École de gestion
TELFER
School of Management

LIÉE au LINKED with LEADERSHIP

Mid-Term Exam #1 (2 hours)

ADM 3345 – Tax I
October 4, 2008

Student Name:: Karl Sabas

Student I.D.: 5039040

Question #1	12 /16
Question # 2	~~15~~ 14 /20
Question # 3	8 /8
Total:	~~35~~ 34 /44 ~~77~~ 80 /100

Statement of Academic Integrity
The School of Management does not condone academic fraud, an act by a student that may result in a false academic evaluation of that student or of another student. Without limiting the generality of this definition, academic fraud occurs when a student commits any of the following offences: plagiarism or cheating of any kind, use of books, notes, mathematical tables, dictionaries or other study aid unless an explicit written note to the contrary appears on the exam, to have in his/her possession cameras, radios (radios with head sets), tape recorders, pagers, cell phones, or any other communication device which has not been previously authorized in writing.

Statement to be signed by the student:
I have read the text on academic integrity and I pledge not to have committed or attempted to commit academic fraud in this examination.

Signed: Karl Sabas

Note: an examination copy or booklet without that signed statement will not be graded and will receive a final exam grade of zero.

Question #1: Employment Income (16 Marks)

Ms. Willow is a sales representative for a large corporation listed on a Canadian stock exchange on January 1, 2008. Her gross salary for the year ending December 31, 2008 is $26,000. In addition, she earned commissions of $163,500, of which $\boxed{\$155{,}500}$ was paid before December 31, 2008. For the 2008 taxation year, Ms. Willow's employer withheld the following amounts from her income:

Federal & Provincial Income Taxes	$79,400	CPP Premiums	~~$2,049~~
Registered Pension Plan Contributions	~~4,200~~	EI Premiums	~~711~~

Ms. Willow's employer made a $4,200 matching contribution to her registered pension. meaning she contributed $4,200 to her RPP.

deduc.

Other Information:

not a tax. benefit

2 quarters

1. Since the time she was hired, Ms. Willow had been driving her own vehicle for her business purposes. She has been receiving a reasonable allowance, based on careful documentation of her business trips. This system has worked well for both Ms. Willow and the company – until the end of March 2008. On January 1, 2008, Ms. Willow purchased a new Lamborghini. Given the increased costs of financing such a vehicle (and paying all those speeding tickets!), Ms. Willow has requested an allowance of $15,000 for each quarter of 2008, beginning with the first quarter ending March 31, 2008, regardless of the mileage she actually drove for business purposes. The company paid her requested amounts. Ms. Willow's business mileage for the first quarter was 23,000 kilometers and 27,000 kilometers for the second quarter. She has retained no receipts related to the operation of her Lamborghini but has complete and accurate records of her business travel.

tax. benefit

not an allowed deduc b/c no records kept to operating cost

2 quarters

2. The company determined that the allowance was too much and it would be preferable to provide Ms. Willow with a new company-owned vehicle. They acquired a BMW at a cost of $65,000 for Ms. Willow's business use. The car has been available to her since July 1, 2008, and she has driven it a total of 218,000 kilometers. Of this total, 4,900 kilometers were for personal use during November and December after Ms. Willow crashed her Lamborghini in November. Ms. Willow did not reimburse her employer for her personal use of the automobile.

3. On April 1, 2008, Ms. Willow received a $150,000 loan from her employer. The loan requires annual interest payments at a rate of 4% but Ms. Willow won't pay the interest for 2008 until January 30, 2009. The prescribed rates for 2008 were as follows:

1^{st} quarter	90 days	4%
2^{nd} quarter	91 days	5%
3^{rd} quarter	92 days	6%
4^{th} quarter	92 days	6%

The anticipated prescribed rate for the first quarter of 2009 (90 days) will be 7%.

No deferral

4. In 2004, Ms. Willow was given options to buy 5000 shares of her employer's stock at a price of $22 per share. At the time the options were issued, the shares had a fair market value of $18 per share. On June 1, 2008, when the shares had a fair market value of $30 per share, Ms. Willow exercised her option and purchased 500 shares.. She anticipates keeping the shares for at least two years and did not make any elections related to her purchased shares. ~~In July, Ms. Willow also purchased another 500 shares of her employer's stock at a price of $31 per share through her broker. By December 31, the company's shares had increased in value to $35 per share.~~

Non-taxable ben.

5. During the year, Ms. Willow 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. Her employer reimbursed her fully for these costs on presentation of the receipts.

$200 watch taxable benefit

allowed

6. At the office Christmas party, everyone including Ms. Willow received a $150 bottle of champagne as a Christmas gift. At the same time, Ms. Willow was lauded as the company's best sales representative. She received a large trophy valued at $350 as an award for her sales accomplishments during 2008. She also received a $200 watch in recognition of her years of service. In addition, throughout the year she received a $100 picture for her 40th birthday and a $40 turkey for Thanksgiving. allowed

allowed allowed

Only allowed 2 gifts
* add $40 to income
- lost 1 mark

Required:

Calculate Ms. Willow's minimum net employment income for the year ending December 31, 2008.

Show all your calculations to obtain full marks!

Net Employment Income

Gross Salary	$26,000
Sales Commissions	155,500
	181,500

Allowances

First two quarters of 2008 [$15,000 x 2] 30,000 ← Add to Income

Company Car Benefit

Kilometers (on average) driven in Nov/Dec '06

$\frac{218,000 \text{ km}}{6 \text{ mths}} = 36\,333$ km/month

36,333 km/mth x 2 mths = 72,666 km

Personal-use Ratio

$\frac{4900}{72,666 \text{ km}} = 6.7\%$ ∴ Eligible for Reduced Standby Charge/Operating Cost Benefit

Standby Charge

= 2% x Cost of Car x Months Available for use in year

= 2% x 65000 x 6 2

= $7800

2

Solution to Question #1:

Operating Cost Benefit

$= \$0.24/km \times$ Personal km driven

$= \$0.24 \times 4900$

$= 1,176$

Reduced Standby Charge

$=$ Regular stdby charge $\times \frac{\text{Personal km}}{1,667 \times \text{\# of months in use}}$

$= 7800 \times \frac{4900}{1,667 \times 6}$

$= 3,821$

Reduced operating Cost Benefit

Lesser of $=$ 50% $\times$ Stdby Charge or Orig. Operating Cost Benefit

$=$ 50% $\times$ 3,821 or 1,176

$=$ 1,911 or 1,176

∴ Company Car Benefit $= 3,821 + 1,176 =$ \$4997. ← Add to Income

Employee Loan Benefit

Imputed Interest

1st quarter:	[150,000 × 4% × 1/4]	= 1,500
2nd quarter:	[150,000 × 5% × 1/4]	= 1,875
3rd/4th quarter:	[150,000 × 6% × 2/4]	= 4,500
Total Imputed Interest		7,875
less: Interest paid by Employee		(0)
∴ Employee Loan Benefit		7875 ← Add to Income

days

← Lost 2 marks there...

Stock option Benefit

$500 \times (30-22)$ $=$ \$4000 ← Add to Income

Gifts (above limit of \$500)

Watch \$200 ← Add to Income

4

Income from all sources = 26,000 + 155,500 + 30,000 + 4997
+ 7875 + 4000 + 200
= 228,572

Deductions

Less: Employee's RPP Contribution	(4,200)
Minimum Net Employment Income	224,372

lost 1 mark there ...

6

FPE of for 2005= 31+30+31+30+31 = 153 days

7% amort. no 1/2 yr rule

Question # 2: Capital Cost Allowance and Cumulative Eligible Capital (20 Marks)

Custom Productions Ltd. (CPL) was incorporated on August 1, 2005 at a cost of $5,500 and selected a December 31st year end. The company produced custom pre-manufactured woodwork which their carpenters install in new, high-end homes. On August 1, 2005, CPL purchased a variety of woodworking equipment, including lathes, band saws and miter saws, for a total $250,000 (Class 8, 20%). All of these assets will be pooled into one class. Business was successful right from the start, and CPL's net income for the 153 days of operation during 2005 was $107,324. ?? relevant ??

Business was booming and therefore in 2006, CPL purchased a competitor, paying a total of $256,000 of which $90,000 was for goodwill.

In 2008, Custom Productions Ltd. sold the business it had acquired in 2006, and the sale price included $112,200 for the goodwill. On December 31, 2008, CPL also sold the equipment it purchased in 2005 for $82,600. New equipment was arriving on January 3, 2009.

Custom Productions Ltd. has a company policy of taking the maximum deductions permitted under tax law.

Required:

Identify any and all tax consequences CPL will incur on all its assets (tangible and intangible) from the year of purchase to the year of disposition.

Show all your calculations and, if required, round decimal points up to the nearest dollar.

Class 8 - Year 2005

Beginning UCC		Ø
Add: Product Additions		250,000
Deduct: (1/2 Net Additions)	2	(125,000)
CCA Base		125,000
Maximum CCA [20% x 125,000 x 153/365]	3	(10,479)
Add: 1/2 Net Additions		125,000
Ending UCC Balance		239,521

Class 8 - Year 2006

Beginning UCC		239,521
CCA Base		239,521
Maximum CCA [20% x 239,520]	1	(47,904)
Ending UCC Balance		191,616

↓

6

1) Why no marks for Yr 2008 CCA?
2) Yr 2007 CEC?
3) Yr 2008 CEC

Subtotal on p.6 s/b 5

Solution to Question #2:

Class 8 - Year 2007		
Opening UCC Balance		191,616
CCA Base		191,616
Maximum CCA [20% x 191,616]		(38 323)
Ending UCC Balance		153 293
Class 8 - Year 2008		
Opening UCC Balance		153 293
CCA Base		153 293
Maximum CCA [20% x 153 293]		(30 659)
Ending UCC Balance		122,634
Product Disposition: 2008		
UCC Balance (given)		122,634
Product disposition: lesser of		
Capital Cost	250,000	
Proceeds from sale	82,600	(82,600)
Terminal Loss		40,034 ← deduc. from Inc
CEC: Year 2006		
Opening UCC Balance		∅
Additions		
Goodwill [3/4 x 90,000]		67,500
CEC Base		67,500
Maximum CEC [7% x 67500]		(4,725)
Ending UCC Balance		62,775
CEC: Year 2007		
Opening UCC Balance		62,775
CEC Base		62,775
Maximum CEC [7% x 62,775]		(4,394)
Ending UCC Balance		58,381

↓ continued

Question 2 (cont'd)

CEC: Year 2008

Opening UCC Balance	58,381
CEC Base	58,381
Maximum CEC [7% x 58,381]	(4,087)
Ending UCC	54,294

Product Disposition: Year 2008

UCC Balance (given)	54,294
Less: Product Disposition [3/4 x 112,200]	(84,150)
Ending UCC	(29,856)

Negative ending UCC is split into 2 components:

Cumulative CEC deducted [4,725 + 4,394 + 4,087] = 13,206 ← Recapture

Difference is treated as a capital gain [29,856 − 13,206 = 16,650]

Capital Gain [16,650 x 2/3] = 11,100 ← Included in Income as a Cap Gain (cannot be reduced by Cap losses

∴ Year 2005
- CCA Deduction = 10,479

Year 2006
- CCA Deduction = 47,904
- CEC Deduction = 4,725

Year 2007
- CCA Deduction = 38,323
- CEC Deduction = 4,394

Year 2008
- CCA Deduction = 30,659
- CEC Deduction = 4,087
- CCA Terminal loss Deduction = 40,034

$\left.\right\}$ Deductions from Income

- CEC Recapture = 13,206 ← Included in Income
- Capital Gains = 11,100 ←

4

Question #3: Calculating Net Income for Tax Purposes (8 Marks)

Desdemona Lafleur worked for the National Art Gallery in Ottawa as an art restorer. Her total employment income for 2008 was $50,000. Evenings and weekends, Desdemona also operated her own unincorporated business selling art posters at various fairs and expositions in the local community. Unfortunately in April 2008, a flood in her basement ruined a large quantity of posters and since Desdemona was not insured, she incurred a business loss of $11,000.

Desdemona earns royalties on a painting that has been turned into a poster, and in 2008 she earned royalties of $12,000. She also earned $5,000 of interest on her investments. Desdemona sold some shares in 2008, incurring an allowable capital loss of $1,000 on Nortel shares and a taxable capital gain of $3,000 on shares of Loblaws.

Desdemona has incurred $7,000 in subdivision e child care expenses.

Required:

Using proper (aggregating formula) format, calculate Desdemona's Net Income for Tax Purposes (NIFTP).

NIFTP = Income from all sources
+ Taxable Capital Gains
− Subdivision e deductions
− Current Year Non-Capital losses

Income from all Sources

Employment Income		$50,000
Royalties		12,000
Interest		5,000
Total		67,000
Taxable Capital Gains		
Loblaws Shares	3,000	
Cap Loss: Nortel	(1,000)	
Taxable Capital Gain		2,000
Subdivision e Child care expenses		(7,000)
Current Year Non-Capital Losses		(11,000)
NIFTP		51,000

8

~~Cars~~

1 buildings

3 buildings - pre 1988

8 machinery equip. furniture

10 Cars

10.1 Cars

12 Comp. software (excl. systems software) and small items

13