maturity amount is paid on December 31, 2015. What are the tax consequences related to this bond issue for Latkin Inc. in each of the years 2010 through 2015? How would these tax consequences differ from the information included in Latkin's GAAP based financial statements? Latkin Inc. uses the straight-line method to amortize the discount on the bonds. In order to simplify your solution, assume that the straight-line amortization of discount is acceptable under GAAP (it is not).

Exam Exercise Seven - 2 (Premium Bonds)

On January 1 of the current year, Dryer Inc. issues 8 year bonds payable with a maturity value of $1,500,000. The bonds have a coupon rate of 14 percent, pay interest on January 1 of each year, and are sold for $1,750,000. The Company has a December 31 year end. Determine the current year tax consequences under each of the following assumptions:

- Dryer is in the business of lending money.
- Dryer is not in the business of lending money and the CRA does not believe that they made a deliberate effort to create a premium on the issuance of the bonds.
- Dryer is not in the business of lending money and the CRA believes that they made a deliberate effort to create a premium on the issuance of the bonds.

Exam Exercise Seven - 3 (Annual Accrual Rules)

On June 1, 2010, Mr. Michael Leiner acquires a newly issued debt instrument with a maturity value of $80,000. It matures on May 31, 2016 and pays interest at an annual rate of 7 percent. Payment for the first three and one-quarter years of interest is due on August 31, 2013, with interest for the remaining two and three-quarters years payable on the maturity date. What amount of interest will Mr. Leiner have to include in his tax returns for each of the years 2010 through 2016?

Exam Exercise Seven - 4 (Prescribed Debt Obligations)

On January 1, 2010, a debt obligation is issued with a coupon interest rate of 10 percent, a maturity value of $275,000, and a maturity date of December 31, 2012. Interest is paid on December 31 of each year. The interest coupons and the maturity amount are sold separately at prices that provide an effective yield of 10 percent. The price of the maturity payment is $206,612, while the price of the interest coupons is $68,388. Calculate the amount of interest that the purchasers of these two financial instruments will have to include in their tax returns in each of the three years 2010, 2011, and 2012.

Exam Exercise Seven - 5 (Accrued Interest At Transfer)

On May 1, 2010, Mrs. Anna White purchases bonds with a face value of $40,000. These bonds pay semi-annual interest of $2,000 on June 30 and December 31 of each year. She purchases the bonds for $41,333, including interest accrued to the purchase date. She holds the bonds for the remainder of the year, receiving both the June 30 and December 31 interest payments. What amount of interest will be included in Mrs. White's 2010 tax return?

Exam Exercise Seven - 6 (Rental Income)

Alex Bodvin acquires a residential rental property in June, 2010 at a total cost of $423,000. Of this total, $132,000 can be allocated to the value of the land. He immediately spends $42,000 to make major improvements to the property. Rents for the year total $32,000, while rental expenses other than CCA total $27,500. This is the only rental property owned by Mr. Bodvin. Determine the maximum CCA that is available for 2010 on the rental property. Indicate how much of this Mr. Bodvin can deduct in calculating his 2010 net rental income.

Exam Exercise Seven - 7 (Non-Eligible Dividend Income)

During 2010, Ms. Marion Blatz receives $5,600 in non-eligible dividends from taxable Canadian corporations. Her income is such that this additional amount will be taxed at a 22 percent federal rate and a 10 percent provincial rate. On such non-eligible dividends, the province has a dividend tax credit equal to 38 percent of the gross up. Determine the total federal and provincial tax that will be payable on these dividends and her after tax retention.

Exam Exercise Seven - 8 (Eligible Dividend Income)

During 2010, Mr. Franz Schlitz receives $23,500 in eligible dividends from Canadian public corporations. His income is such that this additional amount will be taxed at a 29 percent federal rate and a 14 percent provincial rate. On eligible dividends, the province has a dividend tax credit equal to 25 percent of the gross up. Determine the total federal and provincial tax that will be payable on these dividends and his after tax retention.

Exam Exercise Seven - 9 (Mutual Fund Distributions)

John Bordy owns 2,200 units of the DRC Growth Fund. These units were purchased at a price of $8.15 per unit, for a total value of $17,930. His adjusted cost base for these units has not changed since their acquisition. On December 12 of the current year, the Fund has a distribution of $0.27 per unit, resulting in a reinvestment of $594 in John's account. At this time, the purchase price per unit is $10.40. What will be his adjusted cost base per unit after the reinvestment?

Exam Exercise Seven - 10 (Foreign Source Income)

Isaac Lemming has foreign investments that earn $27,000 in income during the current year. As the foreign jurisdiction withholds 22 percent of such income, he only receives $21,060. He has other income such that this foreign source income will be taxed at the maximum federal rate of 29 percent. Determine the amount by which this foreign income would increase Isaac's Taxable Income and federal Tax Payable, assuming that:

A. the foreign source income is non-business income.
B. the foreign source income is business income.

TIF PROBLEM SEVEN - 5
Property Income - Key Term Matching

The following five key terms are listed at the end of Chapter 6, "Property Income".

A. Stock Dividend

B. Dividend Gross Up

C. Foreign Taxes Paid Credit

D. Capital Dividend

E. Eligible Dividends

The following list contains 10 potential definitions for the preceding key terms:
NOTE There is only **ONE** correct definition for each key term.

1. A dividend that is eligible to receive a federal dividend tax credit of either 25 percent of the gross up or, alternatively, 10/17 of the gross up.

2. A credit against Tax Payable based on taxes withheld by a foreign taxing authority on foreign source income.

3. A dividend paid out of the taxable portion of capital gains earned by the corporation. It will be taxed as a capital gain in the hands of the recipient.

4. Dividends that have been designated by the payor as eligible for the enhanced 44 percent gross up and tax credit procedure.

5. A dividend paid in stock of another corporation.

6. A dividend paid out of a private corporation's capital dividend account. It is received on a tax free basis.

7. The 25 percent or 44 percent amount that must be added to dividends received from Canadian and foreign corporations before their inclusion in the Net Income For Tax Purposes of individuals.

8. A pro rata distribution of a corporation's shares to its existing shareholders.

9. A credit for foreign taxes paid on income earned in Canada by foreign corporations carrying on business in Canada.

10. The 25 percent or 44 percent amount that must be added to dividends received from taxable Canadian corporations before their inclusion in the Net Income For Tax Purposes of individuals.

Required: For each of the five key terms listed, indicate the number of the item that provides the **BEST** definition of that term. As only one definition is completely correct, please indicate only one number for each key term. No marks will be awarded if you indicate more than one number for any key term.

TIF PROBLEM SEVEN - 6
Property Income - Alternative Investment Strategies

Mr. Martin Forsythe, as the result of maintaining a modest lifestyle, has accumulated $582,000 in savings. The full amount of these savings is currently in a savings account where it earns a fairly nominal amount of interest. As the result of taking a basic finance course at a local college, he has become aware that better returns are available through making other types of investments. As a consequence, he intends to invest the full amount of his savings in some alternative investment as of January 1, 2010. He is considering the following alternatives:

- Investment of the full $582,000 in 12,000 shares of the common stock of a Canadian public company. The stock has been recommended by his broker and pays a regular annual eligible dividend of $2.25 per share. The stock, which is selling for $48.50 per share on January 1, 2010, is expected to increase in value to at least $49.50 per share by December 31, 2010, at which time he plans to sell the shares.
- Investment of the full $582,000 in a guaranteed investment certificate that will pay annual interest at the rate of 7 percent for the year ending December 31, 2010.
- Investment of the full $582,000 in a bond issued by a publicly traded Canadian company. The bond pays annual interest equal to 4 percent of the maturity amount on December 31 of each year. The bond matures on December 31, 2010, at which time the full maturity amount of $600,000 will be paid. The bond is selling at a discount because its annual interest rate is below the current market rate.

Mr. Forsythe has sufficient employment income that he is in the 29 percent federal tax bracket and the 13 percent provincial tax bracket. The provincial dividend tax credit on eligible dividends is equal to 38 percent of the gross up.

Required For each investment alternative, determine the amount that would have to be included in Mr. Forsythe's 2010 Taxable Income, the total amount of federal and provincial Tax Payable for 2010, and the amount of after tax cash that would be retained by Mr. Forsythe in 2010.

TIF PROBLEM SEVEN - 7
Income Trusts And Mutual Funds

On January 1, 2010, Mr. Irwin Mendez acquires the following investments:

- 2,500 units of the Pepcor Income Trust. The cost is $35.00 per unit for a total cost of $87,500.
- 3,500 units of the Pickett Global Fund, a mutual fund trust. The cost is $54.00 per unit for a total cost of $189,000.

During 2010, the Pepcor Income Trust makes an annual distribution of $2.75 per unit, of which $.75 is designated as a return of capital. The remaining $2.00 is ordinary income. Irwin has elected to use the Trust's DRIP and, as a consequence, the entire distribution is reinvested in new trust units at a cost of $36.00 per unit.

Also during 2010, the Pickett Global Fund makes a distribution of $4.50 per unit. This distribution is made up of capital gains of $2.00, eligible dividends of $1.75, and a return of capital of $0.75. The entire distribution is reinvested in Pickett Global Fund units at a cost of $50.00 per unit.

Irwin has other investment income that places him in the 29 percent federal tax bracket. Taxes on this income are sufficient to use all of his available tax credits before considering the effects of the two investments described above. He lives in a province where the maximum rate is 13 percent and the tax credit on eligible dividends is 24 percent of the gross up.

Required: Calculate the amount of Taxable Income and Tax Payable that will result from the distributions by the two trusts. In addition, indicate the per unit adjusted cost base for each of the trust units on December 31, 2010.

Chapter Eight Test Item File Problems

TIF PROBLEM EIGHT - 1
Capital Gains And Losses - Essay Questions

1. Capital gains have always been given very favourable tax treatment relative to interest income. What is the justification for this treatment?

2. What is a superficial loss? What is the required tax treatment for such losses?

3. Describe three different types of capital asset dispositions. In each case, indicate how the proceeds of disposition would be determined.

4. When a capital asset is sold and not all of the proceeds of disposition are received in the year of sale, the *Income Tax Act* allows a taxpayer to deduct a reserve. How is the maximum amount of this reserve determined?

5. When a taxpayer disposes of a combination of land and buildings, ITA 13(21.1)(a) contains a special rule for determining the amount of proceeds to be allocated to the building. This special rule will generally reduce the amount of the proceeds that will be allocated to the building. What is the tax policy objective of this special rule?

6. ITA 69 deals with non-arm's length transfers of capital property at values that are different from the fair market value of the property. Why would an individual wish to transfer a property to an adult child at a value that is below its fair market value? Briefly explain your conclusion.

7. An individual wishes to transfer several properties to related parties, some of whom are in higher tax brackets, some of whom are in lower tax brackets. What advice would you give this individual with respect to the consideration that he should take back in return for the property transferred?

8. What are the normal tax consequences, at the time of transfer, for an individual who is transferring property to a spouse or common-law partner? In these circumstances, at what value will the transfer be deemed to take place? Is there an election that can be used to alter these results? If so, briefly describe the election.

9. The replacement property rules cover both voluntary dispositions and involuntary dispositions. However, they are applied differently to the two types of dispositions. Briefly describe the differences between the treatment for voluntary dispositions and involuntary dispositions.

10. When the use of a capital property is changed from personal use to business use, there is a deemed disposition/reacquisition of that property. In those cases where the cost of the property is less than the fair market value of the property, the cost of the property for UCC purposes is limited to its cost, plus one-half of the difference between cost and fair market value. What is the reason for this limitation?

11. It is not uncommon for a person, when moving out of a principal residence, to retain that property as a rental unit. If no election is made, this change in use will be treated as a deemed disposition, possibly resulting in capital gains being assessed. Explain how this result can be avoided, as well as the tax consequences of making the required election.

12. Describe the tax treatment that will be given to personal use property dispositions. How does this treatment differ if the property is listed personal property?

13. In terms of tax planning, capital gains and losses have an advantage that is not available for other types of income. Briefly describe this advantage.

TIF PROBLEM EIGHT - 2
Capital Gains And Losses - True Or False

1. One of the reasons for the favourable tax treatment of capital gains is that the amounts received often have to be reinvested in the business in order to maintain its productive capacity.

True or False?

2. A superficial loss occurs when, in the 30 days following the disposition that resulted in the loss, an identical asset is acquired.

True or False?

3. Mr. Schmidt purchased 250 shares of Doss Limited on September 1, 2009 for $20 per share. On May 1, 2010, he purchased 100 more shares for $25 per share. On June 20, 2010, Mr. Schmidt sells 100 shares for $15 per share. His allowable capital loss on June 20, 2010 is $643.

True or False?

4. When there is a disposition of a capital asset and not all of the proceeds of disposition are collected at the time of disposition, a reserve can be deducted. In the year of the disposition, the reserve cannot be less than 80 percent of the total gain.

True or False?

5. A rollover is a term that is used to describe any transfer of assets between parties that are not dealing at arm's length.

True or False?

6. The term arm's length can apply to transactions involving trusts, corporations, and individuals.

True or False?

7. Johan Deroi has securities with an adjusted cost base of $1,000 and a fair market value of $1,500. If he sells these securities to his brother for $2,000, he will have a capital gain of $1,000.

True or False?

8. Martha Stuart has a depreciable asset with a UCC of $50,000, a capital cost of $80,000, and a fair market value of $100,000. If she gifts this property to her spouse without making any election, she will have a capital gain of $50,000.

True or False?

9. When there is an involuntary disposition of a depreciable asset, any resulting capital gain can be eliminated if the asset is replaced by an asset of equal or greater value, no later than the end of the second taxation year following the disposition.

True or False?

10. To be an eligible corporation for purposes of the deferral provisions on small business investments, more than 50 percent of the fair market value of its assets must be used to produce active business income in Canada.

True or False?

11. When there is a change in use, there will be a deemed disposition/reacquisition.

True or False?

12. When an individual emigrates from Canada, there is a deemed disposition of all of his capital property at fair market value.

True or False?

13. When an individual dies, there is a deemed disposition of all of his capital property at fair market value, without regard to his relationship to the beneficiary of his estate.

True or False?

14. At her death on August 1 of the current year, Nancy Mori owned stocks with an adjusted cost base of $11,000 and a fair market value of $20,000, and a term deposit of $30,000. She also owned a building that had a cost of $98,750, a fair market value of $110,000, and a UCC of $70,000.

    a. She bequeaths all of her assets to a spousal trust. Her Taxable Income at death arising from the dispositions is nil.

    True or False?

    b. She bequeaths all of her assets to her daughter, Christine. Nancy's Taxable Income at death arising from the dispositions totals $10,125.

    True or False?

    c. She bequeaths all of her assets to her daughter, Christine, who sells the building before the end of the current year for $125,000. Christine's Taxable Income arising from the sale is $7,500.

    True or False?

15. Capital gains on a principal residence are not taxable.

True or False?

16. Losses on the disposition of listed personal property can be deducted, but only against gains on the disposition of listed personal property.

True or False?

17. A dining room suite that had been purchased for $700 was sold during the year.

    a. The proceeds of disposition totalled $900. The capital gain on the transaction is $200.

    True or False?

    b. The proceeds of disposition totalled $500. The allowable capital loss on the transaction is $100.

    True or False?

    c. The proceeds of disposition totalled $1,500. The taxable capital gain on the transaction is $250.

    True or False?

TIF PROBLEM EIGHT - 3
Capital Gains And Losses - Multiple Choice

General Rules

1. The term proceeds of disposition can be used in a number of situations. Indicate which of the following would not be considered proceeds of disposition for the PD Company.

   A. Amounts paid to PD Company under insurance policies for property that has been damaged.
   B. Amounts paid to PD Company under insurance policies for property unlawfully taken.
   C. Amounts paid to PD Company by a municipal government for property that has been expropriated.
   D. Amounts paid to PD Company on the sale of inventories.
   E. Amounts paid to PD Company on the sale of a warehouse.

2. Which of the following is not included in ITA 53 as an adjustment to the cost base of an asset?

   A. Government assistance with the cost of acquisition.
   B. CCA taken in previous years.
   C. Superficial losses.
   D. In the case of vacant land, interest and property taxes.

Capital Gains Reserves

Question 3 And 4 Questions 3 and 4 are based on the following information:

BMP Products Ltd. (BMP) has been in operation for more than 20 years. Ten years ago, planning for future growth of its manufacturing facilities, BMP purchased a plot of land in an industrial area for $150,000. During the last couple of years, BMP has not met expectations. Business has fallen slightly and cash flows are tight. Due to the decrease in product demand, management does not believe that BMP will use this plot of land in the near future. As a result, during the taxation year ended March 31, 2010, BMP sold this land for $400,000. $150,000 was received in February, 2010, with the remainder to be paid in two equal instalments in February, 2011 and February, 2012. You have been advised that capital gains treatment is appropriate for this transaction.

3. BMP can claim a reserve on the above sale at March 31, 2010 of:

   A. Nil.
   B. $156,250.
   C. $200,000.
   D. $250,000.

4. BMP can claim a reserve on the above sale at March 31, 2011 of:

   A. Nil.
   B. $78,125.
   C. $125,000.
   D. $150,000.

5. Bob sold a capital property on December 31, 2010 for $300,000; $280,000 is payable on December 31, 2016, and the balance was paid immediately in cash. The adjusted cost base of the property was $170,000 and the selling costs totalled $10,000. Which one of the following amounts represents the **minimum** taxable capital gain in 2010?

   A. $4,000.
   B. $10,000.
   C. $12,000.
   D. $24,000.

Non-Arm's Length Transactions

6. John Bartel owns land with an adjusted cost base of $250,000 and a fair market value of $320,000. He sells the land to his son for $250,000. Which of the following statements is correct?

   A. John will have a taxable capital gain of $70,000 and the adjusted cost base of the land to his son will be $250,000.
   B. John will have a taxable capital gain of $70,000 and the adjusted cost base of the land to his son will be $320,000.
   C. John will have a taxable capital gain of $35,000 and the adjusted cost base of the land to his son will be $320,000.
   D. John will have a taxable capital gain of $35,000 and the adjusted cost base of the land to his son will be $250,000.

7. John Bartel owns land with an adjusted cost base of $250,000 and a fair market value of $320,000. He gifts the land to his son for no consideration. Which of the following statements is correct?

   A. John will have a taxable capital gain of $70,000 and the adjusted cost base of the land to his son will be $250,000.
   B. John will have a taxable capital gain of $70,000 and the adjusted cost base of the land to his son will be $320,000.
   C. John will have a taxable capital gain of $35,000 and the adjusted cost base of the land to his son will be $320,000.
   D. John will have a taxable capital gain of $35,000 and the adjusted cost base of the land to his son will be $250,000.

8. Jolinda Morris has a depreciable property with a capital cost of $225,000, a UCC of $175,000, and a fair market value of $240,000. Because of his exceptional performance during the last year, she gives this property to her common-law partner Biff. What is the minimum increase in Net Income For Tax Purposes that Ms. Morris will record as a result of this gift?

   A. $57,500.
   B. $65,000.
   C. $7,500.
   D. Nil

Change In Use

9. Jose Montana owns a cottage that he purchased in 2001 for $330,000, with $100,000 of this amount reflecting the value of the land. On January 1, 2010, this cottage is converted to a rental property. At the time of conversion, it is estimated that the cottage has a fair market value of $600,000, with $150,000 of this amount reflecting the value of the land. For 2010, rental income, net of all expenses except CCA equals $10,200. What is the maximum amount of CCA that Jose can deduct on this rental property for 2010?

A. $10,200.
B. $6,800.
C. $9,000.
D. $18,000.

Departures From Canada

10. When an individual departs from Canada, there is a deemed disposition of several types of property. Which of the following properties would not be subject to this deemed disposition rule?

A. A large painting by a well known Canadian artist.
B. Land and building that is being used as a rental property.
C. Shares in a CCPC involved in earning active business.
D. Shares in a CCPC that is used to hold investments.

Principal Residence Rules

11. Susan Cousins purchased a house in Oshawa from a friend in March, 2008, for $250,000. Even though Susan would be unable to reside in the house immediately, she felt it was a very good price and did not want to miss the opportunity to own this house. She rented out the house as of April, 2008. She will be moving back to Oshawa in January, 2010. Her tenants will move out in December, 2009, and she will move into her house. The fair market value of the house at January 1, 2010 was $300,000.

Which of the following is correct?

A. There is no capital gain on the house for tax purposes at January 1, 2010.
B. Susan must recognize a capital gain for tax purposes of $50,000 on the house at January 1, 2010.
C. Susan must recognize a capital gain for tax purposes of $25,000 at January 1, 2010.
D. Susan can elect to defer the recognition of any capital gain until she disposes of the house.
E. None of the above.

12. In 1987, Ms. Boisvert became a homeowner, acquiring a residence in Halifax at a cost of $135,000. In 1998, she was transferred by her employer to Winnipeg. She rented accommodations in Winnipeg and leased the Halifax residence. Ms. Boisvert filed an election to deem the rental property as her principal residence and therefore, did not claim CCA on the property. In July, 2010, after 24 years, she sold the Halifax house for $207,000, netting a gain of $72,000. She had decided she would not return to Halifax. Which one of the following amounts represents the **minimum** capital gain that she may report in 2010?

A. Nil.
B. $21,000.
C. $33,000.
D. $36,000.

13. Mr. Winestock owned two homes from 2007 to 2009. He had purchased Home A in 1996 for $60,000. In 2007, he purchased Home B for $180,000, with the intention of selling Home A immediately. Due to market conditions, mortgage rates, and the asking price, he was unable to sell Home A until 2009. The proceeds received on the sale of Home A were $150,000. In 2010, he was transferred to a different city and sold Home B. He designated 2007 and 2008 to Home A when it was sold. The proceeds received on the sale of Home B were $200,000. What is his taxable capital gain on Home B?

A. Nil.
B. $2,500.
C. $5,000.
D. $10,000.
E. $20,000.

Personal Use Property

14. Mike sold the following assets in 2010:

	Sales Price	Cost
Painting	$2,500	$ 800
Stamp collection	600	1,200
Outboard motor	900	100
Antique desk	1,300	1,950

Which one of the following amounts represents his capital gain, net of capital losses, for tax purposes in 2010?

A. $650.
B. $1,250.
C. $1,300.
D. $1,500.

15. Indicate which of the following is not listed personal property:

A. A stamp.
B. A rare manuscript.
C. An antique chair.
D. A piece of jewelry.
E. A piece of sculpture.

TIF PROBLEM EIGHT - 4
Capital Gains And Losses - Exam Exercises

Exam Exercise Eight - 1 (Government Assistance)

On January 1 of the current year, Michaels Inc. acquires a used property at a cost of $4,200,000. Of this amount, $375,000 represents the fair market value of the land. In order to encourage Michaels' move to this location, the local government has given them $1,100,000 to assist in the acquisition of the building. What is the maximum amount of CCA that Michaels can deduct on this building for the current year?

Exam Exercise Eight - 2 (Superficial Loss)

Mr. Franklin Sharp owns 750 shares of Guard Inc. They have an adjusted cost base of $21.50 per share. On June 15, 2010, he sells all of these shares at $13.75 per share. On June 21, 2010, he acquires 400 shares of Guard Inc. at a cost of $12.15 per share. What are the tax consequences of these transactions?

Exam Exercise Eight - 3 (Capital Gain On Depreciable Assets)

On July 1, 2010, Lorty Inc. sells equipment for $126,000. This equipment had an original cost of $111,000 and a net book value of $93,000. For tax purposes, these assets were in Class 8. The UCC balance in this class on January 1, 2010 was $103,000. There were no other additions or dispositions of Class 8 assets during the taxation year ending December 31, 2010. Indicate the adjustments that would be required to Lorty Inc.'s accounting income in the determination of 2010 Net Income For Tax Purposes.

Exam Exercise Eight - 4 (Identical Properties)

Mr. Levon Park makes frequent purchases of the common shares of Donner Ltd. During 2009, he purchased 700 shares at $22.75 per share on January 15, and 410 shares at $25.50 per share on March 12. He sold 250 shares on September 15, 2009 at $26.45 per share. On February 14, 2010, he purchases an additional 925 shares at $28.25 per share and, on October 1, 2010, he sells 410 shares at $30.75 per share. Determine Mr. Park's taxable capital gains for 2009 and 2010.

Exam Exercise Eight - 5 (Warranties On Capital Assets)

During the taxation year ending December 31, 2009, Pointer Inc. sells a capital asset with an adjusted cost base of $226,000 for proceeds of $279,000. The Company provides the purchaser with a one year warranty and the Company estimates that it will cost $4,100 to fulfill the warranty provisions. On September 22, 2010, the Company spends $4,400 to fulfill the warranty provisions. Determine the effect of these transactions on Net Income For Tax Purposes for 2009 and 2010.

Exam Exercise Eight - 6 (Capital Gains Reserve)

During June, 2010, Ms. Janet Houston sells a capital asset with an adjusted cost base of $112,500, for proceeds of $172,300. She receives $33,000 of this amount in cash, with the balance due at the end of the following year. What is the minimum amount that she will have to include in her 2010 Net Income For Tax Purposes as a result of this transaction?

Exam Exercise Eight - 7 (Bad Debts On Capital Assets)

During 2010, a capital property with an adjusted cost base of $131,000 is sold for $115,000. The proceeds of disposition are made up of $82,000 in cash, plus the purchaser's one-year note for $33,000. In 2011, the note proves to be uncollectible. What are the tax consequences of these events in 2010 and 2011?

Exam Exercise Eight - 8 (Inadequate Consideration)

Ms. Veronica Lox owns securities with an adjusted cost base of $150,000 and a fair market value of $175,000. She sells these securities to her father for $130,000. He immediately sells them to an arm's length party for $175,000. Determine the tax consequences for Ms. Lox and her father.

Exam Exercise Eight - 9 (Inadequate Consideration)

Ms. Veronica Lox owns securities with an adjusted cost base of $150,000 and a fair market value of $175,000. She sells these securities to her father for $210,000. He immediately sells them to an arm's length party for $175,000. Determine the tax consequences for Ms. Lox and her father.

Exam Exercise Eight - 10 (Transfer Of Depreciable Asset To A Spouse)

During the current year, Geoff Lionel transferred a depreciable property to his spouse. The property had a fair market value of $200,000, a capital cost of $160,000, and a UCC of $107,000. It is the only asset in its CCA class. In return for the property, his spouse pays $200,000 from funds that she has received as an inheritance. Describe the tax consequences to Mr. Lionel and the tax cost of the property to his spouse after the transfer, assuming that he does not elect out of ITA 73(1). How would these results differ if Mr. Lionel elects out of ITA 73(1)?

Exam Exercise Eight - 11 (Non-Arm's Length Transfer Of Depreciable Property)

Mr. Norman Low owns a depreciable asset that he has used in his unincorporated business. It has a cost of $145,000 and a fair market value of $132,000. It is the only asset in its CCA class and the balance in the class is $63,500. Mr. Low sells the asset to his father for $132,000. During the year, prior to taking any CCA on the asset, Mr. Low's father sells the asset for $135,000. Determine the amount of income to be recorded by Mr. Low and his father as a result of these transactions.

Exam Exercise Eight - 12 (Farm Property Transfer To A Child)

Mrs. Betty Wong owns farm property consisting of land with an adjusted cost base of $271,000 and a fair market value of $365,000, along with a barn with a UCC of $90,000, a capital cost of $120,000, and a fair market value of $110,000. The property is transferred to her 67 year old son in return for a payment of $300,000 for the land. No payment is made for the barn. Describe the tax consequences of this transfer, both for Mrs. Wong and for her son.

Exam Exercise Eight - 13 (Involuntary Dispositions)

Multi Inc., a company with a December 31 year end, operates out of a single building that cost $815,000 in 2002. At the beginning of 2009, the UCC for its Class 1 was $648,275. On June 30, 2009, the building was completely destroyed in a tornado. The building was insured for its fair market value of $1,000,000 and this amount was received in September, 2009. The building is replaced in 2010 at a cost of $1,075,000. As the replacement building was not new, it is not eligible for the extra 2 percent allowance on non-residential buildings. Multi Inc. wishes to minimize taxes. Describe the 2009 and 2010 tax consequences of these events, including the capital cost and UCC for the replacement building. Ignore any gain or loss related to the land on which the building is located.

Exam Exercise Eight - 14 (Replacement Property)

On December 1, 2009, Morteaux Ltd. sells its only building in anticipation of moving to a new location in 2010. The property is sold for $2,300,000 and, at the time of the sale, the land had an adjusted cost base of $1,200,000 and a fair market value of $1,200,000, while the building had a capital cost of $1,100,000, a UCC of $250,000, and a fair market value of $1,100,000.

During February, 2010, the store building is replaced at a total cost of $2,700,000, with $1,300,000 allocated to the land and $1,400,000 allocated to the building. The replacement building is not a new building and, as a consequence, it is not eligible for the extra 2 percent allowance. What are the tax consequences of the 2009 sale? Provided the appropriate election is made to minimize total taxes for the two years 2009 and 2010, what will be the maximum CCA that can be taken on the new building in 2010?

Exam Exercise Eight - 15 (Deferral Of Small Business Gains)

On January 15, 2010, Chad Brant sells all of his shares of Brant Inc., an eligible small business corporation. The adjusted cost base of these shares is $600,000 and they are sold for $1,100,000. On February 15, 2010, $940,000 of these proceeds are invested in the common shares of Quint Ltd., a new eligible small business corporation. How much of the capital gain arising on the sale of the Brant Inc. shares can be deferred by the investment in Quint Ltd.? If the maximum deferral is elected, what will be the adjusted cost base of the Quint Ltd. shares?

Exam Exercise Eight - 16 (Change In Use - CCA On Rental Property)

For a number of years, Ms. Danine Post has owned a rural cottage property that has been used for her personal enjoyment. The cottage cost $142,000 in 2006 and, on July 1, 2010, it has a fair market value of $242,000. She estimates that the fair market value of the land on which the cottage is located is $22,000 on both of these dates. It will not be designated as her principal residence for any of the years owned. On July 1, 2010, she rents the property to an arm's length party for an amount of $1,000 per month for a period of three years. Net rental income for the year ending December 31, 2010, before the deduction of any CCA, is $4,800. What is the maximum amount of CCA that she can deduct for 2010?

Exam Exercise Eight - 17 (Change In Use - ACB, UCC And CCA)

On December 1, 2010, Mr. Jordon Jordu converts his summer cottage into a rental property. The cottage has an original cost of $57,000 and it will not be designated as his principal residence for any of the years owned. At the time of the conversion, the fair market value of the property is $136,400. It is estimated that the land value that is included in both the $57,000 cost and the $136,400 fair market value is $20,000. Determine the 2010 tax consequences of this change in use, including the adjusted cost base for the property, the UCC that will be applicable to the rental property, and the maximum CCA that would be available for 2010.

TIF Problem Eight - 4

Capital Gains And Losses - Exam Exercises

Exam Exercise Eight - 18 (Emigration)

Mr. Ryan Marchand owns publicly traded securities with an adjusted cost base of $30,000 and a fair market value of $56,000. On August 15, 2010, he permanently departs from Canada still owning the shares. What would be the tax consequences of his departure, if any, with respect to these securities?

Exam Exercise Eight - 19 (Transfers On Death)

Mr. Norm Norten dies in July, 2010. At the time of his death, he owned two backhoes that were used in his construction business. His will leaves one backhoe to his spouse, Linda, with the other backhoe going to his daughter, Mary. The backhoes cost $180,000 each and each had a fair market value at the time of Mr. Norten's death of $122,000. The UCC balance for the class that contains the backhoes is $148,000. What are the tax consequences resulting from Mr. Norten's death with respect to the two backhoes? Your answer should include the capital cost and UCC for the backhoes in the hands of Linda and Mary.

Exam Exercise Eight - 20 (Sale Of Principal Residence)

Mr. Jerry Haggard owns a house in Calgary, as well as a cottage in Canmore. He purchased the house in 1999 for $186,000. The cottage was purchased in 2002 for $105,000. During December, 2010, both properties are sold, the house for $263,000 and the cottage for $197,000. He has lived in the Calgary house during the year, but has spent his summers in the Canmore cottage. Determine the minimum capital gain that he must report on the 2010 sale of the two properties.

Exam Exercise Eight - 21 (Sale Of Principal Residence)

Ms. Harriet Lowe owns a city home in Vernon, as well as a chalet at the Silver Star ski area. The city home was purchased in 1997 at a cost of $172,000. The chalet was purchased in 2003 for $89,000. On July 1, 2010, the house is sold for $214,000 and the chalet is sold for $122,000. A real estate commission of 6 percent was paid on each sale. She has spent some time in each property in every year from 2003 through 2010. Determine the minimum capital gain that she must report for 2010 as a result of the sale of the two properties.

Exam Exercise Eight - 22 (Personal Use Property)

During the current year, Robert Langois disposes of several items. The proceeds of disposition and the adjusted cost base of the various items are as follows:

	Adjusted Cost Base	Proceeds Of Disposition
Collector Car	$45,000	$61,000
Marble Sculpture	800	13,000
Antique Furniture	21,000	12,000
Stamp Collection	32,000	26,000

What is the net tax consequence of these dispositions?

Exam Exercise Eight - 23 (Foreign Currency Gains And Losses)

During 2007, Ms. Lorenda Jacks acquires 300 shares of a Barbadian company, Tellen Ltd., at a price of 51 Barbadian dollars (B$) per share. She paid for the shares with Barbadian dollars purchased at a rate of B$1 = C$0.50. During September, 2010, the shares are sold for B$85 per share. The Barbadian dollars are immediately converted into Canadian dollars at a rate of B$1 = C$0.52. What amounts will be included in Ms. Jacks' 2010 Net Income For Tax Purposes as a result of these transactions?

TIF PROBLEM EIGHT - 5
Capital Gains And Losses - Key Term Matching

The following five key terms were listed at the end of Chapter 7 on Capital Gains and Losses:

A. Involuntary Disposition

B. Adjusted Cost Base (Non-Depreciable Capital Property)

C. Capital Asset

D. Superficial Loss - ITA 54

E. Listed Personal Property

The following list contains 10 potential definitions for the preceding key terms:
NOTE There is only **ONE** correct definition for each key term.

1. A loss on the disposition of property that is disallowed for tax purposes because the transfer was to a non-arm's length person.

2. A disposition of a capital property resulting from repossession by creditors.

3. The cost of the property to the taxpayer in Canadian dollars.

4. A loss on the disposition of property that is disallowed for tax purposes because the taxpayer has acquired an identical property, either 30 days before the disposition or, alternatively, 30 days after the disposition.

5. A defined subset of personal use property. The included items are works of art, jewelry, rare books, antiques, and coins.

6. An asset that is classified as non-current for accounting purposes.

7. A disposition of a capital property resulting from theft, destruction through natural causes, or expropriation by a statutory authority.

8. An asset that is held for the purpose of producing income.

9. The cost of the property to the taxpayer, subject to ITA 53 adjustments (e.g., deduction of government grants on land purchase).

10. A defined subset of personal use property. The included items are works of art, jewelry, rare books, stamps, and coins.

Required: For each of the five key terms listed, indicate the number of the item that provides the **BEST** definition of that term. As only one definition is completely correct, please indicate only one number for each key term. No marks will be awarded if you indicate more than one number for any key term.

TIF PROBLEM EIGHT - 6
Capital Gains And Losses - Identical Properties

Over the last ten years, Ms. Julie Ho has engaged in the following transactions in the shares of Alcor Ltd.:

Date	Type Of Transaction	Number Of Shares	Cost (Proceeds) Per Share
May, 2000	Purchase	200	$10.00
June, 2001	Purchase	150	14.75
April, 2004	Sale	(75)	(16.25)
July, 2006	Purchase	125	13.50
October, 2008	Purchase	180	12.75
July, 2010	Sale	(200)	(14.00)

Required: Determine the amount of any taxable capital gain or allowable capital loss resulting from the 2010 sale of Alcor Ltd. shares.

TIF PROBLEM EIGHT - 7
Capital Gains Reserves

During 1993, Ms. Helm acquired two tracts of land near Ottawa. Tract A cost $71,000, while Tract B cost $87,000.

On July 1, 2009, Tract A is sold for $127,000. The terms of the sale require a down payment of $17,000. A payment of $25,000 is required on January 1, 2010.

Also on July 1, 2009, Tract B is sold for $106,000. The terms of the sale require a down payment of $32,000. No further payment on the principal amount is required for five years.

Required: Determine the amount of the minimum taxable capital gain that will have to be included in Ms. Helm's Net Income For Tax Purposes for both 2009 and 2010.

TIF PROBLEM EIGHT - 8
Non-Arm's Length Transactions

Ms. Jody Wales owns shares in a Canadian public company that she acquired several years ago at a cost of $220,000. The shares have a current fair market value of $426,000. Ms. Wales and her husband, Jim, have three children. Their daughter Kim is 20 years old, while their sons Jeff and Jerry are respectively 22 and 24 years old.

On November 1 of the current year, Ms. Wales is considering the following alternatives for disposing of the securities:

A. Selling the shares to her daughter for $220,000.

B. Gifting the shares to her older son, Jerry.

C. Selling the shares to her younger son, Jeff, for $500,000.

Required: Indicate the immediate tax consequences to Ms. Wales that will result from making each of the transfers described. In addition, indicate the adjusted cost base of the shares to the transferee.

TIF PROBLEM EIGHT - 9
Replacement Properties - UCC

Farnham Inc. has a taxation year that ends on December 31. The Company carries on its operations in a single building. This building has a capital cost of $850,000 and, on January 1, 2009, its UCC was $113,000. The building's furniture and fixtures (all Class 8) have a capital cost of $220,000 and a January 1, 2009 UCC of $152,000. The Company has no other Class 8 assets.

On February 12, 2009, the building and its contents were completely destroyed in a fire. The building was insured for its capital cost of $850,000 and the furniture and fixtures were insured for $180,000. As the fire completely destroyed all of these assets, on June 18, 2009, the Company received a payment from its insurer for $1,030,000 ($850,000 + $180,000).

In 2010, Farnham Inc. acquires a replacement building for $925,000. As this replacement building is not a new building, it does not qualify for the 6 percent CCA rate.

During the following month, furniture and fixtures are installed in this new building at a cost of $235,000.

Required:

A. Indicate the 2009 tax consequences that would result from the destruction of the building and its contents.

B. Indicate the maximum amendments that could be made to the results described in Part A by filing an election under ITA 13(4). Assuming that these amendments have been made, determine the maximum CCA on the new building and the new Class 8 assets for the year ending December 31, 2010. In addition, calculate the January 1, 2011 UCC balance for each Class.

C. Assume that, instead of having the building and contents destroyed by fire, the Company had sold the building and its contents for $1,030,000 in 2009 in order to voluntarily move to the new location in 2010. How would the results in Part B differ?

D. Assume that the replacement building for the burned building had cost $700,000 instead of $925,000. How would the results in Part B differ?

TIF PROBLEM EIGHT - 10
Involuntary Dispositions

On July 1, 2009, the manufacturing plant of Janchek Ltd. was expropriated by the provincial government in order to make way for a new expressway. It is the only building that Janchek Ltd. owns. The land on which the plant was situated was purchased in 1997 for $88,000. The building, a Class 1 asset, was erected in 1998 at a cost of $290,000. The Company's year end is December 31.

On November 23, 2009, after extended negotiations between Janchek and the provincial government, the Company received compensation in the amount of $130,000 for the land and $430,000 for the building. On January 1, 2009, the UCC balance in Class 1 was $248,000.

On June 20, 2010, a replacement manufacturing plant was purchased for a total cost of $1,050,000. Of this amount, $210,000 was allocated to the land, with the remaining $840,000 going to the building. As this was not a new building, it did not qualify for the extra 6 percent allowance that is available for manufacturing and processing buildings.

Janchek Ltd. will make any available elections in order to reduce the tax effects of the replacement of the expropriated property.

Required:

A. Determine the tax effects in 2009 that will result from the receipt of the expropriation compensation.

B. Indicate how the results in Part A could be altered through the application of ITA 13(4) and 44(1) in an amended 2009 return.

C. Determine the adjusted cost base of the land and the building, as well as the UCC of the building, subsequent to the replacement of these assets and the application of ITA 13(4) and 44(1).

TIF PROBLEM EIGHT - 11
Change In Use - Rental Property

On August 1, 2001, Ms. Marnie Houston acquired a residence for a total cost of $235,000. At the time of purchase, it was estimated that the value of the land on which the house was situated was $85,000. Until January 1, 2010, Marnie and her two children occupied all of the house.

Early in 2010, Marnie's two children moved out, leaving a significant portion of the house unused. Because of this, Marnie decides to move to a small apartment and retain the former residence as a rental property. On April 1, 2010, a tenant moved into the house. Marnie does not make an election under ITA 45(2). (This election deems that the change in use has not occurred.)

Marnie had the house appraised on April 1, 2010. The appraiser indicated that the total value of the property was $392,000, with $112,000 of this amount reflecting the value of the land on which the house was situated.

For the period April 1, 2010 through December 31, 2010, Marnie's expenses on the property were as follows:

Property Taxes	$4,600
Insurance	1,100
Maintenance And Operating Costs	1,850
Mortgage Interest	8,200

The monthly rent was set at $1,900 per month, payable at the beginning of each month. The tenant paid all amounts required during 2010.

Required: For the year ending December 31, 2010, determine Ms. Houston's minimum net rental income (loss). Your calculations should include the maximum available CCA, without regard to whether the full amount can be deducted. Indicate any other tax consequences that will result from the change in use.

TIF PROBLEM EIGHT - 12
Deemed Dispositions On Death And Emigration

Mr. Cheever is 66 years of age and his wife, Doreen, is 56. They have one daughter, Mary, who is 32 years of age. On July 1 of the current year, Mr. Cheever owns the following properties:

> **Rental Property** Mr. Cheever owns a rental building that was acquired at a cost of $550,000 ($100,000 of this amount represents the estimated value of the Land on which the building is situated). On July 1 of the current year, its UCC is $270,000 and its fair market value is estimated to be $970,000 (the estimated value of the land is unchanged at $100,000).
>
> **Brazeway Dynamics** Mr. Cheever owns 2,500 shares of Brazeway Dynamics, a Canadian public company. These shares have a cost of $275,000 and a current fair market value of $425,000. Mr. Cheever has never owned more than 1 percent of the outstanding shares of this Company.
>
> **Farm Land** Mr. Cheever owns farm land with a cost of $525,000 and a current fair market value of $750,000. The land is farmed on a full time basis by Mr. Cheever's daughter, Mary.
>
> **Cheever Inc.** Mr. Cheever owns 100 percent of the voting shares of Cheever Inc., a Canadian controlled private corporation. The Company was established with an investment of $155,000 and it is estimated that the current fair market value of the shares is $227,000.

Required: Explain the tax consequences to Mr. Cheever for the current year, in each of the following Cases:

A. Mr. Cheever dies on July 1 of the current year, leaving all of his property to his spouse, Doreen.

B. Mr. Cheever dies on July 1 of the current year, leaving all of his property to his daughter, Mary.

C. Mr. Cheever departs from Canada and ceases to be a resident on July 1 of the current year.

In providing your answers, assume that Mr. Cheever has used all of his lifetime capital gains deduction on dispositions that occurred prior to his death (Cases A and B) or departure from Canada (Case C).

TIF PROBLEM EIGHT - 13
Principal Residence Designation

In early 2010, Miss Stern advises you that it is her intention to sell both her Ottawa residence and her condominium at Mt. Tremblant. She acquired both of these properties in 1996 and has spent at least a part of each subsequent year in residence at each property. The cost of the Ottawa house was $173,000, while the Mt. Tremblant condominium was $131,000. She provides you with the following additional information:

	City Home	Condo
Estimated Selling Price	$325,000	$304,000
Anticipated Selling Costs	13,500	12,240

She has asked you to determine the minimum taxable capital gain that would result from the sale of the two properties during 2010.

Required: Describe how the residences should be designated in order to accomplish Miss Stern's goal. In addition, calculate the amount of the taxable capital gain that would arise under the designation that you have recommended.

TIF PROBLEM EIGHT - 14
Court Cases - Identification Of Capital Gains

Each of the following Cases contains a brief description of an actual court case involving the identification of capital gains. For each Case, indicate whether you feel the transaction should have generated a capital gain or income. Explain the basis for your conclusion.

Case A An individual constructed an apartment building and operated it for a period of three years. At that time, as the result of an unsolicited offer, he decided to sell the building. His decision was also influenced by the fact that he encountered unexpected difficulties in operating the building. The proceeds of the sale exceeded the cost of the building. (73 DTC 5060)

Case B An operator of a taxicab business decided to dispose of it as it had proved to be unprofitable. He was not able to obtain a favourable price for the business as a complete unit and, as a consequence, he decided to sell the individual cars. During the subsequent two year period, he engaged in over 40 transactions involving the cars, largely because some worn out cabs had to be replaced and some trade-ins were accepted. A profit was made on most transactions. (57 DTC 144)

Case C A taxpayer carried on a full time business as an interior designer. While carrying on this business he bought, lived in for short periods of time, and resold numerous residential properties. In most cases, improvements were made and the property modernized prior to resale. The sales prices were usually well in excess of costs. (64 DTC 56)

Case D An optical organization bought the assets of an optical company whose shares were held by a group of medical doctors. The sale was accompanied by an agreement to pay each doctor a “kickback” for every prescription filled. A provincial statute eventually made these payments illegal, at which point the doctors sold their shares to the optical organization. Even though each doctor sold one share, the payments to them varied from $1,800 to $57,000. The payments were to be made over a period of ten years and the agreement required the doctors to continue sending patients to the optical company. The amounts paid to the doctors were proportional to the size of their practices. (57 DTC 48)

Case E A private company with broadly stated charter powers claimed that it was engaged in the business of dairy farming. Three different farms were acquired and operations started. However, in each case a loss was experienced. The parcels of farmland were then subdivided and sold at a price in excess of their cost. (65 DTC 89)

Case F The manager of a company that operated vans designed for the transportation of horses engaged in several transactions involving the purchase and sale of racehorses. He attended race tracks on a regular basis and kept numerous horses for his own personal enjoyment. On most of the purchase and sale transactions, the proceeds of the sale exceeded the cost of the horse. (67 DTC 240)

Chapter Nine Test Item File Problems

TIF PROBLEM NINE - 1
Other Income/Deductions, Attribution - Essay Questions

1. What is a retiring allowance? What are the tax consequences associated with receiving a retiring allowance?

2. What is a death benefit? Indicate any special tax features associated with the receipt of a death benefit.

3. As evidenced by the ability to deduct these items in the calculation of Taxable Income, the government does not intend to tax social assistance payments or worker's compensation payments. Given this, why are these amounts included in Net Income For Tax Purposes?

4. Under what conditions can an individual deduct moving expenses?

5. Can an employer compensate an individual for a loss on a home that was sold because the employee was required to move, without creating a taxable benefit for the employee? Explain your conclusion.

6. For purposes of deducting child care costs, how is an "eligible child" defined?

7. What are the conditions that must be met for spousal support payments to be deductible to the payor and taxable to the recipient?

8. John Withers is receiving an annuity payment of $500 per month. How will this payment be taxed?

9. What are the tax advantages and other benefits associated with making contributions to a Registered Education Savings Plan?

10. What is the Canada Learning Bonds program? Briefly describe the program.

11. Distributions from a Registered Disability Savings Plan will include a taxable component and a non-taxable component. How is the non-taxable component of the current year's distribution determined?

12. What is the major tax advantage of Tax Free Savings Accounts (TFSAs)?

13. What are the normal tax consequences, at the time of transfer, for an individual who is transferring property to a spouse or common-law partner? In these circumstances, at what value will the transfer be deemed to take place? Is there an election that can be used to alter these results? If so, briefly describe the election.

14. When a transfer is made to a spouse or common-law partner, the income attribution rules may be applicable. Briefly describe the conditions under which the income attribution rules would be applicable on such transfers.

15. An individual is considering making a gift of a portfolio of public company common stocks. On the basis of tax considerations, provide advice to this individual as to whether he should give the stocks to his 12 year old daughter or, alternatively, to his spouse.

16. One of your clients is a successful businessman with both a spouse and a minor child that have no income of their own. He would like to transfer some of his income into their hands for tax purposes. However, he is concerned about the income attribution rules. Provide him with three tax tips for dealing with these rules.

TIF PROBLEM NINE - 2
Other Income/Deductions, Attribution - True Or False

1. The widow of Peter Toscan received a death benefit from his employer of $25,000. She must include the $25,000 in income in the year of receipt.

   True or False?

2. The entire amount of a retiring allowance received must be included in income, even if some part of the allowance is transferred to an RRSP.

   True or False?

3. Chris Shaffer is being transferred by his employer from Prince George, British Columbia to Red Deer, Alberta.

   i. His airfare from Prince George to Red Deer is a deductible moving cost.

      True or False?

   ii. His wife spent $750 for gas, meals, and lodging while driving their car from Prince George to Red Deer. The $750 is a deductible moving cost.

      True or False?

   iii. The Shaffers paid $1,000 in legal fees to sell their Prince George home and $800 in legal fees to buy their new home in Red Deer. The total $1,800 in legal fees is a deductible moving cost.

      True or False?

   iv. Before moving into their new home, the Shaffers had to pay $2,000 to repair faulty wiring. The $2,000 is a deductible moving cost.

      True or False?

   v. The $5,000 in real estate fees paid to sell their Prince George house is a deductible moving cost.

      True or False?

   vi. All moving expenses can only be deducted from income earned in Red Deer in the year of the move. There are no carry forward provisions for moving costs.

      True or False?

4. Sarah and David Johnston paid $5,500 during the year for child care for their three children, aged 3, 5, and 7. Her annual salary was $8,000 and his annual salary was $30,000. Sarah can deduct the $5,500 paid from her income.

   True or False?

5. For purposes of deducting child care costs, an "eligible child" must be under 16 at some time during the year.

   True or False?

6. If the lower income spouse was in prison for the entire year, the higher income spouse would be able to deduct child care costs during this period.

   True or False?

7. Jim and Shirley Noonan decide to separate after ten years of marriage. They have no children. To keep the separation amiable, they decide not to involve lawyers or the courts at this stage. They have a written separation agreement in which Shirley agrees to pay Jim $500 per month until he remarries. The payments will be taxed in Jim's hands and will be deductible from Shirley's income.

True or False?

8. The tax treatment of payments received under an annuity contract will depend on whether the annuity was purchased with after tax funds or, alternatively, from funds that are in an RRSP.

True or False?

9. The contributions that can be made to an RESP for one beneficiary are limited to $50,000.

True or False?

10. Earnings on amounts contributed to an RESP accumulate on a tax free basis.

True or False?

11. While contributions to a Registered Disability Savings Plan (RDSP) are subject to an overall limit of $200,000, there is no limit on the amount of this total that can be contributed in a single year.

True or False?

12. While earnings on assets held in a Tax Free Savings Account (TFSA) will not be taxed while the assets are in the plan, the accumulated income will be subject to tax when it is withdrawn from the plan.

True or False?

13. A father gives $10,000 in securities to his 19 year old daughter who is living at home. Any dividends declared on the securities will be attributed to the father.

True or False?

14. Martha Stuart has a depreciable asset with a UCC of $50,000, a capital cost of $80,000, and a fair market value of $100,000. If she gifts this property to her spouse without making any election, she will have a capital gain of $50,000.

True or False?

15. Brian Lawson gives equity securities to his 15 year old son. If the securities are sold, in the following year, for more than their fair market value at the time of the gift, the resulting capital gain will be taxed in the hands of Mr. Lawson.

True or False?

TIF PROBLEM NINE - 3

Other Income/Deductions, Attribution - Multiple Choice

Other Inclusions

1. Which of the following statements with respect to Subdivision d income inclusions is correct?

   A. 100 percent of any death benefit received by a spouse must be included in income.
   B. 100 percent of any scholarships received must be included in income.
   C. 100 percent of any retiring allowance received must be included in income.
   D. Social assistance payments received do not have to be included in income.

Moving Costs

2. Stan Aiken changed employers during 2010 and, as a result of the change, moved 150 kilometers, from Windsor to London. His new employer was located in London and reimbursed 50 percent of Stan's eligible moving expenses. On his 2010 personal tax return, Stan can:

   A. Claim 0 percent of his moving expenses.
   B. Claim 50 percent of his moving expenses against his income from employment.
   C. Claim 50 percent of his moving expenses against his income from his new employer.
   D. Claim 100 percent of his moving expenses against his income from employment.

3. In 2010, Mr. Kumar moved from Saskatchewan to Prince Edward Island to start a new business. In his 2010 fiscal year, the business generated income in excess of $50,000. Mr. Kumar incurred the following costs of moving:

Transport of household effects	$5,000
Travel - self, spouse, and three children	2,000
Legal fees - house purchase in PEI	900
Cancellation costs - lease in Saskatchewan	750
Temporary accommodation while waiting for new house at $70 per day for 30 days	2,100
House-hunting trip (prior to move)	500

   Which one of the following amounts represents the **maximum** amount that Mr. Kumar may deduct for moving expenses in his 2010 personal income tax return?

   A. $ 8,800.
   B. $ 9,850.
   C. $10,350.
   D. $10,750.

4. During 2010, Jan Harding accepted a job transfer from British Columbia to Ontario. She will begin her new position on December 1. Her new salary will be $102,000 per annum. Upon arriving, Jan spent 25 days staying in a hotel due to an unfortunate delay in moving into her new residence. Jan incurred expenses related to the move of $13,402. Included in this total was $1,125 for meals and $2,125 for hotel stays while waiting for her new residence to be ready. How much can she claim on her 2010 tax return for moving expenses?

   A. $ 8,500.
   B. $12,102.
   C. $12,952.
   D. $13,402.

5. Maxine used to work and live in Alberta, but has accepted a new job in Ontario. The new job has a starting salary of $105,600 per year, or $8,800 per month. She moved there with her family in October, so she could start her new job on November 1. While she had rented her accommodations in Alberta, she bought a new house in Ontario. She incurred the following expenses as a result of the move:

   - canceling the lease on her rental apartment, $1,200.
   - hiring movers to pack and move her household effects, $12,000.
   - legal fees on the house purchase, $1,400.
   - land transfer tax on the house purchase, $3,000.
   - cost of disconnecting utilities in Alberta, $100.
   - cost of connecting utilities in Ontario, $200.
   - gas, food, and lodging while traveling from Alberta to Ontario, $2,800.

   How much can she claim for moving expenses for the year of the move?

   A. $16,000.
   B. $16,300.
   C. $20,400.
   D. $20,700.

Child Care Costs

6. John and Alexandria are married and they have two children, aged 2 and 5. They pay Alexandria's 22 year old sister $150 per week to take care of their children for 48 weeks each year. John works full time and earns a salary of $90,000 per year. Alexandria works part time, earning a salary of $28,000 per year. She also goes to college part time during the fall semester, for a total of 17 weeks, or 4 months, each year. Which of the following is correct with respect to John and Alexandria's ability to claim a deduction for child care expenses?

   A. Neither John nor Alexandria can claim child care expenses because they paid a relative to take care of their children.
   B. Alexandria must claim all of the child care expenses because she is the supporting person with the lower Net Income.
   C. John can claim child care expenses of $5,950 and Alexandria can claim the remaining $1,250.
   D. John can claim child care expenses of $7,200.

Spousal And Child Support

7. Which of the following is not a requirement for spousal support payments to be deductible?

   A. The payments must be made on a periodic basis.
   B. The payments must be made for a period of time that the spouses, or former spouses, are living apart.
   C. The payments must be made pursuant to a separation agreement.
   D. The amount for child support must be specified separately.
   E. None of the above.

8. Jack and his wife, Sally, separated during 2004. The written separation agreement requires Jack to make payments for the maintenance of Sally and their child. Payments were set at $250 per month for Sally and $150 per month for their child. During 2010, Jack's payments totaled $4,000. How much of the 2010 payments can Jack deduct on his 2010 personal tax return?

    A. $4,000.
    B. $3,000.
    C. $1,800.
    D. $2,200.

Registered Savings Plans

9. With respect to the tax rules for Registered Education Savings Plans (RESPs), which of the following statements is not correct?

    A. The total contributions to one individual's plan cannot exceed $50,000.
    B. Earnings paid out of the plan are subject to tax in the hands of the recipient.
    C. The annual contributions made by any one individual cannot exceed $4,000.
    D. Distributions can be made to a beneficiary of a plan when they commence full-time studies at an institution that would qualify the individual for the education tax credit.

10. There are a number of benefits and tax advantages associated with Registered Education Savings Plans (RESPs). Which of the following is not a benefit or advantage?

    A. Contributions to the plans are deductible.
    B. Earnings on assets within the plan are not subject to tax.
    C. The government makes contributions in the form of Canada Education Savings Grants and Canada Learning Bonds.
    D. Distributions from the plan may be received by some recipients without incurring any additional taxation.

11. With respect to Registered Disability Savings Plans (RDSPs), which of the following statements is correct?

    A. Contributions to the plan are deductible.
    B. Distributions to beneficiaries are not subject to tax.
    C. Earnings on assets in the plan will accumulate tax free.
    D. While the beneficiary has to have a disability, they do not have to qualify for the disability tax credit.

12. With respect to Tax Free Savings Accounts (TFSAs), which of the following statements is not correct?

    A. Contributions to the accounts are not deductible.
    B. Contributions to the accounts can be returned tax free at any time.
    C. Earnings on assets in the accounts can accumulate tax free.
    D. Withdrawals of accumulated account earnings will be subject to tax.

Income Attribution

13. Mr. Johnson wants to help his daughter, Erin, save for her college education. To this end, in 2008, when she was 15 years old, he put $3,000 into a GIC in her name, for a one year term. The GIC renews on an annual basis. On its maturity in 2009, Erin rolled the $3,000 into another GIC for one year and the interest earned during the first year into a second one-year GIC for $300. In 2010, the interest earned on the two GICs was $240 and $24 respectively.

    How much of this interest, if any, must Mr. Johnson report on his 2010 income tax return?

    A. Nil.
    B. $24.
    C. $240.
    D. $264.
    E. None of the above.

14. Agatha Harkness wishes to gift mutual funds to her three grandchildren, all of whom are under the age of 6. She wants to minimize any income that will be attributed to her. Which one of the following mutual funds will best accomplish this goal?

    A. An equity fund that invests in preferred shares of top Canadian corporations and earns primarily dividend income.
    B. A bond fund that invests in long-term, interest-bearing Government of Canada bonds, earning interest income and capital gains.
    C. A growth fund that invests in corporations with a history of paying minimal dividends and earns its income primarily in the form of capital gains.
    D. A money-market fund that invests in short-term treasury bills and earns only interest income.

15. William Choring owned shares of two publicly traded companies, as follows:

	Fair Market Value On Date Of Disposition	Adjusted Cost Base
TriStar Limited	$1,000	$10,000
Global Inc.	2,500	200

William gifted the TriStar Limited shares to his wife on July 1, 2010. His wife kept the shares and received $125 of taxable dividends (grossed up amount) in September, 2010. William sold the Global Inc. shares on the open market. Assuming William earned no other income, did not elect out of ITA 73(1), and these are the only transactions that occurred in the year, which one of the following represents William's 2010 Net Income For Tax Purposes?

A. Nil.
B. $1,150.
C. $1,250.
D. $1,275.

Other Income/Deductions, Attribution - Multiple Choice

16. Hans Myers wishes to transfer an investment to his wife, Olga. However, Olga does not have sufficient cash to purchase the investment for fair value. Hans would like to loan the funds to Olga to facilitate the purchase, as he wants the income on this investment to be reported by her. Olga will pay interest on the loan, as Hans expects the investment to generate substantial income. Which one of the following is **not** a requirement to ensure that the income on this investment will be taxable to Olga, and not attributed to Hans, in the future?

    A. Hans must elect to realize any gains inherent in the property at the transfer date.
    B. Interest on the loan must be paid from Olga to Hans annually, by January 30 of the following year.
    C. Olga must pay no less than the full fair market value of the investment (although this can include the loan's face value).
    D. The interest rate on the loan must be at fair market value, even when that rate is greater than the prescribed rate.

17. Martin has a marginal tax rate of 52 percent. His wife, Carmen, has a marginal tax rate of 26 percent. In order to give his wife a supplemental source of income, he gave her a portion of his investment portfolio. Carmen's new investment portfolio generated interest income of $6,800 and taxable capital gains of $9,900. Which of the following statements is not correct?

    A. Martin faces an additional tax liability of $3,536 as a result of Carmen's interest income.
    B. Martin faces an additional tax liability of $5,148 as a result of Carmen's capital gains.
    C. Carmen has no additional tax liability as a result of the investment portfolio.
    D. Carmen faces a tax liability of $2,574 as a result of her capital gains.

18. Joan Marx loaned $22,000 to four different people. Each of them used the money they received from Joan to invest in bonds. In which situation will the resulting interest income not be attributed to Joan?

    A. The loan is interest free and made to Joan's 15 year old daughter.
    B. The loan is interest free and made to Joan's 14 year old nephew.
    C. The loan is interest free and made to Joan's 19 year old son.
    D. The loan is interest free and made to Joan's husband.

19. Sandy gives a gift of $12,000 to each of the following people. Each of them used the money they received from Sandy to invest in shares of publicly trading companies. In which situation will the resulting dividend income not be attributed to Sandy?

    A. The gift is to Sandy's long-time business partner.
    B. The gift is to Sandy's wife.
    C. The gift is to Sandy's 14 year old nephew.
    D. The gift is to Sandy's 10 year old daughter.

TIF PROBLEM NINE - 4
Other Income/Deductions, Attribution - Exam Exercises

Exam Exercise Nine - 1 (Moving Expenses)

On November, 15, 2010, at the request of his employer, Mr. John Havlik moves from Halifax to Moncton. He lived in a rented apartment in Halifax, but has purchased a house in Moncton. Legal fees and other costs associated with the acquisition of this house totaled $3,250. The total cost of the actual move, including the costs of moving his personal possessions, is $8,300. In addition, he spent $650 on a house hunting trip to Moncton, but he did not decide on a house until his return to Halifax. He also incurred a $1,200 penalty for breaking his lease in Halifax.

During the year, his salary totaled $53,000, of which $6,625 can be allocated to the period after November 15, 2010. His employer is prepared to pay up to $6,000 towards the cost of the move. Determine Mr. Havlik's maximum moving expense deduction for 2010, as well as any carry forward available.

Exam Exercise Nine - 2 (Child Care Expenses)

Mr. Renaud and Ms. Fortune have lived together for over 15 years and have three children. The ages of the children at the end of 2010 are 3, 11, and 15. All three children enjoy good mental and physical health. Mr. Renaud works as a carpenter and has received income for the year of $52,000. However, he will only report $12,000 of this total in his current tax return (he believes that, because most of the income is received in cash and he has no receipts for his expenses, he does not have to report the full amount).

Ms. Fortune has business income of $62,000, all of which she reports. As Mr. Fortune is the lower income spouse, he receives $1,200 in universal child care benefits during 2010. The child care costs for the current year, all paid for by cheque and properly documented for tax purposes, total $11,200.

Determine the maximum deduction for child care costs and indicate who should claim them.

Exam Exercise Nine - 3 (Child Care Expenses)

Mrs. and Mr. Anders have three children who, at the end of 2010, are 4, 12, and 21 years of age. The 21 year old child lives at home because of a physical infirmity. He does not, however, qualify for the disability tax credit.

Mrs. Anders had earned income of $18,000, while Mr. Anders had earned income of $69,000. Payments for child care were $190 per week for a total of 50 weeks. As the lower income spouse, Mrs. Anders received $1,200 in universal child care benefits during 2010.

During 2010, Mrs. Anders spent six weeks in jail as the result of a conviction for possession of an illegal substance. Following her release, Mr. Anders spent three weeks in the hospital because of a stress related disorder.

Determine the maximum deduction for child care costs and indicate who should claim them.

Exam Exercise Nine - 4 (Support Payments)

On May 1, 2010, Leon and Shannon Weiss sign a separation agreement that calls for Shannon to pay Leon $1,200 per month in child support (Leon will have custody of their three children) and $2,100 per month in spousal support beginning on June 1. To the end of 2010, Shannon's payments total only $9,500. How will these payments be dealt with in Shannon and Leon's 2010 tax returns?

Exam Exercise Nine - 5 (Annuity Payments)

On January 1 of the current year, Ms. Lorraine Brock uses $10,000 of her savings to acquire a fixed term annuity. The term of the annuity is three years, the annual payments are $4,020, the payments are received on December 31 of each year, and the rate inherent in the annuity is 10 percent. What is the effect of the $4,020 annual payment on Ms. Brock's Net Income For Tax Purposes?

Exam Exercise Nine - 6 (Income Attribution - Spouse)

On December 28, 2009, Mrs. Chastity Blue gives her husband shares in a public company with an adjusted cost base of $42,000 and a fair market value of $38,000. During 2010, the shares pay taxable dividends of $5,184 [(144%)($3,600)]. On December 1, 2010, Mr. Blue sells the shares for $53,000. Assume that Mrs. Blue does not elect out of ITA 73(1). What are the tax consequences for Mr. and Mrs. Blue in each of the years 2009 and 2010?

Exam Exercise Nine - 7 (Income Attribution - Spouse)

On December 31, 2009, Mr. Tom London gives shares with an adjusted cost base of $21,500 and a fair market value of $35,200 to his wife, Barbara London. On February 24, 2010, the shares pay eligible dividends of $2,060 ($2,966 taxable amount) and, on August 31, 2010, Mrs. London sells the shares for $39,800. Assume that Mr. London does not elect out of ITA 73(1). What are the tax consequences for Mr. and Mrs. London in each of the years 2009 and 2010?

Exam Exercise Nine - 8 (Income Attribution - Related Minor)

On December 31, 2009, Mr. Tom London gives shares with an adjusted cost base of $21,500 and a fair market value of $35,200 to his 9 year old son, Patrick London. On February 24, 2010, the shares pay eligible dividends of $2,060 ($2,966 taxable amount) and, on August 31, 2010, Patrick sells the shares for $39,800. What are the tax consequences for Mr. London and Patrick in each of the years 2009 and 2010?

Exam Exercise Nine - 9 (Income Attribution)

Mr. Randy Cleroux owns 1,000 shares of Lyton Industries Ltd. These shares have an adjusted cost base of $105 per share. On December 31, 2009, the shares are trading at $156 per share. At this time, he gives 400 of these shares to his 12 year old son. He gives the remaining 600 shares to his wife.

During 2010, the shares pay eligible dividends of $4.50 per share. On December 31, 2010, both his son and his spouse sell their shares for $142 per share. Assume that Mr. Cleroux does not elect out of ITA 73(1). Indicate the tax consequences of these transactions for Mr. Cleroux, his son, and his spouse, in each of the years 2009 and 2010.

Exam Exercise Nine - 10 (Income Attribution - Use Of Loans)

On December 31, 2009, Mrs. Danielle Lafarge gives corporate bonds to her husband in exchange for a note with a face value of $131,000. The corporate bonds have an adjusted cost base of $119,000 and a fair market value of $131,000. The note from her husband does not pay interest and has no specific maturity date. Mrs. Lafarge does not report a gain or loss on these bonds in 2009.

During 2010, the bonds pay interest to Mr. Lafarge in the amount of $5,600. On October 1, 2010, immediately after an interest payment, Mr. Lafarge sells the bonds for $134,000. He uses $131,000 of the proceeds to pay off the loan owing to his wife. What are the tax consequences for Mr. and Mrs. Lafarge in each of the years 2009 and 2010?

TIF PROBLEM NINE - 5
Other Income/Deductions - Key Term Matching

The following five key terms were listed at the end of Chapter 8, “Other Income, Other Deductions And Income Attribution”.

A. Canada Learning Bonds

B. Child Support

C. Disability Supports Deduction

D. Registered Education Savings Plan

E. Death Benefit

The following list contains 10 potential definitions for the preceding key terms.
NOTE There is only **ONE** correct definition for each key term.

1. A deduction available to individuals for medical expenses incurred to allow the disabled individual to work or to attend a designated educational institution.

2. A system of grants under which the federal government makes contributions to an individual's RESP based on a percentage of the contributions to that individual's RESP that have been made by others.

3. A trusteed arrangement that allows individuals to make deductible contributions that will be invested on a tax-free basis, with the accumulated funds being used to provide for the post-secondary education of a child.

4. A support amount that is not identified as being for the benefit of a spouse or common-law partner, or a former spouse or common-law partner.

5. All amounts in excess of $10,000 that are received from an employer by a spouse or other related party in a taxation year, on or after the death of an employee, in recognition of the employee’s service in an office or employment.

6. A deduction available to individuals for attendant care and other disability support expenses, incurred to allow the disabled individual to work or to attend a designated educational institution.

7. All amounts in excess of $10,000 that are received by a taxpayer in a taxation year, on or after the death of an employee, in recognition of the employee’s service in an office or employment.

8. A system of grants under which the federal government makes contributions to an individual's RESP based on the number of years in which the individual's family is eligible for the National Child Benefit supplement.

9. A non-deductible support amount that is for the benefit of a child of the payor.

10. A trusteed arrangement that allows individuals to make non-deductible contributions that will be invested on a tax-free basis, with the accumulated funds being used to provide for the post-secondary education of a child.

Required: For each of the five key terms listed, indicate the number of the item that provides the **BEST** definition of that term. As only one definition is completely correct, please indicate only one number for each key term. No marks will be awarded if you indicate more than one number for any key term.

TIF PROBLEM NINE - 6
Child Care Expenses

Both Mr. Fortin and Mrs. Fortin are employed. During 2010, Mr. Fortin had opened a restaurant and had business income of $8,000. Mrs. Fortin had employment income of $63,000, mostly from commission sales during 2010. Since Mrs. Fortin's work required a good deal of travel away from home and Mr. Fortin's new restaurant required him to work long hours, including many evenings, they had to pay for care of their children. Payments for child care amounted to $200 per week, for a total of 48 weeks.

Also during the current year, there was a period of six weeks during which Mr. Fortin was hospitalized due to injuries suffered during a game of Ultimate Frisbee. This period was part of the 48 weeks for which child care payments were made. During 2010, as the lower income spouse, Mr. Fortin received $2,400 in universal child care benefits.

Required: Determine the maximum amount that can be deducted by Mr. and Mrs. Fortin for the year ending December 31, 2010 for child care expenses under the following assumptions:

A. They have two children, neither of whom qualify for the ITA 118.3 disability tax credit. Their ages are 2 and 4 years old.

B. They have three children, none of whom qualify for the ITA 118.3 disability tax credit. Their ages are 2, 4, and 15 years old.

TIF PROBLEM NINE - 7
Income Attribution

Mr. John Tucker is 45 years old and married to Janet Tucker. On December 31, 2009, their son, Martin, is 23 years old, while their daughter, Doreen, is 12 years old.

At the end of 2009, John is holding equity securities of a public company with an adjusted cost base of $85,000 and a fair market value of $123,000. He is considering transferring these securities to either his wife or to one of his two children. He seeks your advice as to the tax consequences, both to himself and to the transferee, that would result from such a transfer.

During your discussions, Mr. Tucker has indicated the following:

- The transfer will take place on December 31, 2009.
- Any proceeds he receives from his family on the share transfer will not be invested in income producing assets.
- He wishes you to assume that the securities would pay eligible dividends during 2010 of $6,500 ($9,360 taxable amount) and that the transferee would sell the securities on January 1, 2011 for $151,000.

Required: Each of the following independent Cases involves a transfer by Mr. Tucker to a member of his family. Indicate, with respect to the Net Income For Tax Purposes of both Mr. Tucker and the transferee, the 2009, 2010, and 2011 tax effects of:

- the transfer on December 31, 2009,
- the assumed 2010 receipt of the dividends, and
- the assumed 2011 disposition by the transferee.

Case A Mr. Tucker gives the securities to his wife and does not elect out of the provisions of the ITA 73(1) spousal rollover.

Case B Mr. Tucker's wife uses money from her savings account to purchase the securities for their fair market value of $123,000. Mr. Tucker does not elect out of the provisions of the ITA 73(1) spousal rollover.

Case C Mr. Tucker's wife uses money from her savings account to purchase the securities for $95,000. Mr. Tucker elects out of the provisions of the ITA 73(1) spousal rollover.

Case D Mr. Tucker gives the securities to his daughter, Doreen.

Case E Mr. Tucker's son, Martin, uses funds from his stock trading account to purchase his father's securities at their fair market value of $123,000.

Chapter Ten Test Item File Problems

TIF PROBLEM TEN - 1
Retirement Savings - Essay Questions

1. What are the tax advantages associated with making contributions to an RPP or an RRSP?

2. In many cases, investors with various types of investments in their RRSPs also have a portfolio of investments that are held outside of their RRSPs. When this is the case, tax advisors will indicate that, to the degree possible, they should include their debt securities inside of their RRSP, while allocating equity securities to their non-RRSP investment portfolio. What is the basis for this advice?

3. How is Earned Income defined for purposes of determining the RRSP Deduction Limit?

4. In calculating an individual's Pension Adjustment, it is necessary to have a mechanism for equating contributions in defined contribution plans with benefits earned in defined benefit plans. How does the RRSP legislation deal with this issue? Would you consider this approach to be fair to all taxpayers? Explain your conclusion.

5. One of your friends, a very wealthy businessman, has indicated that he never makes contributions to his RRSP in excess of amounts that he can deduct. His reasoning is that this doesn't make sense because, even though the contributions cannot be deducted when they are made, they will be subject to tax when they are withdrawn. Do you agree with your friend? Explain your conclusion, indicating any assumptions that you have made.

6. Briefly describe the options available to an individual in the year he reaches age 71 with respect to the assets in his RRSP. Also indicate the tax consequences of each alternative.

7. Under what circumstances would it be desirable for an individual to make contributions to an RRSP in favour of their spouse or common-law partner? What are the advantages of making such contributions?

8. One of your clients is considering the withdrawal of a portion of his RRSP balance under the provisions of the Home Buyers' Plan. List and briefly explain any factors that should be considered before deciding to make this withdrawal.

9. Profit Sharing Plans (PSPs) are not as effective as Deferred Profit Sharing Plans (DPSPs) in providing tax advantaged compensation to employees. Briefly explain this statement.

10. Describe the basic differences between an RRSP and a RRIF.

TIF PROBLEM TEN - 2
Retirement Savings - True Or False

1. In terms of tax planning, the use of Registered Retirement Savings Plans can provide for both tax deferral and tax avoidance.

   True or False?

2. A pension plan that provides for a pension equal to 3 percent of an employee's average annual salary for each year of service is a defined benefit plan.

   True or False?

3. Earned Income for RRSP purposes includes taxable spousal support received, business losses, and net rental income.

   True or False?

4. All RRSP contributions that cannot be deducted in the current year will be subject to a penalty of 1 percent per month.

   True or False?

5. A Registered Retirement Savings Plan is considered to be a spousal Registered Retirement Savings Plan if a spouse or common-law partner has made any contributions to the plan at any time since its inception.

   True or False?

6. Amounts withdrawn from a Registered Retirement Savings Plan under the provisions of the Home Buyers' Plan must be repaid over a period of 15 years, beginning in the second calendar year after the year of withdrawal.

   True or False?

7. Amounts withdrawn from a Registered Retirement Savings Plan under the provisions of the Lifelong Learning Plan must be used to pay tuition fees for a qualifying educational program at a designated educational institution.

   True or False?

8. An employer contributes $25,000 to a Registered Pension Plan on March 1, 2010. Each of the 15 employees in the plan has contributed $1,000 to the plan during 2010. The employer can deduct a maximum of $15,000 in contributions for the taxation year ending December 31, 2010.

   True or False?

9. Employees are allocated a taxable benefit for all amounts that an employer contributes to a Deferred Profit Sharing Plan.

   True or False?

10. There is no limit on the amount of a retiring allowance that can be transferred to a Registered Retirement Savings Plan on a tax free basis as long as the employer was not making vested contributions to a Registered Pension Plan or a Deferred Profit Sharing Plan for the employee.

    True or False?

TIF PROBLEM TEN - 3
Retirement Savings - Multiple Choice

Defined Benefit Vs. Defined Contribution

1. With respect to a defined benefit Registered Pension Plan, which of the following statements is correct?

   A. The employer is required to make a specific contribution to the plan in each year.
   B. The employer promises each employee a retirement benefit that is based on a contractually specified formula.
   C. The Pension Adjustment that will be calculated for each employee is based on the amounts of contributions that have been made by the employer.
   D. Employees cannot make contributions to this type of plan.

2. With respect to a defined contribution Registered Pension Plan, which of the following statements is not correct?

   A. The employer agrees to make a specified contribution for each year of service.
   B. The Pension Adjustment that will be calculated for each employee is based on the amounts of contributions that have been made by the employee and employer.
   C. Both the employee and employer can make contributions to such plans.
   D. The employee's ultimate pension benefit is not affected by rates of return on the pension plan assets.

RRSPs

3. With respect to self-administered Registered Retirement Savings Plans, which of the following is not a qualified investment?

   A. Shares in a publicly traded company.
   B. A mortgage on the principal residence of the plan beneficiary.
   C. Direct investments in rental properties.
   D. Canada Savings Bonds.

4. During the year ending December 31, 2009, Ms. Donna Collins has employment income before the deduction of any RPP contributions of $40,000, a net rental loss of $16,000, interest income of $6,000, and income from royalties of $7,000. The royalties were on a book written by Ms. Collins in her undergraduate years at university. She has no Unused RRSP Deduction Room from previous years.

   For each of the **independent** parts of the question, choose one of the following answers. Each answer can be used more than once.

A.	Nil	F.	$3,580.
B.	$ 400.	G.	$4,320.
C.	$ 580.	H.	$5,400.
D.	$1,660.	I.	$5,580.
E.	$2,580.	J.	$6,660.

   i) Ms. Collins is a member of a money purchase Registered Pension Plan in which, during 2009, she has contributed $2,000 and her employer has contributed $3,000. Her maximum deductible Registered Retirement Savings Plan contribution for 2010 is:

   ii) She is a member of a Deferred Profit Sharing Plan in which, during 2009, her employer has contributed $3,000 per employee. Assume that instead of having a 2009 net rental loss of $16,000, she had a net business loss of $16,000. Her maximum deductible Registered Retirement Savings Plan contribution for 2010 is:

TIF Problem Ten - 3

Retirement Savings - Multiple Choice

iii) She is not a member of a Registered Pension Plan during 2009. Assume that instead of receiving 2009 interest income of $6,000, she received dividends from taxable Canadian corporations with a total grossed up amount of $6,000. Her maximum deductible 2010 Registered Retirement Savings Plan contribution is:

iv) She is not a member of a Registered Pension Plan during 2009. She has contributed $2,000 to her husband's Registered Retirement Savings Plan in 2010. The maximum deductible 2010 Registered Retirement Savings Plan contribution to a plan in her name is:

5. Mrs. Jacks is employed by RME Industries Ltd. RME Industries Ltd. does not offer a Registered Pension Plan or a Deferred Profit Sharing Plan to its employees. She has no Earned Income prior to 2008. Given the following, what is the maximum RRSP contribution that Mrs. Jacks can deduct for the 2010 taxation year?

	2008	2009	2010
Earned Income	$50,000	$52,000	$53,000
RRSP Contributions Deducted	Nil	$ 6,000	?

A. $9,000.
B. $9,360.
C. $12,000.
D. $12,360.
E. None of the above.

6. Which one of the following lists describes items that are all included in the determination of Earned Income for RRSP purposes?

A. Author's royalties, net rental income or losses, and spousal support received/paid.
B. Auto standby charge, salesperson's expenses, and resource royalties.
C. Business income or losses, CPP retirement benefits, and research grants.
D. Rental income or losses, salaries, and scholarships.

7. With respect to RRSP contributions, which of the following statements is correct?

A. Contributions made during the current year and within 30 days of the end of the current year, must be deducted in the current year.
B. Contributions in excess of available deduction room cannot be deducted in the current year or in any subsequent year.
C. There is no penalty for making contributions that are in excess of available deduction room.
D. Contributions made during the current year can be deducted in any subsequent year.

Home Buyers' Plan

8. Which of the following statements with respect to the Home Buyers' Plan (HBP) is not correct?

A. All amounts withdrawn must be repaid within 10 years of the year of withdrawal.
B. Amounts withdrawn must be used to acquire a dwelling by October 1 of the year following withdrawal.
C. The maximum RRSP withdrawal is $25,000 per individual.
D. In the year an individual departs from Canada, any outstanding HBP balance must be repaid by the due date for his tax return for the year of departure.

RPPs

9. Eileen is a member of her employer's Registered Pension Plan to which her employer contributed $3,500 and Eileen contributed $2,600 in the current year. Which of the following statements is correct?

   A. Eileen can deduct her contribution from her Net Income For Tax Purposes and her employer's contribution is not considered a taxable benefit.
   B. Eileen cannot deduct her contribution from her Net Income For Tax Purposes and her employer's contribution is not considered a taxable benefit.
   C. Eileen can deduct her contribution from her Net Income For Tax Purposes and she must include her employer's contribution in her income.
   D. Eileen cannot deduct her contribution from her Net Income For Tax Purposes and her employer's contribution is considered a taxable benefit.

RRIFs

10. Which of the following statements with respect to Registered Retirement Income Funds (RRIFs) is correct?

    A. An individual can make non-deductible contributions to a RRIF.
    B. The minimum annual withdrawal from a RRIF is always determined by dividing the fair market value of the assets in the plan by 90, less the age of the beneficiary at the beginning of the year.
    C. Earnings accumulate within the RRIF on a tax free basis.
    D. A RRIF can only be established by individuals over the age of 71.

Transfers Between Plans

11. There are a number of tax free transfers of accumulated pension entitlements. Indicate the transfer that is not tax free.

    A. Registered Pension Plan to Registered Retirement Savings Plan.
    B. Registered Retirement Savings Plan to Registered Retirement Income Fund.
    C. Profit Sharing Plan to Deferred Profit Sharing Plan.
    D. Deferred Profit Sharing Plan to Registered Pension Plan.
    E. Registered Pension Plan to different Registered Pension Plan.

Retiring Allowances

12. Mr. Smith, the sole shareholder and employee of Smithco Ltd. since its incorporation in 1976, has decided to sell the corporation and retire in 2010. He has never belonged to a pension plan, and wishes to maximize his RRSP. Which one of the following amounts represents the **largest** retiring allowance from Smithco that Mr. Smith can transfer to his RRSP in the year he retires?

    A. $40,000.
    B. $56,000.
    C. $59,500.
    D. $70,000.

TIF PROBLEM TEN - 4
Retirement Savings - Exam Exercises

Exam Exercise Ten - 1 (Earned Income)
Mr. Marco Marconi has net employment income of $78,300, after the deduction of $2,400 in RPP contributions for the year. In addition, he has a business loss of $6,750, taxable dividends of $5,640, and pays $12,400 of deductible support to his former spouse. What is the amount of Mr. Marconi's Earned Income for RRSP purposes for the year?

Exam Exercise Ten - 2 (Pension Adjustments)
Ms. Calvin's employer sponsors both a money purchase RPP and a DPSP. During the current year, her employer contributes $2,600 to the RPP and $1,700 to the DPSP on behalf of Ms. Calvin. Ms. Calvin contributes $2,600 to the RPP. Calculate the amount of the Pension Adjustment that will be included on Ms. Calvin's T4 for the current year.

Exam Exercise Ten - 3 (Unused RRSP Deduction Room)
Mrs. Alison Lair has 2009 Earned Income for RRSP purposes of $43,500. She is not a member of an RPP or a DPSP. At the end of 2009, her Unused RRSP Deduction Room was $5,100. During 2010, she contributes $7,000 to her RRSP and makes an RRSP deduction of $5,200. What is the amount of Mrs. Lair's Unused RRSP Deduction Room and undeducted RRSP contributions at the end of 2010?

Exam Exercise Ten - 4 (Maximum RRSP Deduction)
During 2009, Mrs. White has taxable capital gains of $21,750, net rental income of $5,720, pays spousal support of $15,000, and has net employment income of $80,200. Based on her RPP contributions of $3,000 and the matching contributions made by her employer, her employer reports a 2009 PA of $6,000. At the end of 2009, Mrs. White has Unused RRSP Deduction Room of $11,120. Also at this time, her RRSP contains undeducted contributions of $6,275. During 2010, she makes contributions to her RRSP of $13,000.

Determine Mrs. White's maximum RRSP deduction for 2010. Assuming she deducts her maximum, determine the amount of any Unused RRSP Deduction Room that she will have available at the end of 2010, and indicate the amount of any undeducted contributions remaining at the end of 2010.

Exam Exercise Ten - 5 (Excess RRSP Contributions)
Mr. Jack Parnell is not a member of an RPP or a DPSP. At the beginning of 2009, Mr. Parnell has no Unused RRSP Deduction Room. During 2008 and 2009, he has Earned Income of $75,000 each year. On July 1, 2009, he makes a $13,500 RRSP contribution, but does not make any deduction for the year. In 2010, he has Earned Income of $60,000, makes a $16,000 contribution on May 1, but still does not make a deduction for the year. Determine any penalty that will be assessed to Mr. Parnell for excess contributions during either 2009 or 2010.

Exam Exercise Ten - 6 (Spousal RRSP Withdrawal)
During 2009, Austin Peters makes a $1,500 contribution to a new RRSP in which his wife is the registrant. His wife also makes a $2,800 contribution to this RRSP in 2009. During 2010, he makes a $2,000 contribution to this RRSP. During 2011, Mr. Peters' wife makes a withdrawal of $4,300 from this RRSP. How will this withdrawal be taxed?

Exam Exercise Ten - 7 (Home Buyers' Plan)

During 2008, Mr. John Debon withdraws $15,000 from his RRSP, using the provisions of the Home Buyers' Plan (HBP). As he received the proceeds from a winning lottery ticket in 2009, he repaid $8,500 of the HBP balance in that year. What is the minimum repayment that must be paid during 2010? If he makes no payment during 2010, what will be the minimum payment that must be made during 2011?

Exam Exercise Ten - 8 (Lifelong Learning Plan)

Mr. Jules Forsyth enrolls in a four year university program running from September, 2009, through April, 2013. In order to finance this program under the provisions of the Lifelong Learning Plan (LLP), he withdraws $10,000 from his RRSP in September, 2009, a further $5,000 in September, 2010, and an additional $5,000 in September, 2011. The university course is completed successfully.

In June, 2014, a designated repayment of $2,900 is made. In November, 2015, a designated repayment of $1,500 is made.

Explain the tax consequences of the withdrawals and repayments described for Mr. Forsyth.

Exam Exercise Ten - 9 (Minimum RRIF Withdrawal)

On January 1, 2010, Ms. Sheila Salon transfers all of her RRSP balances into a RRIF. At this time, Ms. Salon is 67 years of age. On January 1, 2010, the fair market value of these assets is $1,450,000. The corresponding balance on January 1, 2011 is $1,350,000. What is the minimum withdrawal that Ms. Salon must make from the RRIF during 2010 and during 2011?

Exam Exercise Ten - 10 (Retiring Allowance)

As of December 31, 2010, Mrs. Mary Barth has worked for her current employer for 27 years. On this date she retires and, in recognition of her devoted service, her employer pays her a retiring allowance of $85,000. Her employer has never sponsored an RPP or DPSP. What is the maximum deductible contribution that Mrs. Barth can make to her RRSP as a result of receiving this retiring allowance?

TIF PROBLEM TEN - 5
Retirement Savings - Key Term Matching

The following five key terms were listed at the end of Chapter 10 on Retirement Savings:

A. RRSP Deduction Room

B. Pension Adjustment (PA)

C. Salary Deferral Arrangement

D. Lifelong Learning Plan

E. Money Purchase Plan

The following list contains 10 potential definitions for the preceding key terms.
NOTE There is only **ONE** correct definition for each key term.

1. A funded arrangement under which an individual who has the right to receive compensation, postpones the receipt of that compensation, and it is reasonable to assume that one of the main purposes of this postponement was to defer the payment of taxes.

2. A provision that allows individuals to make permanent non-taxable withdrawals from their RRSP when they are enrolled in a qualifying education program at a qualifying educational institution.

3. A retirement savings plan in which the plan sponsor (employer or individual) makes known or determinable contributions. The retirement benefit is based on the accumulated contributions and earnings on investments within the plan.

4. The amount that is the sum of the unused RRSP deduction room at the end of the preceding year, plus the amount by which the lesser of the RRSP Dollar Limit and 18 percent of earned income for the preceding year exceeds the Pension Adjustment for the preceding year. This sum is adjusted for any Past Service Pension Adjustment or Pension Adjustment Reversal. It represents the maximum amount of contributions that have been made to an RRSP that can be deducted for a year.

5. An arrangement, whether funded or not, under which an individual who has the right to receive compensation, postpones the receipt of that compensation, and it is reasonable to assume that one of the main purposes of this postponement was to defer the payment of taxes.

6. An adjustment reported by employers which reflects, for an individual employee, the employee and employer contributions to RPPs and DPSPs for the previous year (in the case of defined benefit RPPs, benefits are converted to an equivalent amount of contributions).

7. A retirement savings plan in which the plan sponsor (employer or individual) makes known or determinable contributions. The retirement benefit is based on a formula which is tied to the individual's historical earnings record.

8. The excess of the RRSP deduction limit, over the amount of RRSP contributions that have been deducted.

9. A provision that allows individuals to make temporary, non-taxable withdrawals from

their RRSP when they are enrolled in a qualifying education program at a qualifying educational institution.

10. An adjustment reported by employers which reflects, for an individual employee, the employer's contributions to RPPs and DPSPs for the previous year (in the case of defined benefit RPPs, benefits are converted to an equivalent amount of contributions).

Required: For each of the five key terms listed, indicate the number of the item that provides the **BEST** definition of that term. As only one definition is completely correct, please indicate only one number for each key term. No marks will be awarded if you indicate more than one number for any key term.

TIF PROBLEM TEN - 6
Deductible Retirement Savings Contributions

Henry Plate's Earned Income for RRSP purposes for 2009 was $52,000. During the year ending December 31, 2009, Mr. Plate's records indicate that he contributed $2,500 to a money purchase RPP sponsored by his employer. His employer contributed the same amount on his behalf during this period. At the end of 2009, he had no Unused RRSP Deduction Room or undeducted RRSP contributions.

Mr. Plate's 2010 Earned Income was $65,000. During the year ending December 31, 2010, Mr. Plate's records indicate that he contributed $2,800 to a money purchase RPP sponsored by his employer. His employer again matched his contribution to his RPP during 2010.

Mr. Plate made a $5,000 contribution to his RRSP on April 30, 2010.

Required: Indicate which of the contributions that have been made by Mr. Plate can be deducted in calculating his Net Income For Tax Purposes for the 2010 taxation year and any carry forwards available to him at the end of 2010.

TIF PROBLEM TEN - 7
RRSP Contribution Calculations

During 2009, Mr. Bornstein has the following income and loss data:

Salary	$51,450
Taxable benefits	1,580
Profit from investment advisory business	3,925
Net loss on rental property	(10,750)
Spousal support received from ex-wife	2,520
Eligible dividends from Canadian public corporations	2,850
Interest on Ontario Hydro bonds	3,750

In addition to the preceding information, Mr. Bornstein paid union dues of $110. During 2009, Mr. Bornstein was not a member of a Registered Pension Plan or a Deferred Profit Sharing Plan.

At the end of 2009, Mr. Bornstein had Unused RRSP Deduction Room of $900 and no undeducted contributions in his RRSP account. On June 15, 2010, he contributes $10,000 to his RRSP. Mr. Bornstein deducts the maximum allowable contribution to his RRSP in 2010.

Required: Determine Mr. Bornstein's 2010 RRSP Deduction Limit, his Unused RRSP Deduction Room at the end of 2010, and any RRSP contributions available for carry forward purposes.

TIF PROBLEM TEN - 8
Employment Income With RRSP

During the year ending December 31, 2010, Ms. Nancy Harcourt earned a gross salary of $72,000. Her employer withheld the following amounts from her salary:

Canada Pension Plan Contributions	$ 2,163
Employment Insurance Premiums	747
Income Taxes	18,500
Registered Pension Plan Contributions	4,200
Parking Fees - Company Garage	480
Donations To United Way	800
Union Dues	360

Other Information:

1. Ms. Harcourt is a member of her employer's money purchase RPP. Her employer made a contribution on her behalf that was equal to the $4,200 contribution that was withheld from her salary.
2. As a reflection of the excellent service rendered by Ms. Harcourt over several years, one of her employer's customers gave her an all expense paid trip to the Bahamas in March, 2010. The cost of this trip was $5,600 and, in addition, Ms. Harcourt was provided with $1,000 in cash for incidental expenses during the month that she was on the trip.
3. Ms. Harcourt's employer provides her with a car that cost the company $53,000, plus $2,650 in GST and $4,240 in PST. The employer purchased the car in 2009. Ms. Harcourt drives the car a total of 36,000 kilometers during the year, 16,000 kilometers of which were for employment related purposes. The car was available to Ms. Harcourt for the entire year, with the exception of the one month that she was in the Bahamas. She left the keys to the car with her employer during this period.
4. Ms. Harcourt's employer provides a 20 percent discount to employees on all merchandise sold by the enterprise. During the year, Ms. Harcourt purchased merchandise with a list price of $12,000 and received a discount of $2,400.
5. In addition to her employment income, Ms. Harcourt had taxable capital gains from stock market trading of $6,200, a net rental loss of $3,900, and a self-employed business loss of $24,600.
6. At the end of 2009, Ms. Harcourt's Unused RRSP Deduction Room was $4,500 and she had no undeducted RRSP contributions. Her employer reported that she had a 2009 Pension Adjustment of $7,000. Her Earned Income for 2009 is equal to her 2010 Earned Income.

Required:

A. Calculate Ms. Harcourt's net employment income for the year ending December 31, 2010.

B. Calculate Ms. Harcourt's maximum deductible RRSP contribution for 2010.