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YEAR-END TAX PLANNING

52(1)

Some 2000 year-end tax planning tips include:

1. If the following *expenditures* are made by *individuals* by **December 31, 2000** they will be eligible for 2000 tax deductions: moving expenses, child care expenses, safety deposit box fees, charitable donations, political contributions and medical expenses.
2. **2000 eligible Registered Retirement Savings Plan (RRSP) contribution** amounts are noted on the 1999 *personal income tax return assessment notices*. You have until **March 1, 2001** to make a tax deductible RRSP contribution for the 2000 year.
Consider contributing to a *spousal RRSP* to achieve income splitting in the future.
The maximum 2001 addition to deductible *RRSP contribution room* is \$13,500. Therefore \$75,000 of **2000 earned income** is needed to reach this maximum.
3. Persons turning **age 69 in 2000** must *mature* their RRSP into cash, an annuity or a Registered Retirement Income Fund by December 31, 2000. Certain 2000 *excess* contributions may be deducted in the year 2001 if *contribution room* is available.



4. If you own a business, consider paying a *reasonable salary* to family members for their services rendered to the business.
5. Ensure that all deductible *alimony or maintenance payments* are made by December 31, 2000.
6. An individual whose **2000 net income** exceeds \$53,960 will lose all, or part, of their *old age security*.
Senior citizens will begin to lose their income tax *age credit* if net income exceeds \$26,284.
Individuals facing these problems should contact their professional advisors for assistance in *managing* their 2000 personal income.
7. Consider purchasing assets eligible for *capital cost allowance* before the yearend. For example, *employees* may claim capital cost allowance on *automobiles, aircraft* and *musical instruments* required to be used in their employment.
8. If you have had taxable capital gains in the *year*, or any of the *preceding three years*, consider selling capital properties with an *underlying capital loss* prior to the yearend. This capital loss may be offset against capital gains in the *year*, or in the *three preceding years*.
9. If income in an *inter vivos trust* is to be taxed on a beneficiary's return, the income must be *paid or payable* to the beneficiary by **December 31, 2000**.

IN THIS ISSUE

YEAR-END TAX PLANNING
2000 REMUNERATION
PERSONAL TAX
EMPLOYMENT
MARRIAGE BREAKDOWN
RRSP/RRIF
DONATIONS
FARMING
GST
INTERNATIONAL
DID YOU KNOW...

10. Individuals may claim a non-refundable *federal credit of 17%* on the *interest portion* of student loan payments made in 2000.
11. **Registered Education Savings Plan (RESP)**
A *Canada Education Savings Grant (CESG)* for RESP contributions will be permitted equal to 20% of annual contributions for beneficiaries up to and including age 17 (maximum \$400 per child per year).
However, contributions for 16 and 17 year olds will only qualify for certain previous plans. Therefore, consider establishing a RESP for a 15 year old before the end of the year.
12. **Health and dental premiums for the self-employed**

Tax Tips & Traps

Individuals will be allowed to **deduct** amounts payable in respect of the year for **Private Health Service Plan** coverage in computing **business income** provided they are actively engaged alone, or as a **partner**, in their business, and either self-employment is their primary source of income or their income from other sources does not exceed \$10,000.

13. **Tax on Split Income**

The Income Tax Act applies the **maximum marginal tax rate** to certain passive income of *individuals* under the **age of 18** commencing in the year 2000.

This includes:

1. Taxable **dividends**, and other **shareholder benefits**, on **unlisted shares** of Canadian and foreign companies (received **directly** or through a **trust** or **partnership**); and
2. Income from a **partnership or trust** where the income is derived from providing goods or services to a business carried on by a **relative** of the child or, of which the relative participates.

Therefore, consider **minimizing** this type of income in 2000.

14. **Lump-Sum Payments**

The Income Tax Act allows an **individual** to **deduct** a **portion** of a **qualifying amount** received in the year.

This includes **lump-sum spousal or child support**, superannuation or **pension** benefits, **employment insurance** benefits, benefits paid under **wage loss replacement plans**, and income received from an **office or employment** under a court order or judgment, an arbitration award or in settlement of a

lawsuit that related to a prior year and is **\$3,000** or more.

The **tax payable** on the deducted amount is based on the prior year's tax rate.

This applies to amounts received **after 1994**.

15. **Same-Sex Common-Law Couples**

The Income Tax Act extends benefits and obligations to **same-sex** couples effective **2001** unless the couple **elects**, in which case it may be effective for the years 1998, 1999 and 2000.

2000 REMUNERATION

52(2)

Some general guidelines to follow in remunerating the owner of a Canadian-controlled private corporation earning "active business income" include:



1. **Bonus down** active business earnings in excess of \$200,000.
2. Elect to pay out tax-free "**capital dividend account**" dividends.
3. Consider paying dividends to obtain a refund of "**refundable dividend tax on hand**".
4. Corporate earnings in excess of personal requirements could be left in the company to obtain a **tax deferral**. The effect on the "**Qualified Small Business Corporation**" status should be reviewed before selling the shares.

Some other considerations include:

1. Salary payments require **source deductions** to be remitted to Revenue Canada on a timely basis.
2. Individuals that wish to contribute to

the Canada Pension Plan or a Registered Retirement Savings Plan may require a salary to create "**earned income**".

3. Salaries paid to family members must be **reasonable**.
4. Some provinces have "**payroll taxes**" thereby increasing the costs of paying salaries versus dividends.

Reasonability of Salary:

Revenue Canada has a general practice **not to challenge** the reasonableness of **salaries or bonuses** paid to a principal shareholder who is **active** in the corporation's business. Revenue Canada may limit this position in bonuses paid out of a corporation's **investment income, inter-corporate management** fees, remuneration paid to **spouses**, other **family members** or **non-residents**. Revenue Canada **reserves the right** to require **evidence** that the remuneration is **reasonable**.

PERSONAL TAX

52(3)

CANADA CHILD TAX BENEFITS (CCTB)

In a **Tax Court** case, Alain and



Nicole were **separated** and the Court granted **shared custody** of the minor child - one week in Alain's home and the next week in Nicole's home. Both parents applied for the **CCTB** and CCRA determined, and the Tax Court agreed, that **Alain** was the person who **mainly cared** for the child even though, the **female** parent is usually **presumed** to be the one eligible for the CCTB benefit.

Also, remember that **Form RC65** should be

Tax Tips & Traps

completed where *marital status changes*. For example, if the new status is married or common-law, and you or your new spouse have children who are residing with you, CCRA will move all the children to the female spouse's account. To receive CCTB, *both spouses* have to *file* a tax return.

If a taxpayer is recently widowed, separated or divorced, CCRA will *recalculate* the benefit so it is based *only on your income*.

MEDICAL EXPENSES

In *Technical Interpretations* Canada Customs and Revenue Agency (CCRA) noted that:

1. *Wheelchairs*, including scooters and wheel-mounted geriatric chairs, qualify as *medical expenses*. Also included are electric scooters if acquired in substitution for a wheelchair.
2. *Beds* normally found in hospitals may qualify as a medical expense however, this may not include the cost of a chiropractic bed.
3. *Orthopaedic shoes or boots* made in accordance with a prescription to overcome a physical disability will be eligible medical expenses.

In a *Tax Court* case, the Court permitted as a medical expense special *tuition fees* paid by the taxpayer for her fifteen year old son who suffered from a learning and attention deficit disorder. After the Toronto school system determined that they could not handle this case, a doctor was engaged to provide care and training.

Also, the Court permitted as a medical expense *renovation costs* of \$77,667 incurred with respect to another child who had *cerebral palsy* and was confined to a wheelchair with the loss of the use of both legs and his right arm. The renovation was to construct a modest addition occupied solely by the child.

For greater certainty, the February 28, 2000 *Federal Budget* proposes to expand medi-

cal expenses to include *new home incremental costs* enabling access to, or mobility within, for individuals with severe mobility impairments - commencing in the year 2000.

SAME-SEX COMMON-LAW COUPLES

Bill C-23 received Royal Assent on June 29, 2000 extending benefits and obligations to *same-sex* couples effective 2001 unless the couple *elects*, in which case it may be effective for the years 1998, 1999 and 2000.

Benefits of electing include:

1. claim the *spousal credit* for a low-income partner,
2. make *spousal RRSP* contributions,
3. *transferring property* on death or breakup tax free to the surviving partner,
4. transferring *donations, medical* expenses and other items from one partner to the other,
5. receiving a \$10,000 tax-exempt employment *death benefit*.

Some *disadvantages* include:

1. *combining income* for purposes of the Canada Child Tax Benefit, the GST credit and other provincial tax benefits and income supplements based on family net income,
2. non-spouses may take advantage of income transfers without being subject to the *attribution rules*,
3. non-spouses may each have a *principal residence* eligible for the exemption,
4. *child care expenses* are limited to the income of the lower income partner.

These *pros and cons* should be considered before electing prior to the year 2001.

PRINCIPAL RESIDENCE EXEMPTION

In a *Technical Interpretation*, CCRA note that even where a taxpayer is required by law or regulation to acquire land that *exceeds one-half hectare*, all the land may be considered necessary for the use and enjoyment of the residence and eligible for the *principal residence exemption*.

EMPLOYMENT

52(4)

GOLD RING

In a *Tax Court* case, the employer gave a *gold ring* to



Mr. W upon reaching fifteen years of service. CCRA assessed a taxable benefit of \$562 based on the cost of the ring to the employer. The Court agreed that this was an employment taxable benefit however, they reduced the benefit to \$73 based on two independent evaluations which concluded that, because of the *corporate logo*, the value is *its scrap value*.

EMPLOYER-PAID EDUCATIONAL COSTS

In a *Technical Interpretation*, CCRA note that where an employer pays for *courses* of an employee for maintenance or upgrading of *employer-related* skills and it is reasonable to assume that the employee will resume his or her employment for a reasonable period of time after completion of the course, the benefit will generally be *non-taxable*. This may include fees and other costs such as meals, travel and accommodation.

However, these *Guidelines* do *not* necessarily apply in *non-arm's length relationships* or where the benefit was primarily for the *employee*. For example, where the employee and the employer agree to reduce salary in exchange for tax-free

Tax Tips & Traps

salary in exchange for tax-free training costs.

AUTOMOBILE STANDBY CHARGE

In a *Technical Interpretation*, CCRA note that an employee's requirement to take an employer-provided automobile home, for reasons of *security* of the automobile, does not diminish the *personal use* aspect of travelling from the home to the office and vice versa. However, where the employee proceeds directly from *home to a point of call* other than the employer's place of business (e.g. to make repairs at customers' premises), or returns home from such a point, these trips are *not* considered to be *personal*.

Also, in a *Ministerial Letter*, CCRA note that even when an employer provides an *older company-owned vehicle* to an employee, the *standby charge* is based on the *original cost* of the vehicle. The *Letter* notes that many practitioners recommend avoiding any benefit by having the *employee purchase* the vehicle and the employer compensate them for the use of the vehicle.

HAIRCUTS

In a *Tax Court* case, the Court *disallowed* employment expenses for haircuts of \$182 and cleaning and repairing military uniforms of \$140. The taxpayer testified that he had to have his hair cut every two weeks to comply with the *Army's haircut requirement* and that the clothing allowance received of \$17 a year was inadequate.

MARRIAGE BREAKDOWN

52(5)

SAME RESIDENCE

In a *Technical Interpretation*, CCRA note that



Tax Tips & Traps

it is possible for spouses to be living "*separate and apart*" for alimony deduction purposes while still occupying the *same residence*. The Court looks to see if the *customary behaviour* of spouses is present, such as joint social ventures, communication and discussion of family problems, and so on. Of somewhat less importance is whether either spouse performs *domestic services* for the other such as cooking meals or doing laundry. The Courts may also look *as to why* both spouses continue to reside in the same residence if they intended to live "separate and apart".

For example, where one spouse agrees to let the other spouse live with them during the winter because she has difficulties walking and is unable to leave the house during the winter, they may still be considered to be *living separate and apart* even though they are in the same residence. In this example, they had *separate quarters* and maintained each *other's privacy*.

ASSIGNMENT OF PENSION

In a *Technical Interpretation*, a Court Order required Mr. A to pay \$X to Mrs. A to *equalize* the net family assets. *Pension entitlements* were taken into consideration in this Order.

CCRA confirmed that Mr. A would still be required to *pay tax on 100%* of the pension receipts unless there was a formal "*division of pension benefits*".

CHILD SUPPORT

In a *District Office Memo*, CCRA note that the *new Child Support Provisions* eliminate both the requirement to report child support in *income* and, the *deduction* available to payors. Generally, the new rules apply to agreements made *after April, 1997*.

However, the new rules may apply to agreements made *before May, 1997* if a *joint election* is filed by the parties, if the child support *amounts change*, if another

agreement is made *after April, 1997*, or if the agreement specifically provides that the new tax rules *will apply* after April, 1997. CCRA also note that a payment which is for *both* child and spousal support is deemed to be entirely child support and, *none* of the amount is *deductible* or *taxable*.

In a *Tax Court* case, Ms. C received a lump-sum *child support* payment in 1997 for arrears related to a *1983 Agreement*. The Court found that the amounts must be included *in income* because the new *non-taxable/non-deductible* child support rules only apply to agreements that have a *commencement* day after *April, 1997* or, where there is a *joint election* or, a *payment variance*.

LEGAL FEES

In a *District Office Memo*, CCRA permitted a deduction for *legal fees* incurred to *enforce* a right to *child support*.

In a *Tax Court* case, Mrs. M incurred *\$10,950 of legal fees* in obtaining a separation agreement paying \$1,200 per month for child support and \$2,500 per month spousal support. All of the legal expenses were incurred to determine her *husband's income* to enforce the *pre-existing right* to child support. Mrs. M acknowledged that she benefitted from the final agreement but the costs incurred were primarily directed at enforcing the *child's pre-existing rights* to maintenance payments.

The Court noted that the legal costs incurred to enforce a *pre-existing right* are deductible.

RRSP/RRIF

52(6)

SECURITY

In a *Tax Court* case, Mr. D gave the bank as *security* for a personal loan a *Certificate of Deposit* of \$85,380 which was part of

Mr. D's *Registered Retirement Savings Plan*.

Ouch!

CCRA successfully included the \$85,380 in Mr. D's *income*.

DECEASED ANNUITANT

In a *Technical Interpretation*, CCRA notes that a deceased annuitant must include in *income* an amount equal to the *fair market value* of all property of the *RRSP at death* unless the amounts are rolled over to a spouse or, in certain circumstances to a financially dependent child or grandchild. The amount may then be rolled over to the recipient's *RRSPs*.



DONATIONS

52(7)

LIFE INSURANCE

Where a donor *gifts a life insurance policy* to a charity who becomes the *new owner* and *beneficiary* of the policy, the premiums paid by the donor are eligible *charitable donations*. A donation will also be available based on the *value of the policy*. There would be a *deemed disposition* of the policy possibly resulting in a taxable gain. Also, the *Federal Budget 2000* extends the *charitable donation tax credit* to donations of *RRSPs*, *RRIFs* and insurance proceeds that are made as a consequence of *direct beneficiary designations* for deaths after 1998. The donation credit is on the *terminal return* of the deceased taxpayer.



GIFTS TO ORGANIZATIONS OUTSIDE CANADA

Taxpayers may make *charitable donations*

to organizations *outside Canada* provided the federal government, or its agents, have already made a gift to them in the year or, in the previous year. Also, Canadians may receive a *donation tax credit* for donations to over 400 *listed foreign universities*. To get on the list, the university must be able to grant degrees at least at the bachelor level and must establish that the student body normally includes *students from Canada* in each of the last ten years. The list is in Schedule VIII of the Income Tax Act. The Charities Division of CCRA has a *list of charitable organizations* outside Canada to which the federal government has made gifts. (1-800-267-2384)

FARMING

52(8)

TRANSFER OF FARM PROPERTY TO A CHILD

In a *Technical Interpretation*, CCRA note that to satisfy cash bequests to other beneficiaries, a Will might specify that a *mortgage* equal to a stated percentage of the estate is to be placed on the *farm property* prior to the transfer to a particular beneficiary.

QUALIFIED FARM PROPERTY

In a *Technical Interpretation*, CCRA note that where Mrs. X and the children inherit farm property upon Mr. X's death, the farm property may be *qualified farm property* for purposes of a future *capital gain exemption* if a *gross revenue test* is met by the taxpayer, parent, spouse, grandparent or great-grandparent.

TRIP TO NEW ZEALAND

In a *Technical Interpretation*, CCRA responded to a question regarding the *deductibility* of expenses incurred by a group of farmers who visited New Zealand. They note that the tax deduction is *limited*

to expenses incurred to *earn income*, *excludes personal* or living expenses and must be *reasonable*. In most cases an *allocation* on a reasonable basis to eliminate non-deductible expenses is necessary.

SALE OF LIVESTOCK

In a *Technical Interpretation*, CCRA note that when livestock is sold by a *livestock auction mart* it is usually done as an *agent* for the vendor. Therefore, the farmer may be taxable based on the date of the purchaser's cheque to the auction mart, even if the farmer requests the auction mart to issue a post-dated cheque to him/her.



FARM LOSSES

In a *Tax Court* of Canada case, the taxpayer was permitted a *full deduction* for farm losses, *rather* than the *restricted farm loss* applied by CCRA, even though they were also full-time employees. The off-farm work was a direct result of Farm Credit Corporation's requirement that Mr. F obtain off-farm income. The Court noted that this assessment should *never have occurred* and the farmer was *awarded costs*.

GST

52(9)

WASH TRANSACTIONS

In a *GST Memoranda*, CCRA note that a "*wash transaction*" occurs when a supply that is taxable at 7% or 15% (HST) is made and a supplier has not correctly remitted GST/HST and the recipient is a registrant who would have been entitled to claim a full *input tax credit* (ITC) if the tax had been correctly applied. Where there is a wash transaction, CCRA

Tax Tips & Traps

will consider *waiving or cancelling* the portion of the penalty and interest in excess of 4%. Also, where the person has exercised *due diligence*, this remaining 4% penalty may be *cancelled* under the Fairness Provisions. In addition, where there is a *Voluntary Disclosure*, the 4% penalty will *not apply* and only the *GST/HST* that should have been collected originally by the supplier will be sought by CCRA.

SORRY NO INPUT TAX CREDITS



In a *Tax Court* case, the appellant operated a *courier service* in Toronto. The appellant used approximately seventeen subcontractors who were advised to register under the Excise Tax Act to collect GST. Documentation was provided to assist them in this registration.

Ouch!

CCRA successfully *disallowed* the input tax credit where the *GST registration number* was not included on the *invoice*. The reassessment imposed GST of \$76,294 plus interest and penalties.

NEW HOUSING REBATE

In a *Tax Court* case, the taxpayers were *prevented* from obtaining a "*new housing rebate*" because they did not make their application within *two-years* of acquiring a home or making substantial renovations.

NEW RESIDENTIAL RENTAL PROPERTY REBATE

The *February 28, 2000 Budget* proposes to introduce a *New Residential Rental Property Rebate*, generally equal to a maximum of 2.5% for newly-constructed, substantially renovated or converted *residential rental accommodation*. This rebate will be available in respect of rental accommodation including *single unit* and *multiple unit* rental housing, additions to multiple unit rental housing, and land leased for residen-

tial purposes - provided the rental accommodation or land is used, or intended to be used, as an individual's *primary place of residence* on a *long-term* basis.

DIRECTOR LIABILITY

In a *Saskatchewan Court of Queens Bench* case, the corporation failed to file quarterly GST returns for two years (eight quarters) and, therefore, the corporation was fined the minimum fine of *\$1,000 per quarter* for a total of \$8,000. Also, Mrs. D was fined \$1,000 per quarter as the *director* of the corporation thereby resulting in a double up of the penalty. The Saskatchewan Court found that there was *no evidence* that *Mrs. D* was aware the corporation had received a Notice of Demand and, therefore, she was *not guilty*. However, the corporation continued to be liable for the \$8,000.

DETAX

CCRA advise that vendors should be aware that a number of individuals are claiming *GST exemptions* and, in some cases, presenting cards, such as "*Corporation Sole*" and "*International Humanity House*", in an attempt to avoid paying GST on their purchases. These people are *not exempt* for GST. If the vendor does not collect GST/HST they will still be *liable for the tax*.

INTERNATIONAL

52(10)

SNOWBIRDS VISITING THE UNITED STATES

Most "*snowbirds*" that spend a few months in the United States *continue to be residents* of Canada and subject to Canadian income tax on their world income. However, snowbirds that have a "*substantial presence*" in the United States may also be

considered to be a resident in the United States and taxed in the U.S.. This test applies if the individual spends more than thirty-one days in the United States in the current year and; the total days in the current year in the U.S. plus one-third of the days in the preceding years plus one-sixth of the days in the second preceding years exceeds 183 days. (approximately 122 days per year)

However, if a person meets this test, but did not spend 183 days in the United States in the current year, the person *will not* be considered a *U.S. resident* if they have a "*tax home*" in Canada thereby permitting most snowbirds to avoid being treated as U.S. residents. To claim this exemption the Canadian must file *Form 8840* - Closer Connection Exception Statement for Aliens.

DOT-COM CORPORATIONS

Many new Canadian dot-com companies are managed from a Canadian office but have a *U.S. parent corporation*, usually in Delaware. This is because U.S. dot-com companies often command higher valuations and have easier access to cash.

TAX HAVENS

The Organization for Economic Co-operation and Development (*OECD*) has issued a *black list of thirty-five tax havens* that must change their tax policies within a year, or face *economic sanctions*. Most of the countries are in the Caribbean or Pacific but also include countries like Bahrain, Belize, Gibraltar, Liberia, Liechtenstein, Monaco, Panama, Channel Islands and the British Virgin Islands.



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DID YOU KNOW...

52(11)

NIGERIAN SCAM

There are many variations of *Nigerian scams*, one of which may include the request to use your Canadian bank account to deposit ill-gotten gains (say \$30 million) and your fee would be, say, \$6 million, subject to providing, say, \$250,000 to cover some administrative costs. Of course, this is *a scam* and the \$250,000 will be lost if paid.

KIDDIE TAX

Dividends paid by a *public company* to a *minor* are *not* subject to the Kiddie tax, however, if the minor owns shares in a private *holding company* which owns shares in a public company and dividends are paid by the public company to the holding company and then out to the minor, the dividends paid to the minor *will be subject* to the Kiddie tax because they are from a *private company*.



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CONTRACT PAYMENT REPORTING

There is a requirement to file an Information Return under the new *Contract Payment and Reporting System* for a taxpayer whose business income is derived primarily from "*construction activities*". For this purpose, "*construction activities*" include the erection, excavation, installation, alteration, modification, repair, improvement, demolition, destruction, dismantling or removal of all or any part of a building, structure, surface or sub-surface construction, or any similar property.

DIRECTOR LIABILITY

In a *Tax Court* case, the corporation *failed to remit* income tax deductions, CPP and EI premiums for July, September, December, 1994 and February and March, 1995. Mr. W indicated that he *sent a letter* to the corporate lawyer on March 21, 1995 noting that he was *resigning* as a *director* and, because the assessment was not issued until July 21, 1997, he could not be assessed

because of the *two year* Statute of Limitations.

Ouch!

The Court did *not accept* that the *unsigned letter* to the lawyer constituted a formal resignation. Therefore, the taxpayer's only defense was *due diligence*. This was *not accepted* by the Court because the taxpayer was an *inside director* and, *he knew* of the financial difficulty and that amounts had not been remitted to CCRA.

PERSONAL INJURY

In a *Technical Interpretation*, CCRA note that amounts received by a taxpayer as damages for *personal injury* are *excluded* from income. This includes special or general damages as a result of having acquired *Hepatitis C* through a blood transfusion. Also, income replacement indemnities received in respect of *personal injuries* as a consequence of a *motor vehicle accident* are *non-taxable*.

Tax Tips & Traps
