# Intro to Income Tax

# Popular Conception

Canada Customs and Revenue Agency | Agence des douanes et du revenu du Canada

**1040 EZ 2 DO TAX FORM**
**New Simplified Tax Form**

1. How much money did you make? $___________

2. Send it to us.

Canada

# Forms of Taxation

- Income Tax
- Property Tax
- Consumption Tax
- Value Added Tax
- Tariffs or Customs Duties
- Transfer Tax
- User Tax
- Capital Tax
- Head Tax

# Classifications of Taxation

Regressive

The HST is considered Regressive. As income rises, an individual spends less of their income on goods as a %. Therefore pays less HST.

Ex.
Mr. A earns $300,000 and incurs $10,000 in HST (3% of income paid).

Mr. B earns $40,000 and incurs $10,000 in HST (25% of income paid).

# Classifications of Taxation

Progressive

The Income Tax is considered Progressive. As income increases, tax rates rise.

Example:

| | |
|---|---|
| Up to $43,000 | 24.1% |
| $43,001 to $87,000 | 34.1% |
| $87,001 to $135,000 | 38.4% |
| $135,000 and up | 43.3% |

# Pitfalls from Progressive

**Complexity** – splitting income to reduce rates

**Income Fluctuations** – high/low year over year

**Family Unit Problems** – one earner vs. two

**Economic Growth** – Disincentive to earn more

**Tax Concessions** – Ability for high income to plan

**Tax Evasion** – Discourages income reporting

# History of Income Tax

‘Temporary’ war tax established to fund World War I in 1917.

Used for:

- Resource Allocation
- Distribution Effects
- Stabilization Effects
- Fiscal Federalism

Textbook quote on the ITA. “..running about 2,000 pages and which in our opinion, cannot be readily understood by most individuals.”

# Why Study Tax?

Large Corporate Planning – Offshoring?

Entrepreneurs – Local sources of employment

Individuals – Optimizing resources

# Goals of Planning

Tax avoidance or reduction

Tax deferral

Income Splitting

# The Income Tax Act (ITA)

6(1) "There shall be included in computing the income of a taxpayer for a taxation year as income from an office or employment such of the following amounts as are applicable:

(a) The value of board, lodging and other benefits of any kind whatever received or enjoyed by the taxpayer in the year in respect , in the course of, or by virtue of an office or employment, except any benefit…

# The Income Regulations (ITR)

ITA

Elections available to be late filed are as prescribed.

ITR

For the purposes of subsection X(X) the following are prescribed elections:

# Treaties

Example: US-Canada Income Tax Convention

If a taxpayer is liable for tax in both the US and Canada, the treaty will intervene so the taxpayer only pays tax in one country.

Uses: Avoiding Double Taxation OR Create Tax Avoidance

Bermuda does not tax capital gains. Gains that can be shifted into Bermuda instead of Canada will reduce overall taxes owing.

# Interpretation Bulletins (Folios)

IT-533-- Interest Deductibility and Related Issues

*Disappearing source rules* 19. In general terms, the disappearing source rules in section 20.1 apply where borrowed money ceases to be used for the purpose of earning income (i.e., the borrowed money can no longer be traced to any income earning use). Generally, the borrowed money that is no longer linked to any income earning use is nonetheless deemed to be used for the purpose of earning income such that interest continues to be deductible for that portion of the borrowed money. Several specific conditions in section 20.1 must be met for that section to apply.

*Example 6* Mr. O acquired property P with $1,000 of borrowed money, the entire amount of which remains outstanding and the interest thereon is deductible. Mr. O subsequently disposed of property P for its fair market value of $600 and used the $600 to reduce the outstanding loan. If the conditions in section 20.1 apply, the remaining $400 of borrowed money would be deemed to be used for the purpose of earning income and the interest thereon would continue to be deductible.

# Others

Court Cases

Tax Court of Canada, Federal Court of Appeal, Supreme Court of Canada

CRA website

www.cra.gc.ca (old)
www.Canada.ca/en/revenue-agency.html (new)

# Levels of Courts - Taxation

Level 3 — Supreme Court

Level 2 — Federal Court of Appeal

Level 1 — Tax Court of Canada

Tax cases are heard by lower courts first.

The decision of a lower court can be "appealed" to a higher court for a new answer.

The higher court does not have to agree to the appeal.

Higher court decisions have greater precedence.

# Liability for Taxes

# Persons

Include:

- Individuals (Natural persons)
- Corporations (Limited, Ltd, Incorporated, Inc.)
- Trusts


But not:

- Partnerships

# Provincial and Federal Taxation

- Separate Tax Acts.
- Federal is more comprehensive, provinces tend to mimic
- Combined Reporting (except QC)

Credits used in this course will be the Federal, where possible I will use combined tax rates assuming residence in NB.


N
W
E
S
Alaska
Yukon
Northwest
Territories
Nunavut
Labrador
Labrador
Sea
Newfoundland
British
Columbia
Hudson
Bay
Alberta
Manitoba
Quebec
Prince Edward
Island
Ontario
Pacific
Ocean
Nova
Scotia
Saskatchewan
New
Brunswick
Atlantic
Ocean
USA
©VRBO 2009

# Residency in Canada (Federal)

**Corporations**

- Incorporated in Canada
- Shareholders or directors reside in Canada

**Individuals**

- House
- Spouse
- Children
- Employment
- Investments/bank accounts
- Assets and licenses
- Time and duration of visits

# Residency in a Province

**Corporations**

- Wages paid in the province
- Revenues earned in the province

**Individuals**

- Location of residency on December 31st.

# Basic Tax Concept

+ Earnings
- Expenditures to earn income (deductions)

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Taxable Income

x Applicable Rate (provincial + federal)

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Taxes Owing

(tax credits)

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Net Taxes Owing

# Net Income for Tax Purposes

- Net Employment Income
- Net Business Income
- Net Property Income
- Capital Gains and Losses
- Other Income
- Other Deductions
- Losses – Capital or Non-Capital

# Administration

# Who is in Charge of Tax?

| Department of Finance (Government) | Canada Revenue Agency (CRA) | Department of Justice (Courts) |
|---|---|---|
| Creates the laws | Administer the laws<br>Collect the taxes | Settle Disputes |

# fis·cal

/ˈfiskəl/

*adjective*

1. of or relating to government revenue, especially taxes.
   "monetary and fiscal policy"
   *synonyms:* budgetary; More

*noun* *archaic*

1. a legal or treasury official in some countries.

# Fiscal

- Wrong
  - This information you gave me is very **fiscally**
- Right
  - The match-making industry is subject to special **fiscal** conditions.

# Important Individual Dates

- Individual Fiscal Year Ends
  - December 31 if alive
  - Date of death if died in the year
- Individual Tax Return Due Dates
  - April 30 if alive and no Business Income
  - June 15 if alive with Business Income
  - The later of regular due date or 6 months after death.

# Important Individual Dates

- Individual Tax Payment Due Date
  - April 30th if alive
  - April 30th (!!) if alive with Business Income
  - The later of April 30th or 6 months after death.**

# Important Individual Dates

- Example:
  - Sam has business income, and hasn't passed away in 2014
  - Tax Return due June 15, 2015
  - Tax Payment due April 30, 2015

- Example:
  - Sam has business income, and passes away Sept 15, 2014
  - Tax Return due June 15, 2015 (later of 6 mo & reg due date)
  - Tax Payment due April 30, 2015

# Important Individual Dates

- Example:
  - Sam has no business income, and hasn't passed away in 2014
  - Tax Return due April 30, 2015
  - Tax Payment due April 30, 2015

- Example:
  - Sam has no business income, and passes away Dec 25, 2014
  - Tax Return due June 25, 2015 (later of 6 mo & reg due date)
  - Tax Payment due June 25, 2015

# Individuals – How Taxes Are Paid

- **By Employers**
  - Payroll taxes are withheld by an employer before salary or wages are paid to an employee.

- **By Banks**
  - Lump sum payments such as: Retiring allowances, RRSP withdrawals, and RESP withdrawals typically also have withholding tax on them.

# Individuals – How Taxes Are Paid

- **Self-Employed**
  - No withholdings for self-employed individuals or contractors. These individuals may end up owing tax on their tax returns.

- **Quarterly Instalments**
  - Where taxes owed on filing an individual tax return are $3,000 or higher in the current year, and in one of the two preceding years, instalments will be required in the next fiscal year.

# Individuals - How Taxes Are Paid

- **Instalments - Example**
  - $3,000 taxes owing on tax return in 2012, $1,000 owing in 2011, and $4,000 owing in 2010. Instalments required for 2012.

- **Final Calculation on T1**
  - After taxes are withheld or instalments are made, the personal tax return calculates final taxes owing. Any shortfall is owed to CRA and any excess is refunded.

# Individual Interest & Penalties

- Prescribed Amount – 2% currently
- + 2% = what CRA pays on refunds owing (4% total)
- + 4% = what CRA charges on balances due (6% total)
- Compounded Daily
- Interest is charged on top of penalties. Late filing penalty for personal tax returns is 5% of the balance owing plus 1% for each month to a maximum of 12 months (17%).
- For second offenses or where negligence exists, late filing penalties can be higher.

# Reference

- T1 Personal Income Tax and Benefit Return
- T2 Corporate Income Tax Return
- T3 Trust Return (beneficiaries receive T3 Slips)
- T4 Statement of Remuneration Paid (employees receive T4 Slips)
- T5 Statement of Investment Income (investors receive T5 Slips)
- Other information forms exist. T3010 for charities, T1044 for Not-for-Profits, T2057 for Reorganization Transactions, etc, but these five are the basics.

# Definition: Statute Barred

- Statute Barred is a term that means that a tax year is no longer eligible for review by the CRA or for requests by a taxpayer.

- In ordinary circumstances, 3 years after a tax return is assessed it becomes statute barred and CRA cannot open it for investigation unless fraud or negligence can be proven.

- In the case of fraud or gross negligence, an additional 3 year period is granted.

# Tax Evasion

- **Definition**
  - Willful intent to mislead the government and misrepresent taxable income.
- **Example**
  - contractors paid in cash – CRA is clever at finding ways to identify these individuals.
- **Impact**
  - Ability to impose fines and jail time where evasion is identified.

# Tax Avoidance/Planning

- **Definition:**
  - Does not involve breaking the law
  - May circumvent the concept of fairness or the "spirit" of the law.
- **Where we come in**
  - To be effective, tax planning should achieve the most positive result for taxpayers while agreeing with the intent of the law.
- **General Anti-Avoidance Rule (GAAR)**
  - A 'smell test' provision to assist where the spirit of the act is violated but not the wording of the act.

Questions?

# Income from Office & Employment

# To Be Covered

- Key Terms & General Information
- Taxation of Fringe Benefits
- Deduction of Employment Expenses

# Employment Definitions

Wages - $10/hour

Salary - $30,000/year

Remuneration – broad enough to mean any benefit received, not just payments.

# Employment Definitions

Employment Insurance (EI)

Canada Pension Plan (CPP)

Old Age Security (OAS)

# Who is an Employee?

An individual in the service to some other person

- Control over work performed
- Ownership of tools
- Ability to subcontract
- Financial Risk
- Investment Capital & Management Duties
- Opportunity for Profit
- Integration

Alternative: Independent Contractor

# Example – Who is an Employee?

Claire has just gotten a job with XYZ Company.

She works from 9am – 5pm Monday to Friday at XYZ's office.

XYZ provides her with her computer, pens, and paper needed for the job.

Claire is not allowed to work for XYZ's competitors

Retrieved September 16, 2014 from:
http://wellbeingmagazine.co.uk/article/exercise-posture

# Example – Who is an Employee?

Retrieved September 16, 2014 from: http://multics.co.tz/index.php/about

Claire has just gotten a contract with ABC Company.

She is working on a project called HeliumX and believes it will take 6-8 months to complete.

Claire charges $15,000 for her work on the project.  She works from home but occasionally travels on site to check on progress.

Claire's business card says '*Claire McCormick – Construction Consultant*'

# Employee Perspective

**Deductions** – greater deductions available to Independent Contractors (self-employed)

**CPP & EI** – Greater benefits available to employees to draw on, Contractors must pay employee and employer share of CPP

**Fringe Benefits** – Employees Receive better benefits

**Tax Evasion** – Contractors under less reporting and withholding.

# Employer Perspective

**CPP & EI** – Cheaper to hire contractor, but will be liable if 'accidentally' an employee

**Fringe Benefits** – Cheaper to hire contractor, may need to increase pay to compensate

**Contracts** – Commitments to contractors are usually less stringent.  Short term projects

**Legal Liability** – a Contractor is liable for their own work quality.  Employer is liable for employee work.

# Net Employment Income

Wages, Salary, & Remuneration (Income Inclusions)

Less:

Expenses incurred to earn employment income (Deductible Expenses)

Equal:

Net Employment Income

# Income Inclusions

# Employment Income

Salary, Wages, Bonuses, and Benefits received by being an Employee of an organization.

Includes signing bonus, severance pay, and non-compete clauses.

Includes tips- which can be self assessed, otherwise CRA will deny.

Generally on a cash basis

# Timing – Ordinary Payroll

Corporations use the accrual method

Payroll liabilities are deductible to them when incurred, or earned, by employees.

Individuals use the cash method

Employment income is taxable to them when received.

Retrieved September 15, 2014 from: http://business.financialpost.com/2013/08/07/employees-pay-capitalism/

# Timing – Ordinary Payroll

A Co. has a Dec 31, 2014 year end. They pay their payroll on the 1st and 16th day of the month. As of year end, they will have accrued payroll from December 17-31st available to deduct on their Dec 31, 2014 tax return.

Because their employees don't receive the payroll until Jan 1, 2015, they won't pay taxes until their Dec. 31, 2015 tax return.

**Deduction------Pay Salary-------------Save Tax-----------------------------------**
**Dec 31, 2014 January 1, 2015 June 30, 2015**

**-------------------Receive Pay-------------------------------------------Pay Tax-----**
**January 1, 2015 April 30, 2016**

# Timing - Bonuses


Taxable to the individual when received

Deductible to the employer when accrued

**IF:**

Bonuses must be paid within 180 days (on the $179^{th}$ day) for these rules to apply, otherwise deductible when paid.

Retrieved September 15, 2014 from:
http://www.talentbridgeusa.com/referral-bonus-program/

# Timing – Bonuses

A Co. Decides to pay a bonus to Jill on December 31, 2014. A Co. gets a deduction on their Dec. 31, 2014 tax return.

Because Jill doesn't receive the bonus until 2015, she won't pay taxes until her Dec. 31, 2015 tax return.

**Deduction---------------Pay Bonus--------------Save Tax---------------------------**
**Dec 31, 2014 March 31, 2015 June 30, 2015**

**-------------------------Receive Bonus----------------------------------------Pay Tax**
**March 31, 2015 April 30, 2016**

# Example

Sam is an employee at XYZ Limited. In 2014 he received an annual salary of $35,000. He also calculated that he collected $6,000 in tips and his employer gave him a bonus for coming in over the New Years holiday. He received this bonus on January 2, 2015.

Calculate Sam's taxable income for 2014.

$35,000 – Salary (assumed received in cash) is taxable
$6,000 - Tips are taxable as received
<u>$0</u> - Bonus is taxable in 2015, since that is when it was received
**<u>$41,000</u> Taxable Income**

# Fringe (Taxable) Benefits

Non-cash compensation provided by an employer.

In some cases may be received tax free, but in other cases must be included in the income of the employee.

These are considered: Taxable Benefits


Retrieved September 16, 2014 from: http://www.personneltoday.com/blogs/workplace-advice/2007/07/do-employees-know-what-their/

# Gifts

Expected to be taxable
CRA provides exceptions where non-cash (but not ‘near cash’)

Non-taxable if:

$500 or less/employee annually for special events
$500 or less/employee for long service awards (5 year increments)

Must be arm’s length with employer, excess is taxable

# Gifts - Examples

Q. $600 in gift cards on a birthday

A. $600 Taxable

Q. $600 Figurine given on their anniversary

A. $100 taxable ($600 - $500 annual special occasion allowance)

Q. $300 given to a spouse of sole shareholder at Christmas

A. $300 taxable

# Gifts - Test

Q. $300 in watch for birthday

A. $0 Taxable

Q. $700 25 year service award & $200 cash bonus for Christmas. Last service award was for 20 years.

A. $400 taxable ($200 cash + $200 excess long service award)

Q. $100 picture for Wedding & $400 earrings for Birthday

A. $0 taxable

# Loyalty Programs

Example: Airmiles

Earned because of employment, but owned personally.

No taxation if not converted into cash or near-cash.
Otherwise taxable when converted at the fair market value received.

- Exemption removed if clearly to avoid tax.
- Taxable if company card with points used by employee
- Taxable if single employee builds points by paying for many employees

# Tuition

1. Specific Employer Related Training – No Benefit
   CPA training in a CPA firm

2. General Employment Related Training – No Benefit
   MBA/First Aid in a CPA firm

3. Personal Interest Training – Taxable Benefit
   Knitting, Music (unless musician)

Employer deducts regardless
Benefit rules apply to meals, travel and accommodations required for the training.

# Taxable Benefits - Example

Harry Simpson works at XYZ Nuclear Company. He earns an annual salary of $50,000 and his employer also paid for him to take jazz saxophone lessons which cost $2,000. Harry's job is as a safety technician.

Calculate Harry's Taxable Income.

$50,000 – salary assumed received is taxable
$2,000 - tuition is taxable benefit – not for benefit of employer
$52,000

# Taxable Benefits - Example

Harry Simpson works at XYZ Nuclear Company. He earns an annual salary of $50,000 and his employer also paid for him to take pipe fitting lessons which cost $2,000. Harry's job is as a junior plumber.

Calculate Harry's Taxable Income.

$50,000 – salary assumed received is taxable
$0 - tuition is non-taxable –directly relates to Harry's work
$50,000

# Board & Lodging


Retrieved September 16, 2014 from:
http://canada.phillipmartin.info/canada_oilrig.htm

Taxable Except:

Employment at a temporary special work site

- Unreasonable to expect employee to commute

Employment at a remote work site

- Unreasonable to expect employee to establish residence because of distance to a community

# Other Benefits

Taxable:

- Flights & Holidays
- Income tax preparation
- Spouse Costs
- Life Insurance

Non-Taxable:

- Employee Discounts (not below cost)
- Required Uniforms or Safety Gear
- Employer Provided Recreational Facilities
- Counseling re Health, Re-Employment, Retirement.
- Professional Membership Fees
- Health & Dental

# When in Doubt

Consider the economic benefit and government intentions

# Planning – Use of Benefits

Tax Avoidance

- Deductible to Employer – Health Plans, Tuition
- Non-Taxable to Employees

Tax Deferral

- Deductible to Employer Immediately – RPP
- Taxable to Employees in future

# Allowances vs. Reimbursements

## Allowances

- If not based on a reasonable measure – per/km for travel, it will be taxable.
  - $0.55 per km
  - $17 per meal

- General allowances for other items are taxable (educational allowance where costs aren't tracked)

## Reimbursements

- Reimbursement of food, lodging, registration fees paid by the employee on behalf of the employer are non-taxable.

# Examples

- Jimbo receives a $600 allowance per month to pay for his vehicle which he uses for work.
- $600 x 12 = 7,200 income
- Not reasonable since not based on mileage

- Jimbo receives an allowance of $0.52 per km that he drives. In 2013 he drove 2,000 km.
  - $0 taxable
  - Not in excess of CRA rates. Appears reasonable

# Examples

- Jimbo recently paid $1,500 for registration in a conference and $425 for a hotel. His employer reimbursed him $1,925 once he submitted receipts.
- $0 taxable
- Direct reimbursement based on receipts

- Jimbo's employer paid him $2,000 so that he could enroll in a conference. They did not require any support for his costs.
  - $2,000 taxable
  - No support required, not a direct reimbursement.

# Cars

- When employee provided, can charge back $0.55/km driven for the first 5,000 km and $0.49/km after
- When employer provided, employee receives taxable benefit for personal use:
  - Standby Charge +
  - Operating Benefits

# Standby Charge

- When owned by corp:
  - 2% x (original cost of vehicle x # of days available to employee/30)
  - Easiest to think of as 2% x cost x months
- When leased by corp:
  - 2/3 x (lease costs for period available to employee – insurance) x (# of days available to employee/30)
- Reduction if used mostly for business:
  - Multiple: personal km / (1,667 per month) by each formula (can’t be used to increase the charge)
  - Only available if less than 50% is for personal use

# Operating Benefit

- If the employer pays for the operating costs (fuel, maintenance), the lesser of:
  - Employee is charged $0.26/km for personal kms.
  - 50% of standby charge.  This option available only if the car is used at least 50% for business.

- Reimbursements by employee to employer
  - Reduce the standby charge and the operating benefit

# Stock Options

- What they are:
  - An option to purchase the shares of a company, at a certain price.
  - Example: I have the option to purchase 10 shares of ABC Co. for $10 each. If the shares are currently worth $12 on the open market, these options are worth $2 each ($12 FMV - $10 option price)
- Purpose:
  - To encourage performance that improves the company's value (increasing the value of the options)
- Definitions:
  - Exercise price : what the options give the right to purchase at.
  - In the Money: When the option price is less than FMV

# Stock Options

Exercise price (strike price) - $10

FMV at date of grant - $8

FMV at date of exercise - $13

FMV at date of sale - $17

In the money-Strike<FMV grant
Not in the money – strike>FMV
Grant

| | Public | CCPC |
|---|---|---|
| Grant date | Nothing | Nothing |
| Exercise Date | $13-10=$3 | $0 |
| - Not in the money | ($1.50) | |
| Sale Date | $17-$13=$4 | $13-10=$3 |
| | x 50% = $2 | ($1.50) |
| | | $17-$13=$4 |
| | | x 50% = $2 |

CCPC: Canadian controlled private corporation

# Stock Options

| Public | (Year of Exercise) | Year of Sale |
|---|---|---|
| Employment Income | $3 | |
| Taxable Capital Gain | | $2 |
| Net income for tax purposes | $3 | $2 |
| | | |
| Stock Option Deduction | (1.50) | $0 |
| Taxable Income | 1.50 | $2 |
| | | |
| CCPC | | |
| Employment Income | | $3 |
| Taxable Capital Gain | | $2 |
| Net income for tax purposes | | $5 |
| | | |
| Stock Option Deduction | | (1.50) |
| Taxable Income | | 3.50 |

# Stock Options

Exercise price (strike price) - $10

FMV at date of grant - $12

FMV at date of exercise - $13 (in 2014)

FMV at date of sale - $17 (in 2017)

| | Public | CCPC |
|---|---|---|
| Grant date | Nothing | Nothing |
| Exercise Date | $13-10=$3 | $0 |
| **- IN the money** | **($0)** | |
| Sale Date | $17-$13=$4 | $13-10=$3 |
| -**YES held for two yrs** | x 50% = $2 | **($1.50)** |
| | | $17-$13=$4 |
| | | x 50% = $2 |

# Stock Options

| Public | (Year of Exercise) | Year of Sale |
|---|---|---|
| Employment Income | $3 | |
| Gain | | $2 |
| Net income for tax purposes | $3 | $2 |
| | | |
| Stock Option Deduction | (0) | $0 |
| Taxable Income | $3 | $2 |

| CCPC | | |
|---|---|---|
| Employment Income | | $3 |
| Capital Gain | | $2 |
| Net income for tax purposes | | $5 |
| | | |
| Stock Option Deduction | | (1.50) |
| Taxable Income | | 3.50 |

# Employee Loans

- Difference between loan rate and the prescribed rate is taxable benefit

- Exceptions – Relocation, Home Purchase, Share Purchase Loans

Retrieved Sept 17, 2014 from:
http://www.clipartbest.com/clipart-9cpEXdRcE

# Employee Loans

Mr. Gilbert gives low interest loans to employees who want to take vacations. He charges 2% and thinks he has issued around $300,000 in loans this year and has yet to collect any (if fact some employees didn't come back). The prescribed rate is 5%.

$15,000 – interest calculated at prescribed rate ($300,000 at 5%)
(6,000) – interest collected ($300,000 at 2%)
------------
$9,000 – interest to be included as benefit to employees

# Deductions

# Very Specific for Employees

- Legal Expenses to collect or defend salary
- Clergyman's residence
- Dues and Memberships
- RPP Contributions
- Travel Expenses – see next slide
- Automobile Expenses – see next slide
- Apprentice mechanic & Tradespersons Tools

# Employee Travel Expenses

Must be:

- Required to pay their own expenses
- Ordinarily required to carry on duties away from employer's place of business
- Cannot be receiving a travel allowance unless it is included in income

# Employees Expenses

<u>Can Deduct:</u>

- Meals & Entertainment (50%) – 12 hours out of town
- Lodging
- Vehicle (actual costs x kms drive for work/total km)
- Parking
- Home Office – special tests
- Training Costs
- Licenses
- Insurance


Retrieved Sept 17, 2014 from: http://www.uforgegallery.com/2013/09/assignment-inspiration-pop-culture/

# Expenses

Jimbo earns a salary of $30,000 and is required to pay for certain expenses as part of his employment. He pays association dues of $1,000. He also supplies his own car. He drove 10,000 km total last year, of which 4,000 km were for business. He estimates he spent $3,000 on gas, insurance, and repairs for his vehicle (and has receipts to support this).

Calculate Jimbo's Taxable Income:

$30,000 Salary Income
(1,000) Association dues
(1,200) Vehicle costs ($3,000 x 4,000km / 10,000km)
-----------
<u>$27,800 </u>Total Taxable Income

# Salespersons Expenses

Must be:

- Required to pay their own expenses
- Ordinarily required to carry on duties away from employer's place of business
- Cannot be receiving a travel allowance unless it is included in income
- **Must receive some income as commissions**

# Salespersons Expenses

Can Deduct:

- **Advertising & Promotion**
- Meals & Entertainment (50%) – 12 hours out of town
- Lodging
- Vehicle
- Parking
- Home Office – special tests
- Training Costs
- Licenses
- Insurance

Total limited to the amount of commissions received

# Home Office

Must be:

- Principle Place of Business (no other office); OR
- Regularly used solely for the purpose of meeting clients

What can be claimed:

- Employees – Maintenance, Hydro, Power
- Salesperson – Employee Expenses + Insurance and Property Tax
- Sole-Proprietor – Salesperson + CCA/Mortgage Interest

Based on percentage use of house (Sq footage)

Cannot be used to create or increase an employment loss

# Home Office

Sam is employed as a marketing salesperson. He earns a salary of $60,000 and had commissions of $3,000 in 2014.

He works from home since he doesn't have another office. His office is 200 sq ft, and his total house is 2,000 sq ft.

He costs are outlined on the right:

- $500 Maintenance
- $600 Insurance
- $2,000 Power
- $300 Internet (full house)
- $6,000 Mortgage Interest
- $8,000 Mortgage Principle
- $2,500 Property Tax

# Home Office

- $500 – yes for employees
- $600 yes since commissioned
- $2,000 – yes for employees
- $300 (yes –related to work)
- $0 – No Not self-employed
- $0 – Never, not a current expense
- $2,500 – Yes since commissioned

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$5,900 x 200 / 2,000 sq ft

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$590 Deduction (less than commission so ok)

- $500 Maintenance
- $600 Insurance
- $2,000 Power
- $300 Internet (full house)
- $6,000 Mortgage Interest
- $8,000 Mortgage Principle
- $2,500 Property Tax

# When in Doubt

<u>Home Office</u>

Consider whether it is deductible…current or capital expense?

Consider whether it is related to the business and if so, by what %

# Topics Covered

- Key Terms & General Information
- Taxation of Fringe Benefits
- Deduction of Employment Expenses

# Extra Examples

# Example:

Steve C. works at an office and sometimes take the office BMW to client meetings to impress clients, it also saves him money since the office pays all the costs. The office purchased the vehicle in 1990 for $25,000 so it's pretty much a classic. Steve has been working with the company for years so he didn't feel guilty about taking sick leave from May 1 until Sept 1. Other than that time he could take the car whenever he wanted. He actually borrowed it to drive to Toronto to watch a Jays game in September. He estimates the trip was around 2,700 km, but that's the only time he's ever used it personally. He estimates he drove 10,000km in total for the year.

# Example:

Steve C. works at an office and sometimes take the office BMW to client meetings to impress clients, it also saves him money since the office pays all the costs. The office purchased the vehicle in 1990 for $25,000 so it's pretty much a classic. Steve has been working with the company for years so he didn't feel guilty about taking sick leave from May 1 until Sept 1. Other than that time he could take the car whenever he wanted. He actually borrowed it to drive to Toronto to watch a Jays game in September. He estimates the trip was around 2,700 km, but that's the only time he's ever used it personally. He estimates he drove 10,000km in total for the year.

## Standby Charge

- 2% x (original cost of vehicle x # of days available to employee/30)
- Easiest to think of as 2% x cost x months

2% x $25,000 x 8 months (All but May-August) = $4,000 Standby Charge before reduction

Reduction if used mostly for business:

- Multiple: personal km / (1,667 per month) by each formula (can't be used to increase the charge)
- Only available if less than 50% is for personal use

$4,000 standby charge before reduction x 2,700 personal km / (1,667 x 8 months of use) = **$810 Reduced Standby Charge**

**Standby Charge = $810**

**Operating Benefit**

Personal use km x $0.24 = 2,700 x $0.26 = $702

OR

50% of Standby Charge if used less than 50% for personal = $810 Standby Charge x 50% = **$405**

**Total Income**

Standby Charge + Operating Benefit

**$810 + $405 = $1,215**

Retrieved September 16, 2014 from: http://www.mlmgenerationplan.com/

# Stock Option Example A

- Jan 1, 2009
  - Stock options on A Co (Public) issued to Mr. X, an arm's length employee. 100 options, Exercise price $30, FMV $50
- Jan 1, 2010
  - Mr. X exercises his options and purchases 100 shares of A Co at $30. At that time the shares' FMV was $40 on the open market.
- Jan 1, 2011
  - Mr. X sells his shares of A Co for $50.
- What is Mr. X's income inclusion and when does it occur?

# Stock Option Example A

- Public – No deferral
- Exercise Price $30 vs FMV $50 = YES in the money
- 1) Exercises option when shares are worth $40 - $30 exercise price = $10 income x 100 shares = $1,000 Total Income in 2010 (no 50% reduction since <u>was</u> in the money)
- 2) Sells 100 shares for $50 - $40 FMV at time of exercise = $10 income x 50% reduction = $5 income x 100 shares = $500 Total Income in 2011

# Stock Option Example B

- Jan 1, 2009
  - Stock options on A Co (Private) issued to Mr. X, an arm's length employee. Exercise price $30, FMV $25
- Jan 1, 2010
  - Mr. X exercises his options and purchases 100 shares of A Co at $30. At that time the shares' FMV was $40 on the open market.
- Jan 1, 2013
  - Mr. X sells his shares of A Co for $50.
- What is Mr. X's income inclusion and when does it occur?

# Stock Option Example A

- Private – Can Defer Income + Extra 2 Year Rule
- Exercise Price $30 vs FMV $25 = NOT in the money
- 1) Exercises option when shares are worth $40 - $30 exercise price = $10 income x 50% reduction since held for two years = $5 income x 100 shares = $500 Income in 2013
- 2) Sells 100 shares for $50 - $40 FMV at time of exercise = $10 income x 50% reduction = $5 income x 100 shares = $500 Income in 2013

# Net Income to Taxable Income for Individuals

# Net Income for Tax Purposes

- Net Employment Income
- Net Business Income
- Net Property Income
- Capital Gains and Losses
- Other Income
- Other Deductions
- <u>Current Year Losses – Capital or Non-Capital</u>

- = Net Income For Tax Purposes

# From Where We Were:

| | | |
|---|---|---|
| Net Income for Tax Purposes | | = |
| Less: | Allowable capital losses | - |
| | Employee Stock Options | - |
| | Deductions – sections 60 to 66.8 | - |
| | Capital gains deduction | - |
| | Losses from an office or employment | - |
| | Losses from a business | - |
| | Losses from property | - |
| Taxable Income | | = |

# Critical Thinking

- Why are there two totals?

  - Net Income For Tax Purposes – used to calculate eligibility for assistance programs and low income tax credits. (more inclusive)

  - Taxable Income – income actually intended to be taxed. (adjusted for losses & tax free income)

# Tax Calculation and Credits

# Calculation of Personal Tax

# Marginal Tax Rates

| | | |
|---|---|---|
| Up to $43,000 | 24.1% | (+ $0) |
| $43,001 to $87,000 | 34.1% | (+ $10,363) |
| $87,001 to $135,000 | 38.4% | (+ $25,367) |
| $135,000 and up | 43.3% | (+ $43,799) |

Example:

Mr. X makes $93,000 in taxable income. How much tax will he pay before personal credits?

What about if he makes $148,000?

# Example

| | | |
|---|---|---|
| Up to $43,000 | 24.1% | (+ $0) |
| $43,001 to $87,000 | 34.1% | (+ $10,363) |
| $87,001 to $135,000 | 38.4% | (+ $25,367) |
| $135,000 and up | 43.3% | (+ $43,799) |

Example:

Mr. X makes $93,000
in taxable income.
How much tax will he pay
before personal credits?

Longhand:

43,000 – 0 = 43,000 x 24.1% = $10,363
87,000-43,000 = 44,000 x 34.1% = $15,004
93,000 – 87,000 = 6,000 x 38.4% = $2,304

$10,363 + 15,004 + 2,304 = $27,671

# Example

| | | |
|---|---|---|
| Up to $43,000 | 24.1% | (+ $0) |
| $43,001 to $87,000 | 34.1% | (+ $10,363) |
| $87,001 to $135,000 | 38.4% | (+ $25,367) |
| $135,000 and up | 43.3% | (+ $43,799) |

Example:

Mr. X makes $93,000
in taxable income.
How much tax will he pay
before personal credits?

Shorthand:

93,000 – 87,000 = 6,000 x 38.4% = $2,304

$25,367 + 2,304 = $27,671

# Example

| | | |
|---|---|---|
| Up to $43,000 | 24.1% | (+ $0) |
| $43,001 to $87,000 | 34.1% | (+ $10,363) |
| $87,001 to $135,000 | 38.4% | (+ $25,367) |
| $135,000 and up | 43.3% | (+ $43,799) |

Example:

Mr. X makes $148,000
in taxable income.
How much tax will he pay
before personal credits?

Longhand:

43,000 – 0 = 43,000 x 24.1% = $10,363
87,000-43,000 = 44,000 x 34.1% = $15,004
135,000 – 87,000 = 48,000 x 38.4% = $18,432
148,000 – 135,000 = 13,000 x 43.3% = $5,629

$10,363 + 15,004 + 18,432 + 5,629 = $49,428

# Example

| | | |
|---|---|---|
| Up to $43,000 | 24.1% | (+ $0) |
| $43,001 to $87,000 | 34.1% | (+ $10,363) |
| $87,001 to $135,000 | 38.4% | (+ $25,367) |
| $135,000 and up | 43.3% | (+ $43,799) |

Example:

Mr. X makes $148,000 in taxable income. How much tax will he pay before personal credits?

Shorthand:

148,000 – 135,000 = 13,000 x 43.3% = $5,629

$43,799 + 5,629 = $49,428

# Example – Knowledge Check

| | | |
|---|---|---|
| Up to $43,000 | 24.1% | (+ $0) |
| $43,001 to $87,000 | 34.1% | (+ $10,363) |
| $87,001 to $135,000 | 38.4% | (+ $25,367) |
| $135,000 and up | 43.3% | (+ $43,799) |

Example:

Mr. X makes $57,000
in taxable income.
How much tax will he pay
before personal credits?

# Choose an Answer

A. $19,437

B. $4,774

C. $15,137

D. $42

Retrieved September 23, 2014 from:
http://wall.alphacoders.com/by_sub_category.php?id=212731

# Credit vs. Deduction

- Deduction
  - Income – Deduction = Taxable Income (reduces tax by highest marginal rate)
- Credit
  - Taxes Owing – (Credit x lowest rate) = Net Taxes Owing. (reduces tax by lowest marginal rates).
  - Credits may be refundable or non-refundable.

# Tax Savings Example

**Deductions**

$146,000 Income before

(11,000) Deduction is a reduction of income.

-------------

<u>$135,000 </u>Income After

*Income over and above $135,000 taxed at 43.3% so…

$11,000 x 43.3% = $4,763 tax savings

**Credits**

$146,000 Income before

-

------------

$146,000 Income After

*Credits reduce tax at lowest marginal tax rate of 24.1% so…

$11,000 x 24.1% = $2,651 tax savings

# Provincial vs. Federal

- Rates
  - Varying rates with varying cutoff levels (federal at $43,000, provincial at $37,000)

  We use combined federal & provincial rates with rough cutoff levels for this class to simplify this concept.

- Credits
  - Credit amounts may vary between Federal and Provincial.
  - Some credits may be only available provincially or federally.

Where there is a difference we use Federal credits as will future courses.

# Personal Tax Credits

# Family Based Credits

# Family Based Credits

- Definition: Common Law
  - Cohabited in a conjugal relationship for a continuous period for at least one year; or
  - Is the parent of a child of whom the taxpayer is also a parent.

No requirement they be of the opposite sex

Possible to have both

# Family Based Credits

- Definition: Child
  - Natural or adopted children of the individual or of their spouse/common law partner.

# Family Based Credits

- Personal Credits - $11,000
  - For yourself

- Spousal Credits - $11,000
  - For your spouse if they can't use
  - Reduced by your spouses Net Income For Tax Purposes.

# Family Based Credits

- Eligible Dependant Credit - $11,000
  - If you have no spouse or common-law partner
  - have a dependant minor child, disabled adult child, parent, or grandparent
  - Must be dependant on you for food, clothing, shelter & living with you.
  - Reduced by dependants Net Income for Tax Purposes

Key to remember – these three are all the same.

# Family Based Credits

<u>Example</u>

George and Marie are married. George earns $50,000 from interest and Marie does not work. Calculate the reduction of George's taxes based what you know about him.

$11,000 Personal Credit

$11,000 Spousal Credit

---------

$22,000 x 24.1% = $5,302 Reduction in Taxes.

# Family Based Credits Cont'd.

- Age Credit
  - Taxpayers 65 and over - $6,900
  - Reduced if they earn too much income. ($38,000 starts, eliminated by $89,000)
  - Transferable to a spouse

Retrieved September 23, 2014 from: http://kristiholl.net/writers-blog/2011/11/age-are-you-too-old-to-write/

# Family Based Credits Cont'd

Disability Tax Credit - $8,000 (T2201)

- Available to individuals with an impairment that results in a "marked" restriction in a basic activity of daily living, that has lasted or is expected to last for at least 12 months
- Mental or physical infirmity must be certified by a medical doctor or similar professional.

- A $4,732 supplement is added on for disabled children under the age of 18

- The credit may be transferred to:
  - a spouse, or
  - A supporting person who claimed the caregiver credit, or eligible dependent credit on behalf of the impaired individual.

# Family Based Credits

<u>Example</u>

George is 70 years old, unmarried, and has 3 children age 6, 7 and 8. George earns $30,000 annually. Not enough to reduce any of his credits. Calculate the reduction of George's taxes based what you know about him.

$11,000 Personal Credit

$11,000 Eligible Dependant Credit

$6,900 Age Credit

---------

$28,900 x 24.1% = $6,964.90 Reduction in Taxes.

# Family Based Credits

<u>Example</u>

George is 73 years old and married. His spouse has a registered disability certified by a doctor, and is 66 years old. Their combined income for the year is $30,000, all of which is George's. Calculate George's Personal Credits.

$11,000 Personal Credit

$11,000 Spousal Credit

$6,900 Age Credit

$6,900 Age Credit from spouse

$8,000 disability credit transferred from spouse

---------

$43,800 x 24.1% = $10,555.80 Reduction in Taxes.

# Family Based Credits Cont'd.

- Canada Caregiver Amount. – 6,900
  - For supporting an infirm adult relative, including a child, grandchild, parent, grandparent, brother, sister, aunt, uncle, niece, or nephew
  - Must be dependent because of mental or physical infirmity
  - Relative need not live with the taxpayer
  - Credit is reduced by 15% of the relative's net income in excess of $16,163

- If eligible for dependant credit, can't claim Canada Caregiver amount.

# Family Based Credits Cont'd.

- <u>Family caregiver amount for infirm dependent. – 2,150</u>

  - One family caregiver amount is allowed for each infirm dependent, for which the spousal or equivalent to spouse is claimed.
  - Also available on a standalone basis for an infirm child under 18 for the 2017 year and onward.

# Family Based Credits Cont'd

<u>Home Accessibility Amount - $10,000</u>

- Available to taxpayers 65 years of age or older, or who are eligible for the disability tax credit.
- For eligible renovations to improve safety and accessibility of a home.
- The basis for the credit is the lesser of the cost of the eligible renovations and $10,000.

# Family Based Credits

Example

George is 45 years old and unmarried. He supports his 23 year old niece, since his brother (her father) passed away. She has an registered disability. Calculate George's Personal Credits.

$11,000 Personal Credit

$6,900 Canada Caregiver

$8,000 disability credit transferred from niece since George claimed the caregiver credit for her.

---------

$25,900 x 24.1% = $6,241.90 Reduction in Taxes.

# Family Based Credits Cont'd

- First Time Homebuyers Tax Credit
  - $5,000 – where individual or spouse hasn't purchased a home or lived in one they owned in the last 4 years.

- Adoption Expenses Tax Credit
  - $15,000 in Eligible Adoption Expenses
  - For the adoption of a child under 18
  - Must be claimed in the year adoption finalized
  - Includes agency fees, court costs, travel & living expenses of child & adoptive parents, etc.

# Income Based Credits

# Income Based Credits

- EI/CPP Credits
  - Credit for amounts paid up to annual max
  - EI Max is $891, CPP Max is $2,356
  - Remainder deducted from pay is refunded

- Employment Credit
  - $1,117 for having employment income (at least $1,117 of it)

# Income Based Credits

- Pension Credit
  - $2,000 for having pension income (at least $2,000 of it)
  - Not available on OAS, CPP, or Death Benefit Income
  - Transferable to a spouse if unused


Retrieved September 23, 2014 from:
http://pensionsatwork.ca/

# Income Based Credits

Example

George is 34 and earns $500 in employment income in 2012. Calculate the reduction of his income tax from credits.

$11,000 Personal Credit

$500 Employment Credit (lesser of emp income or $1,117)

---------

$11,500 x 24.1% = $2,771.50 (potential) Reduction in Taxes.

# Income Based Credits

<u>Example</u>

George is 34 and earns $25,000 in pension income in 2012. Calculate the reduction of his income tax from credits.

$11,000 Personal Credit

$2,000 Pension Credit (Lesser of pension income or $2,000)

---------

$13,000 x 24.1% = $3,133 Reduction in Taxes.

# Income Based Credits

<u>Example</u>

George is 34 and earns $25,000 in employment income in 2012. George contributed $1,000 to EI from his employment income. Calculate the reduction of his income tax from credits.

$11,000 Personal Credit

$1,117 Employment Credit (Lesser of employ income or $1,117)

$891 EI Credit

---------

$13,008 x 24.1% = $3,135 + ($1,000 – 891) = $3,244 Reduction in Taxes.

# Miscellaneous Credits

# Miscellaneous Credits

- Tuition Tax Credits
  - Tuition paid at university, college, post-secondary institution
  - Unused credits can be carried forward
  - Can be transferred up to $5,000 in the current year to parents – not mandatory – balance with unlimited carry-forward
  - Not claimable if reimbursed by employer unless it was a taxable benefit

- Exam Fees
  - Exam fees $100 or more

# Miscellaneous Credits

- Student Loan Interest
  - Credit available for interest paid on government student loans.  Lines of credit generally not applicable.  5 yrs forward

# Tuition Credits

<u>Example</u>

George is 23 attends the University of New Brunswick for 4 full time months in 2012. His tuition costs $6,000. Calculate the reduction of his income tax from credits.

$11,000 Personal Credit

$6,000 Tuition Credit

---------

$17,000 x 24.1% = $4,097 Reduction in Taxes.

*If unable to use the tuition amount, George can carry them forward to a future year.

# Miscellaneous Credits

- <u>Volunteer Firefighters Credit</u>
  - $3,000
  - Individuals volunteering 200 hours a year
  - Cannot use volunteering hours from a fire department the individual also works for.

Retrieved September 23, 2014 from: http://www.clipartlord.com/category/people-clip-art/men-in-uniform-clip-art/fireman-clip-art/

# Miscellaneous Credits Cont'd

- <u>Medical Expense Credits</u>

  - Total expenses for the family (spouses, minors, adult children with disabilities)
  - Reduced by: 3% of net income or $2,152 (lesser of).
  - Includes: Prescriptions, glasses, premiums, dentistry, etc.
  - Federal Doesn't include: Cosmetic surgery
  - NB Doesn't include: acupuncture, natural remedies
  - Any 12 month period ending in the year & 24 months at death.

# Miscellaneous Credits Cont'd

- Medical Expense Credits Continued…

  - Can include spouse & minor children with no reduction, and
  - Adult children less 3% of their income or $2,152 (lesser of)
  - Does not include any amounts reimbursed by medical insurance.

# Medical Credits

<u>Example</u>

George is married to Marie.  George spent $6,000 and Marie spent $8,000 in medical expenses from November 2011 to October 2012. George estimates that $2,000 was reimbursed by Blue Cross Insurance.  He earns $50,000 annually and she earns $8,500. Calculate his tax reduction JUST from medical.

$6,000 George's Medical

$8,000  Marie's Medical

(2,000) Less: reimbursement

(1,500) Less: 3% of $50,000 (less than $2,152)

---------

$10,500 x 24.1% = $2,530.50 Reduction in Taxes.

# Miscellaneous Credits Cont'd

- Charitable Donations
  - Preferential treatment. First $200 at lowest bracket – afterwards at highest tax bracket.
  - Limited to 75% of net income for tax purposes
  - Able to be carried forward for 5 years
  - Better to lump spousal donations together.

First-time Donors Super Credit (new in 2013)

- Extra 25% on donations up to $1,000
- Available to individuals (or couples) who haven't donated since 2007.

# Donation Credits

<u>Example</u>

George contributes $10,000 in donations in 2012. Calculate his tax reduction from donations only.

$200 x 24.1% = $48.20

$9,800 x 43.3% = $4,243.40

Total Tax Reduction: 48.20 + 4,243.40 = $4,291.60

# Donation Credits

Example

George contributes $10,000 in donations in 2014. Calculate his tax reduction from donations only, assuming he has never donated before.

$200 x 24.1% = $48.20

$9,800 x 43.3% = $4,243.40

$1,000 x 25% = $250 ($25% of the first $1000)

Total Tax Reduction: 48.20 + 4,243.40 + 250 = $4,541.60

# Changing Province of Residence

In general, provincial tax credits are lower than federal. This results in a faster use of the provincial portion of your tuition credits than your federal (you will run out of provincial sooner).

However, when changing provinces of residences, some provinces allow you to “reset” your provincial tuition credit carry forward to the federal amount. Watch for this potential benefit if you move.

# Miscellaneous Income and Deductions

# Income Inclusions

# Income that isn't:

Employment Income

Business/Property Income

Capital Gains

# Pension Income

- Canada Pension Plan (CPP) & Other Pensions
  - Registered Pension Plans (RPP)
  - Old Age Security (OAS), Guaranteed Income Supplement (automatic)
  - Canada Pension Plan (CPP) (separate from death benefits)
  - Provincial Pension plans

# Retiring Allowances

- Retiring Allowances
  - An amount received on retirement from employment in recognition of long service; or
  - On loss of employment as damages.
  - Unused Sick Pay
  - NOT unused vacation.

Special transfer available to RPP or RRSP which can be deducted from income.

# Retiring Allowances - Transfer

<u>Contribution Room</u>

- $2,000/yr employed prior to 1996

  Plus
- $1,500/yr employed prior to 1989 where NOT a member of an RPP or DPSP.

Transferred amount does not decrease RRSP contribution room.

# Example:

Jim receives a retirement allowance worth $80,000 From Aco Ltd.

Jim began working at Aco Ltd. in 1975 and he was never part of a retirement plan.

Jim has $10,000 in RRSP contribution room available.

How much of his allowance can he transfer to his RRSP and how much contribution room will be left afterwards?

retirement allowance worth $80,000
began working at Aco Ltd. in 1975
never part of a retirement plan.
$10,000 in RRSP contribution room available.

How much of his allowance can he transfer to his RRSP

1989-1975 = 14 years before 1989 x $1,500 per year = $21,000
1996-1975 = 21 years before 1996 x $2,000 per year = $42,000

$21,000 + $42,000 = $63,000 can be rolled over without RRSP room

how much contribution room will be left afterwards?

$80,000 allowance ordinarily taxable - $63,000 into RRSP without reducing room
= $17,000 taxable allowance remaining - $10,000 RRSP room = $7,000 taxable allowance

$10,000 original RRSP contribution room - $10,000 deduction taken = $0 RRSP room

# Example:

Jim receives a retirement allowance worth $40,000 From Aco Ltd.

Jim began working at Aco Ltd. in 1980 and he was never part of a retirement plan.

Jim has $20,000 in RRSP contribution room available.

How much of his allowance can he transfer to his RRSP and how much contribution room will be left afterwards?

retirement allowance worth $40,000
began working at Aco Ltd. in 1980
never part of a retirement plan.
$20,000 in RRSP contribution room available.

How much of his allowance can he transfer to his RRSP

1989-1980 = 9 years before 1989 x $1,500 per year = $13,500
1996-1980 = 16 years before 1996 x $2,000 per year = $32,000

$13,500 + $32,000 = $45,500 can be rolled over without RRSP room

how much contribution room will be left afterwards?

$40,000 allowance ordinarily taxable - $40,000 into RRSP without reducing room
= $0 taxable allowance remaining (cannot roll over more into RRSP than received)

$20,000 original RRSP contribution room - $0 deduction taken = $20,000 RRSP room

# Death Benefits

- On the death of an employee, $10,000 can be given tax free.
- Can be to one or several beneficiaries, but a max of $10,000 will be tax free.
- Consider: who gets it?  Who gets it tax free?
- Any excess is taxable


http://thecareercafe.co.uk/blog/?attachment_id=1945
Obtained August 31, 2012

# Death Benefits

- If just to a spouse – first $10,000 non taxable
- If just to non spouse – first $10,000 non taxable

- If to a spouse and non-spouse
  - spouse gets first $10,000 tax free,
  - non-spouses share any remainder of 10,000 exemption, in proportion to the FMV of their benefit

- If to two spouses
  - $10,000 exemption split in proportion to the FMV of their benefit


http://thecareercafe.co.uk/blog/?attachment_id=1945
Obtained August 31, 2012

# Death Benefits

Dave and his mother in law, Kerry, each receive \$6,000 in death benefits on the death of Dave's wife, Sandra.

What should Dave and Kerry report as income from the death benefit?

Dave will report \$0 of income, as he receives a tax free benefit up to either the amount paid, or the \$10,000 limit.

Kerry is a non-spouse, and so would receive any residual benefit

\$6,000 – (\$10,000 tax free - \$6,000 used by dave) = \$2,000 taxable.

# Death Benefits

Dave and his mother in law, Kerry, each receive $20,000 in death benefits on the death of Dave's wife, Sandra.

What should Dave and Kerry report as income from the death benefit?

Dave - $10,000 income ($20,000 received – $10,000 exemption)

Kerry - $20,000 income ($20,000 received – $0 exemption)

# Various Minor Items:

- Employment Insurance
  - Taxable when received & deductible if repaid.
- Social Assistance Received – tax exempt but must be included in income and then removed
- Workers Compensation – tax exempt but must be included in income and then removed

# Various Minor Items:

- Pension Splitting
  - Eligible pension included in the income of recipient
  - Deduction from income for pension split with spouse
  - Proportionate share of tax withheld is also transferred
  - CPP & OAS cannot be split


Retrieved September 30, 2014 from: http://www.retirementcommunications.com/the-employer-does-not-offer-a-pension-you-can-build-your-own/

# Pension Splitting - Example

Michelle and Jon are each 75  years old and are married.

- Michelle earns the following income: OAS $5,000, RPP Pension Income $70,000, Interest $16,000
- Total Income $91,000
- Jon earns no income.

What is Jon's optimum income level?

- Jon's optimum income is $35,000.  ($0 + $35)
- Jon not using credits, Michelle has higher income
- Maximum is 50% of eligible pension income or $35,000 ($70,000 x 50%).

# Pension Splitting - Example

Michelle and Jon are each 75 years old and are married.

- Michelle earns the following income: OAS $5,000, RPP Pension Income $70,000, Interest $16,000
- Total Income $91,000
- Jon earns no income.

What is Michelle's optimum income level?

- Michelle's optimum income is $56,000. ($91 - $35)
- Jon not using credits, Michelle has higher income
- Maximum is 50% of eligible pension income or $35,000 ($70,000 x 50%).

# Support Payments

- Recipient must have discretion over its use
- Periodic Payments
- Receivable under a court order or separation agreement
- If agreement doesn't specify, and there is a child, we assume it is Child Support

- <u>Spousal</u> – Deductible to payer, Taxable to recipient
  - Must be living separate and apart at the time the payment is made.

- <u>Child</u> – Non-Deductible to payer, Non-Taxable to recipient

# Support Payment - Example

Jane and Nick sign a divorce agreement on May 1, 2013 stipulating that Nick will pay Jane $2,000 per month beginning immediately. They do have a child who continues to live with Jane.

What must Jane include in her 2013 income?

- Nothing
- As not specified whether child or spousal support, we assume it is child support.
- Child support non-taxable to recipient

# Support Payment - Example

Jane and Nick sign a divorce agreement on May 1, 2013 stipulating that Nick will pay Jane $2,000 per month in spousal support beginning immediately.

What must Jane include in her 2013 income?

- $16,000 (May – December x $2,000 per month)
- Periodic spousal support based on an agreement
- Spousal support taxable to recipient

# Annuities

- Periodic Payments (monthly, annually, etc.)
- Types:
  - Life Annuity – Guaranteed payments for life of the annuitant (or minimum 10 years for example)
  - Term Annuity – Payments for 25 years

- Tax Treatment
  - RRSP/RRIF withdrawals- 100% taxable
  - Non-Registered - Some portion is a return of capital and the rest income. An information sheet will be provided by investment provider (T3).

# Life Insurance Proceeds

<u>Tax-free</u> if paid as a consequence of death

Because you pay the premiums yourself they haven't been deducted for tax purposes.

This is an important principle.  Paid in after tax dollar – typically tax free benefits.

Retrieved September 30, 2014 from: http://www.abouttermlifeinsurance.com/term-life-insurance-riders.html

# Scholarships

- Fully exempt if you get the tuition tax credit (college diplomas, bachelor, masters, or doctoral degree costs)

- Grants for artists & research projects are taxable only where they exceed the expenses to complete the project

- $500 base exemption applies even where the two above criteria aren't met

- $500 exemption doesn't apply where the prize is a benefit of employment (ie, your employer gives you a scholarship)

# Scholarships

Craig attends the University of Waterloo. He is taking a Bachelor in Computer Science and received $35,000 in scholarships in 2014. Craig also had a part time job at Tim Hortons where he earned $6,000.

Calculate his taxable income in 2014.

$0 Scholarship not taxable
$6,000 Employment Income
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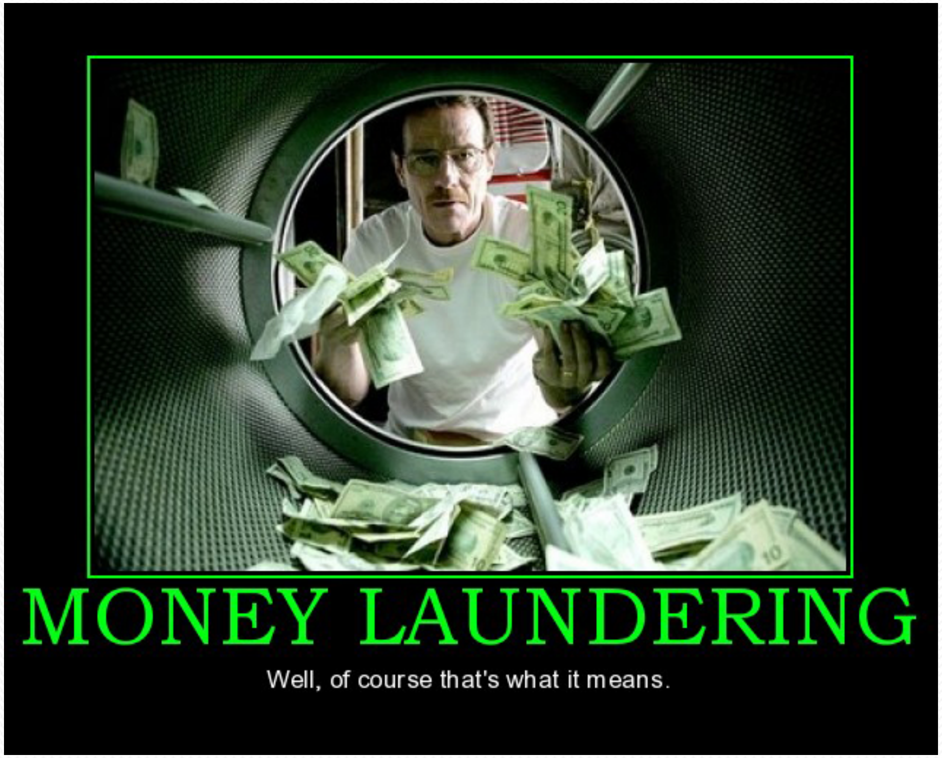
$6,000 Total Taxable Income

# Indirect Payments

- Payments made to a third party at the request or direction of someone else, are included in the requestor's income.
- Example: A husband receives a bonus but asks his company to pay it to his wife. It's still his income for tax purposes.
- Example: an employee receives a bonus but asks his company to pay it to his bookie. It's still his income for tax purposes




http://hustedia.com/blog/2011/05/16/hiding-money/
Obtained August 31, 2012

# Deductions

# Various Minor Items:

- Support Payments
  - Spousal – Deductible to payer, Taxable to recipient
  - Child – Non-Deductible to payer, Non-Taxable to recipient

- CPP
  - Credit up to annual max, refund of remainder ($2,356)
  - Self-employed can deduct ½ of CPP contributions (the employer's half of $2,356)

- RRSPs
  - Contributions to an RRSP are deductible
  - Contributions to RPP by employer are deducted from your contribution room. Because not included in income, no deduction

# Various Minor Items:

- Legal Payments
  - To object or appeal a tax assessment
  - Remember that also to obtain or defend employment income
- Pension Splitting
  - Those receiving pension income can split up to 50% of it with a spouse if it is advantageous. The amount split is a deduction.
- OAS
  - Clawback - important to know they may take it back if you make too much money. Starts around $65,000. Deductible.

# Moving Expenses

- 40km closer to employment or school
- Reduced by any allowances paid by your employer
- Limited to the income after the move, from the new place (scholarships/Empl. $)
- Remainder can be carried forward (but must be used if able)


Obtained from Spruce Island
August 31, 2012

# Moving Expenses

- Travel Costs – Actual Meals/Lodging or simple method. $0.59/km $21/meal/person
- Transportation & Storage Costs for Household Items
- Costs of Meals & Lodging near either residence for 15 days.
- Lease Cancellation Costs
- Selling costs of old home:
  - Advertising, legal, real estate, mortgage fees.
  - Excludes renovations/repairs.
- Legal & land transfer fees for new residence
- Mortgage interest, property tax, insurance, maintenance on old home while vacant (Max $5,000)

# Moving Expenses

- Revision of personal documents: driver's license, car permits, utility hookups.
- House or job hunting costs are <u>not</u> deductible.


Obtained from Spruce Island
August 31, 2012

# Moving Expenses

- Loss on old residence is not deductible from income.
- However, only ½ of employer reimbursement in excess of $15,000 for this loss is a taxable benefit.
- Effective tax planning strategy.

- Example: $40,000 Reimbursement on $60,000 loss.
- (40,000 – 15,000) x ½ = $12,500 taxable

# Moving Expenses

Example:

- 2 people travel for 3 days from BC to PEI (3,000 km)
- Old home didn't sell for 2 months. Estimate power, hydro, and maintenance while waiting to sell was $6,000.
- Storage at new place to hold household effects $2,000
- Cost to hire a moving company $1,500

Income in new location:

- Scholarships $15,000 from BBA
- Employment Income of $3,000

# Moving Expenses

- Simplified KM = 3,000km x $0.59 = $1,770
- Simplified Meals = 2 people x 3 days x $21/meal x 3 meals per day = $378
- Maximum reached on old home maintenance $5,000
- Storage is deductible = $2,000
- Moving Company Costs are deductible $1,500
- **Total Moving Expenses: $10,648**

Income in new location:

- Scholarships $15,000 from BBA
- **Employment Income of $3,000 (limited to income)**

# Child Care Expenses

Retrieved September 30, 2014 from: http://www.little-u.com/

- For children under 16 or who have a disability
- Must be a child of the individual, their spouse, or a legal dependant with income less than the basic personal credit (around $11k).
- Can't be paid to the mother, father, or a person under 18 related to the individual.

# Child Care Expenses

- Amounts paid must be to allow the individual to earn employment income or go to school.  Ie. No tuition or no employment income = no deduction.

- Must be deducted from lower income spouse EXCEPT…

- Deductible from higher income spouse when:
  - Lower earner is in school
  - Lower earner is infirm for at least two weeks (broken leg) or has a long term infirmity (blind)
  - Lower earner is in Jail
  - Spouses are separated for 90 days

# Child Care Expenses

- Babysitting, Daycare, or Day Camps (no weekly limit)

- Boarding school or camp:
  - $275/week per disabled child.
  - $200/week for under 7 yrs
  - $125/week for 7-16 yrs

- **Limit 1:**
  - $11,000/child with disability
  - $8,000/child under 7 yrs
  - $5,000/child 7-16 yrs
- **Limit 2:**
  - Actual expenses
- **Limit 3:**
  - 2/3 of earned income of the individual.

# Child Care Expenses

Aaron and Miranda have three children, Bruce, Bob, and Bambi aged 5, 8, and 10, respectively.

Aaron earned $25,000 and Miranda earned $15,000 in employment income in 2012.

The couple paid for a babysitter for the full year costing $8,200.

The couple also enrolled Bambi in an seven day overnight summer camp that cost $5,000.

**Calculate the maximum amount that can be claimed for Child Care and who claims it.**

# Child Care Expenses

- Miranda is lower income earner – no exceptions present
  - **Limit 1**: 2/3 of her income is: $10,000 maximum
  - **Limit 2**: Total annual limit $5,000 + $5,000 + 8,000 = $18,000 (two children age 7-16 and one under 7)
  - **Limit 3**: Actual expenses
    Babysitting - $8,200
    Overnight camp = (1 week x $125 per week maximum)=$125
    **Total Expenditures** = **$8,325.00**