Grant Thornton
An instinct for growth™

Tax planning guide
2014–2015
Introduction

The 2014–2015 edition of our planning guide is an up-to-date reference on the latest business and individual tax developments. The planning suggestions in this guide are general in nature and should not be considered a substitute for the recommendations of your tax adviser. We hope you enjoy this year’s edition.
# Table of contents

## Section I – Businesses

1. Are you self-employed? .............................................. 15
2. Taxing partnership income ........................................ 15
   Rules for corporate partners .................................. 16
3. Rules for joint ventures .......................................... 16
4. Which province gets your tax? ................................. 17
5. Paying your spouse or common-law partner
   and/or children .................................................. 18
6. Employment Insurance (EI) and family members ........ 18
7. Calculating depreciation .......................................... 19
   The half-year rule .............................................. 20
   Available-for-use rules ....................................... 21
   Special rules and restrictions ................................ 21
8. Amortization and sale of eligible capital property ...... 21
9. The home office .................................................. 22
   You're self-employed ......................................... 22
   You're an employee .......................................... 24
10. Paying your dues ............................................... 25
11. Meals and entertainment (M&E) expenses ............... 26
   Rules for long-haul truck drivers ......................... 27
12. Convention expenses .......................................... 28
13. Canada Pension Plan (CPP) contributions ............... 28
   Employer CPP remittances ................................ 30
14. Deduction of health/dental insurance premiums ....... 30
15. Self-employed wage-loss replacement plans ............ 30
16. Deduction of life insurance premiums ..................... 31
17. Deduction of fines and penalties ........................... 31
18. Valuation of inventory ........................................ 31
19. Operating losses and prior years' taxes ................... 32
20 Apprenticeship job creation tax credit ....................... 33
21 Investment tax credit (ITC) for childcare spaces .......... 33
22 To incorporate or not to incorporate.......................... 33
    Transferring your business assets to the corporation on a
tax-deferred basis .............................................. 34
23 Incorporating your professional practice ................... 34
24 The small business deduction .................................. 35
    Other corporate tax rates .................................... 36
    Personal services business ................................... 36
25 Capital tax.......................................................... 37
26 Associated-company rules ....................................... 38
27 Salaries and bonuses to shareholders ....................... 38
28 Salary vs. dividends ............................................. 39
29 Salary deferral arrangements ................................. 39
30 Directors' fees..................................................... 40
31 Loans from your corporation .................................. 41
    Some exceptions apply ....................................... 41
    Deemed interest benefit on “excepted” loans ............ 42
32 Taxable benefits .................................................. 42
    Christmas parties and other special events .............. 42
    Non-cash gifts and awards ................................... 43
    Employer-paid professional membership fees ............ 43
    Group sickness or accident insurance plans ............. 44
    Non-taxable benefits ......................................... 44
33 Employee loans ................................................... 46
34 Personal use of a company-owned automobile ............ 46
    Operating costs ................................................ 48
    Self-employed persons and business use .................. 50
36 Tax-free travel allowances ...................................... 51
37 The taxation of stock options .................................. 52
    How is the benefit taxed? ..................................... 52
    What if the stock declines in value? ....................... 54
    Public company stock options ................................ 54
38 Qualified scientific research expenditures .................. 55
    What can you deduct? ......................................... 55
Claiming SR&ED .......................................................... 56
Investment tax credit (ITC) ............................................. 57
Proxy amount .................................................................. 58
SR&ED contract payments ............................................. 58
Filing due date .............................................................. 59

Shareholder agreements .................................................. 59

Reporting system for contractors ................................... 60
What payments must be reported? ............................... 60
What information must be reported? ............................. 60

Farming businesses ....................................................... 61
Methods of reporting income ......................................... 62
Farming losses ............................................................. 63
Restricted farm losses .................................................... 63
Capital gains deduction for qualified farm property ....... 64
Intergenerational transfers ............................................. 65

Transfer pricing ............................................................ 65

Withholding tax on interest payments to non-residents . 66

Payments to non-residents for services rendered in Canada .......................................................... 66

The goods on the GST/HST ............................................. 67

GST/HST registration, collection and remittance ...... 68
New businesses .......................................................... 69
When to report ............................................................. 69

Input tax credits (ITCs) .................................................. 70
Employee reimbursements .......................................... 72
Allocation of tax between taxable and exempt supplies 73

GST/HST streamlined accounting thresholds .......... 73

GST/HST and automobiles .......................................... 74
How much do you owe? .............................................. 75
Employee or partner expenses rebate ......................... 76
Travel and other allowances ....................................... 77

GST/HST and real property sales ............................... 78
Sales of real property to a registered purchaser ......... 78

GST/HST and buying and selling a business .......... 79

Filing a tax return ...................................................... 80
Who claims the childcare costs?............................... 104
How much can you deduct?................................. 105
74 Alimony and maintenance ................................ 105
   Agreements or court orders after April 1997........ 105
   Registration of agreements................................ 106
   Agreements or court orders prior to May 1997..... 106
   Payments to a third party.................................. 107
75 Deductibility of legal fees during separation or divorce 107
   Legal expenses incurred to obtain a lump-sum payment......................................................... 108
   Legal expenses incurred to obtain periodic support payments..................................................... 108
76 Deductibility of other legal expenses.................. 108
77 Moving expenses............................................. 109
   Costs you can claim .......................................... 109
   Other amounts received from your employer .......... 110
   Student eligibility............................................. 110
   Optional method for claiming certain moving expenses ............................................................... 110
78 Scholarship income ......................................... 111
79 What is a tax credit?........................................ 111
   Basic personal credit ....................................... 112
   The spouse or common-law partner credit......... 112
   The eligible dependant credit ......................... 112
   Credit for children under age 18..................... 113
   The infirm dependant credit ............................ 113
   The caregiver credit ....................................... 113
   Family caregiver credit ................................... 114
   The age credit ............................................... 114
80 Disability tax credit........................................ 114
81 Tax credits for charitable donations.................... 116
   Donating property instead of cash........................ 117
   Art and other charitable donation arrangements ... 118
   Other receipting guidelines for charities ............. 120
   Donations from state supporters of terrorism ...... 120
82 Political donations........................................ 120
83 Medical expenses.......................................... 121
Eligible expenses .......................................................... 121
Medical expenses of dependants other than a spouse or common-law partner ....................... 122
Refundable medical expense credit ......................... 123
What you cannot claim as medical expenses .......... 123

84 Disability supports deduction (attendant care expenses) 124
85 Attendant care in a retirement home ...................... 124
86 Adoption expense credit ........................................ 124
87 Tuition fees, education and textbook credits .......... 125
  Tuition tax credit .................................................. 125
  Education tax credit ............................................. 125
  Textbook tax credit ............................................... 126
  Transfer of tuition, education and textbook credits ... 126
88 Interest on student loan credit ............................... 127
89 Pension credit .................................................... 127
90 Claiming your spouse or common-law partner’s unused credits ........................................... 128
91 First-time home buyers’ tax credit ......................... 128
92 Canada Employment Credit ................................... 128
93 Working Income Tax Benefit (WITB) ...................... 128
94 Public transit credit ............................................. 129
95 Children’s fitness credit ....................................... 130
96 Children’s arts tax credit ..................................... 131
97 Canada Child Tax Benefit (CCTB) ......................... 131
98 Universal Child Care Benefit (UCCB) ................. 132
99 Child benefits in shared custody situations .......... 132
100 Taxation of common-law couples ........................... 133
101 Special rules for artists and entertainers ................. 133
102 Apprentice mechanic deduction for tools .............. 134
103 Tradespeople’s tool expenses ............................... 135
104 Northern residents deduction .............................. 135
  Residency deduction ............................................ 136
  Travel deduction .................................................. 136
105 Special rules for the clergy ........................................... 136
106 Taxation of emergency volunteers .............................. 137
   Tax credit for volunteer firefighters ................................ 137
   Search and Rescue Volunteers Tax Credit .......................... 138
107 Principal residence rules ............................................. 138
   Designating a principal residence .................................... 139
   Tax issues ................................................................... 139
   Homes for rent ........................................................... 140
108 Selling personal-use capital property......................... 140
109 Transfers and loans to family members ...................... 141
   Transfers to a spouse or common-law partner ................. 141
   Transfers to other family members .................................. 143
   Interest-free loans to family members ............................. 144
110 Registered Education Savings Plans (RESPs) ............... 144
   Contributions .................................................................. 145
   Transfer to an RRSP or RDSP ........................................... 145
   Canada Education Savings Grants (CESGs) ..................... 145
   Canada Learning Bond (CLB) ............................................ 146
111 Registered Disability Savings Plan (RDSP) ................. 146
   Grants and bonds available ............................................. 146
   Payments .................................................................... 148
   End of plan .................................................................. 148
   Rollover of RRSP/RRIF proceeds to an RDSP ................. 148
112 Splitting CPP benefits with your spouse or common-law partner ............................... 149
113 Income splitting with family members ....................... 149
   Permitted arrangements ............................................... 150
114 Income splitting using family trusts ......................... 151
115 Retroactive lump-sum payments ............................... 152
116 Some income is tax-free ............................................. 152
117 Taxation of non-competition payments ..................... 153
118 Taking up Canadian residence ................................. 153
   Foreign pension plans .................................................. 154
119 Giving up Canadian residence ............................... 155
   Tax implications .......................................................... 155
   Reporting requirement .................................................. 156
120 Temporary assignments outside Canada .................. 157
   Residency defined .............................................. 157
121 Canadian residents working in the United States ...... 157
122 Canadian tax obligations for non-residents ............... 159
123 Disposition of taxable Canadian property by
   non-residents ...................................................... 160
124 US persons resident in Canada............................... 161
   Filing your returns.............................................. 161
   Ownership of registered savings plans by US persons 163
125 US Social Security payments .................................. 163
126 US real estate owned by Canadian residents .......... 164
   Selling your US property ..................................... 165
127 Withholding tax on income from US sources .......... 165
128 US estate tax .................................................... 166
129 US residency regulations ...................................... 166
130 US financial reporting requirements ...................... 168
   Exchange of information between Canada and the United
   States ............................................................... 168
131 Succession and estate planning ............................. 169
   Succession planning ........................................... 169
   Estate freeze/refreeze ........................................ 170
   Life insurance .................................................... 171
   Asset transfers ................................................... 172
   Alter-ego and joint-partner trusts .......................... 172
   Planned giving .................................................... 173
   Will planning ..................................................... 174
132 Deceased taxpayers ............................................ 174
   Executor’s responsibilities ................................... 174
   Instalments ....................................................... 175
   Canada Pension Plan (CPP) and Old Age Security (OAS)
   payments ............................................................. 175
   GST/HST credit ................................................... 175
   Canada Child Tax Benefit (CCTB) and Universal Child
   Care Benefit (UCCB) ............................................. 176
   Tax filing obligations of the legal representative ....... 176
   Income ............................................................ 177
   Capital properties .............................................. 179
Funeral and estate administration expenses .......... 180

133 Rental properties ......................................................... 181
What can I deduct? .............................................................. 181
Joint owner or partner? ...................................................... 181
How much can I claim for depreciation? ...................... 182
What happens if I sell? ...................................................... 182
Terminal loss rules .............................................................. 183

134 What about capital gains? .............................................. 183
When is a gain a capital gain? .......................................... 183
Identical properties .............................................................. 184
Sale of stock option shares .............................................. 185

135 Lifetime capital gains deduction .................................. 185
$100,000 capital gains deduction .................................. 185

136 Qualified small business corporation (QSBC)
capital gains deduction ..................................................... 186
Election for private companies going public ...................... 187

137 Qualified farm property capital gains deduction ......... 187

138 Qualified fishing property capital gains deduction ..... 188

139 Capital gains deferral for investments in small
corporations ............................................................................. 189

140 Capital gains reserves ..................................................... 190

141 Capital loss rules ............................................................. 190

142 Allowable business investment losses (ABILs) .......... 191

143 Taxation of dividends ....................................................... 192
Eligible-dividend rules ......................................................... 192
Dividends and individuals .................................................... 192
Dividends and corporations .................................................. 193
Designating a dividend as an eligible dividend ............... 194
Foreign spinoffs ................................................................. 195

144 Transfer of dividend income between spouses .......... 196

145 Taxation of interest income ............................................. 196
Canada Savings Bonds (CSBs) .............................................. 196
Treasury bills ................................................................. 197

146 Mutual funds ................................................................. 197

147 Income trusts and Real Estate Investment Trusts (REITs) 198

Tax planning guide 2014–2015 9
Corporate taxation

Table 1 Business income eligible for SBD
Table 2 Business income not eligible for SBD
Table 3 Investment income
Table 4 Sales tax
Table 5 SR&ED Investment Tax Credits
Table 6 Capital cost allowance rates
Table 7 Canada Pension Plan
Table 8 Employment Insurance

Individual taxation

The following tables are in each of the provincial taxation tables:

Table 1 Tax table
Table 2 Non-refundable tax credits
Table 3 Marginal rates
Table 4 Tax brackets
<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>ABI</td>
<td>active business income</td>
</tr>
<tr>
<td>ABIL</td>
<td>allowable business investment loss</td>
</tr>
<tr>
<td>ACB</td>
<td>adjusted cost base</td>
</tr>
<tr>
<td>AMT</td>
<td>alternative minimum tax</td>
</tr>
<tr>
<td>CCA</td>
<td>capital cost allowance</td>
</tr>
<tr>
<td>CCPC</td>
<td>Canadian-controlled private corporation</td>
</tr>
<tr>
<td>CCTB</td>
<td>Canada Child Tax Benefit</td>
</tr>
<tr>
<td>CDSB</td>
<td>Canada Disability Savings Bond</td>
</tr>
<tr>
<td>CEC</td>
<td>cumulative eligible capital</td>
</tr>
<tr>
<td>CESG</td>
<td>Canada Education Savings Grant</td>
</tr>
<tr>
<td>CLB</td>
<td>Canada Learning Bond</td>
</tr>
<tr>
<td>CNIL</td>
<td>cumulative net investment loss</td>
</tr>
<tr>
<td>CPP</td>
<td>Canada Pension Plan</td>
</tr>
<tr>
<td>CRA</td>
<td>Canada Revenue Agency</td>
</tr>
<tr>
<td>CSB</td>
<td>Canada Savings Bonds</td>
</tr>
<tr>
<td>DPSP</td>
<td>deferred profit sharing plan</td>
</tr>
<tr>
<td>EI</td>
<td>Employment Insurance</td>
</tr>
<tr>
<td>FMV</td>
<td>fair market value</td>
</tr>
<tr>
<td>GIC</td>
<td>guaranteed investment certificates</td>
</tr>
<tr>
<td>GRIP</td>
<td>general rate income pool</td>
</tr>
<tr>
<td>GST</td>
<td>Goods and Services Tax</td>
</tr>
<tr>
<td>HBP</td>
<td>Home Buyers’ Plan</td>
</tr>
<tr>
<td>HST</td>
<td>Harmonized Sales Tax</td>
</tr>
<tr>
<td>IPP</td>
<td>individual pension plan</td>
</tr>
<tr>
<td>IRA</td>
<td>individual retirement account</td>
</tr>
</tbody>
</table>
ITC    investment tax credit or input tax credit (GST/HST)
ITN    individual tax number
LIF    Life Income Fund
LRIP   low rate income pool
NCB    National Child Benefit
OAS    Old Age Security
PA     pension adjustment
PAR    pension adjustment reversal
PRPP   Pooled Registered Pension Plan
PSPA   past service pension adjustment
QSBC   qualified small business corporation
RDSP   Registered Disability Savings Plan
REIT   Real Estate Investment Trust
RESP   Registered Education Savings Plan
RLIF   Restricted Life Income Fund
RPP    registered pension plan
RRIF   Registered Retirement Income Fund
RRSP   Registered Retirement Savings Plan
SBC    small business corporation
SR&ED  scientific research and experimental development
TFSA   Tax-Free Savings Account
UCC    undepreciated capital cost
UCCB   Universal Child Care Benefit
WAC    web access code
Section I – Businesses

1 Are you self-employed?
If you’re self-employed, you have many more options for tax planning than if you’re an employee. However, determining whether you’re self-employed or employed is not always cut and dried. It depends on your particular circumstances, and often comes down to how much control the person paying for your services exercises over your work.

The Canada Revenue Agency (CRA) has published a guide to assist in determining employed vs. self-employed status. A copy of this guide (“RC4110—Employee or Self-Employed?”) can be found on the CRA’s Web site at www.cra-arc.gc.ca (see “Forms and Publications”).

2 Taxing partnership income
As a member of a partnership, you must report your share of the partnership’s profit or loss for its fiscal period ending in 2014. While you can normally claim your share of partnership losses against your other sources of income, this may not always be the case if you’re a member of a limited partnership (see topic 153).

Certain expenses incurred outside the partnership may also be deductible. For example, if you borrowed money to invest in the partnership, the interest on that loan is generally deductible (see topic 150). Any expenses that you personally incur in the course of carrying on the partnership business (e.g., promotional and automobile expenses) are also deductible. However, meal and entertainment expenses are only partially deductible (see topic 11), and some automobile expenses may be limited (see topic 35).

Although the Act requires that all Canadian partnerships file an information return (Form T5013), the CRA administratively excepts certain partnerships from this requirement.

1 Special rules for corporate partners are discussed below.
The CRA’s current position is that a partnership is required to file an information return if, at the end of its fiscal period, it has an absolute value of gross revenues plus an absolute value of expenses of more than $2 million, or has more than $5 million in assets. A return also has to be filed if, at any time during the fiscal period, the partnership is a tiered partnership; the partnership has a corporation or a trust as a partner; the partnership invested in flow-through shares of a principal-business corporation that incurred Canadian resource expenses and renounced those expenses to the partnership; or if the CRA requests that a return be filed.

As a result, although it’s still a good idea to file the return, partnerships that have simple structures and modest financial activity are not required to file a partnership return.

Rules for corporate partners
In some cases, a partnership can be held by corporate partners. This type of structure used to allow for the deferral of tax where the partnership had a year-end that ended after the year-end of the corporation. Recent rules have eliminated this tax-deferral strategy in a manner that will spread the one-time tax cost from the collapse of the deferral over a five-year period (15% in 2012, 20% in each of 2013, 2014 and 2015, and 25% in 2016). These rules apply where the corporate partner is entitled to more than a 10% income allocation from the partnership and are applicable to a corporation’s first taxation year ending after March 22, 2011.

These rules are extremely complex. If you have an interest in a corporation that is caught by these rules, you should consult with your tax adviser.

3 Rules for joint ventures
For many years, the CRA administratively permitted a joint venture (JV) to have a fiscal period that was different from the fiscal periods of the JV participants. This policy allowed a JV participant to realize a tax deferral similar to that enjoyed by corporate partners of a partnership. The differences between a JV and a partnership are discussed in topic 133.
Due to the rules to limit the tax deferral opportunities for certain corporate partners (discussed above), the CRA announced that for taxation years ending after March 22, 2011, JV participants would also no longer be able to compute income as if the JV had a separate fiscal period. Instead, income from a JV will have to be calculated for each JV participant based on the fiscal period of the particular JV participant. Similar to the rules for partnerships, transitional relief is available to spread the additional income for the stub period over a five-year period—i.e., 15% in 2012, 20% in each of 2013, 2014 and 2015, and 25% in 2016.

**Example**

Assume a JV had a fiscal period ending June 30 and XYZ Co., one of the JV participants, has a December 31 year-end. The JV’s actual amount of its additional income for the period July 1, 2011 to December 31, 2011 was $200,000. Assuming a maximum reserve is claimed each year, the following additional amounts will have to be included in XYZ Co.’s income for its fiscal periods ending in 2012 to 2016:

- 2012 $30,000
- 2013 $40,000
- 2014 $40,000
- 2015 $40,000
- 2016 $50,000

A JV participant who wanted to benefit from this transitional relief for the first taxation year ending after March 22, 2011, had to file an election in writing with the CRA, by no later than September 22, 2012. If the election was not filed, the entire amount of the stub period income had to be included in income for the JV participant’s first taxation year ending after March 22, 2011.

4 **Which province gets your tax?**

Employment and investment income are both taxed by the province in which you reside on December 31. This is the case even if the income was earned in another province. Business income, on the other hand, is taxed in the
province where the business was conducted. If you carry on the same business through a permanent establishment in more than one province, a complicated formula is used to determine what portion of your business income is taxable in each province.

**Tax tip**

Unless you earn self-employed business income (see above), provincial tax is based on your province of residence on December 31. If you’re transferring to a province with a lower tax rate, you should consider accelerating your departure to arrive before the end-of-year deadline. Conversely, if a move to a province with a higher tax rate is in your future, consider postponing your relocation until after the year-end.

5 **Paying your spouse or common-law partner and/or children**

Salaries paid to your spouse or common-law partner and/or children are tax deductible to your business as long as the wages are reasonable in relation to the services they have provided. As a rule, salaries are considered reasonable if they’re representative of an amount that would be paid to an arm’s-length party for similar services—in other words, comparable to what you would pay an unrelated employee to do the same job.

**Tax tip**

There are many advantages to paying reasonable wages to family members for actual services rendered. A key benefit is that salaries will be taxed in their hands, and probably at rates lower than your marginal tax rate. This arrangement will also allow them to make their own RRSP and CPP contributions.

6 **Employment Insurance (EI) and family members**

Employment Insurance (EI) premiums can constitute a considerable expense. There are various exemptions from having to remit EI premiums. For example, if you own more than 40% of the voting shares of a corporation,
your employment is not subject to EI premiums. There’s another exemption for employees who deal at “non-arm’s-length” with their employer. The problem with this rule is that there’s another rule stating that two related persons are deemed to deal with each other at “arm’s-length” if the circumstances of the employment are substantially similar to what they would be if an unrelated person were to perform the same job.

**Tax tip**

Consult your professional adviser to determine if there’s any way you can structure the employment of your spouse or common-law partner or other family members to justify EI-exempt status. Your business and family members could also be eligible for a refund.

**7 Calculating depreciation**

The cost of a capital asset is generally not deductible as an expense. However, you can depreciate certain business assets for tax purposes. The tax term for such depreciation is “capital cost allowance” (CCA).

Depreciable assets are grouped into classes according to their type and use. There are more than 50 different classes, each with its own rate of depreciation.

The government also adjusts CCA rates to provide economic incentives or to better reflect the useful life of the property. The following are some of the more significant examples:

- Manufacturing and processing (M&P) machinery and equipment that would otherwise qualify for a 30% CCA (Class 43) will, for a limited time, qualify for an accelerated write-off. Eligible purchases acquired before 2016 will qualify for a 50% straight line accelerated CCA rate and will be placed in Class 29.
- Buildings acquired after March 18, 2007 and used for M&P in Canada qualify for a CCA rate of 10% as opposed to 4%. To claim the 10% rate, at least 90% of the floor space must be used in manufacturing or
processing in Canada. Other non-residential buildings acquired after March 18, 2007 that are not used 90% for M&P may qualify for a CCA rate of 6% as opposed to 4%. To claim the higher CCA rate, the taxpayer must elect to include the building in a separate prescribed class (Class 1). This election is made by attaching a note in the taxpayer’s income tax return for the tax year in which the building is acquired.

- The CCA rate for computer hardware and systems software has gradually increased from 30% to 55%, except for a temporary period from January 28, 2009 until January 31, 2011 when such property was eligible for a 100% write-off. Such purchases are now placed in Class 50, which is eligible for a 55% CCA rate.

Most classes of assets are depreciated on a declining-balance basis. Some of the more common CCA classes and their applicable CCA rates are noted in the tables at the back of this book.

The amount of depreciation you can claim for a year is determined by multiplying the remaining balance in the asset class by the specified percentage rate for that specific class (generally pro-rated for short taxation years). The remaining balance, referred to as the undepreciated capital cost (UCC), is calculated on a continuous basis.

Each year (subject to the available-for-use rules—see below), you add the cost of assets acquired in the year to the previous year’s closing balance. If you have disposed of an asset, you subtract the proceeds up to the original cost of the asset.

The amount of CCA determined by this method represents the maximum amount that can be claimed. You do not have to claim the maximum amount. For example, if your business is in a loss position, you may decide not to claim depreciation for that particular year.

**The half-year rule**

Most depreciable assets are subject to a rule that reduces the maximum depreciation claim in the year of purchase.
to half the net additions made to the specified class. This “half-year” rule doesn’t apply to the acquisition of certain capital property, such as tools costing less than $500. Such assets can be written off 100% in the year of purchase.

Available-for-use rules
The available-for-use rules determine the taxation year in which an amount can first be claimed for depreciation and whether the half-year rule will apply. Rules with respect to the acquisition, construction and/or renovation of a building are especially complex. It’s best to ask your tax adviser about the rules in this area. However, the general rule is that property may be depreciated for tax purposes at the date it’s first used to earn income, or the second taxation year following the year of acquisition, whichever is earlier.

Special rules and restrictions
Some depreciation restrictions apply to rental property (see topic 133). Others apply to depreciation claims arising from certain “tax shelters” in which the investor is not active in the day-to-day operations of the business. Depreciation claims by taxpayers who lease certain types of property are also subject to certain rules. Since the rules do not apply to all leasing properties, your tax adviser is in the best position to determine if you’re affected by these rules.

8 Amortization and sale of eligible capital property
Eligible capital property (ECP) includes such things as goodwill and other “nothings,” the cost of which neither qualifies for CCA (see topic 8) nor is deductible in the year of its acquisition as a current expense.

For example, if you purchase goodwill (the intangible value of a business, such as a recognized name and reputation), you’re permitted to amortize three-quarters of its cost on a declining-balance basis at the rate of 7%. When the goodwill is sold, three-quarters of the proceeds are credited to the unamortized pool at the time of sale and, if the balance of the pool becomes negative, an amount has to be reported as business income. This amount is split between the recapture of amounts previously claimed as amortization
and, if the proceeds exceed the original cost, an amount that represents the equivalent of a capital gain.

When there’s only one asset in the cumulative eligible capital (CEC) pool, any gain on the disposition of ECP—after the recapture of amounts previously deducted—is taxed like a capital gain: The amount by which the proceeds exceed the original cost is taxed at 50% of the rate applicable to ordinary income. When there are other assets in the pool, the rules are more complicated. There are further adjustments when the taxpayer previously claimed the capital gains deduction with respect to the property disposed of (see topic 135).

If the disposition relates to the sale of qualified farm or fishing property, such as the sale of a quota, all or a portion of the negative balance may qualify for the capital gains deduction provided a special election is made (see topics 137 and 138).

The 2014 federal budget outlined a proposal to simplify the income tax rules dealing with eligible capital expenditures and eligible capital receipts. The proposal is to replace the existing ECP regime by transferring a taxpayer’s existing CEC pools to a new CCA class. Generally, all of the rules applicable to depreciable property would be applicable to this new CCA class and all future eligible capital expenditures and receipts would be accounted for through this new CCA class.

The timing and implementation of this proposal will be subject to public consultation.

9 The home office
If you work out of your home you may be able to deduct a portion of your home office expenses. However, there are a number of rules, and the rules differ depending on whether you’re self-employed or an employee.

You’re self-employed
If you’re self-employed, expenses must relate to a workspace that is either your principal place of business, or used
exclusively for the purpose of earning income from the business. “Principal” is generally interpreted as more than 50% of the time. For the second criterion to apply, the space must also be used on a regular and continuous basis for meeting clients, customers or patients. If you qualify to claim home office expenses, you can deduct a portion of the operating costs of your home. For example, assume your home office takes up 10% of the total square footage of your home. You can claim as a deduction from your business income 10% of your mortgage interest (not principal), property taxes, heat, hydro, water, home insurance and maintenance costs. Any expenses directly related to the home office can be deducted in full.

Home office expenses can only be deducted from the business carried on in the home and cannot be used to create a business loss. Eligible expenses you are unable to use in the year they are incurred can be carried forward to subsequent years and deducted from income generated by the business at that time, as long as the business-use criteria discussed above are still met.

**Example**

Suppose you started a business in 2014. It generated revenues of $60,000 in 2014 and expenses, other than home office expenses, of $55,000. The portion of eligible home expenses attributable to your office space amounts to $6,200. You'll be able to claim only $5,000 of the home office expenses in 2014 (i.e., $60,000 - $55,000). The remaining $1,200 can be carried forward and claimed against income generated by the business in a subsequent year.
In general, it’s not a good idea to claim depreciation on the portion of your home used for business purposes, since there may be negative tax implications if you ever sell your home. If you do not claim depreciation, your entire house may be regarded as your principal residence (see topic 107) and any gain realized on its eventual sale may be tax-free.

If you’re registered for the GST/HST and you qualify to claim home office expenses, input tax credits (ITCs) can be claimed for the portion of your home expenses attributable to the business activity. However, an ITC can only be claimed for those expenses that are subject to GST/HST—for example, heat, hydro, etc. Mortgage interest and property taxes are not subject to the tax.

Example

You’re a GST/HST registrant, and your only office is located in your home. You regularly meet with clients and conduct all your business from this location. The office space occupies 10% of the total area of the house. As such, you’re entitled to claim a deduction for 10% of the eligible home expenses incurred and ITCs for 10% of the GST/HST paid on those expenses.

You’re an employee

The rules for deducting home office expenses are more limited for employees. In this case, you’ll only be permitted to deduct costs related to a home office if your workspace is either the place where you principally perform your employment duties, or the space is used exclusively on a regular and continuous basis for meeting people while performing your employment duties.

Also, as an employee, the home office expenses you can claim are restricted. If you own your home, your deductions are limited to the maintenance of the premises, such as a portion of fuel, electricity, cleaning materials and minor repairs. You cannot deduct mortgage interest or any
depreciation on your home. If you pay rent, a proportionate amount of the rent is deductible. If you’re a salesperson on commission, your deductions may include property taxes and insurance. However, other employees are not entitled to claim a deduction for these expenditures.

Like self-employed persons, you cannot create a loss from employment when claiming home office expenses. Similarly, any eligible expenses that you cannot use in one year can be carried forward to subsequent years.

**Tax tip**

Your employer must certify on Form T2200 that you’re required, under your contract of employment, to use a portion of your home as an office. You must keep this form in the event the CRA requests a copy of it.

If you claim home office expenses, you may also be able to claim a GST/HST rebate for the portion of your home expenses attributable to the employment activity. To qualify, your employer must be a GST/HST registrant other than a listed financial institution such as a bank, insurance company or brokerage firm.

This rebate is calculated as a percentage of eligible expenses (refer to the chart on page 77 for “Employee or partner expenses rebate”—part of topic 49). Although the rebate claim is generally filed with your income tax return, you have up to four years to file a claim.

10 Paying your dues

Many professionals and business people belong to recreational or dining clubs (e.g., golf or tennis clubs). However, you should be aware that annual dues payable to such facilities are not deductible expenses, even if there’s an argument that the expense has been incurred for business purposes. There are also rules that specifically deny the employer a deduction for the use of such facilities. The CRA’s position with respect to expenses incurred at a lodge, golf course or similar facility is as follows: If such
property is used for business purposes, and those purposes do not include the entertainment or recreation of clients, suppliers, shareholders or employees, it will allow a deduction for the related expenses. For instance, if you hold a business meeting at a golf club and it doesn’t involve playing golf or use of the other recreational facilities, any reasonable expenses related to that meeting will be deductible.

As for meals and beverages consumed at such facilities, deductibility restrictions are the same as for those consumed at other establishments (see topic 11). You must ensure that the costs are clearly itemized and, of course, incurred for the purpose of earning income. If your records show an all-inclusive charge that doesn’t itemize specific costs, the deduction won’t be allowed.

If you pay annual membership dues for an employee, the dues will not be regarded as a taxable benefit to the employee if it can be demonstrated that it’s to your advantage for your employee to belong to the club. Similarly, amounts you pay for your employees’ use of the facilities for promotional purposes would not be regarded as a taxable benefit.

Tax tip

Based on the facts, it should be considered whether a club membership is principally for the benefit of the employee or the employer. Regardless of whether the employee has to report a taxable benefit, the employer is not able to claim a deduction for the amount paid.

11 Meals and entertainment (M&E) expenses

In most cases, only 50% of business M&E expenses are deductible. This includes gift certificates to restaurants or places of entertainment. This rule applies to everyone—sole proprietors, corporations and partnerships.

There are a few exceptions to this 50% rule. It doesn’t apply in certain cases, such as the cost of providing meals and recreation for all the employees working at a particular place of business. However, this exception only
applies to up to six special events a year. M&E expenses incurred for an event intended primarily to benefit a registered charity also escape the 50% limit. However, the cost of executive dining rooms and similar facilities is subject to the 50% limit. There are also exceptions from the 50% rule for meals provided for employment at a special work site or to employees lodged at a construction work camp. Finally, if you invoice a client for reasonable meal expenses and you specifically identify such expenses in the accounts submitted to your client, you’ll be entitled to a full deduction for the expenses while your client will be subject to the 50% restriction.

The ability to claim a GST/HST ITC for M&E expenses is subject to a similar restriction—generally, only 50% is creditable. As an alternative, you can claim all the GST/HST paid on such expenses as they are incurred and then make an annual adjustment to your remittance to add back half the amount claimed in the year.

**Rules for long-haul truck drivers**

If you’re a long-haul trucker, special rules apply. The deductible amount for food and beverage costs incurred is 80%. As a result, the amount of the GST/HST ITC that is disallowed is 20%.

For this purpose, you are a long-haul truck driver if you are either an employee whose principal duty of employment is to drive long-haul trucks for the purpose of transporting goods or a self-employed person whose principal business is to drive long-haul trucks for the purpose of transporting goods. In both cases, you must be away for at least 24 continuous hours and the destination for the goods must be at least 160 km away.

**Tax tip**

To simplify the calculation, it’s a good idea to make sure your accounting system keeps such costs segregated from other expenses.
12 Convention expenses
If you’re carrying on a business or practising a profession, you can deduct expenses for attending up to two conventions per year. These conventions must relate to your business and must be held within the territory in which the sponsoring organization conducts its affairs. You can also deduct 50% of the actual cost of meals and entertainment incurred at conventions (see topic 11). If you attend a convention at which meals and/or entertainment are provided, but their cost is not noted separately from other convention fees, $50 per day will be subject to the 50% rule.

Expenses must be reasonable, and you should be able to prove your attendance and support your expenses with vouchers.

Tax tip
When your spouse attends a convention with you, the associated cost is generally viewed as a personal non-deductible expense. But if there are good business reasons for your spouse to accompany you, these expenses may also be deductible.

13 Canada Pension Plan (CPP) contributions
If you earned income from a business as a sole proprietor or partner in 2014, you may be liable for contributions under the Canada Pension Plan (CPP). If you did not earn any employment income in the year, your contribution for 2014 is 9.9% of the difference between your net business income and a $3,500 standard exemption, subject to a maximum contribution of $4,851 (the maximum is reached at a net business income amount of $52,500).

If you also earned employment income, the amount of CPP premiums withheld from this income will be a factor in determining the amount you have to pay.

Contributions commence the month after you reach the age of 18 and can be made until age 70. You can collect CPP benefits beginning as early as age 60 and as late as age 70.
The age that you start to receive CPP benefits, will have an impact on the amount you’ll receive. Your pension amount is reduced for each month before age 65 when you start to receive it, and increased for each month after age 65. For example, for 2014, the early pension reduction is .56% per month, increasing to .58% and .6% in 2015 and 2016 respectively. This means that if you start receiving your CPP pension in 2016 (or any subsequent year) at age 60, your pension amount will be 36% less than it would have been had you started taking it at age 65. Conversely, the late pension increase is now 0.7% per month. This means that, if you start receiving your CPP retirement pension in 2014 at the age of 70 (60 months after age 65), your pension amount will be 42% more than it would have been had you started taking it at age 65. There is no financial benefit to deferring receipt of your pension to after age 70.

You no longer have to stop work or significantly reduce earnings to receive CPP retirement benefits. If you are under the age 65, you will be subject to CPP premiums on your employment or self-employment income even if you are already collecting CPP benefits. However, if you’re between the ages of 65 and 70, and you’re already collecting CPP benefits, you’ll be able to elect out of the requirement to pay premiums by completing Form CPT30 and providing a copy of the form to each of your employers and sending the original to the CRA.

Those who choose to work while receiving the benefit will participate in the CPP and increase their pension entitlement (in the form of a post-retirement benefit).

If you’re self-employed, you can claim a tax deduction for half the CPP contribution that relates to your self-employment income. The remaining half qualifies for a non-refundable tax credit (see topic 79). If you’re 65 or over and self-employed, already in receipt of CPP benefits, and want to opt out of the requirement to pay CPP, you must complete the “Election to stop contributing to the Canada Pension Plan,” which is included on Schedule 8 of your personal tax return.
Employer CPP remittances

Employers are required to match employee CPP contributions. For example, if an employee is required to remit $1,100 for CPP, the employer has to remit the same amount.

In general, the amount an employer must contribute in a year for a given employee is not adjusted for any other amounts remitted for that person by other employers. However, in situations where a company has been restructured—such as in a wind-up or an amalgamation, employees with uninterrupted employment with the old and new employer will be deemed to have continuous employment with the new employer for purposes of the CPP rules. Similar rules apply to EI premiums.

14 Deduction of health/dental insurance premiums

If you’re self-employed, you can claim as a deduction from your business income premiums paid for coverage under a private health services plan, subject to certain limitations.

For the premiums to be deductible, you must be actively engaged in a business as a sole proprietor or partner. Also, self-employment must be either your primary source of income in the current year or your income from other sources must not exceed $10,000.

In addition, equivalent coverage must be extended to all permanent full-time arm’s-length employees. When a deduction is claimed, no amount paid for coverage will be eligible for the medical expense tax credit (see topic 83).

If you have no other full-time employees, the deduction is restricted to an annual maximum of $1,500 for each of you, your spouse or common-law partner and other family members 18 years of age or older, and to $750 for other members of your household.

15 Self-employed wage-loss replacement plans

If you’re self-employed, you may also pay premiums under a disability insurance policy that will provide you with benefits if you lose your income-earning capacity. The premium on this type of policy is considered a personal
expense and is not deductible from income. However, any benefits you may receive under this type of policy will also not be subject to tax.

16 **Deduction of life insurance premiums**
If you’re required to purchase life insurance as part of a package when borrowing money for business purposes, you can deduct the cost of the premiums, provided certain criteria are met. To claim a deduction, the policy must be assigned to the lender as security for the loan, and the lender must require this assignment. In addition, the lender’s principal business must be the lending of money, and the interest payable on the loan must be deductible for income tax purposes (or would be deductible, except in the case of special overriding rules).

The amount that can be claimed is restricted to the premium paid or the net cost of pure insurance, whichever is less.

17 **Deduction of fines and penalties**
You cannot claim a deduction for any fine or penalty imposed by a government agency, regulatory body, court or other tribunal or by any other person having the statutory authority to levy fines and penalties. For example, CRA interest paid for late payments or insufficient instalments is not deductible for tax purposes.

18 **Valuation of inventory**
Two methods can generally be used to establish the value of business inventory for tax purposes. All items may be valued at fair market value (FMV—as at the end of the particular year), or each item may be valued at whichever is lower—its cost or its fair market value.

There are special rules for property that is held as an “adventure or concern in the nature of trade.” Such property must be valued at the cost at which the taxpayer acquired it, although certain additions to this cost are permitted. This means that a loss on such a property cannot be recognized until the property is disposed of. A common example of this type of a situation is where land is held on the speculation that it can be sold at a profit without further development.
Farmers are subject to special rules regarding the valuation of inventory (see topic 41).

19 Operating losses and prior years’ taxes

If you carried on a business as a sole proprietor or partner in 2014 and incurred an operating loss, you can apply the loss against your other sources of income, such as investment income, capital gains and employment income. Losses on certain farming businesses may be restricted for the year (see topic 41).

Any business loss realized in a year must be deducted in full against your other sources of income. As a result, you may find you are unable to claim some or all of your non-refundable tax credits, such as personal amounts and medical expenses. You should check with your tax adviser to assess whether other family members can obtain a benefit from these lost credits.

If the operating loss exceeds your other sources of income, the excess may be carried back three years. To carry back the loss, you must file Form T1A with your return for the year in which the loss arises. If you’re unable to carry back the loss or choose not to, it can be carried forward for up to 20 years (10 years for losses that arose in taxation years ending after March 22, 2004, and before 2006, and seven years for losses that arose in taxation years ending before March 23, 2004). You’re free to choose the year to which you apply the loss. For example, if you expect your marginal rate of tax to increase in the future, you may decide to carry the loss forward rather than back to a prior year.

**Tax tip**

When carrying a loss back to a prior year, you have the option of using only a portion of your loss. For example, you might want to claim only part of the loss against income that was taxed at a higher marginal rate and apply the remaining portion of the loss to another year.
20  Apprenticeship job creation tax credit
If you hire apprentices, you may be able to claim a non-refundable tax credit equal to 10% of the eligible salaries and wages paid to eligible apprentices. Eligible wages are those paid during the first 24 months of the apprenticeship. The maximum credit is $2,000 per year for each eligible apprentice. A listing of the trades that qualify can be found at http://www.red-seal.ca/Site/trades/analist_e.htm.

You can claim the credit on your income tax return, using either Form T2038(IND), “Investment Tax Credit (Individuals),” or Form T2SCH31, “Investment Tax Credit—Corporations.”

Unused credits may be carried back three years and forward for up to 20 years to reduce federal taxes otherwise payable in those years.

21  Investment tax credit (ITC) for childcare spaces
If you create new childcare spaces for children of your employees and the surrounding community, you may be able to claim a non-refundable tax credit. This credit is equal to 25% of eligible expenditures incurred, to a maximum of $10,000 per space created. The credit is not available for any of the ongoing or operating expenses of the childcare facility, such as supplies, wages, salaries, utilities, etc.

Unused credits may be carried back three years and forward up to 20 years. All or part of the credit may be recaptured if, at any time within the five calendar years after the creation of the new childcare space, it ceases to be available or is sold or leased to another person or converted to another use.

22  To incorporate or not to incorporate
If you’re currently carrying on a business as a sole proprietor or in an unincorporated partnership, consider whether you should transfer your business to a corporation. It depends on your circumstances and the amount of income you earn. As a first step, you should talk it over with your tax adviser, who can “crunch the numbers” and examine the advantages and disadvantages of being incorporated.
Business income earned as a sole proprietor or partner is subject to income tax at your personal marginal rates. However, if you operate your business in a corporation, income that qualifies for the small business deduction (see topic 24) is taxed at a relatively low rate.

If you incorporate your business and can retain earnings in the corporation for growth, you’ll be able to defer tax to the extent the earnings are not distributed to you as a salary or dividend (see topic 28).

As an added benefit, with appropriate planning, shares of a small business corporation may be able to qualify for the enhanced capital gains deduction on their disposition (see topic 136). However, if you incorporate your business, you have to be careful that your business is not a “personal services business.” The problems with operating as a personal services business are discussed more fully in topic 24.

Transferring your business assets to the corporation on a tax-deferred basis
Most business assets can be transferred to a corporation without incurring immediate income taxes on the transfer. But there are some rules that apply, which means you must follow definite procedures and meet specific criteria. Your tax adviser can advise you on the merits of incorporation and how it might be accomplished on a tax-deferred basis. Provincial transfer taxes, such as property transfer tax and retail sales tax, also have to be addressed. In some cases, these taxes are unavoidable. There may also be GST/HST considerations on the transfer, as well as other non-tax issues.

23 Incorporating your professional practice
Many provinces allow professionals to incorporate their practice. Professional incorporation can confer many of the same tax and non-tax advantages enjoyed by other incorporated self-employed persons. However, professional liability will not be limited through incorporation and, in many provinces, the shareholders of professional corporations are required to be members of the same profession.
One key benefit of incorporation is the fact that corporations enjoy a considerably lower tax rate on income up to a certain amount (see Table 1 of the Corporate Taxation tables). However, this benefit is only realized if the income is kept in the company. Therefore, incorporating may not be in your best interest unless you’re able to retain some of the income within the corporation. It may also be advantageous to incorporate if you’re planning to sell all or part of your business. In those provinces that allow non-professionals to own shares in a professional corporation, income splitting is also a benefit.

If you wish to incorporate your practice, you should consult your provincial governing body for the conditions of incorporation specific to your profession. Your tax adviser can assist you in determining whether incorporation would be beneficial, given your specific situation.

24 The small business deduction
Canadian-controlled private corporations (CCPCs) are entitled to claim a small business deduction on active business income (ABI) earned in Canada.

Active business includes any business, as well as an adventure or concern in the nature of trade, but excludes: (i) a business that derives its income from property (including interest, dividends, royalties and rent) and has less than six full-time employees (i.e., a “specified investment business”); and (ii) a business that provides personal services through a corporation, has fewer than six full-time employees and where, were it not for the presence of the corporation, the individuals providing the services would be considered employees or officers of the entity using those services (a “personal services business”).

The small business deduction currently provides for an 11% federal tax rate on a CCPC’s ABI. However, only a limited amount of income qualifies for this deduction. The current federal limit is $500,000.

Although all provinces also have a small business rate, the rate and the amount of income that qualifies for this lower
rate varies from province to province (see Table 1 of the Corporate Taxation tables). Both the federal and provincial small business limit must be shared by an associated group of companies (see topic 26).

In addition, larger corporations will find that their ability to claim the small business deduction is restricted. The restriction applies to CCPCs whose taxable capital (generally equal to a company’s retained earnings, share capital and long-term debt) exceeds $10 million for the preceding year. If the taxable capital is between $10 million and $15 million, the amount eligible for the low rate is proportionately reduced. Any eligibility ceases if taxable capital surpasses $15 million. These limits are also determined on an associated group basis.

Other corporate tax rates
The general federal corporate tax rate is 28%. This rate applies to investment corporations, mortgage investment corporations, mutual fund corporations and non-resident-owned investment corporations. It also now applies to income earned in a “personal services business.”

For other corporations, income that is not subject to the small business deduction is subject to a federal corporate income tax rate of 15%.

Example
A CCPC earns income from an active business carried on in Canada and has taxable income of $650,000 for its fiscal period ended December 31, 2014. The income eligible for the small business deduction ($500,000) will be taxed at the lowest federal tax rate of 11%. The $150,000 balance will be taxed at a rate of 15%.

Personal services business
As noted above, active business income does not include income from a personal services business. This is essentially a business carried on by a corporation where the services performed by the corporation are provided by an individual who would otherwise be considered an employee of the
recipient of the services. The individual in this situation is often referred to as an “incorporated employee.”

If a corporation is carried on by a personal services business, there are two main tax consequences:

(1) The corporation is not able to claim the small business deduction, either federally or provincially. Also, such corporations do not qualify for the general corporate rate reduction, as such they are taxed at the highest federal rate of 28%.

(2) When calculating the income from the personal services business, eligible deductions are generally restricted to remuneration and benefits for the incorporated employee (plus a few limited other expenses that would otherwise be allowable as a deduction had the incorporated shareholder incurred the expense as an employee).^2

The 28% federal tax rate on such income creates a significant lack of integration (see topic 148) and acts as a disincentive to operating a personal services business corporation. In the event there are any risks that you may be considered an incorporated employee, you should consult your tax adviser to help you assess and manage those risks.

25 Capital tax
The federal capital tax—often referred to as the large corporations tax—was eliminated several years ago.

A separate federal capital tax still applies for financial institutions and insurance corporations. Taxable capital in excess of $1 billion is subject to the tax at a single tax rate of 1.25%. However, a financial institution can reduce its capital tax payable by the amount of income tax it pays.

None of the provinces assess a general capital tax, although all jurisdictions (except Alberta and the three Territories)

---

^2 i.e., expenses that would otherwise be allowed to a commissioned salesperson and legal expenses incurred to collect amounts owing for services rendered
continue to assess a capital tax on some or all types of financial institutions and, in some cases, resource and Crown corporations.

26 Associated-company rules
To prevent taxpayers from creating more than one corporation to enjoy the benefits of the small business deduction, there are rules that require the small business limit to be shared among associated companies. The concept of associated companies is a common one in the Income Tax Act and the definition, like that of many other tax rules, is quite complex. The simplest cases are those in which companies are under common control or one company controls the other.

The concept of control is quite far-reaching, yet it’s possible for related persons to invest in each other’s companies and still remain non-associated. For example, a limited amount of cross-ownership is acceptable (generally, less than 25%). Also, certain types of shares, known as shares of a specified class, are specifically excluded in determining control and cross-ownership.

Tax tip
Do you have an interest in one or more companies that are related to each other or to other companies? If so, have your tax adviser review the corporate structure to see whether you’re deemed to be associated and whether there are ways to prevent association.

27 Salaries and bonuses to shareholders
One of the basic principles of taxation is that expenses must be “reasonable” to be deductible. The CRA has had a long-standing administrative position on the reasonableness of salaries and bonuses paid to owner-managers. In general, the CRA won’t question the reasonableness of salaries or bonuses paid to principal shareholder-managers of a corporation if the company has a practice of distributing its profits to its shareholder-managers in the form of bonuses. However, this administrative position applies only to shareholders who are Canadian residents actively...
involved in the day-to-day operations of the company, thus contributing to the income-producing activities from which the remuneration is paid.

28 Salary vs. dividends
A corporation is a separate legal entity. To extract funds, you must either receive a dividend from the corporation or have it pay you a salary. In addition, if you have loaned money to your company, you can arrange to receive interest on the loan.

The payment of a salary is deductible to your corporation whereas dividends are paid from after-tax corporate profits. Careful analysis is needed to calculate the best mix of salary, interest and/or dividends for your specific circumstances. The introduction of the eligible dividend regime has further added to the factors that must be considered in making this decision. There are now two tax rates that can apply to dividends, depending on whether they’re eligible or regular dividends (see topic 143). The eligible dividend regime also means that it’s no longer a rule of thumb to bonus down to the small business limit.

Tax tip
Consider paying yourself a salary large enough to make maximum CPP and RRSP contributions.

29 Salary deferral arrangements
If an employee is entitled at the end of the year to receive an amount in a future year and one of the main purposes for this arrangement is to defer or postpone taxation, the amount will be taxed as a benefit to the employee in the current year. This is called a salary deferral arrangement.

Some plans are excluded from this classification, such as arrangements to fund certain employee leaves of absence. As well, the rules will not apply to bonuses that are paid within three years following the end of the year in which the amount became payable. However, if the bonus is not paid within 179 days from the end of the employer’s
taxation year, the employer will not be able to deduct the amount until the year it’s paid.

**Tax tip**

If your corporation’s year-end comes after July 6, it can deduct the bonus in the current year and the employee doesn’t have to report the amount as income until the next year. However, the corporation must declare the bonus as of its year-end but not pay it out until after December 31 and within 179 days of the year-end.

### 30 Directors’ fees

Directors’ fees are considered employment income and also constitute earned income for purposes of determining how much you can contribute to an RRSP (see topics 56 and 57).

**Tax tip**

If your spouse or common-law partner and/or other family members are directors of your corporation, consider paying them a director’s fee for services performed. Such services usually include attending directors’ meetings, directing the management and affairs of the business, approving financial statements, declaring dividends, etc.

On the downside, as a director of a corporation, you should be aware of your responsibility should the corporation fail to deduct and remit income taxes on payments to employees or on certain payments to non-residents. Directors can also be held liable for the corporation’s failure to collect and remit GST/HST.

Should the corporation fail to deduct and remit, as director, you can be held liable along with the corporation for paying the required amounts, including interest and penalties. However, you won’t be held liable if you can demonstrate that you exercised a reasonable degree of care to prevent the failure of withholding and remitting.
31 Loans from your corporation

In general, loans from your corporation not repaid within one year from the end of the year in which they are made must be reported as income for the year the loan was made. For example, if you borrow $10,000 from your company on June 1, 2014 and your company has a September 30 year-end, if the loan remains unpaid on September 30, 2015, you must report the $10,000 as income on your personal income tax return for the 2014 taxation year.

Some exceptions apply
Shareholders who are also employees can be exempted from the above rules. However, only certain types of loans qualify, such as a loan that enables you to acquire treasury stock in your company (or a related company) or finance an automobile to be used in performing your employment duties. There is another exception to these rules if lending money is part of your company’s ordinary business. To qualify for any of the exemptions, at the time the loan is taken out, bona fide arrangements must be made to repay it within a reasonable period. A loan to enable you or your spouse or common-law partner to purchase a home may also qualify—but the rules in this area are complex, and professional advice is recommended. If your company only employs family members, it will likely be difficult to qualify for the exception.

There is another rule to exempt loans made to an employee who owns less than 10% of any class of shares of the employer corporation and who does not deal at arm’s-length with the employer corporation.
Deemed interest benefit on “excepted” loans
If the loan qualifies for one of the above exceptions, this means only that the amount borrowed does not have to be included in your income. However, you will still have to report a deemed interest benefit. This amount is equal to the amount of the loan, multiplied by a prescribed interest rate (to the extent this amount exceeds any interest actually paid on the loan no later than 30 days after the end of the calendar year). These rules also apply to most loans to employees (see topic 33).

If you use the loan to acquire eligible investments or to earn income, as opposed to using the funds for personal purposes, you can claim the amount of the deemed interest benefit as a deductible interest expense.

The rules in this area are quite complex. Before borrowing funds from your company, you should thoroughly discuss this strategy with your tax adviser to make sure you’re aware of the rules.

32 Taxable benefits
If you provide your employees with benefits in addition to a regular salary, an amount must generally be included in their income as a taxable benefit. The most common taxable benefits are company cars (see topic 34), employee loans (see topic 33) and stock options (see topic 37).

In addition, the following less obvious benefits may also have to be included in your employees’ income.

Christmas parties and other special events
Did you provide your employees with a Christmas party this year? In general, no taxable benefit will have to be reported for social events that are made available to all employees, provided the cost per employee is $100 or less. Parties costing more than that will generally be considered to be beyond the “privilege” point and may result in taxable benefits.
Non-cash gifts and awards
The CRA’s administrative policy for non-cash gifts and awards is as follows:

- Non-cash gifts and non-cash awards to an arm’s-length employee, regardless of number, will not be taxable to the extent that the total aggregate value of all non-cash gifts and awards to that employee is less than $500 annually. The total value in excess of $500 annually will be taxable.
- In addition to the above, a separate non-cash long-service/anniversary award may also qualify for non-taxable status to the extent its total value is $500 or less. The value in excess of $500 will be taxable. To qualify, the anniversary award cannot be for less than five years of service, and it must be five years since the employee last received a long-service award.
- Items of an immaterial or nominal value, such as coffee, tea, T-shirts with employer logos, mugs, plaques, trophies, etc., will not be considered a taxable benefit to employees and will not be included in the above $500 threshold.
- Performance-related rewards (for example, for meeting a sales target) and cash and near-cash awards (such as gift certificates) will continue to fall outside the administrative policy and will be taxable to the employee.
- All gifts and awards to non-arm’s-length employees will be taxable.

Employer-paid professional membership fees
In general, the payment of a professional membership fee will not be considered a taxable benefit if the employer is the primary beneficiary of the payment. The employer will be considered the primary beneficiary whenever membership in the association is a requirement of employment. In a situation where membership is not a condition of employment, the question of the primary beneficiary must still be resolved. The employer is responsible for making this determination.
Group sickness or accident insurance plans
Generally, wage-loss replacement benefits payable on a periodic basis under a group sickness or accident insurance plan to which an employer has contributed are included in an employee’s income for tax purposes when those benefits are received. However, no amount is included in the employee’s income when the employer contributions are made. This is in contrast to the situation where employer contributions are made to a non-group plan. In this case, the contributions are taxable to the employee when they are made, but no amount has to be included in income when an amount is received under the plan. In both cases, the premiums paid are deductible by the employer.

For coverage after 2012, premiums paid by an employer to a group sickness or accident insurance plan where benefits are paid on a lump-sum basis will be a taxable benefit to the extent the contributions are not in respect of a wage loss replacement benefit payable on a periodic basis. This change is likely intended to catch plans that provide for the payment of a lump-sum amount in the event that the insured individual is diagnosed with a critical illness. As noted above, if the policy was considered a group sickness or accident insurance plan, then the employer-paid contributions would have been deductible, while the lump-sum benefit received by the employee would not be taxable.

Non-taxable benefits
Although many benefits received by virtue of employment are taxable, the following benefits are not taxable:

- reimbursement of certain moving expenses, including reasonable expenses related to the reinstallation of services and connection of appliances, as well as the modifications required to install moved property
- reimbursement of a loss from the disposal of an employee’s residence subsequent to a move at the employer’s request, up to a maximum of $15,000
- an expense allowance paid to a member of a municipal organization, to the extent that it does not exceed one-third of the remuneration and allowance received
- the employer’s contributions to a private health services plan
• the employer’s contributions to an RPP, a supplementary employment benefit plan or a DPSP
• discounts granted to all employees
• use of the employer’s recreational facilities, subject to certain conditions
• subsidized meals, provided the employee is required to pay a reasonable amount for the cost of food
• meals or meal allowances of up to $17, where an employee works two or more hours of overtime before or after regular hours, and the overtime is infrequent or occasional
• uniforms and special clothing required for work
• transportation to the work location where such transportation is provided by the employer
• meals, lodging and transportation when an employee is performing duties at a remote location or, in some circumstances, at a special work site
• certain transportation passes to employees of bus, rail or air companies
• counselling services relating to mental or physical health, re-employment or retirement of an employee
• allowances paid to a part-time employee for travel expenses, provided that the employee holds another job or carries on a business, the amount is reasonable and this part-time function is performed at a location not less than 80 km from his or her normal place of residence and principal place of employment
• travel expenses incurred by an employee’s spouse, when his or her presence is required by the employer and he or she has a role to play in achieving the business objectives of the trip
• transportation and parking expenses paid by the employer to a blind or motor-impaired employee
• membership dues to a sports club paid by the employer, provided it’s principally for the employer’s own advantage
• Internet services made available to employees, to the extent that they use it in carrying out their work or when such use mainly benefits the employer
• loyalty points collected on an employee’s personal credit card for business expenses (where the employee is reimbursed for such expenses), as long as the points
are not converted into cash and are not indicative of an alternative form of remuneration

- reimbursement of childcare expenses by an employer to an employee if the employee is required to work out of town at the request of the employer

33 Employee loans
If an employee is provided with a loan at little or no interest, he or she must include a taxable benefit in income. As noted above (see topic 31), this benefit is generally calculated as the interest on the loan at a prescribed rate, minus any interest actually paid on the loan within the year or 30 days after year-end.

Special rules apply when you provide your employees with a low-interest or interest-free loan to assist them in buying a home when moving to work at a new location. The taxable benefit arising from such a loan may be partially or entirely offset by a special deduction. To qualify, the new residence must be at least 40 km closer than the old residence to the new work location. In general, this special deduction will entirely offset the taxable benefit arising from low-interest or interest-free loans of $25,000 or less. This deduction applies for a five-year period commencing on the date the loan is made.

Special rules also apply if you provide any of your employees with a “home purchase loan.” It is not necessary for the employee to move to a new work location to qualify under this rule. The borrowed money has to be used to either purchase or refinance the debt on the employee’s home. The benefit from such loans is calculated by applying either the prescribed rate at the time the loan is granted or the prescribed rate for the particular quarter, whichever is lower. A new base rate on the loan will be established every five years.

34 Personal use of a company-owned automobile
If your company provides you or any of its employees with a vehicle for personal use, a taxable benefit has to be reported. This benefit is comprised of two parts: a “standby charge,” which reflects the personal access to the car; and
an operating benefit, which reflects the personal portion of operating expenses paid by your company.

In general, the standby charge is 2% of the original cost of the car, including PST and GST or HST, for each month in the year the car is made available for use. If the car is leased, the standby charge is generally two-thirds of the lease cost, net of insurance costs.

The standby charge can be reduced if the vehicle is used more than 50% of the time for employment purposes and annual personal driving doesn’t exceed 20,000 km. In this case, the standby charge (as calculated above) is multiplied by the following fraction:

Personal km ÷ 1,667 km per 30-day period (to an annual maximum of 20,004 km)

The standby charge included in your income as a taxable benefit is reduced by any reimbursement you make to your employer during the year for the use of the vehicle (other than in respect of operating expenses).

Maintaining accurate mileage records to support this claim should be part of your daily routine. In general, travel between your workplace and residence does not constitute employment use. If you stop at a customer’s location for employment purposes on your way to or from work, however, this travel may be considered employment related.

The Quebec government requires employees to keep a mileage logbook to support their personal and business use of a motor vehicle, and to provide a copy of the logbook to their employers within 10 days of the calendar year-end. Employees who do not provide a copy to their employers may be fined $200.
Employees who sell or lease automobiles may qualify for a reduced standby charge. In these cases, the standby charge is generally calculated at 1.5% instead of 2%. Note that in such cases, the calculation is based on the average cost of the vehicles acquired by the employer for sale or lease. Your tax adviser can help you with the details of the calculation.

There is also an exemption from the automobile benefit provisions for clearly marked police, fire and emergency medical service vehicles. In addition, extended-cab pickup trucks used at remote or semi-remote work sites are also excluded from these provisions. However, there may still be an operating benefit associated with such vehicles.

**Operating costs**

In addition to the standby charge, a separate and additional benefit must be reported when the employer pays any portion of the automobile’s operating costs.

The CRA has indicated that virtually all expenses associated with an automobile are operating costs. This includes the cost of gasoline, oil, tires, maintenance and repairs, net of insurance proceeds. Licence and insurance costs are also considered operating costs. However, parking charges are not considered operating costs.

The operating expense benefit is determined by applying a prescribed amount per km of travel for personal purposes. For 2014 this amount is $0.27 per km of personal use, less amounts reimbursed to the company in respect to the operating costs. This amount includes a GST/HST component. For taxpayers employed principally in selling or leasing automobiles, the prescribed rate is $0.24 per km.
If the automobile is used primarily (more than 50%) for employment purposes, an optional formula—calculated as 50% of the standby charge—can be used to determine the operating cost benefit. To use this method, the employee must inform the employer by the end of the calendar year that she or he would like to use the optional formula to determine the operating cost benefit.

**35 Automobile expenses**

Rather than providing your employees with a vehicle, it may be more tax-effective for the vehicle to be acquired by the employee personally. If it’s used for business purposes, the employee may be able to claim certain deductions. If this is the case, beware—the rules governing automobile deductions are complex and, as such, cannot be covered here in any great detail. They apply equally to corporations, sole proprietors and partnerships, as well as to employees who qualify to claim automobile expenses against their employment income.

Expenses must first be split into two categories: those that are subject to specific dollar limitations and those that are not. Depreciation, interest and leasing charges are subject to specific dollar restrictions. The maximum amount that can be depreciated for vehicles is $30,000 (plus PST and GST or HST on this amount). GST/HST is not included in the depreciation base if it’s refunded as an input tax credit.
The maximum monthly interest deduction is $300 and the maximum monthly lease amount that can be written off for tax purposes is $800 (plus PST and GST or HST on this amount). A separate restriction pro-rates deductible lease costs when the value of the vehicle exceeds the amount that is deductible for tax purposes.

For unincorporated businesses and employees, the total of the restricted and unrestricted expenses is then pro-rated between business and personal use, based on the number of km driven for each purpose. Expenses incurred entirely for business purposes, such as parking, can be claimed in full. Corporations do not have to pro-rate expenses between business and personal use. Expenses can be claimed in full, provided they are reasonable. However, the employee benefit rules may require a benefit to be included in the income of the employee.

**Tax tip**

Detailed records should be kept regarding a vehicle’s business and personal use. These records must be accurately maintained to support the percentage claimed for business use. Keep in mind that it is the CRA’s position that travel between a taxpayer’s regular workplace and home is considered personal.

**Self-employed persons and business use**

The CRA has a policy regarding the documentation that can be kept to support the business use of a vehicle that is used partly for business and partly for other purposes. This method involves establishing the business use of a vehicle in a base year, and then keeping detailed records for at least one continuous three-month period in each subsequent year. The results can then be extrapolated. This method is only available to self-employed persons. It cannot be used by employees who use their vehicle for employment purposes.
36 Tax-free travel allowances

If your employees use their own vehicles for employment purposes, you can help them avoid a lot of paperwork by providing them with a tax-free allowance to cover employment-related travel expenses.

The allowance qualifies for tax-free status if it’s reasonable—and only if it’s based on the actual number of km that the car is used for employment purposes. Provided the per-km reimbursement is reasonable, 100% of the amounts paid are deductible.

Allowances not based on the number of km driven, such as a flat allowance of $400 per month, must be included in the employee’s income. You can reimburse an employee for certain limited expenses (i.e., supplementary business insurance, parking costs incurred for business purposes, and toll and ferry charges) without affecting the tax-free status of the allowance, provided the per-km requirement is met.

If you provide your employees with a combination of flat-rate and per-km allowances (e.g., $200 per month plus $0.25 per km), both components must be included in the employee’s income.

Tax tip

If you currently pay any of your employees a combination of flat-rate and per-km allowance, consider changing the entire allowance to a per-km reimbursement. For 2014, the limit on tax-exempt allowances paid by employers to employees is $0.54 per km for the first 5,000 km driven and $0.48 for each additional km. For Yukon, Northwest Territories and Nunavut, the tax-exempt allowance is $0.04 higher.
As with almost everything else, travel allowances also have GST/HST implications to both the employer and the employee. The treatment varies, depending on whether the payment is taxable to the employee (see topic 49).

37 The taxation of stock options

As an incentive strategy, you may provide your employees with the right to acquire shares in your company at a fixed price for a limited period. Normally, the shares will be worth more than the purchase price at the time the employee exercises the option.

For example, you provide one of your key employees with the option to buy 1,000 shares in the company at $5 each. This is the estimated fair market value (FMV) per share at the time the option is granted. When the stock price increases to $10, your employee exercises his option to buy the shares for $5,000. Since their current value is $10,000, he has a profit of $5,000.

How is the benefit taxed?

The income tax consequences of exercising the option depend on whether the company granting the option is a Canadian-controlled private corporation (CCPC), the period of time the employee holds the shares before eventually selling them and whether the employee deals at arm’s-length with the corporation.

If the company is a CCPC, there won’t be any income tax consequences until the employee disposes of the shares, provided the employee is not related to the controlling shareholders of the company. In general, the
difference between the FMV of the shares at the time the option was exercised and the option price (i.e., $5 per share in our example) will be taxed as employment income in the year the shares are sold. The employee can claim a deduction from taxable income equal to half this amount, if certain conditions are met. Half of the difference between the ultimate sale price and the FMV of the shares at the date the option was exercised will be reported as a taxable capital gain or allowable capital loss.

**Example**

In 2013, your company, a CCPC, offered several of its senior employees the option to buy 1,000 shares in the company for $10 each. In 2014, it's estimated that the value of the stock has doubled. Several of the employees decide to exercise their options. By 2016, the value of the stock has doubled again to $40 per share, and some of the employees decide to sell their shares. Since the company was a CCPC at the time the option was granted, there's no taxable benefit until the shares are sold in 2016. It's assumed that the conditions for the 50% deduction are satisfied. The benefit is calculated as follows:

<table>
<thead>
<tr>
<th>Employment income</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Employment income ($20 – $10) × (1,000 shares)</td>
<td>$10,000</td>
</tr>
<tr>
<td>Income deduction (50%)</td>
<td>($5,000)</td>
</tr>
<tr>
<td>Income inclusion</td>
<td>$5,000</td>
</tr>
<tr>
<td>Proceeds of disposition ($40 × 1,000 shares)</td>
<td>$40,000</td>
</tr>
<tr>
<td>Cost base ($20 × 1,000 shares)</td>
<td>($20,000)</td>
</tr>
<tr>
<td>Capital gain</td>
<td>$20,000</td>
</tr>
<tr>
<td><strong>Taxable capital gain</strong></td>
<td>50%</td>
</tr>
<tr>
<td><strong>Taxable capital gain</strong></td>
<td>$10,000</td>
</tr>
</tbody>
</table>
What if the stock declines in value?
In the above numerical example, the value of the stock increased between the time the stock was acquired and the time it was sold. But what would happen if the share value declined to $10 at the time of sale in 2016? In this case, the employee would report a net income inclusion of $5,000 and a $10,000 capital loss ($5,000 allowable capital loss). Unfortunately, while the income inclusion is afforded the same tax treatment as a capital gain, it isn’t actually a capital gain. It’s taxed as employment income. As a result, the capital loss realized in 2016 cannot be used to offset the income inclusion resulting from the taxable benefit.

Anyone in difficult financial circumstances as a result of these rules should contact their local CRA Tax Services office to determine whether special payment arrangements can be made.

Public company stock options
The rules are different where the company granting the option is a public company. The general rule is that the employee has to report a taxable employment benefit in the year the option is exercised. This benefit is equal to the amount by which the FMV of the shares (at the time the option is exercised) exceeds the option price paid for the shares. When certain conditions are met, a deduction equal to half the taxable benefit is allowed.

For options exercised prior to 4:00 p.m. EST on March 4, 2010, eligible employees of public companies could elect to defer taxation on the resulting taxable employment benefit (subject to an annual vesting limit of $100,000). However, public company options exercised after 4:00 p.m. EST on March 4, 2010 are no longer eligible for the deferral.

Some employees who took advantage of the tax deferral election have experienced financial difficulties as a result of a decline in the value of the optioned securities to the point that the value of the securities is less than the deferred tax liability on the underlying stock option benefit. A special election can be made so that the tax liability on the
deferred stock option benefit will not exceed the proceeds of disposition for the optioned securities (two-thirds of such proceeds for residents of Quebec). If you did not dispose of the securities before 2010 and you want to make the election, you must dispose of the securities at any time before 2015 and then file the election by the due date of your income tax return for the year of the disposition.

38 Qualified scientific research expenditures
Write-offs and tax credits above and beyond your usual business deductions are possible if you conduct scientific research that relates to your business. Scientific research and experimental development (SR&ED) consists of pure research, applied research and experimental development. Of these three activities, experimental development is often the most difficult to evaluate. Part of the problem is the difficulty in defining what constitutes development. It’s equally difficult to distinguish exactly when development ceases and production begins—and production doesn’t qualify as research and development. Your accountant can assess if your SR&ED qualifies and tell you what you may have to do to ensure that your SR&ED activities are recognized by the CRA.

What can you deduct?
For purposes of determining the amount that qualifies as a SR&ED expenditure, all qualifying research expenditures of a current nature may be deducted in full the year they are incurred. However, a current-year deduction won’t be permitted for accrued amounts that are not paid within 180 days of the end of the taxation year. In addition, prior to 2014, new equipment purchased solely for qualified research in Canada qualified for a 100% SR&ED write-off in the year of acquisition; however, capital expenditures incurred in 2014 and subsequent years no longer qualify for this treatment.
**Tax tip**

You don’t have to claim the full amount of eligible SR&ED expenses in the year in which they were incurred. It may make better business sense to carry forward and deduct the amounts in a subsequent year. However, to deduct an amount for SR&ED, you must be carrying on the business to which the research relates in the year you make the claim. Unlike non-capital losses, undeducted SR&ED expenses can be carried forward indefinitely.

**Claiming SR&ED**

To claim special treatment for scientific research expenditures, you must complete Form T661. This requires you to provide a breakdown of the expenditures made, as well as details of the types of projects undertaken, such as the scientific or technological aspects they contained, the advancements they made and the uncertainties they pursued. It’s vital that descriptions of projects are complete. Failure to describe the projects properly could result in a rejection of the claim or, at best, a significant delay in processing.

For claims filed on or after January 1, 2014, the SR&ED claim form now requires more detailed information about SR&ED program tax preparers and billing arrangements. Form T661 has been revised to include a new Part 9 – Claim Preparer Information. As of January 1, 2014, Part 9 of the Form T661 must be fully completed. If any of the prescribed claim preparer information is missing, incomplete or inaccurate, a penalty of $1,000 may be assessed. For claim preparers who have concerns about the confidentiality of their information, the CRA has introduced an administrative measure to permit Part 9 of the Form T661 to be filed separately.

Outlays will not qualify for the beneficial tax treatment afforded research and development expenditures unless Form T661 is filed within 12 months of the filing due date for the taxation year. In other words, if a corporation with a December 31 year-end incurs SR&ED expenditures, Form T661 (for the 2014 taxation year) must be filed by June 30, 2016.
If your company plans to submit a claim, you should be aware that the CRA is not lenient with taxpayers who file claims late. The claim will be rejected if it is not complete within the 18-month deadline. For this reason, it’s important to file your claim early, ideally with the corporation’s income tax return for the year. If any information is missing, the claim will still be accepted, as long as it’s complete within the 18-month period. If you file a claim at or near the deadline, it will be essential to ensure that the form is complete at the time it’s filed, since it may not be possible for the CRA to advise you in time if anything is missing. The end result is that the tax credits will be lost.

**Investment tax credit (ITC)**

Prior to 2014, both current and capital expenditures on scientific research also qualified for a business investment tax credit (ITC). As of January 1, 2014, however, capital expenditures for SR&ED activities are no longer included in the base of eligible expenditures and no longer qualify for ITCs.

A Canadian-controlled private corporation (CCPC) is entitled to claim a 35% ITC on up to $3 million of qualifying expenditures if it meets certain conditions (generally based on the prior year taxable income and taxable capital—those of the corporation and all associated corporations). However, an individual carrying on SR&ED qualifies for only a 15% rate, which is why it’s generally recommended that SR&ED be carried on by a private corporation. Other corporations and partnerships also earn tax credits at the 15% rate. For taxation years ending before 2014, the rate used to calculate SR&ED tax credits for all entities other than CCPCs was 20%.

The amount of the ITC is first claimed as a deduction from federal taxes payable for the year. If there’s any amount remaining, the excess can generate a refund. However, this refundable system is available only to individuals and certain CCPCs. SR&ED ITCs earned at the 35% rate are eligible for a 100% refund if the ITC relates to current SR&ED expenditures. Capital expenditures no longer qualify for ITC treatment. ITCs are included in income in
the year following the year the credit is claimed. Other corporations and partnerships earn tax credits at a 15% rate, which must be applied to reduce taxes payable and are not refundable. Alternatively, if it’s to your advantage, you can carry unused credits back for up to three years or forward for up to 20 years (10 years for credits earned prior to 2006).

Proxy amount
Two methods are available to calculate qualifying SR&ED expenditures for overhead costs. The traditional method requires that you identify each of your overhead expenditures throughout the tax year. The proxy method alleviates the burden of identifying actual SR&ED overhead costs by allowing a proxy amount for overhead expenditures, which is calculated based on a percentage of the total of the eligible portion of SR&ED salaries and wages. The proxy method is simple to use because you don’t have to track your SR&ED overhead during the tax year. It’s also simple to file because you don’t have to itemize all of your expenditures. Due to this simplicity, it’s the most popular method used.

The proxy amount percentage is currently set at 55% of eligible expenditures (60% for 2013). The proxy rate that applies for taxation years that include days in 2013 and 2014 is pro-rated based on the number of days in the taxation year that are in each of those calendar years.

Even though the proxy method has been the most popular method for filing SR&ED claims, it’s worth the time to evaluate which method is best suited for your particular situation. For example, the traditional method may result in higher ITCs where salaries and wages are low but overhead costs are high.

SR&ED contract payments
In some cases, a taxpayer may contract to have SR&ED performed by another party. The entitlement to claim SR&ED tax credits for contract payments made to a non-arm’s-length person is restricted to the amount of the qualified SR&ED expenditures incurred by that person in fulfillment of the contract. This rule ensures that ITCs are
not earned on the profit element of non-arm’s-length SR&ED contracts.

Where contract amounts are paid to an arm’s length party, 80% of the amount paid qualifies for SR&ED tax treatment.

Effective January 1, 2014, amounts paid for capital expenditures incurred in fulfillment of the contract will reduce the amount of the contract payment before the 80% rate is applied.

**Filing due date**

To claim an ITC, a completed form giving details of the qualifying cost or expense must be filed within 12 months of the due date of the return for the taxation year in which the ITC arises. This filing deadline is the same as the filing deadline for SR&ED expenditures. The details are reported on Schedule 31 (for corporations) and Form T2038 (for individuals). To have proof of timely delivery, it’s recommended that the claim be sent by registered mail to the appropriate Tax Services centre.

Some of the provinces also offer ITCs and other tax incentives for SR&ED. The qualifying activities must be carried out in the province that grants these tax benefits.

The rules involved in claiming SR&ED expenditures and related ITCs are extremely complex. Consult your tax adviser to determine if you qualify and ensure that you get the maximum benefit from these tax incentives.

### 39 Shareholder agreements

If your corporation has more than one shareholder, a shareholders’ agreement should be drawn up to establish the ongoing rights and responsibilities of the shareholders in the ownership and administration of the company.

One of the more important aspects of the shareholders’ agreement is that it should specify what should happen in the event of the death or disability of one of the shareholders. Not only will this provide for a smooth transition of the business, but such agreements also generally establish a
purchaser for the shares of the deceased, a formula for determining the purchase price and a method for funding the purchase. By arranging proper tax planning, the buyout can be orchestrated to minimize a drain on cash flow for the company and survivors. A sound arrangement can also minimize or defer the tax liability of the estate. Life insurance is often used to fund a buy-sell agreement or share repurchase on the death of a shareholder. It’s highly recommended that you speak with your tax adviser to develop a plan appropriate to your situation.

40 Reporting system for contractors
If you’re in the construction business and make payments to subcontractors, you have to report certain payments to the CRA. For this purpose, construction is defined as erecting, installing, excavating, altering, modifying, repairing, improving, demolishing, dismantling or removing any structure or part thereof.

What payments must be reported?
You must report payments to subcontractors for construction services if the amount paid for services is $500 or more. Payments for goods are not to be included in determining if a payment satisfies this test. The payments can be reported on a calendar-year or a fiscal-year basis.

What information must be reported?
You must report the name of the subcontractor, the business address, the amount paid for the reporting period and the subcontractor’s business number (BN) or social insurance number (SIN) if no BN is available.

The information can be reported either on a “Statement of Contract Payments” (Form T5018) or on a line-by-line basis in a column format with the appropriate summary information.

In general, the due date for filing the required information is six months from the end of the reporting period.

Although there is no requirement to provide any information slips to the subcontractors, it’s reasonable to assume they
will want to know what information is being reported to the CRA.

41 Farming businesses
While the term “farming business” is not defined, the tax legislation does state that “farming” includes tilling the soil, raising or exhibiting livestock, maintaining horses for racing, raising poultry, fur farming, dairy farming, fruit growing and the keeping of bees, but it does not include an office or employment under a person engaged in the business of farming.

Case law has established that farming can also include other activities, such as forestry operations or the operation of a game reserve, as well as an artificial incubation business, which includes the purchasing and incubating of eggs, followed by the sale of chicks a few days after they have been hatched. Under certain specific circumstances, farming can include fish breeding, market gardening, the operation of nurseries and greenhouses, and aquaculture and hydroponics.

In addition, to benefit from the specific farming rules, your farming operations have to be of a business nature. The CRA has established the following criteria for determining whether a farming operation is a business:

- **The extent of the activity in relation to businesses of a similar nature and size in the same locality** — The best criterion is the area used for farming. If your farm property is much too small to generate a reasonable expectation of profit, it can be assumed that it’s for your personal use or pleasure.

- **The time devoted to farming compared to the time devoted to a job or other means of earning income** — If you devote the major portion of your time to the farm during harvesting season, you’re likely carrying on a farm business.

- **The financial commitments for future expansion in light of your resources** — This criterion is based on the capital you have invested in the operation over a number of years and the acquisition of buildings, machinery, equipment and inventories.
• Your entitlement to some sort of provincial farm assistance.

A farm business that only generates a small amount of gross revenue over a number of years might be indicative of a hobby rather than a business. However, it has to be remembered that this could be the situation during the initial years of operation or during certain periods where there are special circumstances such as prolonged droughts, frost or floods.

A number of related activities can also be considered a farming business: raising and maintaining racehorses to the extent you can demonstrate it’s not a hobby; a woodlot operation carried on jointly with a farming business if you elect to report the income on a cash basis; payments you receive as consideration for the right to use your marketing quotas; the reforestation of land with the intention of letting the trees grow until they have matured, i.e., from 40 to 60 years or longer; the planting and harvesting of Christmas trees (however, if tree sales have not been reported by the sixth year after the trees have been planted—or later, depending on local growing conditions—your operations may be considered forestry).

Methods of reporting income

If you carry on a farming business, you can calculate your farming income using either the cash or the accrual method.

The accrual method means that revenues should be recorded in the year they are earned, regardless of when the cash is received. Similarly, expenses are deducted in the year they are incurred, not when they are actually paid. Inventories at the end of the fiscal year also have to be taken into account.

Under the cash method, you do not account for amounts receivable or payable in computing income. For tax purposes, expenses are recorded when they’re paid and revenues when they’re received. Inventories are not included in determining income, with the exception of the mandatory and optional inventory adjustment.
You can switch from the accrual method to the cash method simply by filing an income tax return using the cash method. However, if you file a tax return using the cash method, you must continue to do so in subsequent years unless permission is obtained from the minister to do otherwise.

There are specific rules for calculating the inventories of a farm business that effectively prevent you from using inventories to create a loss.

Farming losses
There are two types of farming losses: farm losses and restricted farm losses. Where farming is your principal source of income (i.e., more than 50% of all income), you can claim your farm loss realized for the year. However, you’ll have a restricted farm loss if your total income is not principally from farming. In such a case, only a portion of the loss is deductible against your other sources of income. Any excess can only be deducted against farming income.

If farming is just a hobby, you cannot deduct any loss.

Restricted farm losses
A long-standing Supreme Court decision, Moldowan v. The Queen, held that farming that results in a loss could satisfy the chief source of income test (such that the restricted farm loss rules would not apply) if farming was the taxpayer’s chief source of income in combination with a non-farming source of income that was a subordinate source or a side-line employment or business. As a result of this test, if farming was not your principal business, you were restricted in your ability to deduct farm losses from your non-farm income.

A 2012 Supreme Court decision, The Queen v. Craig, overruled this decision by holding that a taxpayer could satisfy the chief source of income test even though his primary source of income was from a non-farming source (such as the practice of law). This case established that a full deduction could be claimed for farming losses if you placed significant emphasis on both farming and a non-
farming source of income, even if farming was subordinate to your other source of income.

The government has introduced rules to override this decision. For taxation years ending after March 20, 2013, your other sources of income must be subordinate to farming in order for farming losses to be deductible in full against your income from those other sources.

Where the restricted farm loss rules apply, the loss otherwise determined for your farming business is limited to a maximum of $17,500 ($2,500 plus 50% of the next $30,000). This loss can then be applied against all other sources of income. To the extent losses otherwise determined exceed the maximum amount, the excess is considered a restricted farm loss, which is deductible only against farming income. Restricted farming losses can be carried back a maximum of three years and carried forward a maximum of 20 years. Losses incurred prior to 2006 were limited to a 10-year carry-forward period.

Example

John incurs a $24,000 loss from his horse-raising business in 2014. Raising horses is not his main source of income. The loss he can deduct against his other sources of income is equal to $13,250; i.e., $2,500 + (50% × ($24,000 – $2,500)). The balance of $10,750 can only be deducted against farming income earned by John in future years.

Capital gains deduction for qualified farm property

Subject to certain conditions, if you sell or transfer a qualified farm property, you can take advantage of a capital gains deduction with respect to the capital gain on the sale or transfer. This deduction is discussed in more detail in topic 137.

---

For taxation years that end after March 20, 2013. A different calculation applies to taxation years ending before this time.
**Intergenerational transfers**

There are rules to permit a deferral of all or part of the income tax arising on the transfer of a farm property to a child, grandchild or great-grandchild. If you transfer or sell farm property to such a person, you can elect proceeds of disposition for the property at any amount between the tax cost and the fair market value. However, if you simply give the farm property to a child, grandchild or great-grandchild, or if you sell it for less than its tax cost, the proceeds of disposition will equal the property’s tax cost.

Similar rules govern the transfer of farm property on death.

There is also an intergenerational tax-deferred rollover for woodlot operations provided you or a family member is actively involved in the management of the woodlot to the extent required by a prescribed forest-management plan.

For transfers that occur in 2014 and later taxation years, eligibility for the intergenerational rollover is extended to situations where you are involved in a combination of farming and fishing (see Topic 138).

### 42 Transfer pricing

A transfer price is the amount charged between related parties involved in international transactions—for example, where a Canadian resident buys goods and services from or sells products to a related non-resident corporation. The government’s concern centres on ensuring that the price charged is equal to the amount that would be agreed upon by parties dealing at arm’s-length. If it’s not, taxable profits may be shifted from one jurisdiction to another.

The Canadian rules on transfer pricing are similar to those that have been put in place in other industrialized countries, such as the United States, the United Kingdom and Australia. The rules require Canadian taxpayers to adopt the arm’s-length principle in setting transfer prices for transactions with related non-resident persons and to document the basis for their transfer prices.
The arm’s-length principle has always been required in transactions with related persons, but there are now specific documentation requirements. These standards stipulate that the documentation for a particular tax year must be completed by the due date for filing that year’s tax return. Failure to complete the required documentation can result in a penalty of 10% of the transfer pricing adjustment, even where no additional tax arises as a result of that adjustment.

This area can be quite complex, as transfer prices must be developed that are acceptable to the tax authorities of both countries: the home country of the non-resident entity and Canada.

**Tax tip**

If you have transactions with related non-resident persons, have your tax adviser review your transfer pricing policies, as well as your related documentation, to determine whether they comply with the transfer pricing legislation.

**43 Withholding tax on interest payments to non-residents**

The tax rules provide that there is generally no Canadian withholding tax on interest paid to all arm’s-length non-residents (regardless of their country of residence). There is also no withholding tax on cross-border (Canada-US) interest payments between related (non-arm’s-length) parties.

**44 Payments to non-residents for services rendered in Canada**

Anyone making payments to non-residents for services rendered in Canada (other than in the course of employment) must withhold and remit tax at a rate of 15%. However, the service provider can reduce or eliminate the withholding tax if they have obtained a treaty-based or income-and-expense waiver from the CRA. Failure to deduct and remit this tax to the CRA can make you liable for the outstanding amount, plus interest and penalty.
The 15% withholding tax applies to a fee, commission or other amount paid to a non-resident individual, partnership or corporation with respect to services rendered in Canada other than in the course of regular and continuous employment.

Non-residents who are employed in Canada are subject to withholding tax deductions in the same manner as Canadian residents (i.e., using graduated tax rates) unless the employee has obtained a treaty-based exemption. To obtain this exemption, the employee must make a request in writing and send it to the tax services office for the area where the services will be provided.

**Tax tip**

If you make payments to non-residents for services rendered in Canada and fail to comply with the withholding requirements, you may be liable for significant penalties and interest in addition to the 15% withholding tax. Amounts should be withheld and remitted on any payments to a non-resident unless a waiver has been obtained.

**45 The goods on the GST/HST**

The current rate of GST in the non-harmonized provinces is 5%. The provinces of Ontario, Newfoundland and Labrador, Nova Scotia, Prince Edward Island and New Brunswick have harmonized their provincial sales taxes with the GST resulting in a single sales tax being levied on goods and services supplied in those provinces. Quebec has also harmonized its provincial sales tax system with the federal GST. However, Quebec Sales Tax (QST) still requires separate registration and collection. Under the HST, the federal portion of the tax is 5%, but the provincial component of the tax varies by province (see Table 4 – Sales Tax).

---

4 British Columbia, Saskatchewan and Manitoba. Alberta, Yukon, North West Territories and Nunavut don’t assess a provincial/territorial sales tax so the sales tax rate is 5% in those jurisdictions as well.
The HST operates in the same manner and is generally applicable to the same base of goods and services as the GST. A business registered for the GST is automatically registered for the HST and both are filed in the same return.

Supplies of goods or services are taxed in three ways. Most goods and services are rated as taxable supplies and are taxed at 5% outside the HST-participating provinces and at the applicable HST rate in the harmonized provinces (refer to Table 4). With certain exceptions, all tax collected is to be remitted. Any GST/HST-registered business that makes only taxable supplies can recover as an input tax credit (ITC) all the GST/HST it pays on supplies it purchases for use in its commercial activities. Tax is not collected on zero-rated supplies, but full ITCs are claimed for the GST/HST paid on related inputs. Zero-rated supplies include most basic groceries, agricultural and fishing products, prescription drugs, medical devices and most goods and services that are exported. ITCs can offset the amount of tax collected that a business is otherwise required to remit on its return.

Exempt supplies are not subject to GST/HST, but a business making them is not entitled to claim an ITC for the GST/HST on related costs. In effect, a business making exempt supplies bears the cost of the GST/HST and must factor it into the price of the goods and services sold. Long-term residential rents, health care services and financial services are some of the most common types of exempt supplies.

46 GST/HST registration, collection and remittance
Businesses that have $30,000 or less in annual worldwide taxable sales are not required to register and collect tax. However, to determine if your business meets this threshold, the worldwide revenues of associated entities are included in measuring annual taxable sales. Associated businesses can include related parties, such as shareholders, corporations, partnerships, trusts or individuals. If their combined taxable revenues exceed the $30,000 threshold, all of the businesses making any taxable supplies must be registered.
A business that is not required to register because it has less than $30,000 in annual taxable sales is called a small supplier. Such businesses can volunteer to register and collect tax as this enables them to claim ITCs for any GST/HST they pay on supplies purchased for use in their commercial activities (see topic 47). This is generally advisable if the recipient of the supply is also registered for the tax.

Separate thresholds are used to determine whether charities and public sector bodies are required to register.

New businesses
Starting a new business? In most cases, it’s generally a good idea to register for GST/HST as soon as you’re allowed. Provided your business makes taxable or zero-rated supplies, early registration ensures that GST/HST paid on costs incurred is recoverable since tax paid prior to registration can generally be recovered in limited circumstances and only on the purchase of inventory, capital property and prepaid services still on hand at the time of registration. Be sure to register early because, in many situations, registering late can result in not recovering any GST paid before registration.

When to report
Every business has a reporting period based on the revenue of the associated group. Most businesses are required to report quarterly. However, large businesses (over $6 million in annual taxable supplies for the associated group) must report monthly, while smaller businesses (under $1,500,000 in annual taxable supplies for the group) are generally put on an annual filing frequency. However, they can elect to file either on a quarterly or monthly basis. New GST/HST registrants with annual taxable supplies of under $1,500,000 for the group are automatically assigned an annual reporting period unless they choose to file more frequently.
Tax tip

You can elect to report more frequently than required. This is advisable if you’re generally in a net refund position, as businesses that sell a large percentage of zero-rated goods (e.g., businesses that export goods to customers outside Canada) often are.

Registrants with a “threshold amount” greater than $1.5 million must file their GST/HST returns electronically. In addition, any registrant that is not required to file electronically is now able to do so if it chooses. Although there are generally three filing options that can be used to electronically file GST/HST returns, certain registrants of Ontario and Prince Edward Island are required to use GST/HST NETFILE.

47 Input tax credits (ITCs)

If you’ve paid GST/HST on goods and services used in making taxable and zero-rated supplies, you can recover the GST/HST paid by claiming ITCs on your GST/HST return. To ensure that your claim will be allowed, you must have supporting documentation in your records in case your claim is ever challenged. Audit problems often arise through deficient documentation, even if the deficiency is minor.

If ITCs claimed in a reporting period exceed the tax collected, the excess is refunded to the business.5

In general terms, the following chart outlines the prescribed information that needs to be included as supporting documentation for the purposes of claiming ITCs.

---

5 Note that if a registrant owes an amount to another CRA account (e.g., payroll or corporate taxes), the CRA will keep the refund and apply it to the other outstanding balances.
<table>
<thead>
<tr>
<th>Information required</th>
<th>Total sale under $30</th>
<th>Total sale of $30 to $149.99</th>
<th>Total sale of $150 or more</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vendor’s business or trading name</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Invoice date</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Total amount paid or payable</td>
<td>✓</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>An indication of the total GST/HST</td>
<td></td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>An indication of which items are taxed at what rate</td>
<td></td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Vendor’s business number (GST/HST number)</td>
<td></td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Buyer’s name or trading name</td>
<td></td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Brief description of goods or services</td>
<td></td>
<td></td>
<td>✓</td>
</tr>
<tr>
<td>Terms of payment</td>
<td></td>
<td></td>
<td>✓</td>
</tr>
</tbody>
</table>

Listed financial institutions and certain registrants with annual taxable supplies (including those of associated businesses) greater than $6 million for each of the preceding two years have only two years to claim ITCs. The CRA, on the other hand, still has four years to audit a GST/HST return. Businesses with taxable supplies of 90% or more in either of the two immediately preceding fiscal years are excluded from the two-year restriction, as are charities. These, and all other registrants, maintain the ability to claim ITCs for a period of four years.

Large businesses in Ontario and Prince Edward Island⁶—those making taxable supplies of more than $10 million annually, as well as certain financial institutions—are temporarily restricted in their ability to claim the provincial

---

⁶ other than farming businesses
portion of certain ITCs. The supplies affected by this restriction are

- telecommunication services other than Internet access or toll-free numbers;
- energy except where purchased by farms or used to produce goods for sale;
- road vehicles weighing less than 3,000 kg and parts, certain services and fuel to power those vehicles; and
- food, beverages, and entertainment.

**Employee reimbursements**

In many cases, employers reimburse employees for expenses incurred on the employer’s behalf (for example, travel and accommodation costs, meals and entertainment, etc.). Employers have the option of claiming ITCs based on either the actual amount of GST/HST paid by the employee, or using a simplified method based on a fraction of the total amount reimbursed, according to the fractions in the chart below:

<table>
<thead>
<tr>
<th>Employee reimbursements</th>
<th>2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>GST provinces</td>
<td>4/104</td>
</tr>
<tr>
<td>Quebec – GST</td>
<td>4/104</td>
</tr>
<tr>
<td>Quebec – QST</td>
<td>9.975/109.975</td>
</tr>
<tr>
<td>British Columbia</td>
<td>4/104</td>
</tr>
<tr>
<td>Prince Edward Island</td>
<td>13/113</td>
</tr>
<tr>
<td>Nova Scotia</td>
<td>14/114</td>
</tr>
<tr>
<td>Ontario, New Brunswick, Newfoundland and Labrador</td>
<td>12/112</td>
</tr>
</tbody>
</table>

Where the ITC restrictions for large businesses apply (Ontario, Prince Edward Island and Quebec), the ITC is reduced.

---

7 Quebec also has restrictions but the Quebec legislation is somewhat different from the other provinces. Input tax refunds are restricted in Quebec
8 See footnote 7
Allocation of tax between taxable and exempt supplies

Businesses that make both taxable and exempt supplies must allocate between the two types of supplies in order to recover the GST paid on purchases. Any fair and reasonable method of allocation is acceptable. It is not necessary to use the same method from year to year, though the same method must be used consistently during the course of the year. Financial institutions may be required to follow specific allocation rules.

**Tax tip**

Businesses that allocate the tax paid on purchases between taxable and exempt supplies should review their method of allocation each year. Inherent changes in business activity may make it advantageous to change the allocation and obtain a higher recoverable percentage.

It’s important that you thoroughly document whatever method of allocation you choose. In the event of an audit, providing this documentation to the CRA will allow them to clearly understand how the allocation was determined.

### 48 GST/HST streamlined accounting thresholds

To simplify compliance, certain small businesses can elect to use the Quick Method of accounting to determine the amount of GST/HST to remit. Under this method, GST/HST-included sales are multiplied by a specified remittance rate to determine the amount of tax that needs to be remitted to the CRA. A small business can elect to use the Quick Method if its annual tax-included sales (including those of its associates) does not exceed $400,000. Input tax credits are not claimed by a person using the Quick Method, except for the GST/HST paid on capital purchases.

Many small businesses can also elect to use the Streamlined Input Tax Credit Method, which provides a simplified process for determining ITCs. This method can be used by a business with annual taxable sales (including the sales of associates) not exceeding $1,000,000 and annual taxable purchases (excluding zero-rated purchases) not exceeding $4,000,000. Under this method, businesses can calculate their ITCs based on a portion of their eligible total tax-
included business purchases. The tax factor used to calculate ITC entitlement is based on the tax rate applicable to the purchases. For instance, where all purchases were subject to only the 5% GST, the business would multiply the total of its tax-included business purchases by a tax factor of “5/105.”

An election must be filed to use the Quick Method; however, an election does not have to be filed to use the Streamlined Input Tax Credit Method.

49 GST/HST and automobiles
Passenger vehicles that cost more than a prescribed amount (currently $30,000, net of PST and GST or HST) are included in a separate depreciable class identified as Class 10.1. For such vehicles, the ITC is limited to the tax on $30,000, excluding PST and GST or HST. Upon the subsequent sale of a Class 10.1 vehicle, it may be possible to recover a portion of the unclaimed GST/HST.

Special rules apply to GST/HST-registered sole proprietors and partnerships where the vehicle is used less than 90% in a commercial activity. In such cases, GST/HST is recovered based on annual deductible capital cost allowance (CCA) claims. Upon the subsequent sale of the passenger vehicle, it may be possible to recapture a portion of the unclaimed GST/HST.

The GST/HST must also be considered if a vehicle is sold or traded in. The rules differ depending on the status of the vendor. Is the vendor registered for the GST/HST? Is the vendor a corporation, a sole proprietor or a partnership? Was the vehicle used exclusively in a commercial activity? Your tax adviser can help you avoid any pitfalls in this regard.

GST/HST also has to be considered if you provide your employees with vehicles for their personal use or pay for any of their vehicles’ operating expenses. If your company is a GST/HST registrant, the resulting taxable benefit is deemed to be a taxable supply and GST/HST must be remitted on the benefit amount. Your company must remit the tax on its GST/HST return that covers the last day of
February each year. The GST/HST with respect to vehicles provided to shareholders who are not employees must be reported on the GST/HST return that includes the last day of the taxation year.

How much do you owe?
The GST/HST to be remitted for automobile benefits is calculated by a formula that varies with the nature of the benefit and whether the employee or shareholder who is being taxed on the benefit works or lives in a participating province. The remittance for 2014 is calculated as follows:

<table>
<thead>
<tr>
<th>2014 standby charge and operating cost benefit</th>
<th>Standby charge</th>
<th>Operating cost benefit</th>
</tr>
</thead>
<tbody>
<tr>
<td>GST provinces(^9)</td>
<td>4/104</td>
<td>3%</td>
</tr>
<tr>
<td>Ontario</td>
<td>12/112 or 4/104</td>
<td>9%/6%</td>
</tr>
<tr>
<td>Quebec – GST</td>
<td>4/104</td>
<td>3%</td>
</tr>
<tr>
<td>Quebec – QST</td>
<td>9.975/109.975</td>
<td>6%</td>
</tr>
<tr>
<td>Prince Edward Island</td>
<td>13/113</td>
<td>10%</td>
</tr>
<tr>
<td>Nova Scotia</td>
<td>14/114</td>
<td>11%</td>
</tr>
<tr>
<td>New Brunswick and Newfoundland and Labrador</td>
<td>12/112</td>
<td>9%</td>
</tr>
</tbody>
</table>

**Example**

During 2014, an automobile is made available to an employee in a GST province. That person drives 15,000 personal km and only 5,000 business km in the year. The employer pays $500 of the operating costs and the employee pays the remainder. An operating cost benefit of $4,050 ($0.27 per personal km) must be reported and the employer must remit $121.50 of GST on the benefit ($4,050 × 3%). If the employee reimburses the employer $500 by no later than 45 days after the year-end, no amount has to be reported as an operating cost benefit and no amount has to be remitted for GST.

\(^9\) This includes British Columbia, Alberta, Saskatchewan, Manitoba and the Territories.
Tax planning guide 2014–2015

I – Businesses

**Tax tip**

If personal use of the automobile is high and the employee or shareholder incurs most but not all of the operating costs, the taxable operating cost benefit and related GST/HST remittance may be higher than the portion of actual operating costs paid by the employer. It’s not a bad idea to review employment arrangements from time to time to determine if any changes should be made.

**Employee or partner expenses rebate**

Certain employees and partners may be able to claim a GST/HST rebate for particular expenses that are deductible in calculating income for tax purposes (for example, deductible automobile expenses).

Although you have up to four years to make a claim, the rebate is generally claimed on an annual basis as part of your personal tax return on Form GST 370 (“Employee and Partner GST/HST Rebate Application”).

The rebate is calculated as a percentage of eligible expenses (according to the chart below). To claim the rebate, your employer must be registered for GST/HST and cannot be a listed financial institution, such as a bank, credit union, insurance company or an investment or insurance business.

<table>
<thead>
<tr>
<th>Employee or partner rebate</th>
<th>2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>GST provinces</td>
<td>5/105</td>
</tr>
<tr>
<td>Quebec – GST</td>
<td>5/105</td>
</tr>
<tr>
<td>Quebec – QST</td>
<td>9.975/109.975</td>
</tr>
<tr>
<td>British Columbia</td>
<td>4/104</td>
</tr>
<tr>
<td>Prince Edward Island</td>
<td>14/114</td>
</tr>
<tr>
<td>Nova Scotia</td>
<td>15/115</td>
</tr>
<tr>
<td>Ontario, New Brunswick, and Newfoundland and Labrador</td>
<td>13/113</td>
</tr>
</tbody>
</table>
If you receive a tax-free travel allowance that you include in income (for example, a per km allowance) and you claim offsetting expenses, you cannot claim the rebate. Your GST/HST-registered employer, however, may be entitled to claim a notional ITC for the amount paid (see below—“Travel and other allowances”). The rules are just the reverse if you receive a travel allowance that has to be included in income, for example, a flat allowance of $400 a month. In this case, you may be able to claim the rebate, but your employer cannot claim an ITC.

**Travel and other allowances**

In situations where the employee is not entitled to claim a rebate (for example, the employee has received a tax-free travel allowance that is not required to be included in income), the employer may be entitled to claim a notional ITC for the amount paid. In such cases, the employer will generally use the same fractions noted in the above chart (for employee and partner rebates), based on when the allowance is paid. Where the employer is entitled to claim the notional ITC, the employee cannot claim the rebate.

The tax fractions noted above for Ontario and Prince Edward Island do not consider the recapture of ITC restrictions for large businesses in those provinces (see topic 47). Where such restrictions apply, the ITC is reduced for the provincial component of the credit. For the province of Quebec, a 3.5% rate may be used where the large business ITC restrictions apply (and 9.975/109.975 otherwise).

If the supplies for which the allowance is paid are made in two or more participating provinces, the lowest tax rate for those participating provinces should be used.
Confused about the application of GST/HST to automobiles and allowances? Don’t be surprised—the rules in this area are extremely complex. It may be well worth a trip to your tax adviser to make sense of the GST/HST rules as they apply to your business.

50 GST/HST and real property sales
As a general rule, real property transactions are taxable, even when the vendor is a small supplier. In such cases, the vendor must collect and remit the tax (unless the purchaser is a GST/HST registrant—see discussion that follows). However, the sale of used residential property and certain sales of real property by an individual who is not engaged in a business are generally exempt from GST/HST. In the case of bare land, if the property has been subdivided into more than two parts, even an individual must charge GST/HST when the property is sold, unless it’s sold to certain related individuals.

Sales of real property to a registered purchaser
A vendor is generally not required to collect the tax where real property is sold to a GST/HST-registered purchaser. A business selling real property should ensure that the purchaser is registered before concluding that no tax will be collected on the sale. Where the purchaser is registered, the sale remains taxable; however, the purchaser is obligated to report the tax on a self-assessment basis. If the property is used primarily in making taxable supplies, an offsetting ITC can usually be claimed on the same GST/HST return that reports the liability. If the property will be used 90% or more in commercial activities, a full ITC is available (except for financial institutions), and no tax has to be remitted. However, if the property won’t be used primarily in making taxable supplies, the purchaser must remit the applicable GST/HST. Under these circumstances, a partial ITC may still be available.
Tax tip

When a non-registrant sells real property and the deal is subject to tax, the vendor can often recover GST/HST previously paid on the acquisition or improvement of the property that has not already been recovered. The eligible amount is claimed by filing a rebate form. If the vendor collects tax on the sale, the result is that the vendor sends the CRA the net amount of the tax collected minus the rebate amount. If the vendor doesn’t collect tax on the sale (because the purchaser is registered), the rebate will be paid to the vendor directly by the CRA. The rebate application must be filed within two years of the date of sale.

51  GST/HST and buying and selling a business

Where a business or a part of a business has been sold, a purchaser and vendor may be able to file a special election to avoid paying GST/HST on the purchase of the assets. This election is usually available if the purchaser is acquiring the ownership, possession or use of all the property needed to carry on the business or part of the business. However, this is often not an easy determination to make. The big difficulty is in determining whether the business assets being sold qualify for this election. Before signing the papers, you should consult your tax adviser to determine if you qualify to make this election.
Section 2 – Individuals

52 Filing a tax return
You’re required to file an income tax return for a taxation year if you

- have tax payable for that year (in excess of amounts withheld on your behalf);
- sold or disposed of capital property in the year, regardless of whether you had a gain or loss on the property;
- claimed a capital gains reserve on your 2013 return, even if the application of losses, exemptions or a new capital gain reserve results in no tax owing;
- have to repay Old Age Security or Employment Insurance benefits;
- elected, along with your spouse or common-law partner, to split pension income for 2014;
- received Working Income Tax Benefit advance payments in 2014 and you want to apply for WITB advance payments for 2015;
- want to apply for the child tax benefit (both you and your spouse or common-law partner must file a return);
- want to reapply for the Guaranteed Income Supplement;
- have self-employed earnings of $3,500 or more in the year and must make CPP contributions, even if your income is otherwise below taxable levels;
- have not fully repaid amounts you withdrew from your RRSP under the Home Buyers’ Plan or Lifelong Learning Plan (see topics 63 and 64);
- ceased to be a resident of Canada in the year and owned capital property at the time of emigration; or
- receive a request to file from the CRA.

Non-residents of Canada who receive certain types of income from Canada may also be required to file returns (see topic 122).

Even though you may not be required to file a return, you may still want to do so for the following reasons:

- If no tax is payable, but tax has been withheld, you must file a return to obtain a refund;
- You may be entitled to claim federal or provincial tax credits, for example, the GST /HST credit;
• You were a student in the tax year and you have excess tuition/education/textbook amounts to be carried forward (see topic 87); or
• You had “earned income” in the year for RRSP purposes (see topic 56).

**Tax tip**

Anyone, including minors, with earned income for RRSP purposes should consider filing an income tax return. Your RRSP contribution room, which may be used in subsequent years, will accumulate only if a tax return is filed.

53 **Your return is due**

Most individuals are required to file their income tax returns on or before April 30 of the following calendar year. Interest on outstanding amounts begins to accumulate after that deadline. If you’re owed a refund, it doesn’t make any sense to wait until that date—much less past that date. File as soon as you have all your documentation.

There is one major exception to the April 30 rule. If you or your spouse or common-law partner carry on a business as a sole proprietor or in a partnership (other than as a member of a limited partnership) during the year, you both have until June 15 of the following year to file your returns. However, any taxes owed by you and your spouse or common-law partner must be paid by the April 30 date to avoid interest charges.

**Tax tip**

Anticipating a refund on your 2014 tax return? Then you should still file your return as early as possible. Interest on refunds will only be paid starting from whichever of the following three dates is latest: May 31, 2015; the 31st day after you file your return; or the day after you overpaid your taxes.

54 **GST/HST credit**

The GST/HST credit is paid in quarterly instalments—in January, April, July and October. An individual’s GST/HST credit entitlement for the calendar quarter will be based on the individual’s family circumstances at the end of the previous calendar quarter.
Subject to income restrictions, you’re eligible to claim the credit. But you must, at the end of the year, be a resident of Canada and either 19 years of age or over, married or a parent. No credit can be claimed for a person who died during the year.

What’s it worth?
For payments from July 2014 to June 2015, the basic GST/HST credit for an individual is $268. For families, the credit is $268 for you and $268 for your spouse or common-law partner (or other parent of your child). An eligible child will be credited with $141. There’s also a GST/HST supplement credit of up to $141 for certain low-income single persons and single parents. If you live with your spouse or common-law partner (or other parent of your child), only one of you may claim the credit for the family unit, and it doesn’t matter which of you claims the credit.

However, the total credit you may claim is reduced by 5% of your combined adjusted net incomes for 2013 in excess of a specified threshold, which is currently $34,872 (this amount is adjusted annually for inflation). Therefore, a married couple with two eligible children qualify for the full credit of $818 if their combined family income is $34,872 or less. Their entitlement decreases to zero once family income exceeds $51,232.

Eligibility for the credit
GST/HST payments can be impacted due to changes in family circumstances during the year, such as the birth of a child. As a result,

- following the birth of a child, a family will receive an additional amount for that child with the next quarterly payment;
- the credit will be available to an individual in the quarter immediately following the individual’s 19th birthday;
- individuals who get married, or become separated or widowed, will have their credits adjusted in the quarter following their change in marital status; and
- new or returning residents to Canada will be eligible for
the credit in the quarter following their entry or return into Canada.

To claim any added benefits, you should inform the CRA of relevant changes in your status. Call 1-800-959-1953.

**Tax tip**

To receive the GST/HST credit, you should file an income tax return—even if you have no income to report. After you file your tax return, the CRA determines whether you qualify for the credit and, if so, will let you know how much you’ll receive.

55 Why buy an RRSP?

There are many good reasons for contributing to a Registered Retirement Savings Plan (RRSP). First, your contribution is tax deductible—and the higher your marginal tax rate, the greater your tax savings. Second, the income generated by the plan is taxed only upon withdrawal from the plan (usually when you’re retired and possibly in a lower tax bracket). That means you can build up quite significant earnings inside your plan on a pre-tax basis. Finally, all or a portion of your annual eligible contribution may be contributed to a plan set up for your spouse or common-law partner.

**Spousal plans**

Setting up a spousal RRSP is a good idea if you expect your spouse or common-law partner to be in a lower tax bracket than you on retirement. When funds are withdrawn from the spousal RRSP, they are taxed in your spouse’s or common-law partner’s hands at his or her lower tax rate (this arrangement is subject to special rules to prevent abuse). This reduces your family’s total tax bill. This strategy also means that benefits such as the pension credit can be made available to both of you, and you may reduce your exposure to the Old Age Security (OAS) clawback (see topic 72).

Regardless of the pension income-splitting rules (see topic 71), spousal plans still have a role to play. Since the pension income-splitting rules limit the ability to income split to
50% of the amount received, a spousal RRSP may still allow for greater income splitting since 100% of the payments from the spousal RRSP can be taxed in the hands of the spouse with the lower income. Spousal RRSPs can also be useful in situations where the funds put aside are not always intended for retirement—for example, where both parties want to access RRSP contributions to purchase a home (see topic 63) and one spouse has not had sufficient income to benefit from making his or her own RRSP contributions.

56 How much can you contribute?
Your maximum annual RRSP contribution is based on your earned income in the previous year. Earned income includes salaries, employee profit sharing income, business income, disability pensions (issued under the Canada and Quebec pension plans), taxable alimony or maintenance, and rental income. Starting in 2014, earned income also includes income contributed to an amateur athlete trust (for purposes of determining the RRSP contribution limit of the trust’s beneficiary). In addition, if an election is filed by the beneficiary before March 3, 2015, income contributed to the trust in 2011, 2012 and 2013 will also qualify as earned income. Your earned income is reduced by business losses, rental losses, union dues, employment expenses, and deductible alimony or maintenance paid. Retiring allowances, investment income, capital gains, pension income and business income earned as a limited partner are not classified as earned income.

If you are not a member of a registered pension plan (RPP) or a deferred profit sharing plan (DPSP), you’ll be able to contribute 18% of your 2013 earned income to an RRSP in 2014 to a maximum of $24,270. That contribution must be made within 60 days of the end of the calendar year which is March 1, 2015 for the 2014 taxation year. If you were not able to make the maximum contribution to your plan in any of the years from 1991 to 2013, you can also make up the difference in 2014 (see topic 59). Your 2014 earned income will determine your 2015 contribution limit.

10 Deadline will be extended to March 2 since March 1 falls on a Sunday.
Making the maximum RRSP contribution in 2014 will require earned income of at least $134,833 for 2013. Check the Notice of Assessment that the CRA sent to you after the assessment of your 2013 return. It will tell you how much you can contribute and should take into account any under contributions since 1991. It will also tell you if you have made any contributions that you have not yet deducted for income tax purposes.

If you have a self-directed RRSP, you can transfer other investments you own into your self-directed RRSP as part of your deductible contribution. Should their fair market value at the time of the transfer exceed your cost, the difference must be reported as a capital gain. However, if the cost exceeds their fair market value, you are not able to claim the capital loss. Therefore, it is not the best idea to sell or transfer losing investments to your RRSP.

It’s also possible to hold the mortgage on your home in your RRSP—it takes a bit of effort to set up and there are costs involved, but this arrangement can offer some advantages.

In certain situations, your RRSP can invest in shares of a Canadian private company if it carries on its business primarily in Canada. However, there are rules that will assess penalties where your RRSP holds a non-qualified or prohibited investment. One example of a prohibited investment is a share in a company in which you (and related parties) have an interest of 10% or more. The rules are extremely complicated, and you should consult with a knowledgeable tax adviser before using your RRSP to invest in private company shares.

When considering long-term investments, such as five-year guaranteed investment certificates (GICs), within your RRSP, keep in mind that you may have a problem if you need to withdraw the funds before the investment matures.
RPP and DPSP members

If you’re a member of an RPP or DPSP, your RRSP contribution limit will be reduced by an amount called the pension adjustment (PA). This adjustment represents the present value of the pension benefits you earned for the previous year in your RPP or DPSP. PA reporting is required as part of the T4 reporting process in February of each year.

There is another adjustment if your pension benefits are enhanced for post-1989 service. This particular adjustment—the past service pension adjustment (PSPA)—reduces your RRSP contribution limit for any given year.

One other adjustment—the pension adjustment reversal (PAR)—can increase your contribution room. You may receive a PAR if you leave your pension plan before retirement. This adjustment is intended to increase your RRSP contribution room where the PAs previously reported on your behalf exceed your termination benefit under the pension plan.

Example

Suppose you were laid off by your employer in 2014 and, based on your earned income for 2013, your 2014 RRSP contribution room was $14,500. If your former employer reports a PAR of $5,000 with respect to your participation in its pension plan, your revised 2014 RRSP deduction room will be increased to $19,500.

Based on the above, your maximum deduction for any one year will be calculated as follows: RRSP contribution room carried forward (see topic 59), plus 18% of your prior year’s earned income (to a stated maximum), plus any pension adjustment reversal (PAR), less your PA for the prior year, less any PSPA for the current year.

Age limits

Subject to age restrictions, you may contribute any amount up to your maximum to your RRSP, an RRSP set up for your spouse or common-law partner, or a combination of both. RRSP annuitants may retain their RRSP and continue
to make contributions to the plan until the end of the year they turn 71. However, if you have earned income and your spouse or common-law partner will be under 72 at the end of the year, you can still make a contribution to his or her plan, even if you’re 72 or older.

57 RRSP contribution limits
The maximum contribution limit is $24,270 for 2014 and is indexed for inflation for each subsequent year.

To make the most effective use of your RRSP, there are several things you can do:

• Depending on the type of investment, you can either contribute to your RRSP early in the year (for fixed income investments) or at regular intervals throughout the year (for most mutual funds) rather than at the end of the contribution year—that way, you can benefit from income sheltering and dollar cost averaging (for investments that fluctuate in value).

• If you make regular contributions to an RRSP, consider applying to have your income tax withholdings reduced on your paycheque—this will improve your monthly cash flow. To do this, simply submit Form T1213 to the CRA for authorization. Once authorized, your employer will be able to reduce the amount of taxes withheld from your pay.

• Pay your RRSP administration fee directly instead of from inside your RRSP—this helps maintain capital in your plan, allowing it to grow on a tax-deferred basis.

• You don’t need to deduct your contribution in the year it’s made. If you’re expecting to be in a higher tax bracket in the future, consider delaying your deduction until that time—you’ll receive a larger tax savings if the deduction is taken when you’re in a higher tax bracket.

• Consider filing tax returns for children or other low-income earners to create contribution room that can be used in the future.

58 RRSP overcontributions
You’re permitted to overcontribute a cumulative lifetime total of $2,000 to your RRSP without incurring a penalty
tax (this limit is increased to $8,000 for anyone who had an overcontribution prior to February 27, 1995). An overcontribution is not deductible from income in the current year, but the advantage lies in the fact that you can put additional cash into your RRSP where it can compound on a tax-deferred basis for as long as it remains in the plan. Overcontributions may be deducted in a subsequent year when your actual RRSP contribution is less than the maximum allowed. A penalty tax of 1% per month applies to the amount of any overcontribution in excess of $2,000 (or $8,000 where that limit applies). The CRA has recently become more stringent in assessing taxpayers who have overcontributed to their RRSPs. If you think you’re in an overcontribution position, you should contact your tax adviser to determine the steps you need to take. The calculation of the penalty tax and the filing of the forms to withdraw the excess amount is not part of the normal engagement to prepare your personal tax return.

**Tax tip**

Consider using your $2,000 overcontribution when you quit working. The earned income you have in your final year of employment will entitle you to an RRSP deduction in the following year.

**59 RRSP carry-forward rules**

Commencing with the 1991 tax year, you’ve been able to carry forward the unused portion of your RRSP contribution room to subsequent years.

If you expect a change in your income in the near future—a change that might see you bumped up into a higher tax bracket—it might make sense to consider delaying your RRSP contributions until then. However, you must also consider the loss of tax-sheltered investment growth by building up your RRSP later rather than earlier.
Tax tip

Where funds are limited and you're in a lower tax bracket, consider if a Tax-Free Savings Account (TFSA) contribution might make more sense (see topic 70).

60 Retiring allowances and RRSPs

Individuals who receive an amount from their former employers upon dismissal or retirement in 2014 may be eligible to contribute an extra amount to their RRSP or RPP.

The maximum amount that can be transferred to your RRSP or RPP is $2,000 multiplied by the number of years you worked for your employer before 1996. You can also add in $1,500 multiplied by the number of years you were employed prior to 1989 in which your employer did not make vested contributions to a registered plan on your behalf. The contribution, which is in addition to your regular contribution limit, must be made to your own retirement plan, not your spouse's.

Tax tip

If the portion of your retiring allowance that's eligible to be transferred to your RRSP is paid directly to your RRSP, your employer will not be obligated to withhold income tax.

61 RRSPs and loans

Interest on loans taken out to invest in an RRSP is not deductible. Therefore, your investments should be structured to take maximum advantage of the interest deductibility rules.

Tax tip

Consider cashing in an existing investment to contribute to your RRSP and then, if you wish, borrowing funds to acquire another investment that is held outside your registered plan. This way, you receive a deduction for your RRSP contribution, and the interest on the loan borrowed for investment purposes should also be tax deductible provided certain conditions are met (see topic 150).
62 Transfer of pension income
If you’re entitled to a lump-sum payment out of a registered pension plan (RPP) or a deferred profit sharing plan (DPSP), that amount may be contributed to another RPP, DPSP or RRSP. However, the lump-sum payment must be made directly from one plan to another, and then only if certain conditions are met.

If you want to transfer a lump-sum payment from a foreign plan to your RRSP you should get professional tax advice. For example, the tax implications of transferring amounts from a US individual retirement account (IRA) to a Canadian RRSP are complex. Your adviser can explore all the options and potential tax obligations of such transfers.

63 Using an RRSP to buy a home
You’re permitted to withdraw up to $25,000 from your RRSP for qualifying home purchases. Form T1036 needs to be filed to report the withdrawal. Under this plan, only first-time homebuyers are eligible to participate, unless the special rules for persons with disabilities (discussed below) apply. You’re considered to be a first-time buyer if, during the four calendar years prior to the year of withdrawal and up to 30 days before the withdrawal, neither you nor your spouse or common-law partner owned a home in which either of you resided. Loan repayments must take place over a period of 15 years, or less if desired, beginning in the second year following the year of withdrawal. If the required repayment is not made, an amount will have to be included as income in the year of the shortfall.
If you contribute an amount to your RRSP, you cannot make a withdrawal under the Home Buyers’ Plan (HBP) within 90 days of that contribution, or your ability to claim a deduction for the contribution may be restricted. As a general rule, you should make your RRSP contribution more than 90 days before the withdrawal. After a waiting period of 90 days or more, your deduction may generate a refund, which can then also be applied toward your down payment.

In a related move, if you have money on hand for a down payment and you’ve accumulated some RRSP contribution room, open an RRSP. Then you can deposit the money into the plan, wait 90 days, be eligible to partake in the HBP and at the same time use whatever refund is issued to bolster your original down payment amount. Be sure to run this by your tax adviser to ensure it’s a sound strategy for your particular financial circumstances.

If you’ve participated previously in the HBP, there are certain situations in which you may be able to participate a second time. First of all, the full amount previously withdrawn must be paid back into your RRSP before the beginning of the given year in which you wish to participate a second time. Also, you must still qualify as a first-time homebuyer.

Each spouse or common-law partner can withdraw eligible amounts under the HBP from any RRSP under which he or she is the annuitant, including spousal RRSPs. Also, each person may withdraw up to the $25,000 limit, or $50,000 in aggregate (if purchasing the property jointly).

Persons with disabilities
If you’re already a homeowner and you have a disability, or if you’re a relative of a person who has a disability, you may withdraw funds from your RRSP under the HBP if
the withdrawal is to assist you or your disabled relative to purchase a home.

Some conditions must be met first:

- You or your disabled relative must qualify for the disability tax credit (see topic 80).
- The home must be more accessible or better suited for the care of the person with a disability.
- If you are not disabled, your disabled relative must live in the home or plan to occupy it within one year after the acquisition.

64 Using an RRSP to finance higher education
Tax-free RRSP withdrawals can also be made to assist you in financing full-time training or education for you or your spouse or common-law partner. Withdrawals are limited to $10,000 per year over a period of up to four calendar years and subject to a cumulative total of $20,000.

To qualify, you or your spouse or common-law partner must be enrolled or committed to enrol as a full-time student in a qualifying education program of at least three months’ duration at a designated educational institution. The full-time criterion is dropped for disabled students.

Withdrawals must be repaid to the RRSP over a maximum 10-year period starting in the year after the last year in which the qualifying individual was enrolled as a full-time student. However, the repayments must commence no later than the sixth year after the initial withdrawal, even if full-time enrolment continues. If the required repayment is not made, an amount will have to be included in income. As with many tax situations, special rules apply.

65 Retirement and your RRSP
You normally have until March 1, 2015¹¹ (see topic 56) to make your 2014 contribution. However, if you turned 71 in 2014, the contribution must be made by December 31, 2014. Unless the RRSP is converted to cash (generally to be

¹¹ Deadline will be extended to March 2 since March 1 falls on a Sunday.
avoided, since the full amount will be taxable as income), it must be converted into a Registered Retirement Income Fund (RRIF) or life or term annuity by December 31 of the year in which you turn 71. If you want, you can do all three—you can put some of the funds into a RRIF, some into an annuity and (if necessary) withdraw a portion in cash.

**Tax tip**

If you turned 71 in 2014, you may be able to make an extra contribution to your RRSP for 2015 before collapsing the plan at the end of 2014. Just before you wind it up in 2014, make a contribution equal to your 2015 contribution room. The amount of your 2015 contribution room is based on your 2014 earned income. The amount contributed can then be claimed as a deduction on your 2015 tax return. This tax-planning tip requires that you have earned income in 2014. It’s important to note that the contribution may trigger a penalty of 1% per month from the date of the contribution to December 31, 2014 (see topic 58). Therefore, it would be wise to make this extra contribution as late in the year as possible.

Before proceeding with this option, you and your tax adviser should review your financial situation carefully in light of your contribution room, the amount of the contribution, the penalty tax, etc. Also, you still have the opportunity to contribute to a spousal RRSP in the future if you have earned income and your spouse or common-law partner is under 72 years of age.

**How RRIFs work**

A RRIF provides you with varying amounts of income during retirement. If the payments are structured properly, a RRIF can continue indefinitely, essentially providing income for life. Payments from a RRIF are quite flexible. You can withdraw as much as you want, although you must take a minimum amount each year. The minimum amount to be withdrawn each year is based on a withdrawal factor that increases slightly each year. RRIF payments are subject to tax in the year of receipt.
How annuities work
If your RRSP funds are transferred to an annuity, periodic payments from the annuity will also be taxed in the year of receipt. Annuities can be arranged to provide payments for either a fixed term (e.g., to age 90) or life. The main advantage of an annuity is that you can have some form of guarantee of the amounts you will receive.

For instance, if you opt for a life annuity, you, or you and your spouse or common-law partner, can be guaranteed a specific income stream regardless of how long either of you survive. Nevertheless, an annuity is not as flexible as a RRIF. Once you purchase a life annuity and the funds are deposited and registered, they are locked in. You generally cannot deregister or cash in the plan or amend the terms of the contract. Also, annuities are not very popular in periods of low interest rates.

Cash withdrawal from your RRSP
If you withdraw funds from your RRSP, you’ll pay a withholding tax on the amount withdrawn. The plan holder is required by law to withhold a certain percentage of the amount and remit it to the CRA. Any additional tax on the withdrawal is paid when you file your tax return for the year. If your income is very low for the year of the withdrawal, you may get a refund. There are many options available to you when you decide to cash in your RRSP. Become familiar with the various alternatives and their tax consequences so you can make an informed choice.

66  Death and your RRSP
Should you die while you still own your RRSP, its entire value must be included in your income in the year of your death unless your spouse or common-law partner or your financially dependent child or grandchild is entitled to the funds. If you designate your spouse or common-law partner or financially dependent child or grandchild as beneficiary of your RRSP, the proceeds from the plan will be taxable in your beneficiary’s hands in the year they’re received, unless they are transferred into his or her own tax-deferred plan.
If none of the above is designated as the beneficiary of your RRSP, its value may still be taxable in his or her hands on your death, provided he or she is a beneficiary of your estate. This approach may provide more flexibility, but more paperwork will be involved.

In addition, proceeds in your RRSP may also be able to be rolled over to an RDSP for the benefit of your financially dependent infirm child or grandchild (see topic 111).

Other rules apply if you die after your plan has matured and you were receiving annuity payments from your RRSP or RRIF.

**Tax tip**

For a taxpayer who dies in 2014, the executor or legal representative can make a spousal RRSP contribution on behalf of the deceased until March 1, 2015 ¹² (see topic 56), provided the surviving spouse otherwise satisfies the age requirements.

As noted above, unless a tax-deferred transfer is available, the fair market value (FMV) of investments held in an RRSP or RRIF must be included in the income of the deceased for the year of death. However, what happens if the value of those investments declines from the date of death to the time of final distribution to the beneficiaries? The post-death decrease may be able to be carried back and deducted against any RRSP/RRIF income inclusion on the deceased’s final tax return.

Two conditions must generally be met for this deduction to be available:

1. The RRSP/RRIF must be wound up by the end of the year following the year of death.
2. The RRSP/RRIF must have held no investments other than qualifying investments during the post-death period.

¹² Deadline will be extended to March 2 since March 1 falls on a Sunday.
Example
Your widowed mother dies in June 2013, at which time the FMV of the assets in her RRIF was $100,000. In March 2014, her estate distributes $80,000 to you (her sole beneficiary) and the RRIF is wound up. Although $100,000 is reported as income on your mother’s final T1 income tax return, a $20,000 deduction can be claimed to offset that income.

67 Company pension plans
In general, if you’re a member of a company pension plan, your RRSP contribution room is reduced by your pension adjustment (PA). As noted in topic 56, this adjustment is intended to represent the present value of the pension benefits you earned for the previous year in your registered pension plan (RPP) or deferred profit sharing plan (DPSP).

There are two main types of RPPs: defined benefit plans, in which pension benefits are specified in the plan, and money purchase (or defined contribution) plans, in which pension benefits are based on combined employer and employee contributions, plus earnings in the plan. The benefits you earn in your defined benefit pension plan, or total contributions to a money purchase plan, determine how much you can also contribute to your RRSP (see topic 56).

Defined benefit plans
As a member of a defined benefit plan, you’re entitled to deduct 100% of all required contributions for current or post-1989 past service. You’re also entitled to deduct a maximum of $3,500 per year for past service contributions for service prior to 1990 while you were not a contributor to a pension plan. This deduction is subject to an overall limit of $3,500 multiplied by the number of years of pre-1990 service bought back. This is in addition to any deduction for post-1989 or current service.

For years of pre-1990 service during which you were a contributor to the plan, the annual deduction is limited to $3,500 less the amount of other contributions deducted in
the current year. This includes amounts for the current year, post-1989 past service, and pre-1990 past service while you were not a contributor. The $3,500 annual limit for deductibility of pre-1990 service contributions is disregarded in the year of death. You should consult your tax adviser if you are subject to these complicated rules.

Example

Assume you make a $4,000 contribution to your defined benefit plan in 2014 with respect to two years of service prior to 1990 while you were not a contributor to a pension plan. Your maximum deduction is $3,500 in 2014. The remaining $500 can be deducted in 2015.

Money purchase plans

You’re entitled to deduct the amount you contributed to a money purchase plan during the year, subject to certain maximum amounts that parallel the RRSP rules. Money purchase plans do not allow for past service contributions.

Money purchase plans can pay pension benefits in the form of a Life Income Fund (LIF), which provides an income stream similar to that currently permitted under a RRIF. However, while a RRIF only has minimum withdrawal limits, LIFs also limit the maximum amount that may be withdrawn on a yearly basis. Therefore, with a LIF you have to withdraw between a minimum and maximum amount from your money purchase account each year, beginning no later than the year in which you reach age 72.

LIF contracts entered into after May 8, 2008 include the option of permitting funds in the LIF to be transferred into a new type of locked-in retirement account—a Restricted Life Income Fund (RLIF). In the year you turn 55, or in any subsequent year, you’ll be allowed to transfer up to 50% of the RLIF’s value into a tax-deferred savings vehicle (i.e., RRSP or RRIF) with no maximum withdrawal limit, as long as this transfer happens within 60 days of the creation of the RLIF. This is a one-time 50% unlocking provision.

13 Also commonly called “defined contribution” plans.
The rules also provide for an increase in the maximum amount that certain individuals facing financial hardship can withdraw from their LIF.

Deferred profit sharing plans (DPSPs)
An alternative to the RPP is a deferred profit sharing plan (DPSP). Under this type of arrangement, your employer makes payments to a trustee, who holds and invests the contributions for your benefit. Unlike RPPs, however, employee contributions are not allowed.

The maximum contribution your employer can make on your behalf in 2014 is, in general, equal to 18% of your earned income or $12,465, whichever is less. Similar to an RPP, employer contributions to a DPSP on your behalf reduce your RRSP contribution room. The contribution your employer makes to your DPSP in 2014 will have an impact on your 2014 RRSP contribution room.

68 Pooled Registered Pension Plans (PRPPs)
A Pooled Registered Pension Plan (PRPP) is a new type of savings plan intended to provide employees and the self-employed with another way to accumulate funds for retirement in a tax-assisted manner. It will operate much like a defined contribution registered pension plan, but will hold assets pooled together from multiple participating employers and will be administered by eligible licensed financial institutions, such as insurance companies and banks.

Employers can offer PRPPs for their employees or, if the company does not offer this option, the employee can become an individual member of the plan.

Since these plans will involve large pooled funds, one of their key benefits is that the plan members should benefit from lower investment management costs.
69 Individual pension plans (IPPs)

An individual pension plan (IPP) is simply a defined benefit pension plan for one member. IPPs specifically benefit owners of companies or executives of incorporated companies who do not participate in an employer pension plan and who have annual earnings in excess of $120,000. Ideally, individuals should be 50 years of age to derive the maximum benefits from the plan. However, such plans have been set up by persons as young as 40. The contribution advantage of using an IPP vs. an RRSP increases with age.

These plans can be either 100% funded by the employer or employer/employee-funded. In general, you won’t be able to fund more than 50% of the cost of the pension.

Subject to certain limitations, a defined benefit plan will provide for an annual pension equal to a percentage of your highest earnings over a given period. One of the main benefits of these plans has been the possibility of making significant contributions for past service. They were also promoted on the basis that they could potentially defer the receipt of retirement income for a longer period of time than was generally possible with other types of retirement plans.

However, for service contributions made after March 22, 2011, the cost of the past service must first be satisfied by transfers from RRSP assets (as well as money purchase registered pension plan assets) belonging to the IPP member or a reduction in the member’s unused RRSP contribution room before new past service contributions are permitted.

Also, the rules now provide for minimum withdrawal amounts from an IPP, similar to those that currently apply to RRIFs.

These two changes, which were aimed at making IPPs more comparable to other retirement savings vehicles, have eliminated many of the advantages that IPPs have had over other plans.
IPPs are not for everyone. It’s an individual decision based on several factors—your age, current and projected income level, the rate of return earned on the plan’s assets, whether you’re an owner-manager or an arm’s-length executive and several other considerations. Due to their complex nature, as well as the recent changes to the rules, it’s recommended that you consult your tax or financial adviser if you have any questions as to whether an IPP is a viable retirement savings vehicle for you.

70 Tax-Free Savings Account (TFSA)
For the years 2009 to 2012 inclusive, every Canadian resident individual (other than a trust) 18 years of age or older has been able to contribute $5,000 a year to a TFSA. Commencing with the 2013 calendar year, the contribution limit increased to $5,500 per year. The limit will continue to increase in increments of $500 in the future as it is indexed to inflation, to the nearest $500. Subject to certain exceptions, a TFSA is generally permitted to hold the same types of investments as an RRSP.

Unlike RRSPs, you will not obtain a tax deduction for contributions to a TFSA. However, you will not include in your income for tax purposes any income, losses or gains from investments held within a TFSA, or amounts withdrawn from it. The amounts withdrawn from a TFSA will also not be included in determining your eligibility for income-tested benefits or credits, such as the medical or age credit (see topics 79 and 83) or OAS clawback (see topic 72). If you do not contribute to a TFSA in one year, the amount can be carried forward indefinitely to future years. Any amounts withdrawn from a TFSA can also be recontributed without impacting your contribution room. For example, if you contribute $5,000 in each of the years 2009 to 2012 inclusive, $5,500 in each of 2013 and 2014 and then withdraw $6,000 in 2015, you’ll be able to contribute $17,000 to your TFSA in 2016 ($5,500 contribution room in each of 2015 and 2016 plus the $6,000 withdrawn in 2014). Interest on money borrowed to invest in a TFSA is not deductible.

14 This assumes that the annual TFSA limit remains at $5,500.
If you can afford it, this plan can prove to be a worthwhile savings vehicle. A TFSA can also provide you with some interesting opportunities to manage your retirement income.

**Tax tip**

If your spouse cannot afford to contribute to a TFSA, you can contribute to your spouse’s TFSA as well as your own without any negative tax consequences. This will allow you to reduce your family’s total tax bill.

**Tax tip**

Although amounts withdrawn from your TFSA can be recontributed without impacting your contribution room, the re contribution should generally not be made until the year following your withdrawal from the account. If you re contribute the amount withdrawn in the same year, you could be subject to an overcontribution penalty.

Your tax adviser can assist you in determining what savings vehicle is the best option for you, given your particular circumstances.

71 Pension income splitting

If you’re receiving income that qualifies for the pension income tax credit (see topic 89), you’ll be able to allocate up to half of that income to your spouse or common-law partner (and vice versa). Although pension income can also be split in the year of death, there are special rules that apply depending on whether it’s the pension income recipient or transferee that has passed away.

The extent to which pension income splitting will be beneficial will depend on the marginal tax bracket of you and your spouse or common-law partner, as well as the amount of qualifying income that can be split. In many cases, the optimal allocation will be less than the allowable 50% maximum.
Example

Your total income for 2014 is $90,000, of which $60,000 is qualifying pension income. Your spouse has no pension income and only $5,000 in other sources of income. You can allocate up to $30,000 of your pension income to your spouse. In this case, you’ll report taxable income of $60,000 and your spouse will report taxable income of $35,000. Both of you can claim the pension income credit (see topic 89), and you will no longer be subject to the Old Age Security (OAS) clawback (see topic 72). The overall savings can be considerable.

To qualify for income splitting, the pension income must satisfy certain criteria. If you’re 65 years of age or older, eligible pension income includes lifetime annuity payments under a registered pension plan (RPP), a Registered Retirement Savings Plan (RRSP) or a deferred profit sharing plan (DPSP), and payments out of or under a Registered Retirement Income Fund (RRIF). If you’re under 65 years of age, eligible pension income includes lifetime annuity payments under an RPP and certain other payments received as a result of the death of your spouse or common-law partner. Eligible pension income doesn’t include payments under the Canada Pension Plan (CPP) or OAS payments.

If you opt to pension split, a special election form (Form T1032) must be signed by you and your spouse or common-law partner and filed with the CRA. If you file your return electronically (see topic 161), you should keep the election form on file in case the CRA asks for it. Another result of pension splitting is that the income tax withheld from your pension income will be reported on your spouse or common-law partner’s return, proportional to the amount of income being split.
Example

Using the figures from the example above, you elect to split 50% of your pension income with your spouse. On your T4A, $10,000 was deducted for income tax. You’ll report 50% of this amount as tax withheld (or $5,000) and your spouse will report the other $5,000. If you had only elected to split 30% of your pension income, $3,000 of income tax withheld would be reported on your spouse’s return.

72 Old Age Security (OAS) clawback

The government imposes a special tax—the “clawback”—on your Old Age Security (OAS) payments if your net income for the year exceeds a certain annual threshold. For 2014, the threshold is $71,592. The amount of the clawback is equal to your OAS payments or 15% of the amount by which your net income exceeds the threshold, whichever is less. For the 2014 year, the full amount of the OAS benefit will be eliminated when your net income reaches approximately $116,000. The clawback amounts are repaid through withholdings from your monthly OAS payments.

How it works

Each OAS payment you receive is reduced by an estimate of the clawback tax. The reduction for the period from January through June 2014 is based on your 2012 net income. The reduction in the payments for July to December 2014 is based on your net income for 2013.

When you file your 2014 income tax return, the CRA will calculate the actual OAS clawback based on your net income for the year. This amount will be compared to the amounts withheld from your monthly payments during the year. Any excess withheld will be refunded or applied against any other tax liability. Conversely, where the amount withheld falls short, you’ll be required to remit the difference.

Although you can start to receive OAS benefits in the month you turn 65 years of age, the age of eligibility will
gradually increase from 65 to 67 starting in April 2023. Also, starting July 1, 2013, you are able to voluntarily defer receipt of OAS for up to five years. This will allow for a higher, actuarially adjusted, annual pension when you finally do start to receive it. This strategy may be beneficial where you are otherwise subject to the full OAS clawback.

### Tax tip

If your net income is over the $71,592 clawback threshold and your spouse or common-law partner’s net income is below it, consider splitting your pension income (see topic 71) or splitting your Canada Pension Plan (CPP) benefits with him or her if that will bring your net income below the threshold (see topic 112). Withdrawals from your TFSA (see topic 70) may also help you keep your net income below the threshold.

### 73 Childcare expenses

Eligible childcare costs include daycare or babysitting, boarding school and certain camp expenses. Medical expenses, education costs, clothing and transportation expenses are not eligible. You are also not allowed to deduct payments made to persons under 18 years of age who are related to you.

### Tax tip

After-school recreational programs can qualify as an eligible childcare expense if the fees are incurred to allow the parent to work. For example, a parent who pays reasonable fees to a gymnastics club for after-school classes may be allowed to claim the amount as a childcare expense provided that the parent needed to make the arrangements for the care of the child after school until she finished work.

**Who claims the childcare costs?**

When the child lives with both parents, the parent with the lower net income must claim the expense deduction. A parent with no income is considered to have the lower
income and, therefore, must claim the expenses. The supporting parent with the higher income may claim a deduction only during the period in which the lower income spouse or common-law partner is mentally or physically infirm, confined to a bed or a wheelchair, attending full-time at a secondary school or a designated educational institution or incarcerated in a correctional facility.

The amount that can be claimed for childcare is subject to special rules when the lower income spouse or common-law partner is in part-time attendance at a designated educational institution. Special rules also apply for single parents and those who have separated during the year or are divorced.

How much can you deduct?
In general, you can deduct up to $7,000 annually for each child who is aged six or under at the end of the year, and up to $4,000 for each child aged seven to 15 at any time in the year. This limit is increased to $10,000 annually for each child who is eligible for the disability tax credit (see topic 80). In general, the total deduction cannot exceed two-thirds of the salary or business income of the parent who is required to claim the deduction. However, it’s limited by the actual amounts paid in the year for childcare.

74 Alimony and maintenance
Rules regarding alimony and maintenance payments changed significantly as of May 1, 1997. The main change was to treat payments for child support differently from payments for spousal support.

Agreements or court orders after April 1997
For new or varied child support agreements made after April 30, 1997, the recipient won’t pay tax on the payments and the payer won’t receive a tax deduction for them. If the agreement or court order doesn’t identify an amount as being solely for the support of a spouse or common-law partner, it will be treated as child support. Similarly, any third-party payments that are not clearly identified as being solely for the benefit of the spouse or common-law partner will be treated as child support.
Periodic payments for spousal support continue to be taxable to the recipient and deductible by the payer, provided certain conditions are met (see discussion below on agreements or court orders prior to May 1, 1997).

**Tax tip**

If you’re party to an agreement or court order entered into before May 1, 1997, and you want the changed rules to apply, you must jointly elect by filing Form T1157. In some cases, you may also be required to file a copy of the agreement itself.

**Registration of agreements**

In some cases, you may be required to file Form T1158 with the CRA, along with a copy of the agreement or court order. Generally, these requirements extend to situations in which payments will continue to be deductible—for example, if an agreement is entered into after May 1, 1997, and it contains a requirement either for spousal payments only or for separate amounts for spousal and child support. Agreements entered into before May 1, 1997 may also have to be filed if they provide for spousal or spousal and child support payments and the agreement becomes subject to the new rules. Your tax adviser will be able to provide you with details on these filing requirements.

Child support payments from a United States resident are not taxable under the Canada-US tax treaty.

**Agreements or court orders prior to May 1997**

For alimony and maintenance payments made pursuant to a written separation agreement or court order in place before May 1997, the old rules apply—i.e., the amounts are deductible for tax purposes if they meet certain criteria. Also, if the person making the payments is allowed to deduct them, the person receiving the payments must include the amounts in income.

In general, to be deductible, the payments must be periodic, for the maintenance of your spouse and/or children and
made pursuant to a written separation agreement or court order. Payments made in the same year (as well as those in the preceding year), before the agreement was signed, may also be deductible, provided the agreement or court order recognizes these payments.

Payments to a third party
There are also rules regarding the tax treatment of alimony and maintenance payments that have been paid to a third party rather than directly to your spouse, former spouse or common-law partner. Such payments, which can include medical bills, tuition fees and mortgage payments, may qualify for a deduction to the payer and a corresponding income inclusion to the recipient. To qualify, the expense must have been incurred at a time when you and your spouse, former spouse or common-law partner were separated and living apart, and such payments must have been specifically provided for in the court order or written agreement.

Where the child support is not taxable, deductibility to the payer and taxability to the recipient only apply to those third-party payments that are not considered to be child support payments.

75 Deductibility of legal fees during separation or divorce
The tax treatment of legal fees paid during a separation and divorce is a complex subject. Although most of the legal fees incurred are not deductible since they are considered a personal or living expense, legal fees incurred with respect to support payments may be deductible. Their deductibility will depend on whether you’re the payer or the recipient of the support payments.

From the payer’s standpoint, legal costs incurred in negotiating or contesting an application for support payments are not deductible, nor are any of the costs incurred to terminate or reduce the amount of such payments. Legal expenses relating to custody or visitation rights are also non-deductible.
From the recipient’s view, some or all of the legal fees may be deductible—depending on the circumstances outlined below.

**Legal expenses incurred to obtain a lump-sum payment**
Legal expenses incurred to obtain a lump-sum settlement are generally not deductible unless the lump-sum payment specifically relates to a number of periodic child support payments that were in arrears.

**Legal expenses incurred to obtain periodic support payments**
The CRA’s position is that the following legal costs are deductible:
- costs incurred to obtain periodic child support payments or to enforce pre-existing rights (regardless of the fact that the amount received for child support may not have to be reported as income)
- costs incurred to enforce pre-existing spousal support
- costs incurred to obtain spousal support
- costs incurred to obtain an increase in support or to make child support non-taxable

**Tax tip**
If you’ve incurred legal fees as part of a separation or divorce, you should contact your tax adviser to determine whether any of the amounts may be deductible. You may also be able to apply for a refund with respect to amounts paid in prior years.

**76 Deductibility of other legal expenses**
Most legal expenses are personal in nature and are not deductible. However, legal costs paid to collect or establish a right to salary or wages from your employer or former employer are deductible. In addition, legal expenses paid to collect or establish a right to a retiring allowance or pension benefit are also deductible within a seven-year carry-forward period. The deduction is limited to the amount of retiring allowance or pension benefits received, less any portion that has been transferred to an RPP or RRSP.
77 Moving expenses

If you moved from one location to another within Canada in 2014, you may be able to deduct your eligible moving expenses on your 2014 return. You must have started work or carried on a business at your new location. In addition, your new residence must be at least 40 km closer to your new work location. A court case has concluded that this distance should be measured using the shortest route normally open to the travelling public.

Costs you can claim

Eligible moving expenses include travelling expenses incurred in connection with the move and the cost of transporting your household goods. The cost of meals and temporary accommodation for a period not exceeding 15 days is eligible, as are the costs of selling your old residence or, if you were renting, of breaking your lease. Any loss incurred on the sale of your former residence cannot be deducted.

You can also claim mortgage interest, property taxes, insurance premiums and costs associated with maintaining heat and power payable with respect to a vacant former residence (to a maximum of $5,000). However, you must be able to show that you were making a reasonable effort to sell the former residence. The costs of revising legal documents to reflect the taxpayer’s new address, replacing driver’s licences and automobile permits and having utilities connected and/or disconnected are also eligible for deduction.

If your employer paid for your moving expenses, you may not claim them as a deduction. If your employer pays or reimburses you for part of your moving expenses, you may deduct all of your eligible moving expenses but must report the amounts paid by your employer as income. Eligible expenses are deductible only from employment or business income earned at the new location. Amounts not deducted in the year of the move may be carried forward to another year to the extent of the employment or business income earned in that year.
**Tax tip**

If you’re moving to a new work location, any relocation payments should generally be structured as a reimbursement of actual expenses incurred. Payments received as a blanket lump-sum allowance, rather than a reimbursement of costs already incurred, may leave you open to tax implications. Talk to your tax adviser about how the payments can be structured to avoid or minimize tax.

**Other amounts received from your employer**

The rules provide that all subsidies paid directly or indirectly by an employer with respect to the financing of an employee’s new or former residence are taxable. Half of any amount in excess of $15,000 paid directly or indirectly to an employee by an employer to compensate for a loss on the disposition of the former residence is also taxable.

**Student eligibility**

Students may claim moving expenses if they move to begin a job (including summer employment) or to start a business. If the move is to attend a full-time post-secondary institution, the expenses can be deducted, but only to the extent of the student’s scholarship or research grant income included in the student’s taxable income for the year (but see topic 78, which comments on the taxation of scholarship and bursary income).

**Optional method for claiming certain moving expenses**

If you’re entitled to claim moving expenses, rather than keeping track of the detailed expenses with respect to the move, you have the option of using a simplified method for claiming your meal and vehicle expenses.

The optional rules are as follows:
- Meal expenses: A flat rate of $17 a meal, to a maximum of $51 per day per person without receipts.
- Vehicle expenses: This method involves the use of various pre-established flat rates. If you choose this option, you do not need to keep receipts. Instead, you
simply keep track of the number of km you drove during the tax year for your trips relating to the move. To determine the amount you can claim, multiply the number of km by the cents-per-km rate that applies for the province or territory from which the travel begins. These rates can be found on the CRA’s Web site.

78 Scholarship income
Scholarships received by a primary or secondary school student as well as scholarships received by a student registered in a program entitling him/her to the education tax credit (see topic 87) are tax-free. There’s a $500 exemption in other cases. A post-secondary program that consists principally of research is only eligible for the 100% scholarship exemption if it leads to a college or CEGEP diploma, or a bachelor, masters or doctoral degree (or an equivalent degree). Accordingly, post-doctoral fellowships will generally be taxable.

Employers often provide scholarships to assist with the education costs of certain of their employees’ children. The CRA’s position is that where an arm’s-length employer provides a post-secondary scholarship, bursary or free tuition to family members of an employee under a scholarship program, the amount will be included in the particular student’s income (subject to the above exemption) and not the employee’s income as a taxable benefit. However, where the scholarship or bursary is used to fund attendance at an elementary or secondary school (private or otherwise), the amount will be treated as a taxable employment benefit to the particular employee.

79 What is a tax credit?
Several of the topics that follow refer to a tax credit. Although there’s a substantial difference between a tax credit and a tax deduction, it’s easy to get the two confused. A tax deduction reduces your taxable income, with the actual amount of tax saved depending on your personal marginal rate of tax.

A tax credit, on the other hand, is a deduction from tax owing. Provided the credit can be used, each taxpayer
receives the same tax relief with a tax credit regardless of his or her particular tax bracket.

The provinces are free to either follow the federal tax credit system or introduce tax credits that are unique to the particular province. In many cases, the amount of the provincial credit will differ from its federal counterpart.

The tax credit sections that follow generally just comment on the federal tax credit. For 2014, federal personal tax credits are calculated as 15% of specified “personal amounts” and are allowed as a deduction in calculating your federal tax liability. Keep in mind that the provincial tax credits may or may not parallel the treatment provided at the federal level.

**Basic personal credit**
For 2014, everyone is entitled to claim a basic personal amount of $11,138.

**The spouse or common-law partner credit**
You may claim the spouse or common-law partner amount if, at any time in the year, you were married or had a common-law partner (see topic 100), and you were not living separately because of a breakdown of the relationship. For 2014, the spouse or common-law partner amount is also equal to $11,138. This amount is reduced on a dollar-for-dollar basis by the dependant’s net income.

**The eligible dependant credit**
If you were unmarried or separated from your spouse or common-law partner at any time in the year, you may be entitled to claim a personal tax credit known as the eligible dependant credit. To qualify, you must have maintained a home in which you and your qualifying dependant lived. As well, your dependant must be related to you and dependent on you for support. The dependant must be your parent, grandparent or child and must be either under 18 years of age at any time during 2014 or mentally or physically infirm. Two or more supporting relatives cannot split this tax credit. This credit is calculated the same way as the spouse or common-law partner credit.
Therefore, the maximum claim for 2014 is $11,138.

Credit for children under age 18
This credit can be claimed for each child under the age of 18 at the end of the taxation year. For 2014, this amount is $2,255 per child.

Where the child resides together with the child’s parents throughout the year, either of those parents may claim the credit. In other cases, the credit can generally be claimed by the parent who is eligible to claim the eligible dependant credit for the year for that child. The full amount of the credit can also be claimed in the year of birth, adoption or death. Any unused portion of the credit can be transferred to the parent’s spouse or common-law partner.

To ensure that sharing a home does not prevent otherwise-eligible parents from claiming the credit, more than one individual per domestic establishment is permitted to claim the credit.

The infirm dependant credit
You may claim the infirm dependant tax credit for a relative who is 18 years of age or older before the end of the year, provided the individual is dependent on you because of mental or physical infirmity. In addition, the individual must be dependent on you for support at any time in the year. Unlike the credits above, it is not necessary that the dependant live in the same residence as you, nor does the disability have to be severe enough that the dependant qualifies for the disability tax credit (see topic 80).

For 2014, the infirm dependant amount is $6,589. This amount is reduced on a dollar-for-dollar basis by the dependant’s income in excess of $6,607.

The caregiver credit
Because of the above income threshold, most taxpayers who provide care to an elderly relative living with them cannot claim the eligible dependant credit because payments under the Old Age Security and Guaranteed Income Supplement programs are well in excess of the threshold.
As a result, there’s another tax credit available if you reside with and provide in-home care for a parent or grandparent who is 65 years of age or older. The age restriction is removed if the relative is dependent on you by reason of mental or physical infirmity.

The maximum caregiver amount for 2014 is $4,530. However, in this case, the eligible credit amount does not start to be reduced until the dependant’s net income reaches $15,472. No credit will be available once the dependant’s net income exceeds $20,002. Also, the caregiver credit won’t be available if any person claims an eligible dependant or infirm dependant tax credit with respect to the dependant.

**Family caregiver credit**

To provide support to caregivers of dependants with a mental or physical infirmity, a family caregiver credit was introduced in 2012.

For 2014, if eligible, an additional $2,058 can be claimed for an infirm dependant under any of the following existing dependency-related credits: spousal, child, eligible dependant, caregiver or infirm dependant. The amount for the infirm dependant credit (noted above) is already increased by the $2,058 enhancement since, by definition, the family caregiver amount would apply.

**The age credit**

Canadian taxpayers 65 or older are entitled to claim an age amount of $6,916 for 2014. It’s reduced at a rate of 15% where a taxpayer’s income exceeds a prescribed threshold, currently $34,873, and it’s fully eliminated once income exceeds $80,980.

**80 Disability tax credit**

Individuals suffering from a severe and prolonged mental or physical impairment can claim a federal disability amount of $7,766 for 2014. If the person with a disability is a child under 18, there’s an additional supplement of $4,530 for 2014, for a total disability amount of $12,296. To qualify, a doctor must certify on Form T2201 that there exists a
severe and prolonged impairment that “markedly restricts” the individual’s daily living activities. The impairment must have lasted, or can reasonably be expected to last, for a continuous period of 12 months.

Those making a new application for this credit will find that the CRA will review the claim to determine eligibility before assessing the tax return. For this reason, if you’re claiming the disability tax credit for the first time, you must paper-file your tax return. Once approved, this credit can continue to be claimed as long as circumstances do not change. There is no requirement to file a new certificate each year unless the CRA asks for one.

A certificate may be requested for a deceased taxpayer, provided it could reasonably be expected that the serious and prolonged mental or physical impairment would have lasted more than 12 months had the taxpayer not died.

If you can’t take advantage of this credit, it may be able to be transferred to your spouse, common-law partner or other supporting person. The list of supporting relatives who can claim a person’s unused disability tax credit includes a parent, child, brother, sister, aunt, uncle, nephew or niece. Key to making the claim is that the person on whose behalf it is made must be “dependent on the taxpayer for support.”

No claim can be made for a person with a disability under this provision if anyone has claimed a medical expense credit relating to a full-time attendant or nursing home care for that person. On the other hand, the attendant care deduction (see topic 84) and the disability tax credit can both be claimed at the same time, as long as no additional attendant or nursing home claim has been made on behalf of the same taxpayer. To confuse this issue even further, the disability tax credit can also be claimed where an amount is claimed as a medical expense for attendant care (see topic 83), to a maximum amount of $10,000 per year. A 2010 tax case\textsuperscript{15} also found that the disability tax credit and a medical expense tax credit could be claimed for

\textsuperscript{15} Greenaway v. The Queen (2010 TCC 42)
amounts paid to a home for the aged, as long as the amounts claimed for payments to the home were not claimed as full-time attendant or nursing home care, but under another qualifying medical expense provision (in this case, payments to a school or institution).

**Tax tip**

If you or anyone else paid for an attendant or for care in a nursing home or other establishment because of your impairment, consider whether the amounts should be claimed as a medical expense instead of claiming the disability tax credit. In some circumstances, both may be claimed (subject to certain restrictions).

The rules relating to this area of credits are exceedingly complex and often confusing. Before filing a return, it’s recommended that you have a tax adviser analyze your particular circumstances to determine the appropriate claim or combination of claims.

**81 Tax credits for charitable donations**

Donations made to registered charities, registered Canadian amateur athletic associations, Canadian municipalities, the federal government or a provincial government are eligible for a tax credit. As a general rule, donations to US charitable organizations qualify for the credit, provided you also have US-source net income that is taxable in Canada.

Donations can only be claimed after they are paid—pledges don’t count. Unused claims may be carried forward for up to five years and donations made in the year of death may be carried back one year. For donations of ecologically sensitive land after February 10, 2014, the carry-forward period is extended from five to ten years.

The general annual limit on charitable donations as a percentage of net income is 75%. However, the limit on gifts by individuals in the year of death (and the prior year) is 100%.
Donations must be supported by official donation receipts. If you’re filing your return electronically (see topic 161), you are not required to file these receipts with your return, but you must keep them on hand in case the CRA asks to see them.

Generally, the federal credit is 15% on the first $200 of donations claimed in the year and 29% on the amount in excess of $200. After factoring in provincial tax savings, donations in excess of $200 will save you anywhere from 40.2% to 50%, depending on your income level and province of residence. The 2013 federal budget introduced a new temporary First-Time Donor’s Super Credit which permits first-time donors an additional 25% federal tax credit on up to $1,000 in donations. This one-time credit may only be claimed once in the 2013 to 2017 taxation years. You are considered a “first-time donor” if neither you nor your spouse claimed a charitable donation tax credit in any of the five previous years.

**Example**

The last time you made a donation to a registered charity was in 2006. In 2014, you make a $500 donation to the Canadian Cancer Society. Your federal donation credit is $242 ([$200 x 15%] + [$300 x 29%] + [$500 x 25%]). When the provincial credit is added, your tax savings can be considerable.

**Tax tip**

If you and your spouse or common-law partner donate more than $200 in any one year, the tax credit will be larger if one of you claims the entire amount. That way, only one $200 amount is credited at 15%.

**Donating property instead of cash**

Subject to special rules (see “Art and other charitable donation arrangements”), if you donate capital property to a registered charity, you can elect to value the gift at any amount not less than its adjusted cost base and not more than its fair market value (FMV). The amount
claimed as a donation must also be reported as your proceeds of disposition of the property.

If you donate “eligible property” to a charity, you’re entitled to additional tax relief. Eligible property includes securities, such as shares and bonds listed on a prescribed stock exchange, as well as mutual fund units. For such donations the taxable portion of the gain is reduced to nil. This tax relief also extends to qualifying donations made to private foundations.

**Art and other charitable donation arrangements**

For several years, there was a tax arrangement whereby taxpayers would buy a series of works of art for, say, $200 each, and immediately donate them to a registered charity or university and receive a donation receipt for a much higher appraised value. Although these “buy low, donate high” gifting arrangements have effectively been stopped by the courts, which generally reduced the donation amount to the cost of the property donated, the government did finally introduce rules to try and put a stop to these planning strategies.

The FMV of a gift of property is deemed to be whichever is less—the actual FMV or the donor’s cost of the property where the property is (i) donated under a gifting arrangement that is a tax shelter; (ii) donated within three years of its acquisition; or (iii) acquired by the donor within the past 10 years in contemplation of making the donation. Special rules apply if the donated property was previously acquired by a person related to the donor. There are certain exceptions to this rule where property is donated as a result of a taxpayer’s death and for donations of certain types of property, such as inventory, real property located in Canada, Canadian cultural property, ecological property and qualifying public securities. Donations of certified cultural property made after February 10, 2014 as part of a tax shelter gifting arrangement are not exempt from this rule.

Many tax shelter promoters state that they have obtained an advance income tax ruling from the CRA. While the
Rulings Directorate will rule on certain aspects of proposed transactions, it will not rule on such issues as the existence of a business, reasonable expectation of profit and the FMV of a property or service. Therefore, if you’re considering investing in a charitable donation tax shelter, you should be aware that an advance ruling is not a guarantee of the proposed deductions.

You should also be aware that a tax shelter identification number is only used for identification purposes. It doesn’t mean that the tax shelter transactions have been approved by the CRA as being legitimate. Previously, a tax shelter identification number didn’t have an expiration date. However, for applications filed after March 28, 2012, a tax shelter identification number will be valid only for the calendar year identified in the application filed with the CRA. Tax shelter identification numbers issued prior to this date expired at the end of 2013.

Over the past several years, the government has gradually introduced more and more rules to deter the promotion of abusive charitable donation planning arrangements. Although not as prevalent as in the past, new arrangements continue to be marketed. However, you should be cautious of all arrangements that promise a donation receipt in excess of the cash donated.

There is the added risk of losing the benefit associated with the actual cash donation. To qualify for a donation credit, a gift must be made voluntarily with no expectation to receive anything in return. In most of the charitable donation arrangements being looked at by the CRA, it would be difficult to argue that the donation would have been made were it not for the expected tax savings.

There is also now the added risk of having to pay disputed amounts to the CRA even if you’re planning to challenge a CRA assessment on a charitable planning arrangement. The CRA is now permitted to collect 50% of disputed income taxes, interest and penalties in situations where a taxpayer is in the process of objecting to an assessment that involves the CRA challenging a charitable donation shelter.
Other receipting guidelines for charities

In general, a charitable organization can issue a tax receipt for the amount of a gift made to the charity. In some cases—for example, when the donor receives some benefit as a result of making the donation—the actual amount of the gift may not be clear. To help resolve some of the uncertainty in this area, the CRA has issued guidelines to describe how the amount of the gift should be determined in various fundraising methods commonly used by the charitable sector, such as fundraising dinners, charity auctions, concerts, shows and sporting events, golf tournaments, etc.

Example

Your favourite charity holds a fundraising dinner for which tickets are sold for $250 each. A comparable meal could be purchased for $100. Each donor is entitled to receive a charitable donation receipt in the amount of $150. There may be further adjustments where the event has door prizes or provides attendees with other complimentary gifts.

Donations from state supporters of terrorism

For donations made after February 10, 2014, the CRA may refuse to register a charity or revoke a charity’s registration where it accepts a donation from a foreign state listed as a supporter of terrorism for purposes of the State Immunity Act.

82 Political donations

For 2014, the credit is calculated as follows: 75% of the first $400, 50% on the next $350 and 33 ¹/³% of any contribution over $750, up to $1,275. This results in a maximum credit of $650. Some provinces provide similar credits against provincial income taxes for contributions made to provincial political parties.

For both federal and provincial purposes, the credit can only reduce taxes paid or payable. If you are not liable for any taxes in 2014, the credit is lost. It cannot be carried forward to 2015. Note that contributions to local mayoral campaigns do not qualify for the political donation tax credit.
Consider spreading your political contributions over two years. For example, if you contribute $750 in 2014, your federal tax credit will be $475. If, instead, you contribute $375 in 2014 and $375 in 2015, your political contribution tax credit will be $281.25 in each of 2014 and 2015, for a total of $562.50.

### 83 Medical expenses

You can claim medical expenses paid for yourself, your spouse or common-law partner and certain related persons (discussed below). Generally, subject to the comments below for other dependants, total eligible medical expenses must first be reduced by 3% of your net income or $2,171, whichever is less. The tax credit is 15% of the amount remaining.

Select your 12-month period to maximize the tax credit. The 12-month period ending in the year may vary from year to year, but you cannot claim the same expense twice. Keep your receipts for next year if some of your 2014 expenses are not claimed as a credit in 2014.

The list of eligible medical expenses is extensive and includes:

- payments to medical practitioners, dentists or nurses, or to public or licensed private hospitals in respect of medical or dental services;
- additional costs related to the purchase of non-gluten food products;
- expenses paid for training courses for a taxpayer or a related person in respect of the care of a person with a

---

16 The reference period is 24 months in the year of death of the taxpayer or a dependent.

17 Certain conditions must be met. Details are provided in government publications, including the list of eligible medical expenses published by the CRA at: [http://www.cra-arc.gc.ca/E/pub/tg/rc4064/rc4064-e.html#eligible](http://www.cra-arc.gc.ca/E/pub/tg/rc4064/rc4064-e.html#eligible)
mental or physical impairment, who lives with or is a dependant of the taxpayer;
• cost of purchased or leased products, equipment or devices that provide relief, assistance or treatment for any illness;
• cost of blood coagulation monitors for use by individuals who require anti-coagulation therapy, including pricking devices, lancets and test strips;
• premiums paid to private health insurance plans;
• expenses incurred after 2013 for specially trained service animals that assist individuals with severe diabetes;
• remuneration for tutoring persons with learning disabilities, or other mental impairments, if the need for such services is certified by a medical practitioner; and
• reasonable supplemental expenses for the construction or renovation of a residence to enable a person with a serious, prolonged handicap to have access to this residence, to move about therein and to carry out activities of daily living.

For 2014 and later years, the list of eligible medical expenses is expanded to include amounts paid for the design of an individualized therapy plan, where the cost of the therapy itself would be eligible for the credit and certain other conditions are met. In particular, the plan must be designed for an individual who qualifies for the disability tax credit (see Topic 80).

Medical expenses of dependants other than a spouse or common-law partner
Subject to special rules, you may also claim medical expenses you have paid for a dependant. In general, a “dependant” is a person who is dependent on you for support at any time in the year, and who is the child, grandchild, parent, grandparent, brother, sister, uncle, aunt, niece or nephew of you or your spouse or common-law partner.
Claims for the medical expense credit for minor children are grouped with claims for you and your spouse or common-law partner. Medical expenses paid for other dependant relatives must first be reduced by 3% of that dependant’s net income, to a maximum of $2,171 in 2014.

**Tax tip**
If you pay medical expenses for a dependant other than your spouse or common-law partner or minor child, the ability to claim a medical expense credit is based on the dependant’s net income, not your own. As a result, even limited payments can qualify where the dependant’s income is quite low. Don’t forget to claim these amounts when you file your tax return.

**Refundable medical expense credit**
Eligible individuals who have business and/or employment income of at least $3,363 may be able to claim a refundable medical expense supplement. The refundable credit is 25% of medical expenses that qualify for the regular medical expense tax credit, up to a stated maximum. It’s reduced by 5% of the taxpayer’s (and spouse or common-law partner’s) income in excess of a specified amount ($25,506 per family). This credit is in addition to the tax credit for medical expenses. The maximum refundable medical expense supplement is $1,152 for the 2014 taxation year.

**What you cannot claim as medical expenses**
Many items do not qualify as medical expenses—for example, non-prescription birth control devices, drugs and medications that you can purchase without a prescription, funeral and burial costs, and gym memberships, to name a few. In addition, you cannot claim medical expenses for which you are reimbursed or are entitled to be reimbursed. Amounts paid for purely cosmetic procedures (including related services and other expenses such as travel) are not eligible for the medical expense tax credit unless they’re required for medical or reconstructive purposes.
84 Disability supports deduction (attendant care expenses)
If you’re entitled to claim the disability amount (see topic 80), you may deduct expenses paid for attendant care from your income. This is a tax deduction, not a tax credit, and includes attendant care expenses as well as other disability supports expenses incurred by disabled persons for education and employment purposes, or for carrying on a business, unless such expenses were reimbursed or were claimed for purposes of the medical expense credit.

85 Attendant care in a retirement home
In general, payments made to a nursing home or long-term care facility qualify for the medical expense tax credit, provided the individual meets all the criteria to claim the disability tax credit. The issue has been less clear with respect to amounts paid to a retirement home. However, it is the CRA’s position that seniors who live in a retirement home and are eligible for the disability tax credit can claim attendant care expenses as medical expenses. The maximum amount that can be claimed under this provision is $10,000 per year ($20,000 in the year of death).

To make the claim, you must have a receipt from the retirement home showing the portion paid for attendant care and be eligible for the disability tax credit.

86 Adoption expense credit
If you adopt a child, you’re able to claim a non-refundable tax credit for certain expenses you incur as part of the adoption process.

Eligible expenses include court, legal and administrative expenses, reasonable travel and living expenses, fees paid to an adoption agency licensed by a provincial or territorial government, any other reasonable expenses required by such an agency, mandatory fees paid to a foreign institution, mandatory expenses paid with respect to the immigration of the adopted child and document translation fees. Eligible costs include those incurred from the time you make an application to register with a provincial ministry or adoption agency, and the time when the application is made to a Canadian court.
The maximum amount that can be claimed for 2014 is 15,000 (indexed to inflation for taxation years after 2014).

87 Tuition fees, education and textbook credits

Tuition tax credit
Tuition fees for students enrolled on a full- or part-time basis in Canada and, in certain instances, outside Canada, are eligible for a non-refundable tax credit, provided they total more than $100 per establishment. A student enrolled at a university outside Canada and taking courses over the Internet may be able to claim a tuition tax credit for the related tuition fees, provided the student is able to demonstrate his or her attendance constituted “full-time attendance.” Canadian students attending foreign universities have to have paid fees in respect of a full-time course of at least three consecutive weeks in order to qualify for the tuition, education and textbook credit.

Tuition fees include entrance fees, use of library or laboratory facilities, issuance of a certificate or diploma and related expenses charged to all students, other than payments to a student association. Eligible fees also include fees paid to an educational institution, a professional association or a provincial ministry or similar institution for an examination required to obtain a professional status. Certain ancillary fees paid in respect of occupational, trade or professional examinations also qualify for the credit.

Where the student attends a post-secondary institution in Canada, the claims for all three credits are normally supported by Form T2202 or T2202A, which is completed by the educational institution. Where tuition fees are paid to a qualifying institution outside Canada, Form TL11A (for a foreign university), TL11C (for commuters attending post-secondary institutions in the United States), or TL11D (for deemed residents of Canada) must be completed and filed with the return.

Education tax credit
Students can also claim a non-refundable credit for each month (or part of month) of study inside or outside Canada at an accredited teaching establishment or during which
they are registered full-time or part-time in a cooperative program or an eligible training program. The federal credit is 15% of $400 per month for full-time students\(^{18}\) and 15% of $120 per month for part-time students.\(^{19}\)

A student who is registered in an eligible training program on a part-time basis because of a mental or physical disability is entitled to a credit as though he/she were a full-time student provided he/she is entitled to the disability credit. This also applies to the textbook tax credit (discussed below).

A student who takes post-secondary courses related to his/her job can claim the education credit provided the costs are not reimbursed by his/her employer.

**Textbook tax credit**

Costs incurred by post-secondary students to purchase textbooks qualify for a non-refundable credit, provided the student is otherwise entitled to the education tax credit. This credit equals 15% of $65 for each month the student is registered full-time or 15% of $20 for each month the student is registered part-time.

Students are entitled to carry forward unused tuition, education and textbook credits indefinitely. As a result, any amount not used by the student in the current year and not transferred to an eligible person (see below) can be carried forward by the student and claimed in a subsequent year.

**Transfer of tuition, education and textbook credits**

If a student is unable to use all or a portion of these credits, he or she can transfer up to $5,000 to an eligible person. That translates into a $750 federal tax credit. Transfer to an eligible person is available only for credits earned in the current year. To make this designation, the student must complete and sign Form T2202. To support the amount claimed, a copy of this form should be kept by the

\(^{18}\) Minimum of three consecutive weeks and 10 hours of courses per week.

\(^{19}\) Minimum of three consecutive weeks and 12 hours of courses per month.
designated person and, if applicable, by the student. Currently, the form doesn’t need to be filed with the return, but it must be available if requested by the CRA.

88  **Interest on student loan credit**
Many students obtain loans to finance their post-secondary education. You can claim a tax credit of 15% of the interest paid in the year or in any of the five preceding years (if not previously claimed) on a federal or provincial student loan provided for post-secondary education. Interest on other loans such as bank loans obtained for post-secondary education does not qualify for this tax credit.

89  **Pension credit**
The first $2,000 of eligible pension income qualifies for a non-refundable tax credit. The type of pension income that qualifies for this credit differs depending on whether you were 65 or older in the year. If you were under 65 as of December 31, 2014, “qualifying pension income” includes life annuity payments out of a superannuation or pension plan and certain payments received as a result of the death of a spouse or common-law partner.

If you were 65 or older in 2014, other defined payments such as lifetime annuity payments out of your RRSP, deferred profit sharing plan (DPSP) or RRIF also qualify for the pension credit. Qualifying pension income doesn’t include Canada Pension Plan (CPP), Old Age Security (OAS) or Guaranteed Income Supplement (GIS) payments.

**Tax tip**

If you don’t already benefit from the pension income tax credit and you’re 65 years of age or older, consider creating pension income by purchasing an annuity that yields $2,000 of interest income annually. Alternatively, you can use some of the funds in your RRSP to purchase an annuity or RRIF to provide you with $2,000 of annual pension income.
90 Claiming your spouse or common-law partner’s unused credits

If your spouse or common-law partner has little or no taxable income and cannot use all the federal tax credits to which he or she is entitled, you can claim the portion of the qualifying credits that your spouse is unable to use. However, you cannot claim these credits if you were separated at the end of the year and for a 90-day period that commenced at any time in the year. The unused credits that can be transferred include the tuition fee and education and textbook tax credits (see topic 87), the pension credit (see topic 89), the disability tax credit (see topic 80) and the age credit (see topic 79).

91 First-time home buyers’ tax credit

Eligible first-time home buyers who acquire a home are entitled to claim a $5,000 credit. The rules to qualify as a first-time home buyer are generally the same as those that apply under the Home Buyers’ Plan (HBP) (see topic 63).

92 Canada Employment Credit

Compared to a self-employed individual, an employee is extremely limited with respect to the deductions that can be claimed against employment income.

To help offset some of an employee’s work-related expenses, all employees are entitled to claim a Canada Employment Credit. The maximum amount of this credit is $1,127 for 2014 and is indexed for inflation.

93 Working Income Tax Benefit (WITB)

For 2013, low-income Canadians in the workforce who are at least 19 years of age are entitled to this refundable tax credit. For single individuals without children, the maximum amount of WITB ($998 for 2014) is paid if working income is between $6,992 and $11,332 for 2014. The WITB payment is gradually reduced when net income is more than $11,332 and is eliminated when net income exceeds $17,986. For families, the maximum amount of WITB ($1,813 for 2014) is paid if the family’s working income is between $10,252 and $15,649 for 2014. The WITB payment is gradually reduced when family net
income is more than $15,649 and is eliminated when family net income exceeds $27,736. Disabled persons are entitled to a supplement. These amounts vary slightly for residents of Alberta, Quebec, Nunavut and British Columbia.

You may apply for an advance payment of one-half of the benefit to which you are entitled for the year. If approved, the prepayments will be made as part of your GST /HST credit payments.

94 Public transit credit
You can claim a non-refundable credit for the cost of eligible travel on a local bus, streetcar, subway, commuter train, commuter bus or ferry. It can be claimed by you, your spouse or common-law partner for eligible transit costs incurred by you, your spouse or common-law partner and any dependent children under 19 years of age. An eligible public transit pass is a pass that is valid for a period of at least 28 days of public transit. It also includes electronic payment cards where the cost relates to the use of public transit for at least 32 one-way trips during an uninterrupted period not exceeding 31 days. Weekly passes also qualify, provided the individual purchases at least four consecutive weekly passes that provide the passholder with the right to unlimited public transit use within a period of between five to seven days.

If your employer reimburses you for your travel costs, the total eligible costs must be reduced by the amount you receive, unless the amount of the financial assistance is included in your income for tax purposes (as a taxable benefit).

Tax tip
If you want to make a claim for this credit, you must keep your receipts to support the claim. Remember to keep the receipts for all eligible family members. There is no maximum limit to the amount that can be claimed.
95 Children’s fitness credit
This credit will be of interest to you if you have children under the age of 16 at the beginning of the year (or under the age of 18 years if the child is disabled).

You may claim a tax credit of up to $500 for eligible fitness expenses paid for each of your eligible children. The expenses can be paid by you, your spouse or common-law partner with respect to the children of either of you.

To qualify for the tax credit a program must be

- ongoing (either a minimum of eight weeks duration with a minimum of one session per week or, in the case of children’s camps, five consecutive days);
- supervised;
- suitable for children; and
- substantially all of the activities must include a significant amount of physical activity that contributes to cardio-respiratory endurance plus one or more of muscular strength, muscular endurance, flexibility or balance.

Example
In July 2014, you sent your 10-year-old son to an away-from-home hockey camp for children. The all-inclusive registration fee is $1,100 for the two-week camp. This fee includes $400 for accommodation and $250 for meals. The portion of the fee that qualifies for the children’s fitness tax credit is $450 ($1,100 – $400 – $250).

Memberships and mixed-use facilities can also qualify for the credit provided either more than 50% of the programs are eligible or more than 50% of available time is devoted to eligible programs for qualifying children. If neither of these tests is met, a receipt can be issued for a pro-rated amount. The portion of a family membership can also qualify if it’s attributable to a qualifying child’s participation in an eligible program or activity.
Tax tip

You should either receive, or ask for, a receipt from organizations providing eligible programs of physical activity in which your child is enrolled. The organizations are supposed to determine the part of the fee that qualifies for the tax credit. It’s also important to note that the year in which the tax credit can be claimed is determined by the date when the fees are paid, not when the activity takes place.

As noted above, if the child qualifies for the disability tax credit, the fitness credit can be claimed as long as the child is under 18 years of age at the beginning of the year. There is also a separate $500 non-refundable amount for such children (subject to spending a minimum of $100 on registration fees for an eligible program).

96 Children’s arts tax credit
You can claim a 15% non-refundable children’s arts tax credit based on up to $500 in eligible expenses per eligible child. The definition of an eligible child, as well as the additional $500 supplement for disabled children parallels the children’s fitness tax credit rules (see topic 95). Eligible programs include those that consist of artistic, cultural, recreational or developmental activities.

97 Canada Child Tax Benefit (CCTB)
The CCTB is a non-taxable monthly benefit paid to low- and middle-income families to help them pay for the needs of their children who are 17 years or younger. To qualify, a taxpayer has to be the father or mother of the child, live with him/her and be the person primarily responsible for his/her care and education.

The CCTB is paid over a 12-month period from July of a particular year to June of the following year. It’s calculated

---

20 The CCTB is reduced when family net income (excluding the UCCB and income from an RDSP) exceeds $43,953. Families whose net income is equal or less than $43,953 receive the National Child Benefit Supplement (reduced when net family income exceeds $25,584).
based on the information in both parents’ tax returns for the preceding year. Accordingly, it’s important for each parent to file a tax return, even if one of them has no income. Payments cease automatically the month following the child’s 18th birthday.

Families who receive the National Child Benefit Supplement in connection with the CCTB may also be entitled to an initial Canada Learning Bond of $500 plus a $100 supplement each year until the child turns 15 years of age (cumulative maximum of $2,000). The bond will be paid into a Registered Education Savings Plan (see topic 110).

A supplement to the CCTB is paid in respect of children who qualify for the disability tax credit.

**98 Universal Child Care Benefit (UCCB)**

The UCCB is administered under the Canada Child Tax Benefit (CCTB) program and is paid to all families with eligible children, regardless of the family’s income level. Families are entitled to a benefit of $100 per month for each child under six years of age. Although this allowance will be taxable in the hands of the spouse or common-law partner with the lower income, amounts received won’t be taken into account for the purpose of calculating income-tested tax benefits.

Single parents have the option of including the total UCCB amount in the income of the child for whom the UCCB is paid.

**Tax tip**

If you have a child under the age of six and you have never applied for the CCTB, you’ll need to complete an application form to receive this benefit. Additional information is available from the CRA’s Web site at http://www.cra-arc.gc.ca/bnfts/cctb/fq_qlfyng-eng.html

**99 Child benefits in shared custody situations**

Parents who share custody of a child are both able to receive the CCTB (see topic 97), UCCB (see topic 98) and
the child component of the GST credit (see topic 54). This ability to share benefits applies when a child lives more or less equally with his/her parents who live separately. Otherwise, they are only available to the parent who primarily fulfills the responsibility for the care and upbringing of the child.

100 Taxation of common-law couples
Common-law couples are treated the same way as legally married couples for all provisions of the Income Tax Act. A common-law partner is defined as a person who has lived with you in a conjugal relationship throughout the 12-month period that ends at that time, or who is the natural or adoptive parent of your child. A common-law partner also includes a same-sex partner. As a result, common-law couples are

- able to claim the married credit,
- permitted to contribute to spousal RRSPs,
- able to benefit from the pension income-splitting rules (see topic 71),
- required to combine their incomes to determine entitlement to the GST credit and the child tax benefit,
- subject to the income attribution rules,
- allowed to transfer assets to a surviving partner on a tax-deferred basis upon the death of the other partner, and
- subject to all other income tax provisions that apply to married persons.

101 Special rules for artists and entertainers
Artists and entertainers are entitled to special treatment under the Income Tax Act.

If you’re employed as a musician and are required to provide a musical instrument as a condition of your employment, you may deduct the cost of maintenance, rent or capital cost allowance (CCA) (see topic 7) and insurance for the instrument. The amount deducted for musical instrument costs cannot exceed the income from employment as a musician after you deduct all other employment expenses.
Artists and entertainers receiving employment income are entitled to deduct related expenses actually incurred, up to a maximum of 20% of such income but not more than $1,000. This deduction is in addition to the deductions that all employees may be entitled to for most other expenses, such as automobile and related travel expenses. However, it’s reduced by the sum of the amounts claimed for interest and capital cost allowance on an automobile and for musical instrument costs (see above). Expenses incurred in the year but restricted by the 20% or $1,000 limit may be carried forward indefinitely.

102 Apprentice mechanic deduction for tools

Before they can gain employment, apprentice mechanics are often required to purchase a tool set that can cost thousands of dollars. To provide relief, the cost of new tools acquired by an eligible apprentice mechanic is deductible in calculating income, subject to certain limits.

The deductible amount is determined by a specified formula (which, in general, allows a deduction for the total cost of eligible tools less the greater of $1,627 or 5% of the individual’s apprenticeship income for the year).

The deduction is optional, and if the employee chooses not to deduct all or a portion of the deductible amount, it can be carried forward and deducted in a subsequent taxation year.

To be eligible for this deduction, the tools must be acquired while the apprentice is registered with a provincial or territorial body in a program leading to a designation as a mechanic licensed to repair automobiles, aircraft or any other self-propelled motorized vehicles. In addition, the mechanic’s employer must certify in prescribed form (Form T2200) that the tools were required as a condition of and for use in the apprentice’s employment.

Since this deduction has a much higher threshold than the deduction for tradespeople’s tools (see topic 103), where you qualify for both in the year, you may be able to claim under that provision where you cannot claim under this one.
**103 Tradespeople’s tool expenses**
If you’re an employed tradesperson, you may be entitled to a tax deduction for the cost of new tools used in carrying out your employment duties.

For 2014, the amount you can claim is equal to the cost of new tools in excess of $1,127 that you’re required to purchase as a condition of your employment, subject to a maximum claim of $500. This measure applies to new tools, other than electronic communication devices and electronic data-processing equipment (such as computers, pagers and cell phones), and is in addition to the Canada Employment Credit (see topic 92).

It’s the CRA’s view that any person engaged in an occupation that demands a certain level of skill may be considered a “tradesperson” for purposes of this deduction.

If you’re an apprentice vehicle mechanic, you’ll also be eligible to claim this tax deduction in addition to the existing apprentice vehicle mechanics’ tools deduction (see topic 102).

**104 Northern residents deduction**
You may qualify for the northern residents deduction if you lived in a prescribed area in northern Canada (northern or intermediate zone) on a permanent basis for a continuous period of at least six consecutive months commencing or ending in the taxation year for which a return is being filed. The deduction is claimed by filing Form T2222 with your return. You can review the CRA publication T4039, “Northern Residents Deduction—Places in Prescribed Zones,” to determine if you live in a prescribed northern or intermediate zone.

There are two deductions you may be able to claim:

1. A **residency deduction** for living in a prescribed zone
2. A **travel deduction** for taxable travel benefits you receive from employment in a prescribed zone
Residency deduction
If you live in a prescribed northern zone, you can claim $8.25 for each day in the taxation year that you lived there and an additional residency amount of $8.25 per day if you’re the only person in your household claiming the residency deduction. If you live in an intermediate northern zone, the residency deduction is half the above amounts.

The residency deduction is reduced by the non-taxable benefit for board and lodging at a special work site (box 31 of your T4 slip, or from the footnotes area of your T4A slip) and is limited to 20% of your net income.

Travel deduction
Subject to certain limits, you can also claim a travel deduction to the extent the value of travel benefits is included in your income from employment. This amount is reported in box 32 or 33 of your T4 slip, or box 28 of your T4A slip.

This deduction applies with respect to all trips made by you or a member of your household for the purpose of obtaining necessary medical services not available locally. It also applies to a maximum of two trips per person made by you or a member of your household (e.g., for vacations).

The maximum travel deduction you can claim cannot exceed the taxable travel benefits you received from your employer. The deduction for an employee in the intermediate zone is 50% of the amount that would be calculated for an employee in the northern zone.

105 Special rules for the clergy
If you’re a member of the clergy or a religious order or a regular minister of a religious denomination, you may be able to claim a deduction with respect to your residence. The amount of the deduction depends on whether your employer provides the residence or you provide your own residence.

Where your employer provides you with living accommodations, you can deduct the value of the
accommodation to the extent that it’s included in your employment income as a taxable benefit.

Where you provide your own living accommodations, you can claim a deduction equal to the least of the following three amounts:

1. Your total remuneration from the office or employment
2. One-third of that total remuneration or $10,000, whichever is greater
3. The rent paid for your residence, including utilities (or an amount equal to the fair rental value of your residence, if owned)

The calculation is adjusted if you’re employed as a clergy for only part of the year or if other amounts are claimed as a deduction with respect to the same accommodation.

To claim the clergy residence deduction, you must file with your income tax return a prescribed form signed by your employer stating that you qualify to claim this deduction.

106 Taxation of emergency volunteers
If you provide volunteer emergency services (volunteer firefighters, ambulance technicians and other emergency service volunteers who are called upon to assist in emergencies), you’re entitled to a $1,000 tax exemption for allowances received. Amounts paid in excess of this limit are taxable. This $1,000 exemption is not available if you were employed by the same authority to perform the same or similar work other than as a volunteer.

Tax credit for volunteer firefighters
Volunteer firefighters who perform at least 200 hours of volunteer firefighting services in a year can claim a 15% non-refundable tax credit based on an amount of $3,000 ($450).

To claim this credit, you may have to obtain written certification confirming the number of eligible hours performed. Also, if you claim this credit you cannot also claim the tax exemption of up to $1,000 for honoraria received as an emergency volunteer.
Search and Rescue Volunteers Tax Credit
For the 2014 and subsequent tax years, there is a new Search and Rescue Volunteers Tax Credit (SRVTC) to allow eligible ground, air and marine search and rescue volunteers to claim a 15% non-refundable tax credit based on an amount of $3,000.

To qualify, you must be a search and rescue volunteer who performs at least 200 hours of volunteer search and rescue services in a taxation year, for one or more ground, air or marine search and rescue organizations. Volunteer services will not qualify if you also provide search and rescue services, other than as a volunteer, to the organization.

If you perform both eligible volunteer firefighting services and eligible volunteer search and rescue services for a total of at least 200 hours in the year, you will be able to claim either the Volunteer Firefighters Tax Credit or the SRVTC.

Similar to the Volunteer Firefighters Tax Credit, you may have to obtain written certification confirming the number of eligible hours performed. Also, if you claim this credit you cannot also claim the tax exemption of up to $1,000 for honoraria received as an emergency volunteer.

107 Principal residence rules
Your “principal residence” is generally any residential property owned and occupied by you or your spouse or common-law partner, your former spouse or common-law partner or your child at any time in the year. It can be a house, condominium, cottage, mobile home, trailer or even a live-aboard boat, and it need not be located in Canada. Any gain on the sale of a principal residence is tax-free. However, if you sell your residence, you should be aware that some tax rules apply.

Just because you live in a house that you own doesn’t automatically qualify it as a principal residence. For example, building contractors or house renovators who follow a pattern of living for a short period of time in a home they have built or renovated, and then selling it at a profit, may be subject to tax as ordinary business income on their gains.
Designating a principal residence

A home can be designated as your principal residence for each year in which you, your spouse or common-law partner and/or your children were residents in Canada and ordinarily lived in it for some time during the particular year. You’re only allowed to designate one home as your principal residence for a particular year. If you’re unable to designate your home as your principal residence for all the years you owned it, a portion of any gain on sale may be subject to tax as a capital gain. The portion of the gain subject to tax is based on a formula that takes into account the number of years you owned the home and the number of years it was designated as your principal residence. Suppose you and your spouse own two residences, a home in the city and a cottage out of town. Only one of these homes can be designated as your family’s principal residence each year. Before 1982, each spouse could designate a separate property as a principal residence for a particular year, provided the property was not jointly owned. However, for each year after 1981, couples and their unmarried minor children can only designate one home in total as their principal residence each year.

To help you make this designation, you should determine the fair market value (FMV) of both homes as of December 31, 1981. Factors to consider will include the relative appreciation of each house and the expected timing of any sale.

Tax issues

If you made a capital gains election on a residential property such as a cottage (see topic 135), the tax implications on the eventual disposition of the property will depend on a number of factors. These include the value of the property at the time of disposition, the number of years it was designated as a principal residence at the time of making the capital gains election and the years after 1994 it was designated as a principal residence. The rules in this area are quite complex and well worth a trip to your tax adviser’s office.
Tax tip

Be careful before designating a foreign-owned home as your principal residence. Even though the gain under Canadian rules is tax-free, you may incur a foreign tax liability when you sell your home.

Homes for rent

If you move out and rent your home, you can continue to treat the house as your principal residence for four additional years, or possibly more if you move as a consequence of a change of your place of employment with your employer. There are also rules that apply if you own property to earn rental income and subsequently convert the property to personal use. Basically, at the time of the change in use, you’re deemed to have disposed of the property at its FMV. If this value exceeds your original cost, you will have to report a capital gain. However, you can make a special election to defer recognizing this gain until you ultimately sell the home. This election is not available if you have claimed depreciation on the property for any year after 1984.

108 Selling personal-use capital property

Profits from the sale of almost all capital assets, with the exception of your principal residence, are subject to tax as a capital gain. Unfortunately, losses from the sale of most personal capital assets are not deductible.

For example, if you sell your boat or car at a loss, you cannot claim it as a capital loss. But if you sell it at a profit, half the gain is taxable (see topic 134). With the exception of certain donations (see topic 81), assets that have a cost of $1,000 or less and are sold for $1,000 or less are exempt from this rule. However, assets that cost less than $1,000 and are sold for more than $1,000 still face a tax bill on the difference between their sale price and the $1,000 cut-off point.
Losses from the sale of certain types of personal property, referred to as listed personal property, can be applied against gains from the sale of such property. Listed personal property includes coins, stamps, jewellery, rare books, paintings or sculptures and similar works of art. Listed personal-property losses can be carried back for up to three years and forward for up to seven years, but they can only be applied against gains from the sale of similar property.

109 Transfers and loans to family members

Transfers to a spouse or common-law partner

All capital properties, such as shares in companies and real estate, are automatically transferred between spouses or common-law partners on a tax-free basis. If you want the transfer to take place at FMV, you must file a special election requesting this treatment when you file your tax return for the year of the transfer.

When the transferred property is eventually sold to a third party by your spouse or common-law partner, you’ll have to report any capital gain or loss realized on the sale unless all of the following conditions are met. First of all, your spouse or common-law partner must have paid FMV for the property at the time of the transfer. You must also have made the FMV election (as noted above), and sufficient annual interest on any unpaid purchase price must have been paid in full no later than January 30 of the following year. If all of these conditions have been met, any subsequent capital gain or loss realized on a sale to a third party can be taxed in your spouse or common-law partner’s hands (rather than in your hands).
Example

In June 2014, you decide to transfer your shares of XYZ Co. to your spouse. You acquired the shares in 2000 at a cost of $1,000 and they have a current FMV of $6,000. For tax purposes, your spouse will be deemed to have acquired the shares from you at a cost of $1,000. Therefore, you won’t recognize a capital gain or loss on the transfer. However, you’ll be taxed on any capital gain or loss that results when your spouse disposes of the shares (based on an original cost of $1,000).

Alternatively, by attaching a note to your tax return, you may elect to have the transfer to your spouse take place at FMV. As a result of making this election, you’ll report a capital gain of $5,000 and your spouse will be deemed to have acquired the shares from you at a cost of $6,000. If your spouse paid you $6,000 for the shares (say, by way of a loan from you) and the shares are subsequently sold for $8,000, the $2,000 gain would be taxable in your spouse’s hands—provided your spouse pays a reasonable rate of annual interest on the loan within the required time period.

Special rules apply in situations where the property has been transferred between spouses or common-law partners as part of a property settlement or where the couple is separated when the property is sold to a third party.

Tax tip

With current interest rates at fairly low levels, you might want to consider an income-splitting loan to your spouse or common-law partner. The attribution rules won’t apply if you are paid interest on the loan at the prescribed rate in effect at the time the loan is made. For example, the prescribed rate in effect for the third quarter of 2014 is 1%. This rate will remain in effect for as long as the loan is outstanding—even if rates increase in the future.
In implementing any income-splitting strategy, you have to be careful if you want to avoid the attribution rules. In situations where property is transferred to your spouse or common-law partner, attribution can apply to both income and capital gains. Contact your tax adviser to discuss the steps you need to take to accomplish this or other income-splitting strategies.

Transfers to other family members
A transfer of capital property to other family members is taxed just as if you sold the property at its FMV. If the property has been transferred to a child, grandchild, niece or nephew, you must continue to report any income earned on such property after it has been transferred—such as interest or dividend income—until the child reaches 18 years of age. After 18, attribution no longer applies and that individual must report the income. Capital gains, on the other hand, do not have to be attributed to you (regardless of the age of the child). This can be a useful income-splitting tool. However, make sure that any capital gain realized by a minor child is not subject to the “kiddie tax” rules (see topic 114).

Tax tip
Unless the person receiving the property is your spouse or common-law partner, there is no requirement to attribute capital gains to you, the transferor. Consider buying in the names of your children capital property (such as equity-based mutual funds) with a low yield but high capital gains potential. The income will be attributed to you, but any future capital gains will be taxed in your children’s hands.
Tax tip

The deemed cost base of property received as a gift or inheritance is its FMV at the time of transfer. However, if you charge a nominal amount for the transfer of property—for example, $10—you're deemed to receive FMV for the property, but the recipient's cost base remains at $10. Therefore, it's better to gift property than to charge a nominal amount, since the recipient will receive the full increase in the cost base.

Interest-free loans to family members
Caution should be exercised if you provide low-interest or interest-free loans to family members, either to enable them to purchase income-producing assets or as consideration for the transfer of assets. If one of the main reasons for the loan is to reduce or avoid tax, you must report any income earned on the property, regardless of the age of the loan recipient. An outright gift to a child who is 18 years or older—or anyone other than a spouse or common-law partner—is not subject to this rule.

110 Registered Education Savings Plans (RESPs)
An RESP is a type of trust through which you can save for a child’s education. If you make contributions to such a plan, the amounts are not tax deductible, but the major advantage is that earnings accumulate on a tax-deferred basis. Also, when the funds are finally paid out to the child, the accumulated income earned in the plan (such as dividends or interest) is taxed in your child’s hands at his or her lower tax rate.

RESPs are often set up as family plans. This allows you to allocate the plan assets among related children or change the beneficiary of the plan to someone else in the family. Individual plans now have this same flexibility.

An RESP has a maximum life of 35 years and contributions can only be made until the beneficiary reaches 31 years of age. The contribution and termination period is extended by 10 years for beneficiaries who qualify for the disability tax credit (see topic 80).
To enroll your child in an RESP you must obtain a Social Insurance Number (SIN) for the child.

**Contributions**

There is no annual contribution limit and the cumulative ceiling is $50,000 for each beneficiary, regardless of the number of subscribers. Overcontributions are computed at the end of each month and are subject to a special 1% monthly tax. It’s possible to reduce overcontributions by withdrawing funds from an RESP.

**Transfer to an RRSP or RDSP**

If all intended beneficiaries have reached the age of 21 years, and the plan has been in place for at least 10 years, you can withdraw the principal and the income from the plan. If you have sufficient RRSP contribution room, you can transfer the RESP income to your RRSP (or a spousal RRSP). Any excess income that cannot be transferred to an RRSP will be subject to a 20% penalty tax, in addition to regular income tax.

For transfers after 2013, investment income earned in an RESP can also be transferred on a tax-free basis to an RDSP provided the plans share a common beneficiary.

The total RESP income that you can transfer to an RRSP is subject to a lifetime limit of $50,000.

**Canada Education Savings Grants (CESGs)**

The federal government pays a subsidy for each child that is a beneficiary of an RESP from the day the child is born until his/her 17th birthday. The current annual maximum CESG per beneficiary is $500 (i.e., 20% of the first $2,500 of contributions paid annually). Each child is entitled to a cumulative limit of $7,200.

A family that did not contribute to its child’s RESP for a year or more can receive a grant of not more than $1,000 as a

---

21 Contributions for a child aged 16 or 17 will receive a grant only if certain conditions are met.
CESG in a year (i.e., on a maximum contribution of $5,000).22

The maximum annual grant on the first $500 contributed per child is increased slightly for low- and mid-income families.

An RESP will be required to repay CESG money in certain situations, such as when a beneficiary does not pursue higher education or the plan is terminated.

Canada Learning Bond (CLB)
Under the Canada Learning Bond (CLB) program, every child is entitled to assistance, provided the family receives the National Child Benefit (NCB) Supplement.23 An initial $500 bond is provided in the year of the child’s birth with subsequent annual instalments of $100 until the age of 15 for each year the family is entitled to the NCB supplement.

111 Registered Disability Savings Plan (RDSP)
The RDSP is intended to encourage saving for the long-term financial security of a person eligible for the disability tax credit. An RDSP may be set up by the disabled person, a parent or a legal representative. Once it has been set up, anyone can contribute to the plan for the benefit of the beneficiary up to a lifetime maximum of $200,000 per beneficiary. There is no annual limit. Contributions may be made until the end of the year the beneficiary attains 59 years of age.

Grants and bonds available
RDSP contributions qualify for a Canada Disability Savings Grant (CDSG) at matching rates of 100%, 200% or 300%, depending on family net income and the amount contributed, subject to a lifetime limit of $70,000. An RDSP will be eligible to receive a CDSG until the end of the year in which the beneficiary reaches 49 years of age. In addition, a Canada Disability Savings Bond (CDSB)

---

23 Families whose net income is equal or less than $43,953 receive the National Child Benefit Supplement (reduced when net family income exceeds $25,584).
of up to $1,000 is paid annually to the RDSPs of low- and modest-income beneficiaries and families (subject to a lifetime limit of $20,000).

In recognition of the fact that families of children with disabilities may not be able to contribute regularly to their plans, the rules provide for a 10-year carry-forward of CDSG and CDSB entitlements. Upon opening an RDSP, CDSB entitlements will be determined and paid into the plan for the preceding 10 years,24 based on the beneficiary’s family income in those years. CDSGs will be paid on unused entitlements, up to an annual maximum of $10,500.

Under previous rules, when an amount was withdrawn from an RDSP, all the CDSGs and CDSBs (and related investment income) paid into the RDSP in the preceding 10 years had to be repaid to the government (subject to certain exceptions). There is now a proportional repayment rule that applies when a withdrawal is made from an RDSP in 2014 or later. For every $1 withdrawn from an RDSP, $3 of any CDSGs or CDSBs paid into the plan in the 10 years preceding the withdrawal must be repaid, up to the maximum of the assistance holdback amount—which is generally defined as the total amount of bonds and grants paid into an RDSP within a particular 10-year period.

Example

Jane opens an RDSP in 2009 and contributes $1,500 to her plan annually, attracting the maximum amount of CDSGs ($3,500) each year. In 2014, the assistance holdback amount for her plan is $21,000. In 2014, Jane withdraws $600 from her RDSP. Under the 10-year repayment rule, the entire assistance holdback amount ($21,000) would have to be repaid. Under the proportional repayment rule, only $1,800 of the assistance holdback amount has to be repaid. The plan’s assistance holdback amount will be reduced to $19,200.

24 But not before 2008, the year RDSPs became available.
Payments
Payments from an RDSP must start before the end of the year the beneficiary attains 60 years of age. Prior to 2014, the rules limited the minimum and maximum amount that could be withdrawn annually. New rules provide greater flexibility for withdrawals from an RDSP after 2013.

Since the RDSP contributions are not deductible for tax purposes when they are made, they are not taxable when withdrawn. The investment income and the capital gains realized in the plan and the grants and bonds that have been put into the plan are taxable in the beneficiary’s hands when amounts are withdrawn from the plan.

End of plan
On the termination of the plan (e.g., the beneficiary ceases to qualify for the disability tax credit or dies), the funds in the RDSP are then paid to the beneficiary or his/her estate. The amount received, net of the contributions and any repayments, has to be included in the taxable income of the beneficiary for the year the amount is received or for the year of death.

Although the rules provide that a RDSP has to be terminated by the end of the year following the year the beneficiary ceases to qualify for the DTC, the plan may be able to remain open if a medical practitioner certifies that it is likely that the beneficiary will be eligible for the DTC again in the foreseeable future.

Rollover of RRSP/RRIF proceeds to an RDSP
Subject to certain limits, RRSP/RRIF proceeds can be rolled over to an RDSP for the benefit of the deceased’s financially dependent infirm child or grandchild. The rolled-over proceeds will reduce the beneficiary’s RDSP contribution room, but will not result in any CDSGs from the government.
Example

If you have an infirm financially dependent child or
grandchild, you should consider if any changes need
to be made, either in your will or by way of beneficiary
designations, to accommodate this new rule.

112 Splitting CPP benefits with your spouse or common-law partner

The Canada Pension Plan Act permits you to assign a portion of your retirement pension to your spouse or common-law partner.

For example, suppose you’re entitled to $10,000 in annual CPP benefits, but your spouse or common-law partner is entitled to only $4,000. This assignment will generally result in each of you receiving $7,000 annually. If your spouse or common-law partner is in a lower tax bracket than you, shifting this income to his or her hands helps lower the total family tax bill. The number of months you have lived together is a factor in determining how the benefits are split.

If you both receive a CPP retirement pension, the assignment must be made for both retirement pensions. But if only one of you receives a retirement pension, the assignment can only be made if the other spouse or common-law partner has reached 60 years of age and is not a contributor to the CPP.

113 Income splitting with family members

Income splitting is a tax-planning technique designed to shift income from a taxpayer paying a high rate of tax to another taxpayer within the family unit paying tax at a lower rate. Unfortunately, there are a number of legislative provisions—“attribution rules” and other anti-avoidance measures—designed to prevent saving taxes by shifting income between taxpayers.
Permitted arrangements

There are still a number of legitimate tax-planning arrangements that can be used to effectively redistribute income in a family unit:

- Have your business pay a reasonable salary to your spouse or common-law partner or children (see topic 5).
- Make contributions to a spousal RRSP (see topic 55).
- Invest child tax benefit payments in your child’s name (see topic 97).
- Share CPP payments (see topic 112).
- Pension income splitting (see topic 71).
- Have the higher income spouse or common-law partner assume most or all of the personal household expenses, leaving the person with the lower income with as much disposable income as possible to invest.
- Transfer or sell assets to family members for FMV consideration (see topic 109).
- Gift to minor children capital assets that are appreciating in value so they can earn capital gains not subject to attribution (see topic 109). However, watch certain capital gains on private company shares (see topic 114).
- Make an income splitting loan (see topic 109).
- Use a management company. However, if the management company provides services to a professional who provides tax-exempt services under the GST, the taxable GST charge will present an absolute increase in cost that may outweigh the income-splitting benefits of the management company.
- Create testamentary trusts in your will to split income.25
- Contribute to an RESP (see topic 110).
- Give cash or other assets to your adult children (see topic 109). Gifts of cash could enable them to maximize their deductible RRSP contributions.
- Have your spouse or common-law partner and/or adult children participate in an incorporated business by owning shares acquired with their own funds. This would allow company profits to be distributed to them in the form of dividends.

25 See Topic 154 on proposed testamentary trust rules.
• Take advantage of the fact that income earned on income is not subject to the attribution rules. Although the initial income earned on property loaned to a non-arm’s-length person may be attributed back to the person making the transfer, income earned on that income will not be attributed.

It’s crucial that you confer with your tax adviser, who can review your personal situation and give you advice about which income-splitting strategies best fit your circumstances.

114 Income splitting using family trusts
Family trusts are often used to own shares in a private corporation. This can provide flexibility in the payment of dividends to different family members; a structure to minimize taxes paid by your family unit; multiple access to the qualified small business capital gains deduction (see topic 136); and some creditor-proofing for cash presently accumulated in your company.

However, there are rules to prevent income splitting with minors—these are referred to as the “kiddie tax” rules. These rules assess tax at the top marginal rate on taxable dividends from a private corporation received by any child under the age of 18. It doesn’t matter if the dividends are received directly or through a trust or other structure. The tax will also apply to income from property such as certain rental and financing income that is allocated to minor children. Income from property inherited from the minor’s parent is excluded from this rule. The “kiddie tax” also applies to capital gains allocated to a minor child from the disposition of shares to a non-arm’s-length person, provided dividends received on those shares would have been subject to the tax. Recent proposals will extend the tax to income paid to a minor from a trust or partnership if it is derived from a business or rental property for activities conducted with third parties, and a person related to the minor is actively engaged on a regular basis in the business or rental activity.
There is certain planning that can be done to deal with these rules. You should contact your tax adviser to review your situation and determine the best planning strategy.

115 Retroactive lump-sum payments
If you’ve received a retroactive lump-sum payment, you may be eligible for a special tax calculation to provide tax relief. The calculation will effectively recalculate your tax liability by assuming the lump-sum payment had been taxed in the year(s) to which it relates. It will only be applied where the calculation results in a decreased tax liability.

The following types of income qualify for this calculation:

- periodic superannuation or pension benefits
- Employment Insurance benefits
- spousal or child support amounts
- employment income payments received under a court judgement or arbitration award

The lump-sum payment must be at least $3,000, excluding any interest amount included in the payment.

116 Some income is tax-free
Almost all types of income are subject to income tax. However, there are some exceptions.

Lottery winnings in Canada and gains from casual gambling are not taxable. Proceeds from damage awards are generally tax-free and, under certain circumstances, income earned on damage awards for taxpayers under 21 years of age is also exempt until the taxpayer turns 21. Various defined payments to war veterans are also exempt.

Although Workers’ Compensation benefits and welfare payments are not directly subject to tax, the amounts are included in your net income (but not taxable income) for purposes of determining your eligibility for certain tax credits.

If you’re in receipt of pension income from a foreign country, you may be eligible to claim an offsetting
deduction from income. This will depend on the terms of the tax treaty between Canada and that country.

117 Taxation of non-competition payments
If you receive an amount in exchange for agreeing not to compete (for example, on the sale of shares or assets of your business), the amount received must be treated as ordinary income, subject to two main exceptions:

1. You and the purchaser jointly elect to have the amount treated as eligible capital property; or
2. You sell shares of a corporation or an interest in a partnership to an arm’s-length person. In this case, the amount will be treated as additional proceeds of disposition, unless the covenant has value over and above this amount. If so, the excess will be reported as income. You and the purchaser must also jointly elect to have this exception apply.

**Tax tip**
If you’re thinking of entering into a non-competition agreement on the sale of your shares or your business, you should consult your tax adviser to determine the tax consequences.

118 Taking up Canadian residence
If you become a resident of Canada during 2014, you’re generally deemed to have disposed of and immediately reacquired each property you own (with the exception of taxable Canadian property) at proceeds equal to its FMV on the date you take up residence. This FMV becomes your adjusted cost base when determining any future capital gain or loss.

If you were employed or carried on a business in Canada prior to becoming a resident, you’ll be taxed in Canada on that income for the part of the year you were a non-resident of Canada. Once you become a resident of Canada, you’re taxed in Canada on your worldwide income from the date you establish residency.
You are entitled to claim personal tax credits, but the amounts are generally reduced on a pro-rata basis according to the number of days in the year you are taxed on your worldwide income.

If you arrived from a country that has a tax treaty with Canada, any provision in the treaty that conflicts with the Canadian tax rules may override the Canadian rule.

It used to be good planning to set up a non-resident trust prior to becoming a resident of Canada (commonly referred to as an immigration trust). Foreign investment income could be sheltered from Canadian tax for a period of up to 60 months, provided income from the trust was not distributed to the Canadian resident who settled the trust. Proposals introduced in the 2014 federal budget will eliminate the tax benefits of such trusts. The proposals amend the non-resident trust rules to remove the 60-month exemption for taxation years ending after February 10, 2014. As a result, an immigration trust will be deemed resident in Canada and subject to taxation on its worldwide income. Limited relief is available for immigration trusts established and funded before February 11, 2014. The trust can continue to benefit from the exemption until December 31, 2014, as long as no contributions are made to the trust after February 10, 2014. However, the trust will become subject to worldwide income taxation starting January 1, 2015.

**Foreign pension plans**

If you become a resident of Canada, there may be Canadian tax consequences if your employer continues to contribute to a foreign pension plan on your behalf. In general, provided you have not been a resident of Canada for more than 60 months in the preceding 72-month period, and you were a member of the foreign plan prior to establishing Canadian residence, contributions by your employer won’t be subject to tax. However, membership in this type of foreign plan will diminish your ability to take advantage of Canadian tax-deferred savings plans, such as RRSPs, RPPs and DPSPs. Employer contributions outside these timelines may still be exempt from Canadian taxation,
provided your employer files an election, you were a plan member prior to becoming a Canadian resident and you are not a member of an RPP or DPSP.

Distributions received from a foreign pension plan while you’re a resident of Canada are generally taxable. However, the tax treaty between Canada and the foreign country may provide some relief.

119 Giving up Canadian residence
In general, if you cease to be a resident of Canada, you’ll be deemed to have disposed of and reacquired your capital property at its FMV on that date. You’ll be subject to tax on any taxable capital gain resulting from this deemed disposition.

These deemed disposition rules apply to all capital property unless specifically excluded. Such excluded property includes Canadian real estate, Canadian business property and certain other exclusions, such as retirement savings in RRSPs, stock options and interest in some trusts. Shares in a private company are not exempt from these rules. Therefore, if you own such shares, you must report a deemed disposition at FMV. Professional assistance will likely be required to obtain this value.

Tax implications
You can either pay the tax on the deemed disposition when you file your tax return for the year of emigration or you can opt to post security in lieu of paying tax for any particular property. The security will remain in place until the property is actually disposed of or until the taxpayer returns to Canada and “unwinds” the deemed disposition. As a relieving measure, security is not required with respect to the tax on the first $100,000 of capital gains that arise as a result of the deemed disposition rule.

If you subsequently dispose of property that has been excluded from the deemed disposition rules, you’re generally required to file a Canadian income tax return and pay tax on any resulting gain. In some cases, a return is not required, but the proceeds of disposition will be
subject to non-resident withholding tax (see topic 123). Other filings may also be required. There are also special rules if you leave Canada for only a few years to work or study. The rules in this area are complex, and professional tax assistance is required. Review the tax implications with your tax adviser prior to departure.

**Reporting requirement**

If you emigrate from Canada, you’re required to report your property holdings to the CRA if you own “reportable property” with a total value of more than $25,000 at the date of departure from Canada. Exceptions will be provided for personal-use property with a value of less than $10,000. Other exceptions include cash (including bank deposits) and the value of pension plans, annuities, RRSPs, RRIFs, retirement compensation arrangements, employee benefit plans and deferred benefit plans.

Form T1161 must be filed regardless of whether you’re subject to the departure tax discussed above. The requirement is also independent of the tax return requirement—you must file Form T1161 regardless of whether you’re otherwise required to file a return for the year of emigration. To avoid late-filing penalties, this form must be filed on or before your filing due date for the year of emigration from Canada.

**Tax tip**

The capital gains deduction is not available to a non-resident of Canada. If you have shares of a corporation that is a “qualified small business corporation” (see topic 136) or an interest in a farming or fishing operation (see topics 137 and 138), there may be opportunities to utilize the $800,000^26 capital gains deduction. Review this with your tax adviser, as extensive planning is required.

\(^{26}\) Indexed for inflation after 2014.
120 Temporary assignments outside Canada
Many assignments outside Canada are only temporary, ranging from a few weeks to several years. For income tax purposes, it’s important that you determine your residency status during the period you’re outside Canada. A resident of Canada is taxed on his or her worldwide income. Therefore, if you’re a Canadian resident for income tax purposes, any income you earn during an assignment abroad will be subject to Canadian tax.

Residency defined
Residence is a question of fact and the term “resident” is not defined in the Income Tax Act. The courts, however, have held that you’re a resident of Canada for tax purposes if Canada is the place where you regularly or customarily live.

In prior years, the CRA administratively took the position that, unless the circumstances indicated otherwise, you would likely be considered a non-resident if you were absent from Canada for two years or longer and you had severed your ties with Canada. It is now the CRA’s position that there is no particular length of stay abroad that necessarily results in an individual becoming a non-resident. In making a determination of residence status, all of the relevant facts in each case must be considered, including residential ties with Canada and length of time, object, intention and continuity with respect to stays in Canada and abroad.

Canada also has income tax treaties with a number of countries that contain tie-breaker rules to determine residency when you’re considered to be a resident of both Canada and the other country.

If you cease to be a resident of Canada for income tax purposes, special rules apply (see topic 119).

121 Canadian residents working in the United States
If you’re a resident of Canada but work in the United States, the Canada-US Tax Treaty provides special rules to determine how you are taxed. Provided you’re not a US citizen, you’ll be exempt from US taxation on
employment income earned in the United States if either of the following conditions is met:

- Your US employment income does not exceed US $10,000.
- You are present in the United States for less than 184 days in any 12-month period beginning or ending in the fiscal year concerned, and your remuneration is not paid by, or on behalf of, a person who is resident in the United States and is not borne by a permanent establishment in the United States.

If you do not meet either of the above tests, you must pay US federal and, if applicable, state income tax in the United States on your US-source wages (income is sourced to the jurisdiction where the services are performed, not where you’re paid from). You will also have to report this income on your Canadian tax return. To avoid double taxation, you will generally be allowed to claim a foreign tax credit on your Canadian return for any tax you pay to the United States. You should note that the individual US states are not bound by the treaty. Therefore, even though you may be subject to an exemption from US federal tax under the treaty, there is no guarantee that you will not be subject to a state’s income tax. If you do any significant amount of work in the United States, it’s best to consult with your tax adviser to determine your Canadian and US filing requirements.

If you’re self-employed, the rules are different. US-source self-employment income is not subject to US tax if you do not have a fixed base or permanent establishment in the United States. In such cases, you’ll be required to file a treaty-based return if you are relying on the treaty to exempt you from US tax. Again, you may be subject to a state’s income tax even if you are exempt from US federal tax under the treaty. However, you should keep track of the number of days you are present in the US as you may be deemed to have a permanent establishment in the US if you or your employees spend significant time in the US in any twelve month period.
122 Canadian tax obligations for non-residents
A non-resident of Canada (see topic 118 for residency) is subject to Canadian income tax on certain types of income from Canadian sources, including

- income/loss from employment in Canada,
- income/loss from a business carried on in Canada, and
- capital gains/losses from dispositions of taxable Canadian property (see topic 123).

A non-resident of Canada is required to file a special income tax return (Income Tax and Benefit Return for Non-Residents and Deemed Residents of Canada) to report the above sources of income. A non-resident who doesn’t have a social insurance number is required to obtain an individual tax number (ITN). The ITN can be obtained by completing Form T1261, “Application for a Canada Revenue Agency Individual Tax Number (ITN) for Non-Residents.” Although certain deductions and tax credits are allowed, there are some restrictions.

Non-residents of Canada are not required to file a Canadian tax return if their only income from Canada is from certain types of passive income, such as dividends, and pension income. In such cases, tax is withheld at source by the payer when the amount is paid to the non-resident. The general rate of withholding tax is 25%, but this may be reduced to a lower rate pursuant to the tax treaty that Canada has with the non-resident’s country. In the vast majority of cases, the non-resident may be able to claim a foreign tax credit in their country of residence for Canadian taxes paid. Rental income earned by a non-resident is also subject to the 25% withholding tax (on the gross rents received). However, in the case of real property rentals, there is the option for the non-resident to file a special return under Section 216 whereby tax is paid on the net income earned from the property. There are also additional procedures and filings that can be undertaken to reduce the amount of tax withheld to that based on estimated net income.
Non-residents are also generally exempt from filing Canadian income tax returns if the following criteria are satisfied:

- No tax is payable by the non-resident for the current taxation year.
- Each taxable Canadian property disposed of in the year is either exempt from Canadian tax due to a tax treaty or a property for which the CRA has issued a clearance certificate to the non-resident (see topic 123).

**Tax tip**

If you’re a non-resident of Canada with Canadian-source income, you should consult a tax adviser to determine your tax obligations and ways to minimize your Canadian tax.

**123 Disposition of taxable Canadian property by non-residents**

As noted above, a non-resident of Canada is liable to pay Canadian income tax on capital gains from dispositions of “taxable Canadian property.” Taxable Canadian property includes real estate situated in Canada, capital interests in certain partnerships and trusts, and shares of some corporations, certain business assets used in a business carried on in Canada and, in some cases, a Canadian resource property, a timber resource property, an income interest in a trust and a life insurance policy in Canada. “Taxable Canadian property” excludes shares of corporations (and partnership interests and interests in trusts) that did not, at any time during the preceding 60 months, derive their value principally from real or immovable property situated in Canada, Canadian resource property or timber resource property.

The purchaser of taxable Canadian property is required to withhold tax from the purchase price and remit it to the CRA unless the non-resident vendor obtains a “clearance certificate” from the Minister of National Revenue verifying that the non-resident vendor has made arrangements for the payment of any resulting tax. There’s another exemption from the withholding tax requirement where the purchaser...
concludes after reasonable inquiry that the vendor is resident in a country that has a tax treaty with Canada;
• at the time of the disposition, the applicable tax treaty provides that the property is treaty-protected; and
• the purchaser sends to the CRA, no later than 30 days after the date of the acquisition, a notice setting out basic information about the transaction, the vendor and the purchaser.

This exemption is intended to ease the administrative burden by allowing an exception for withholding tax in a situation in which there will ultimately be no Canadian tax liability due to an exemption under a tax treaty. However, the onus is on the purchaser to confirm the vendor’s country of residence, as well as the fact that the property disposed of is treaty-protected.

124 US persons resident in Canada
The United States taxes its citizens, residents and green-card holders (collectively, US persons) on their worldwide income, regardless of whether they live in the United States. As a result, if you’re a US person living in Canada, you’re generally required to file both a Canadian and a US income tax return.

Although there are several mechanisms in place to prevent double taxation, the many differences between the two tax systems can still lead to unexpected tax liabilities—for example, capital gains or losses on the sale of capital property, exempt municipal bonds, income earned in a TFSA and RESP, and many others. In 2013, the US introduced a new Net Investment Income Tax which can create a US tax liability which cannot be offset with a foreign tax credit for Canadian taxes paid. For this reason, you should always obtain professional tax advice if you’re a US person residing in Canada. Based on your holdings, special US reporting (in addition to income tax filings) may be required.

Filing your returns
For Canadian tax purposes, each taxpayer must file a separate return. For US tax purposes, you have the option
of filing a joint return with your spouse. If your spouse has little or no income, but you’re paying tax to the United States, filing a joint return will generally be beneficial.

If your spouse is not a US person, you can still file a joint return, but the rules are a little more complicated. First of all, you must file an election to treat your non-resident spouse as a US resident. Once this election is made, your spouse must file a US income tax return each year until the election is revoked. Once revoked, the election cannot be reinstated. During the years in which the election is in force, you and your spouse may decide annually whether to elect to file a joint return. This decision can change from year to year. A discussion with your tax adviser is recommended.

If you’re a US person, you’re generally required to file a US tax return even if you owe no US tax. If you have not been filing a US return, you should get professional advice. As well as filing a tax return, you may also be required to disclose a substantial amount of other financial information to the US government. US legislation has significantly increased penalties for non-compliance. There are special voluntary disclosure programs and new guidance available from the IRS for US persons who are delinquent in some or all of their US tax and financial information filings. If you are not compliant with your US tax obligations, you should discuss your options with your tax adviser.

If you’re a US person living in Canada, you have an automatic extension to June 15 to file your US tax return, but any tax due must be paid by April 15. Interest will be charged on any unpaid tax from April 15, but no late-filing penalties will be assessed if you file by June 15 and attach the required statement to your tax return. You can also receive an automatic extension to October 15 if you file an application and pay at least 90% of your final tax liability. Late-filing income tax penalties are assessed only if there’s a balance due on your return. Therefore, if there’s no balance due, you should not be subject to any late-filing income tax penalties.
Ownership of registered savings plans by US persons
If you’re a US citizen, permanent resident visa (green card) holder or US resident, and you hold an interest in a Canadian RRSP or RRIF, you should contact your tax adviser to determine your filing obligations under these rules. In many cases, you are well-advised to make a special election under the Canada-US tax treaty to defer the US taxation of income earned in the RRSP until such time as a distribution is made from the plan. IRS Form 8891 must be filed as part of this election. The filing requirements are more complex in situations where you have received a distribution from the plan during the year. There are also special reporting requirements for RESPs, RDSPs and TFSAs as they are not deferred plans under US tax rules.

125 US Social Security payments
US social security benefits received by residents of Canada are only subject to tax in Canada. The United States will not tax these benefits pursuant to the Canada-US Treaty.

Generally, Canadian residents receiving US social security benefits are required to include 85% of those benefits in computing their Canadian income. However, the inclusion rate is 50% for Canadian residents (and their spouses or common-law partners eligible to receive survivor benefits) who have been in receipt of benefits since before January 1, 1996.

The full amount of benefits received is included in net income for purposes of assessing various clawbacks and other net income-based calculations: the OAS clawback (see topic 72) and the age credit (see topic 79). The non-taxable amount (15% or 50%) is claimed as a deduction from net income in calculating taxable income.

27 Collectively defined as ‘US Persons’ under the relevant legislation.
**Tax tip**

Make sure you consider applying for US social security if you have ever worked in the US in the past. You could be surprised at your benefit entitlement!

---

**US real estate owned by Canadian residents**

If you’re a Canadian resident who receives rent from US real estate, you’re normally subject to a US withholding tax of 30% of the gross amount of any rent paid. As an alternative, you can elect to pay tax on the US rental income you receive on a net basis. In this case, you must file a US tax return at the end of the year, reporting your net rental income. By making this election with the IRS and providing appropriate information to the tenant, the 30% withholding tax is not required. Once you make this election, it’s permanent and can only be revoked in limited circumstances.

Many people mistakenly assume that because their expenses always exceed their rental income, there’s no need to file a US tax return or to have tax withheld at source. The IRS requires that a withholding agent (such as a real property manager who collects the rent on behalf of the non-US resident) be personally and primarily liable for any tax that must be withheld from the rental income. If the non-resident fails to submit a timely filed return, not only will the withholding agent be liable for outstanding amounts, interest and penalties, but also the non-resident will lose the ability to claim deductions against the rental income causing the gross rents (instead of net rents) to be subject to the 30% tax.

In addition, unlike Canadian tax rules, depreciation is a mandatory deduction in the US. If you don’t file a return, you’re still deemed to have claimed depreciation and could be subject to recapture. Failure to file a tax return also reduces your ability to carry forward passive activity losses since the IRS has no record of them. As a result, on a subsequent sale of the property, you would have a taxable income inclusion in the form of recapture with no offsetting loss carry-forward.
Tax tip

Professional advice should be obtained if you receive rental income from US real property and have not filed a US tax return because your expenses exceed your rental income.

Selling your US property

The general rule is that 10% must be withheld from your gross proceeds on the sale of US real property if you are not a US person. There are certain exceptions to this rule. For example, this withholding won’t apply if the property is sold for less than US$300,000 and the purchaser intends to use the property as a residence. Also, you can apply to the IRS to have the withholding tax reduced if the expected tax liability on the sale will be less than 10% of the sale price.

Regardless of the amount of withholding tax, the gain on the sale of any US property is still taxable in the United States and a US tax return must be filed. The 10% withholding is applied against the tax balance owing in the US. If the tax is less than the 10% withheld, you’ll receive a refund for the difference. You should ensure that you apply for a US Individual Taxpayer Identification Number (ITIN) as part of the withholding tax process to ensure the tax gets properly credited to your account with the IRS.

The US tax paid on the sale generates a foreign tax credit that can be used to reduce the Canadian tax payable on the sale. If you’ve owned the property continuously since before September 27, 1980 for personal use only, there’s a provision in the Canada-US tax treaty that can be used to reduce the gain. In such cases, professional advice should be sought.

127 Withholding tax on income from US sources

If you are not a US person and you receive certain types of income from US sources—such as dividends, royalties or annuities—you’re generally required to complete Form W-8BEN to benefit from the reduced rates of withholding tax under the Canada-US treaty. If this form is not remitted to the payer of the income, the payer is required to withhold
up to 30% on any reportable distributions. Certain types of US source interest income also require completion of the Form to avoid withholding at 30%.

128 US estate tax
If you die owning certain US property, your estate could be subject to US estate tax. Estate tax applies to the fair market value, net of liabilities, of the US property at the time of your death. US citizens are subject to estate tax on their worldwide estates. However, Canadian residents who are not US citizens are only taxed on certain US properties, such as US real property, shares of US companies, tangible personal property located in the US and debts issued by US residents, including the US government.

For 2014, the US estate tax exemption amount for a US citizen is $5.34 million with a top estate tax rate of 40%. In general, if the estate of a non-US person resident in Canada is less than this exemption amount, there should be no US estate tax. It’s important to note that even if a Canadian estate has a value which is less than the exemption amount, there may well be a requirement to file a US Estate Tax Return. Consult with your tax adviser if you are unsure about your obligations.

Tax tip
Do you own or are you about to acquire property situated in the United States? If so, consult your tax adviser to review your exposure to US federal estate tax. Planning strategies are available to defer, reduce or eliminate this potential liability.

129 US residency regulations
Many Canadians who regularly spend winters in the United States may find that they are required to fill out a special declaration—the Closer Connection Exemption Statement—to be exempt from paying US taxes.
To determine whether you are one of the Canadians who should file this declaration, you must add up the number of days (or part days) you spent in the United States in 2014, one-third of the days in 2013 and one-sixth of the days in 2012. If this calculation adds up to 183 days or more and you were present in the US for more than 30 days during 2014, you may be considered a US resident for tax purposes under US domestic tax law.

However, you can qualify for the “closer connection” exception if you meet the following provisions:

- You have not applied for a US permanent resident visa (green card).
- You were present in the United States for fewer than 183 days in 2014.
- You have maintained a permanent place of residence in Canada throughout 2014.
- You can claim a closer connection to Canada.
- You file the special declaration by June 15, 2015.

The “closer connection” form (Form 8840) cannot be filed late. If you miss the June 15 deadline, you must file Form 1040NR and make a treaty election to avoid US taxation. Green-card holders are not entitled to file this declaration. If you hold a green card, or if you spent more than 182 days in the United States in the current year, you’ll have to rely on the tie-breaker rules in the Canada-US tax treaty to avoid US resident status. In such cases, you’ll be required to file a treaty-based US tax return if you’re relying on the treaty to exempt you from US tax. However, the tax treaty does not relieve the requirement to file foreign reporting forms such as, for example, the FBAR (see Topic 130). As a cautionary note, the US Citizenship and Immigration Service has issued a warning to green-card holders that they may jeopardize their green-card status if they use treaty provisions to be taxed as a non-resident of the United States.
Tax tip

Over the past several years, the United States has issued numerous rules and regulations of concern to Canadians with interests in that country. If you spend a considerable amount of time in the United States each year, contact your tax adviser to ensure you’re complying with these rules.

130 US financial reporting requirements

US persons are required to file a “Report of Foreign Bank and Financial Accounts” (FBAR), FinCEN Form 114, each year if they have a financial interest in any financial accounts, including bank, securities or other types of financial accounts, in a foreign country, and if the aggregate value of these foreign (non-US) financial accounts exceeds $10,000 at any time during the calendar year. In addition, a US person who has signing authority over a foreign bank or financial account, even if they have no financial interest in the account, must also file this report.

Among others, this filing requirement will impact US citizens resident in Canada that have Canadian bank, investment, and registered accounts, such as RRSPs or RESPs, if the total value in all of their non-US financial accounts exceeds US $10,000 at any time in the 2014 calendar year.

The 2014 report must be e-filed with FinCEN by June 30, 2015. Since significant penalties can be assessed for failure to file the report when required, you should consult with your professional adviser to determine if you’re required to file this report.

Exchange of information between Canada and the United States

An agreement between Canada and the US was signed on February 5, 2014, under which Canadian financial institutions will be required to report to the CRA certain information that will then be provided to the Internal Revenue Service (IRS). The CRA will similarly receive

---

28 This includes US citizens or residents, US corporations, partnerships, trusts or estates.
financial information from the US in respect of Canadian residents who hold accounts at US financial institutions.

A variety of registered accounts (including RRSPs) and smaller deposit-taking institutions with assets of less than $175 million will be exempt from these reporting requirements.

This new reporting regime came into effect in July 2014, with information exchanges beginning in 2015.

131 Succession and estate planning
At a time when many baby-boomers are planning their retirement, the preservation and eventual transfer of your family assets are becoming a major concern. Estate planning aims to minimize the income tax consequences of meeting these objectives.

You will likely own capital property at the time of your death and, in most cases, there will be a tax liability associated with this property. Although you want your estate to be transferred in accordance with your wishes, you also want to pay as little income tax as possible. Therefore, planning has to be done during your lifetime. The main steps in the process include

- financial planning;
- estate freeze;
- life insurance;
- shareholders’ agreement, if any;
- powers of attorney in the event of incapacity;
- planned charitable giving, and
- will planning.

Succession planning
The family business brings together a number of players, including shareholders, family members and employees. The survival of a business will depend on the development and implementation of a succession plan. This involves the consideration of a number of issues:

- continuation of the business
- development of children’s talents
• preparation of succession
• choice of successor
• transfer of ownership, leadership and control of the business
• adequate retirement income
• reduction of income taxes

If you can determine your objectives in advance and start the succession process early, you have a better chance of succeeding.

Estate freeze/refreeze
You are deemed to dispose of all of your capital property at FMV immediately prior to death. This can produce a significant income tax liability in the year of death. While this deemed disposition can be deferred when assets are left to a spouse or a spousal trust, this is only a temporary solution to the problem and doesn’t solve the issue of eventual transfer to your children.

An estate freeze is a popular method of limiting death taxes. It consists primarily of transferring to a younger generation the growth potential of assets such as real estate or shares of corporations. By doing so, the asset value to the transferor is frozen at its value at the date of transfer. Accordingly, the amount of potential capital gain on death is also frozen. This will allow you to estimate your potential tax liability on death and better plan for the payment of income taxes.

You can usually accomplish an estate freeze through a transfer of assets to a corporation or an internal reorganization of capital. The mechanics can vary, but the transfer must be professionally planned to avoid the many punitive provisions of the Income Tax Act.

But what if the value of the frozen assets actually decreases after the date of the freeze? For example, assume you have an investment company that was frozen in the past few years while businesses and markets were still in bull mode, but now, due to the recent market turmoil, the value of the company is now less than it was on the date of the estate freeze. This presents an excellent tax-planning opportunity.
The previously frozen assets can be “refrozen” at the lower current value, and the future increase in value can accrue to other (generally younger) family members. If you have already undertaken an estate freeze, you should consider if now is the time to do a refreeze.

When new shareholders are brought in as part of an estate freeze, a shareholders’ agreement should be prepared. At the minimum, this agreement should ensure that there are provisions for the disposal of the company’s shares, either by means of a purchase, redemption or transfer. The financing for such transactions should also be considered.

Life insurance
Life insurance is a fundamental estate planning tool. If your estate has enough liquid assets, the payment of income taxes may not be much of a problem. But if a major portion of your estate consists of shares of private companies or real estate, it may not be possible to satisfy your tax bill on death without selling off the assets.

Funding potential income taxes through the purchase of life insurance can be an effective estate-planning tool. If sufficient insurance proceeds are available and the policies are properly structured, any income tax arising on the deemed dispositions of assets on your death can be paid without resorting to the sale of your assets. As insurance needs are constantly evolving, it’s important to review your coverage on a regular basis.

As a cautionary note, the government is always looking at ways to close “loopholes” and has recently put a stop to certain more aggressive planning strategies using life insurance. As changes can be announced at any time, it’s best to consult with your tax adviser before getting involved with any planning arrangement involving life insurance.
Tax tip

If you decide to acquire life insurance to fund any income taxes owing on the deemed disposition of your private company shares, plan carefully to determine whether you or your company should own the policy. Both options have different advantages. Consultation with your tax and insurance adviser is a must.

Asset transfers
If you have decided that you have more assets than you need, you can reduce your estate probate and executor fees, and possibly income taxes upon death, if you transfer assets during your lifetime. If these assets have increased in value since acquisition, however, the transfer could cause an income tax liability. You should carefully assess which assets to transfer, to whom, and how to avoid triggering a tax liability. Complicated rules apply to income and capital gains on gifts to spouses or common-law partners and children under 18 (see topic 109).

Alter-ego and joint-partner trusts
To avoid probate fees, will substitutes—such as inter vivos trusts—have been used to transfer assets to the beneficiaries. However, a gift of assets to a non-spousal trust that names other persons as beneficiaries usually results in a disposition of those assets at fair market value for income tax purposes. This can result in the payment of significant tax at the time of the transfer.

If you’re 65 years of age or older, alter-ego and joint-partner trusts can be used to avoid having to dispose of the assets at fair market value. One of the advantages of these types of trusts is that assets can be transferred to them on a tax-deferred basis, thereby avoiding triggering any tax on accrued gains. However, there will be a deemed disposition of all property in the trust on the day you or (where applicable) your spouse or common-law partner dies, whichever is later.
Another advantage of these trusts is that they can avoid the application of wills variation legislation in those provinces that have this legislation.

If you establish an alter-ego or joint-partner trust, you (or you and your spouse or common-law partner) must be entitled to receive all of the trust’s income prior to death, and no other person can obtain the use of any of the trust’s income or capital before your death (or that of your surviving spouse or common-law partner in the case of a joint-partner trust).

**Tax tip**

If you own assets with an accrued gain and live in a jurisdiction with high probate rates, talk to your financial adviser about the advisability of setting up an alter-ego or joint-partner trust.

**Planned giving**

The value of your estate—and, as a consequence, income taxes and estate administration fees—can be reduced by making charitable donations during your lifetime (see topic 81). The added benefit is that you also earn income tax credits during your life rather than on your death. Other benefits may include the reduction of probate fees and other estate costs.

Planned giving can take many forms. It can involve gifts of life insurance or the establishment of a private foundation, or can be as simple as reviewing your charitable objectives with a view to accelerating your intended donations now to maximize tax savings.

Since many of the planned-giving strategies involve the disposition of capital, you may also have to report income or a capital gain as the result of making a gift. As the name suggests, planned giving consists of planning and giving. “Planning” refers to a careful consideration of estate planning, financial planning and tax planning as part of making the gift. Your tax adviser can help you develop a planned-giving strategy that is most appropriate to your individual situation.
Will planning

Both you and your spouse or common-law partner should have wills. This is probably one of the most critical elements of your estate-planning strategy, as dying intestate (without a will) can defeat almost all the estate-planning arrangements you have put into place. If you die intestate, your assets will be distributed to your spouse, children and parents in accordance with the laws of the province where you resided. This may produce quite different results from what you would have wanted.

An up-to-date will sets down the parameters of your estate plan, indicating in particular the manner in which assets are to be distributed to your heirs and ensures that your wishes are respected. A will also makes it possible to minimize the taxes payable by your estate and your beneficiaries through the use of various provisions in the tax legislation such as testamentary trusts. Since amendments to the tax laws and changes in your personal situation might change your objectives, your will should be reviewed on a periodic basis.

Tax tip

A periodic review of your will is part of prudent estate planning. It should ensure that your assets will be dealt with in accordance with your wishes in the most tax-effective manner and that your will complies with current laws, such as provincial family law acts.

132 Deceased taxpayers

Executor’s responsibilities

A deceased’s legal representative is the person named in the will (executor) or a person appointed to handle the estate if there’s no will or executor.
From a tax perspective, the main responsibilities of the legal representative are as follows:

- File all tax returns for the deceased.
- Make sure all taxes are paid.
- Obtain clearance certificate or authorization from the tax authorities to distribute the assets of the deceased.
- Let the beneficiaries know which of the amounts they receive from the estate are taxable.

Government authorities and financial institutions should be notified as soon as possible of the date of death. The deceased’s social insurance number and date of birth must be provided if

- the person was receiving OAS, CPP or QPP benefits;
- the person was receiving the GST/HST or QST credit;
- the person or his/her spouse was receiving the CCTB or the UCCB;
- the person was a child in respect of whom the CCTB or UCCB was being paid; or
- the person was receiving benefits under a RRIF or RRSP.

**Instalments**

No instalments have to be paid for a deceased person for the period after the date of death. Nevertheless, the legal representative should ensure that any amounts due prior to the date of death were in fact paid.

**Canada Pension Plan (CPP) and Old Age Security (OAS) payments**

The CPP and OAS pensions are paid for the month during which the taxpayer died and have to be reported in the tax return of the deceased. Any cheques received for months following the month of death have to be returned to the federal government.

**GST/HST credit**

GST/HST credit payments are issued in July, October, January and April. If a single individual dies before one of these months, any payment must be returned to the government. If a person dies during the month the payment is made, the estate will be entitled to it.
If the deceased had a spouse, the surviving spouse may be eligible for the GST/HST credit. The spouse should contact the CRA and request any remaining credit for the year and file a tax return for the preceding year (if this has not already been done).

Canada Child Tax Benefit (CCTB) and Universal Child Care Benefit (UCCB)
If the deceased leaves a surviving spouse who is the father or mother of a child with respect to whom the deceased was receiving the CCTB (see topic 97) or the UCCB (see topic 98) benefit, the surviving spouse should contact the tax authorities to have the benefits transferred to her or him. If, on the other hand, the surviving spouse was the recipient of these benefits, he or she can ask the tax authorities to recalculate the benefits taking only his or her income into consideration.

If the person now responsible for the care of the child is someone other than the father or mother, this person has to submit a written request to the tax authorities to be recognized as eligible to receive these payments.

If the deceased was an eligible child, the benefit entitlement ceases the month following the death. Any amounts received in that or subsequent months have to be returned.

Tax filing obligations of the legal representative
As a legal representative, one of your main responsibilities is to ensure that the deceased’s taxes are paid. This may necessitate obtaining tax information that is available from the respective tax authorities. To have access to this information, you’ll have to present a copy of the death certificate, the deceased’s social insurance number and a certified copy of the will or other document to show that you’re the legal representative of the deceased person.

You must also file, where applicable, tax returns for the year of death and any prior years for which the deceased had not filed a tax return. In addition, for the year of death, you may be able to elect to file more than one return for certain types of income. These are referred to as the final
The deadlines for filing returns may vary depending on whether it’s a final return, an optional return or a return for a year prior to death.

In general, for the final return, you must comply with the filing dates for tax returns (April 30 of the following year or June 15 for taxpayers carrying on a business). However, you have up to six months from the date of death if this is later. For example, if a person dies on December 20, 2014, you have until June 20, 2015 to file the final return. On the other hand, if the taxpayer died on May 10, 2014, the filing deadline would be April 30, 2015.

Taxes must be paid no later than the filing due date for the returns, unless the filing date is June 15 (for taxpayers carrying on a business), in which case the payment date will be April 30. If a return is filed late, a late-filing penalty and interest are charged.

There may be as many as three other separate types of returns for a deceased taxpayer:

1. A “rights or things” return (see “Income,” below)
2. A return reporting business income
3. A return arising from a testamentary trust

The filing dates for optional returns and the payment of any balances owing are the same as those for a final return, except for the “rights or things” return, where the filing date and the date for the payment of any balance owing is one year following the date of death or 90 days after the date a Notice of Assessment or Notice of Reassessment is mailed with respect to the final return for the year of death (if this is a later date).

Income
The final and optional returns of a deceased taxpayer have to report all income for the period from January 1 of the
year of death to the date of death. Income earned after that date should generally be reported in the estate’s return.

All periodic amounts earned prior to death—such as salary, interest, rent and most annuities—must be reported in the final return, even if the deceased did not receive them before he or she died. This rule doesn’t apply if the amounts were not payable prior to death or if such annuities were considered as having matured at the time of death. If this is the case, certain income of this nature can be reported in an optional return.

“Rights or things” are income amounts that the deceased was entitled to receive before he or she died but that had not yet been paid. The main rights or things are

- employment income (salaries, commissions, vacation pay) owing by the employer but not payable at the time of death for a pay period that ended before the date of death, as well as retroactive payments paid pursuant to a collective agreement signed before the date of death;
- uncashed matured bond coupons;
- accumulated unpaid bond interest;
- unpaid dividends declared before the person died;
- OAS, EI and CPP benefits not yet received for a period ended before the date of death or for the month of death;
- work-in-progress if the deceased carried on a business and had elected to exclude work-in-progress when calculating income;
- retroactive payment of a disability annuity or EI benefit paid after the date of death, but to which the deceased was entitled prior to that date; and
- pension plan, RRSP or RRIF payments for the month of death that had not been received at the date of death.

If you elect to file an optional return, all rights and things have to be reported therein except those transferred to beneficiaries. Rights or things transferred to a beneficiary before the filing deadline for an optional return have to be reported by the beneficiary.
If the deceased was a beneficiary of a testamentary trust in the year he or she died, the fiscal year of the trust was not the calendar year, and the deceased died after the end of the trust’s year, income from the trust from the end of the trust’s year to the date of death can be taxed in an optional return.

If the deceased carried on business as a partner or sole proprietor and the fiscal year of the business was not the calendar year, the legal representative can elect to report the business income earned between the end of the fiscal year and the date of death in an optional return.

Capital properties
In general, deceased persons are deemed to dispose of all of their capital property at FMV immediately before death.

There is an exception to this rule for capital properties left to a spouse or common-law partner or a qualifying spouse trust. In this case, any capital gain or loss is deferred until the property is disposed of by the spouse or common-law partner or the spousal trust. The legal representative can still elect to have the transfer take place at FMV. For example, you might want to make this election if the deceased owned shares in a qualified small business corporation (see topic 136), owned qualified farm or fishing property (see topics 137 and 138), or had capital losses that had not yet been utilized.

Unused capital losses from prior years may be claimed in the year of death or the immediately preceding year. Available capital losses must first be used to reduce capital gains in those years. Any remaining capital losses may then be deducted from other sources of income, subject to a restriction based on the total capital gains deduction that has been claimed over the years. As these special rules on the deductibility of capital losses for deceased persons are quite complex, consult your tax adviser for further details.

There are also rules where a decrease in the value of investments held in an RRSP or RRIF that occurs after death but before the final distribution to the beneficiaries...
may be able to be claimed on the final return for the deceased (see topic 66).

Funeral and estate administration expenses
Funeral and estate administration expenses are personal expenses and are not deductible in calculating the income of the deceased or the estate.
Section 3 – Investors

133 Rental properties
If you owned a rental property in 2014, any net income or loss must be reported on your 2014 income tax return. Rental income is usually reported on a calendar-year basis. Any income or loss from a rental property you own outside of Canada must also be included in your return.

What can I deduct?
All reasonable expenses incurred in operating the property can be deducted. This can include the cost of insurance, property taxes, mortgage interest, electricity, heat, repairs and even advertising for tenants. If you borrowed money to make the down payment on the rental property, interest on that loan is also deductible. In certain circumstances, you may also be able to claim depreciation. However, you should be careful if you expect your expenses will consistently exceed your income from the property. If there is no reasonable expectation of making a profit from the investment, there is the possibility that your losses may be denied (see additional comments below).

Tax tip
Keep accurate records of all expenses relating to your rental property. Retain all receipts—make a small note on each one indicating what the money was spent on and why. It will help your adviser determine quickly if it’s a valid expense and eligible for deduction or depreciation.

Joint owner or partner?
If you have acquired a partial interest in a rental property, it’s important to know whether it’s in a partnership or in a joint venture. If you don’t know which it is, consult your tax adviser.

With an interest in a partnership, you must report your share of its net profit or loss on your personal tax return. Depreciation is calculated at the partnership level, not by each individual partner.
As a joint owner, you have to report your share of the revenue and expenses related to the property. Next, you calculate depreciation based on the cost of your share of the property. Your depreciation claim is independent of the depreciation that may be claimed by the other joint owners.

**How much can I claim for depreciation?**

In general, depreciation on a rental property cannot be used to either create or increase your rental loss. When more than one rental property is owned, all net rental income (or loss) is combined to determine the total income or loss for the year.

**What happens if I sell?**

Two different types of income may arise on the sale of your rental property. If you sell your property for more than its original cost, you have to report a capital gain to the extent that the proceeds exceed that cost. If the property was purchased before February 1994, some or all of this gain may have been eligible for the capital gains deduction. To take advantage of this, however, you should have made a special election when you filed your 1994 return (see topic 135).

You may also have to pay tax on income that represents previously claimed depreciation. If proceeds from the sale exceed the undepreciated capital cost (UCC) of the property, the excess, up to the original cost, is taxed as recaptured depreciation in the year of sale.

In some cases, where the property was destroyed or expropriated and another property was purchased, the gain and/or recapture may be deferred.

If you did not receive the full proceeds of the sale in the year of the sale, you may be able to claim a capital gains reserve (see topic 140). However, you cannot claim any reserve against the recaptured depreciation.
Terminal loss rules
You may have a terminal loss if the proceeds from the sale are less than the UCC of the property. You should consult with your tax adviser to assess whether this loss is deductible from your other sources of income. Based on your particular fact situation, the CRA could attempt to disallow the terminal loss on the basis that you had “no reasonable expectation of profit” from the rental of the property. This could be of particular concern where you have always reported net rental losses from the property.

There are also special rules that can reduce a terminal loss for tax purposes. If the building was sold together with the underlying land, the transaction is treated as if you sold two separate items. If the portion of the sale price attributed to the building is less than its undepreciated cost, you may be required to increase the portion allocated to the building and reduce the portion allocated to the land. This will result in a reduced terminal loss on the building.

These rules only apply to depreciable buildings and do not apply to a real estate developer who is holding real estate as inventory.

134 What about capital gains?
A capital gain occurs when you sell a capital property for more than its original cost. In general, half the gain is included in your income for the year. The other half is not subject to tax. Certain dispositions resulting in a capital gain are not subject to any tax (see topic 81).

When is a gain a capital gain?
In most circumstances, there is no set rule that determines whether a particular gain should be treated as a capital gain. Most individuals who invest in the stock market can treat their gains and losses as capital gains or losses. However, if you spend considerable time playing the market and/or borrow money to make your purchases, your profits or losses may be taxed in full as business income.

Similarly, if you bought a property intentionally to resell at a profit, the entire gain would be taxable, rather than
just half the gain. For example, taxpayers who purchase property for immediate resale—“flipping”—are subject to tax on the full gain, even though they may have spent little time on the venture and may have sold only one or two properties. In some cases, there is no clear-cut answer. If in doubt, consult your tax adviser.

**Tax tip**

Most taxpayers are eligible to elect capital gains treatment from the disposition of qualifying Canadian securities by filing Form T123. Once you make the election, however, all subsequent gains and losses from the disposition of qualifying securities will be recorded as capital gains and losses. Be sure you understand the implications of making this election before you file the form.

**Identical properties**

Subject to the special rules for stock option shares (see the following subsection), when you acquire securities that are exactly the same—for example, Class A common shares of XYC Corp.—the shares are pooled for purposes of determining your cost when you sell a portion of the shares.

**Example**

Assume you buy 100 shares today for $20 each (total cost $2,000) and 50 shares next month for $26 each (total cost $1,300). Your cost per share for tax purposes is $22 (150 shares at a total cost of $3,300). If you then sell 75 shares for $30 each, your capital gain is $600 \((30 – 22) \times 75\) shares.

There are also special rules if you own identical properties, some of which were acquired before 1972. In this case, two separate pools will determine the cost of the properties sold: one comprising the pre-1972 properties and the other for properties acquired after 1971. On a disposition, you’ll be deemed to have sold the pre-1972 properties before those acquired after 1971.
Sale of stock option shares
The cost base of shares acquired through stock option plans equals the sum of the option price plus the amount of any taxable employment benefit reported with respect to the shares. The amount of a deferred stock option benefit (see topic 37) is added to the cost base of the stock option share at the time the share is acquired, even though the amount is not taxed until the share is disposed of.

But what happens if you acquire shares under a company stock option plan and you already own other identical shares in the company, or if you exercise more than one stock option at the same time? If you sell only some of the shares, how do you calculate the tax cost of the shares sold? The rules in this area are extremely complex. Special rules deem the order in which the shares are disposed of. In addition, in certain cases, a special designation may be available that permits you to designate the new stock option shares as the shares being sold, provided they are sold within 30 days of exercising the option.

Tax tip
Before selling or otherwise disposing of shares acquired under a stock option plan, consult your tax adviser to determine the tax consequences and whether you qualify for the special designation.

135 Lifetime capital gains deduction
The capital gains deduction can be claimed with respect to three types of property: qualified small business corporation shares (see topic 136), qualified farm property (see topic 137) and qualified fishing property (see topic 138).

$100,000 capital gains deduction
The $100,000 capital gains deduction for other capital property (other than the three types listed above) was eliminated on February 22, 1994. At this time, everyone was permitted to make a special one-time-only capital gains election. In most cases, this election had to be made on your 1994 tax return. The election allowed you to opt to have a deemed disposition of any capital property you
owned on February 22, 1994, at any amount up to its fair market value on that day.

In most cases, the amount you elected as a deemed disposition became your new cost base. The election was made by filing Form T664 with your 1994 income tax return.

Tax tip

If you still own property for which a capital gains election was made, you should continue to monitor the revised cost base to ensure it’s taken into consideration on a subsequent sale of the property.

136 Qualified small business corporation (QSBC) capital gains deduction

Shares of a qualified small business corporation (QSBC) continue to qualify for the capital gains deduction. To qualify as a QSBC, a company must be a Canadian-controlled private corporation and at least 90% of its assets must be used in an active business in Canada. There are additional conditions that must be met for up to two years before the sale. Further complications may arise where there are investments in related companies.

Each individual is entitled to a lifetime cumulative capital gains deduction of $800,000, indexed to inflation after 2014. The maximum capital gains deduction available on the disposition of QSBC shares will be reduced by the amount of QSBC or other capital gains deductions previously claimed on any property.

The amount of capital gain that is eligible for the capital gains deduction may be affected by the balance in your cumulative net investment loss (CNIL) account (see topic 149) and if you have ever claimed an allowable business investment loss (ABIL) (see topic 142).

29 For dispositions on or after March 19, 2007 up to 2013 (inclusive), the lifetime limit was $750,000. Prior to March 19, 2007, the lifetime limit was $500,000.
In some cases, it may be appropriate to consider various tax-planning techniques that can be used to obtain the deduction. The end result of most of these planning strategies will be to increase the cost base of your shares for purposes of a future sale or deemed disposition. Professional tax advice on these matters is essential.

**Tax tip**

For a company to qualify as a QSBC at the time of a future sale, it may be necessary to take steps now to remove from the company non-active business assets, such as excess cash or portfolio investments. This can be as easy as having the company use its excess cash to pay off debts or pay dividends to its shareholders, or it may involve a corporate reorganization to transfer the non-active assets into a separate company.

**Election for private companies going public**

Shares of a public corporation do not qualify for the enhanced capital gains deduction. However, if you own shares in a small business corporation (SBC) that is about to go public, you can make an election to be treated as having disposed of all the shares of a class of the capital stock of the SBC immediately before it becomes a public corporation. The amount you can elect as the deemed proceeds of disposition can be anywhere between the cost and fair market value of the shares. The shares are deemed to be reacquired for the same amount. This will increase the adjusted cost base of the shares and reduce the amount of any future gain on those shares when they are ultimately disposed of.

**137 Qualified farm property capital gains deduction**

Qualified farm property is also eligible for the enhanced $800,000 capital gains deduction (again, reduced by the amount of capital gains deductions claimed on other property). The amount of gain eligible for this deduction may be affected by the balance in your cumulative net investment loss (CNIL) account (see topic 149) and if you have ever claimed an allowable business investment loss (ABIL) (see topic 142).
A qualified farm property includes
• a building used in carrying on a farm business;
• a share of the capital stock of a family farm corporation;
• an interest in a family farm partnership; or
• a qualified capital property used in carrying on a farm business, e.g., a quota.

In general, if you acquired certain property before June 18, 1987, and it was used in the business of farming by you or a member of your family, it will be qualified farm property, provided the property was used for farming in the year you sell it or in any five previous years during which you or a member of your family owned it.

If you acquired the property after June 17, 1987, you must normally have owned it for at least two years, been engaged in farming on a regular and continuous basis and earned more gross income from farming than from other sources. Similar rules also apply to allow the deduction to be claimed for gains realized on the sale of shares of a family farm corporation and on an interest in a family farm partnership.

However, if you made a capital gains election (see topic 135) on property that would otherwise be considered qualified farm property, the qualifying tests may be different than outlined above. Discuss this with your tax adviser.

138 Qualified fishing property capital gains deduction
Qualified fishing property is also eligible for the enhanced $800,000\(^{30}\) capital gains deduction. Similar to the rules for farm property and small business shares, the available capital gains deduction will be reduced by the amount of capital gains deductions claimed on other property. In addition, the amount of gain eligible for this deduction may be affected by the balance in your cumulative net investment loss (CNIL) account (see topic 149) and if you have ever claimed an allowable business investment loss (ABIL) (see topic 142).

\(^{30}\) Qualified fishing property became eligible for the deduction effective for dispositions of property after May 1, 2006.
A qualified fishing property includes

- real property and fishing vessels used in a fishing business;
- eligible capital property, such as an interest in a fishing license;
- a share of the capital stock of a family fishing corporation; or
- an interest in a family fishing partnership.

The 2014 federal budget introduced proposals to accommodate persons (individuals, partnerships and corporations) involved in a combination of farming and fishing.

Prior to 2014, a property used in a combination of farming and fishing could qualify for the lifetime capital gains deduction only if it was used principally (generally interpreted as 50% or more) in one of those activities. Effective for dispositions in 2014 and subsequent years, eligibility for the enhanced deduction is extended to property that is used principally in a combination of farming and fishing.

139 Capital gains deferral for investments in small businesses

If you realize a capital gain on the disposition of shares of a small business corporation, you may be able to defer tax on the capital gain if the proceeds from the disposition are reinvested in another eligible small business investment. Eligible investments are newly issued common shares in an SBC with assets not exceeding $50 million after the investment.

To qualify, the shares disposed of have to satisfy certain criteria, and the proceeds must be reinvested in the eligible small business within 120 days after the end of the year.

There is no limit to the amount of the gain that can be deferred. The cost base of the new investment is reduced by the capital gain deferred.
140 Capital gains reserves
When you sell capital property, such as real estate or shares in a corporation, and the proceeds from the sale will not all be receivable in the year of sale, you can defer a portion of the capital gain by claiming a reserve.

The rules provide that at least one-fifth of your taxable capital gain must be reported in the year of sale and each of the four following years. An exception is provided if you transfer certain farm property, fishing property or shares in an SBC to your children. In these cases, you can claim a reserve over a maximum 10-year period. Reserves deducted from income in one year must be added to income in the subsequent year.

Tax tip
Claiming a reserve is optional—any amount up to the maximum allowed can be claimed. To make a claim, you must file Form T2017 with your income tax return.

Capital gains reserves included in income will be eligible for the capital gains deduction if the property is a share of a QSBC, a qualified farm property or a qualified fishing property (see topics 136, 137 and 138).

Tax tip
In structuring the sale of property, make sure you have sufficient funds to pay the taxes required. If proceeds are deferred over a long period, the tax may be due before the proceeds are received. Suppose you sell real estate for a significant capital gain in 2014 and the proceeds are due over the next 10 years. The taxes arising on the capital gain must be paid in full by 2018, even though all proceeds will not be received until 2023.

141 Capital loss rules
Generally, capital losses are only deductible against capital gains. Capital losses can be carried back for up to three tax years and forward indefinitely.
There are also special rules—often referred to as “stop loss” rules—that will deny a capital loss in certain situations. For example, if you transfer a property with an accrued loss to an “affiliated person,” the loss will be denied. In general, you’re affiliated with yourself and your spouse or common-law partner and with a corporation that you control, or you and your spouse or common-law partner control—but not with your children.

Similar rules will deny the loss if you sell investments with an accrued loss and the property or an identical property is acquired by you or your spouse or common-law partner within the period beginning 30 days before and ending 30 days after the disposition, and it is still owned 30 days after the disposition.

**Tax tip**

If you realized a capital gain in the current year, consider selling investments with accrued losses before the end of the year. Keep in mind that transactions involving publicly traded securities take place on the settlement date, which is generally three business days after the trading date in the case of Canadian stock exchanges.

142 Allowable business investment losses (ABILs)

An allowable business investment loss (ABIL) is one-half of a capital loss incurred on the disposition of a share or debt of an SBC. Unlike capital losses, an ABIL is deductible against any other source of income, not just capital gains.

However, this loss must be reduced by any capital gains deduction claimed in previous years, and net capital gains qualifying for the capital gains deduction are reduced by such losses incurred since 1985, including the current year.
Example

You realize a capital gain of $800,000 on May 15, 2014 on the sale of qualifying small business shares, but you claimed a business investment loss of $200,000 in 2005. You will only be entitled to a capital gains deduction of $600,000 in 2014.

Specific conditions must be met before a capital loss can be classified as a business investment loss. You should consult with your tax adviser if you realize a capital loss on the disposition of shares or debt of an SBC. In some cases, you may have to make a special election with your tax return in order to claim the loss as a business investment loss.

143 Taxation of dividends

There are three types of dividends you can receive from your corporation: an “eligible” dividend, a regular dividend (also referred to as an “ineligible” dividend) or a capital dividend (capital dividends are received tax-free).

Eligible-dividend rules

These rules apply to certain dividends paid after 2005 by corporations resident in Canada to shareholders resident in Canada.

Dividends and individuals

For 2014, dividends designated as eligible dividends are subject to a dividend gross-up of 38% and a federal dividend tax credit equal to 20.73% of the actual dividend.

Taxable dividends from Canadian resident corporations that are not designated as eligible dividends are ineligible (or regular) dividends. For 2014, these dividends are subject to an 18% dividend gross-up and a federal dividend tax credit equal to 13% of the actual dividend. The provinces all have their own dividend tax credit rates (refer to the individual tax tables for a comparison of the top marginal eligible and ineligible dividend rates by province).
As a result of the dividend gross-up and tax credit mechanism, dividends are taxed more favourably than most other types of income (except for capital gains). In a few provinces/territories (Alberta and the Yukon for 2014), eligible dividends are taxed at a lower rate than capital gains.

Dividends received from a foreign corporation are not subject to the gross-up and dividend tax credit mechanisms. Therefore, you’ll pay a higher rate of tax on dividends from a foreign corporation.

Dividends and corporations
A corporation’s ability to pay an eligible dividend depends on its status. A Canadian-controlled private corporation (CCPC) can only pay an eligible dividend to the extent that it has a balance in its “general rate income pool” (GRIP) at the end of the taxation year in which the dividend is paid. Although the actual formula is quite complex, the GRIP generally reflects taxable income that has not benefited from preferential tax rates, such as the small business rate, or from refundable dividend tax treatment afforded to investment income earned by a CCPC. There is an exception for public company dividends that have been designated as eligible dividends. Such dividends retain their status as eligible dividends when they pass through a private corporation.

A non-CCPC that is resident in Canada can pay eligible dividends without restriction, unless it has a balance in its “low rate income pool” (LRIP) at the time the dividend is paid. The LRIP is generally made up of taxable income that has benefited from the small business deduction, either in the hands of the dividend-paying non-CCPC itself (at a time when it was a CCPC) or in the hands of a CCPC that paid an ineligible dividend to the non-CCPC. Many non-CCPCs will never have an LRIP, and thus will be able to designate all of their dividends as eligible dividends. However, if a non-CCPC does have an LRIP balance, it must reduce its LRIP through the payment of ineligible dividends before it can pay an eligible dividend.
Designating a dividend as an eligible dividend

For a dividend to be an eligible dividend, it must be designated as such in writing by the corporation paying the dividend. For private corporations, the CRA has indicated that proper notice will include: (i) a letter to the shareholders; (ii) a notation on dividend cheque stubs; or (iii) in cases where all shareholders are directors, a notation in the corporate minutes. The notification procedure for public corporations is more simplified. Before or at the time the dividend is paid, the corporation only needs to make a designation stating that all dividends are eligible dividends unless indicated otherwise. This designation can generally be found on the corporation’s Web site (under Investor Services). For eligible dividends paid after March 28, 2012, the CRA will accept a late designation (i.e., after the time the dividend is paid) at its discretion in certain limited situations. An example would include a corporation making such a request because it faces circumstances beyond its control preventing it from designating dividends by the payment date. The corporation must make the designation no later than three years following the day on which the dividend was paid.

Any taxable dividend paid prior to March 29, 2012 had to be paid as either a designated eligible dividend or a non-eligible dividend. Split-dividend designations were not permitted. For taxable dividends paid after March 28, 2012, a corporation can designate any portion of a taxable dividend to be an eligible dividend.

If a corporation makes an eligible dividend designation that exceeds its capacity, the corporation will be subject to a penalty tax. However, there are special rules that may allow the corporation to retroactively undo all or part of an excessive designation by making an election to treat the excess eligible dividend as being a taxable dividend.
Tax planning guide 2014–2015

III – Investors

SYSTÈME FISCALL’INDIVIDU ET SA FAMILLE

INVESTORS

SANTÉEMPLOYÉS

Tax tip

If you’re the owner-manager of a CCPC and you want to pay a dividend from the company, consult with your tax adviser to determine if all or part of the dividend should be designated as an eligible dividend.

Tax tip

If you have no other sources of income, you can receive a significant amount of Canadian dividend income and pay little or no tax. The amount will vary depending on your province of residence at the end of the year and whether the dividend is an eligible or an ineligible dividend. Note, however, that alternative minimum tax (see topic 157) may apply—in particular, on the receipt of eligible dividends.

Foreign spinoffs

If you receive shares of a foreign corporation from another foreign corporation as part of a “spinoff” transaction, you may have to report foreign-source dividend income.

However, if the transaction was not a taxable transaction in the US, you may be able to make a special election that will allow you to avoid being taxed on the foreign-source dividend. You can elect to take advantage of the deferral by including a letter with your tax return for the year in which the distribution occurs. Under the taxpayer relief provisions (see topic 166), a taxpayer is allowed to late-file this election.

To qualify for the deferral, shares must be distributed by an actively held and widely traded US public corporation. In addition, US tax law must provide for a tax deferral to the distributing corporation and its US resident shareholders.

If the election is made, there’s a cost-base adjustment to the original and spinoff shares based on their relative fair market values.
Tax tip

If you receive or have received shares of a foreign corporation as part of a share restructuring, you might qualify for a tax deferral or tax refund under these rules. You should contact your tax adviser to determine if you qualify and to assist you in making the special election.

144 Transfer of dividend income between spouses
If your spouse or common-law partner has little or no income except for taxable dividends from Canadian corporations, you may be able to reduce your family’s tax bill by including his or her dividends in your income. The election must apply to all of your spouse or common-law partner’s dividends from taxable Canadian corporations—you cannot pick-and-choose.

You can only do this if it results in your being able to increase the claim you make for your spouse or common-law partner as a dependant.

145 Taxation of interest income
With the exception of certain investments made before 1990, you’re required to report interest on investments on an annual basis, regardless of when the interest is actually paid. Similar rules apply to certain life insurance policies and annuity contracts. For investments purchased before 1990, you have the option of reporting interest income on either an annual or three-year accrual basis. Once you opt to report annually, however, you must continue to use that method of reporting in subsequent years.

Canada Savings Bonds (CSBs)
There are two different types of Canada Savings Bonds (CSBs): regular and compound interest. With regular bonds, you’ll receive and report the interest each year. Compound bonds, however, are something else entirely. If you own compound bonds, you will not receive the interest until the bond matures or is cashed in. Nevertheless, the interest must still be reported annually. The government will provide you with an information slip indicating the amount of income to be reported.
**Tax Tip**

When you purchase CSBs with a loan that is repaid through a payroll deduction plan, any interest you pay on the loan is tax deductible.

**Treasury Bills**

In general, the difference between the purchase cost and the selling price of Treasury bills is deemed to be interest. A capital gain is realized only if market interest rates drop and the Treasury bills are sold before maturity. In such situations, the capital gain equals the selling price minus the purchase cost plus accrued interest up to the date of disposition. Conversely, a capital loss will arise if interest rates increase and the Treasury bills are sold before maturity.

**Mutual Funds**

Mutual funds are pools of assets that are invested by professional managers, either in general investments or in a particular sector.

Some mutual funds pay dividends but may designate all or a portion of the dividends as capital gains dividends to reflect capital gains earned by the mutual fund. Such dividends are treated as capital gains for income tax purposes.

If you sell or redeem mutual fund units, you have to recognize a capital gain (or loss) to the extent the disposition proceeds exceed the cost base of the units sold (and vice versa). As mutual fund units are identical properties, a new tax cost calculation has to be made each time other units are purchased or distributions are reinvested. The cost base of mutual fund units needs to be tracked on an ongoing basis and is rarely the amount you paid for the units. Your broker and/or professional adviser can assist with this calculation.

Most mutual funds allocate their income to registered owners as of December 31 of the particular year. Therefore, if you invest in a fund near the end of the year, you may receive an income information slip showing income that has to be reported for tax purposes even if you have only owned the fund units for a few days.
Segregated funds
Segregated funds are actually insurance contracts with two components: an investment that produces the return and an insurance contract that covers the risk. Like mutual funds, these funds cover a wide variety of asset categories. However, they also provide some benefits that are not available in a mutual fund. For example, segregated funds guarantee either 75% or 100% of your principal. They can also offer protection from creditors if certain conditions are met. This can be a benefit if you’re a sole proprietor or in partnership and want to save for your retirement without putting those funds at risk. Finally, like all insurance contracts, they allow you to name a beneficiary. This means that after your death, the fund proceeds can be paid to the beneficiary without having to go through probate.

147 Income trusts and Real Estate Investment Trusts (REITs)
Every year, in addition to a share of the income earned, this type of trust distributes part of the capital to its unit holders. For this reason, the amount distributed to you is not the same as the amount on which you have to pay tax. Each capital distribution reduces the tax cost of the units, which generally results in a capital gain when the units are sold.

Example
You hold income trust units with a value of $10 each and an annual distribution of $1 per unit. This distribution is made up of taxable income of $0.20 and a non-taxable return on capital of $0.80, which reduces the tax cost of the investment. In five years of distributions, each unit will yield $1 of taxable income and $4 in non-taxable return of capital. The tax cost of the holding is now $6 ($10 – $4). If you sell your units for the purchase price of $10, you’ll have a capital gain of $4 ($10 – $6).

148 Investment holding companies
The tax system contains special rules that are intended to eliminate any preference for earning income in a corporation as opposed to personally. These rules—referred to as integration rules—are technically designed to ensure that the after-tax return on income realized through
a corporation and subsequently distributed to the shareholder is roughly the same as if the shareholder had received the income from the investments directly.

Nevertheless, there may still be some situations where you might want to use a company to hold your investments. For example, individuals eligible for OAS benefits whose personal income (excluding investment income) is $71,592 or less (see topic 72) may come out ahead by holding their investments in a corporation. Investment holding corporations can also be used to implement an estate freeze (see topic 131).

Every situation is unique and requires a separate analysis. Your tax adviser can assist you in determining whether this strategy is suitable for your particular situation.

**Tax tip**

A regular review of your tax situation, including an annual look at your portfolio, is the best way to determine the most advantageous structure in light of any tax rate adjustments, new legislation and changes to your business.

**Tax tip**

The eligible dividend rules (see topic 143) may affect a decision to hold your investments in a corporation. If you already have an investment holding company, you should contact your tax adviser to determine if any restructuring might be needed.

**149 Cumulative net investment loss (CNIL) rules**

The cumulative net investment loss (CNIL) rules are intended to prevent individuals from reducing their income by claiming investment losses, such as rental losses, interest expense and other carrying charges, and subsequently recouping the losses by selling the underlying investment and then not paying any tax on the resulting gain by using the capital gains deduction. With the elimination of the $100,000 capital gains deduction on other property, your CNIL is only relevant if you have a gain from the
disposition of qualified farming or fishing property or a share of a qualified small business corporation.

What is a CNIL?
Your CNIL account is the cumulative excess of your investment expenses over your investment income. Investment expenses include losses from rental property, non-active partnership losses (such as tax shelters), interest on money borrowed for investments and 50% of resource-related deductions.

Investment income includes all income from property (including rental income, interest income and dividends), non-active partnership income and 50% of the recovery of resource-related deductions. Investment income doesn’t include taxable capital gains, although capital gains that cannot be sheltered by the capital gains deduction reduce the impact of the CNIL account.

Tax tip
If you’re an owner-manager of a corporation and have a CNIL problem, you should consider receiving enough interest or dividend income from your corporation to eliminate the balance in your CNIL account.

150 Deductibility of interest expense
The general rule is that interest expense is deductible for income tax purposes if the borrowed funds are used to earn income and certain other conditions are met. The CRA has also adopted a number of administrative positions with respect to special situations that might not strictly satisfy the income earning test. For example, interest will generally be deductible if the funds are borrowed to pay dividends or redeem shares, provided the amount of the dividend or redemption doesn’t exceed the accumulated profits of the company. In addition, funds borrowed by individual shareholders to loan to their corporation at no or low interest will continue to be deductible, provided the company uses the funds to earn income, no unfair advantage is derived and the company is unable to obtain the same terms of financing from a third party without the guarantee of the individual.
Many court cases have dealt with the deductibility of interest. Some of these cases have been contrary to the CRA’s administrative position. As a result, the CRA has either decided to accept the court’s decision or has persuaded the Department of Finance to introduce new legislation to get the result it wants.

One of the more significant Supreme Court decisions was *The Queen v. Singleton*. In this case, the taxpayer (a partner in a law firm) withdrew funds from his capital account in the firm to finance the purchase of a house. The same day, he borrowed money to replace the funds in his capital account. The Minister of Revenue attempted to deny the interest deduction on the grounds that the borrowed money was used to finance the house, not as a business investment. The Supreme Court determined that the interest on the borrowed funds was deductible. A direct link could be drawn between the borrowed money and an eligible use—i.e., the taxpayer had used the borrowed funds for the purpose of refinancing his partnership capital account with debt. The CRA has since accepted this decision.

In another case—*Stewart v. The Queen*—the CRA attempted to disallow rental losses on the basis that the taxpayer had no reasonable expectation of profit from his investment. The losses resulted from the deduction of interest (due to the fact that the investment properties were almost 100% financed). The Supreme Court concluded that since the taxpayer had used borrowed money to engage in a bona fide investment from which he had a reasonable expectation of income (before deductions), the interest should be deductible and the losses allowed.

In October 2003, the Department of Finance introduced draft legislation that would effectively disallow losses from a business or property where it is not reasonable to expect that the taxpayer will realize a cumulative net profit over the whole period that the taxpayer carries on the business or holds the income-producing property. These rules were referred to as the “reasonable expectation of profit”
(REOP) rules. In 2005, due to concerns expressed with respect to these proposals, the Department of Finance announced that it intended to make changes to the rules to address some of the concerns that had been raised. As of June 2014, there has been no further word on the status of these proposed measures.

**Tax tip**

As new legislation could be introduced at any time, and current assessing practices are always subject to change, you should check with your tax adviser to determine the CRA's position if you're borrowing funds and want to deduct the interest.

If you no longer own the income-producing property, there are also rules that may permit a continued deduction for interest expense. It’s not clear how the proposed REOP rules will affect these “loss of source” rules, although the Department of Finance has indicated that the loss of source rules are intended to override the REOP rules. Due to the complexity of the rules, professional tax advice is recommended.

**Tax tip**

When you borrow, try to borrow for investment or business purposes before you borrow for personal reasons. Conversely, when repaying debt, consider repaying loans on which interest is non-deductible before you repay those on which the interest is deductible.

**151 Resource sector as a tax shelter**

Most investors do not invest directly in the resource sector. Instead, they obtain tax write-offs or tax credits by investing in limited partnerships created for that purpose or in shares (flow-through shares) whereby the companies pass on the deductions to the shareholders, who claim them on their own tax returns.

There are various types of resource expenses you can claim, and each one is subject to special rules regarding the amount
that can be claimed as a deduction. As with any other investment, your decision to invest in the resource sector should consider its overall investment potential rather than just focusing on the write-offs. Your financial adviser can assist you in making this assessment.

152 Mineral exploration tax credit
Flow-through shares allow companies to renounce or “flow-through” tax expenses associated with their Canadian exploration activities to investors, who can deduct the expenses in calculating their own taxable income. The mineral exploration tax credit is an additional benefit, available to individuals who invest in flow-through shares, equal to 15% of specified mineral exploration expenses incurred in Canada and renounced to flow-through share investors. Eligibility for this credit is extended to flow-through share agreements entered into before April 1, 2015 and in respect of eligible expenses which may be incurred until the end of 2016.

153 Limited partnerships
Another type of tax shelter involves the purchase of an interest in a limited partnership. In this type of arrangement, you share the profits or loss of the business with the other partners and include in your income or loss a percentage of the partnership’s income or loss. However, your liability with respect to the partnership’s debts is limited. In general, you can only lose up to your original investment.

Special rules also prevent you from writing off more than the amount you have invested in the partnership (these are called the “at risk” rules). The write-off you can claim is further restricted if the purchase is financed with certain types of “limited recourse” financing.

If the adjusted cost base of your interest in a limited partnership becomes negative, you’ll have to report a capital gain equal to the negative amount.

Some limited partnerships have been scrutinized by the CRA. Investors should be aware that if the limited partnership is found to have no reasonable expectation
of profit, the losses may be disallowed (see topic 150). As you would with any other investment, you should thoroughly evaluate the investment potential of a tax shelter. It doesn’t make any economic sense to invest in a shelter if there’s little chance of either earning a return on your investment or recovering the amount you have at risk.

The alternative minimum tax (AMT) (see topic 157) and cumulative net investment loss (CNIL) rules (see topic 149), as well as restrictions on the deductibility of limited partnership losses, make it imperative that you pursue expert tax advice about your situation before making an investment.

154 Taxation of personal trusts
A trust is an arrangement under which a trustee holds property for the benefit of one or more beneficiaries. It can be created through your will at any time, including on death. Trusts are taxed as separate taxpayers. A trust created on death is currently taxed at the same rate as an individual while other trusts are taxed at the highest marginal individual rate of tax (from 39% to 50%, depending on the province in which the trust is taxed). The Department of Finance has recently introduced proposals that would also assess the highest marginal rate of tax to trusts created on death.

These proposals provide that flat top-rate taxation will apply to existing and new testamentary trusts for the 2016 and later taxation years. Exceptions will exist for the first 36 months of an estate and for testamentary trusts created for the benefit of disabled individuals who are eligible for the federal disability tax credit (see topic 80).

Testamentary trusts that do not already have a calendar year-end will have a deemed taxation year end on December 31, 2015 (or the year in which the first 36-month period ends).
Tax tip

If you are the trustee of a testamentary trust that is currently subject to graduated rates of tax, you should consult with your tax adviser to determine if there is any planning that can be done to mitigate the impact of this change in tax rates.

Flexibility in taxation

The income of the trust will be subject to tax, but there’s flexibility in the determination of exactly who gets taxed. If the trust agreement requires the income to be paid to beneficiaries, the general rule is that the beneficiaries will pay the tax. However, it’s possible to make an election to have some or all of the income taxed in the trust. Alternatively, the trust agreement may provide that the income stays in the trust for a set period of time. In this case, the general rule is that the trust will pay the tax.

Tax tip

Consider creating a trust to hold investments for the benefit of a child or parent with a physical or mental disability. If the trustee makes a preferred beneficiary election, the income can be retained in the trust but taxed in the hands of the lower income beneficiary. This reduces taxes while allowing the trustee to control the investments.

The 21-year rule

Under this rule, most trusts are deemed to dispose of all their property every 21 years for proceeds equal to the fair market value of the property.
**Tax tip**

If you’re the trustee of a trust that will soon be subject to the 21-year rule, you should contact your tax adviser to determine what strategies are available to avoid or defer the tax on the deemed disposition. If the trust document permits, it might be advantageous to transfer out of the trust to the capital beneficiaries the capital property with the accrued gains. If there are no accrued gains on the property, the 21-year rule is not an issue and the property can remain in the trust.

### 155 Foreign taxes on investment income

As a resident of Canada, you’re subject to Canadian income taxes on your worldwide income, even if it was earned in another country. If the amount of foreign income received is net of foreign taxes withheld, you must gross-up the amount received by the amount of income taxes withheld. For example, if you receive a $170 foreign dividend payment ($200 in foreign dividends minus $30 in withholding tax) you must include the full $200 in your income. The foreign income is to be converted into Canadian dollars by using the average rate of exchange for 2014 or the actual exchange rate in effect when you received the income. The withholding tax can be claimed as a foreign tax credit with certain restrictions.

The foreign tax credit is calculated on a per-country basis, and separate calculations are required for business and non-business income tax.

### 156 Foreign reporting requirements

If you’re a resident of Canada, you must declare your income from all sources—Canadian and foreign. In addition, if the total cost of your specified foreign property exceeds CAN$100,000 at any time in 2014, you also have to report information about these foreign investments on your tax return (Form T1135). This form must be filed by the due date for filing your income tax return for the particular year.
Specified foreign property includes
- bank accounts held abroad,
- debt securities and shares of foreign corporations,
- real estate, and
- other tangible and intangible properties located outside Canada.

It does not include
- property used or held exclusively in the course of carrying on an active business,
- registered pension fund investments,
- foreign investments held in Canadian-registered mutual funds,
- personal-use properties, and
- shares of a foreign affiliate.

**Example**

You own shares of non-resident corporations with a cost amount of $140,000. The shares are held by a Canadian broker. You must report these investments, as well as the income earned thereon, even if the shares are physically held in Canada because the cost amount is greater than $100,000.

Reporting may also be required if you have transferred or loaned funds or property to a foreign-based trust (Form T1141); have received funds or property from, or are indebted to, a foreign-based trust (Form T1142); or for the ownership of shares of a foreign affiliate (Form T1134).

Form T1135 has recently been revised to require more detailed reporting for each specified foreign property held during the year.

**What additional information is required?**

Prior to 2013, the rules provided that the cumulative cost (generally, the original purchase price) in Canadian dollars of all specified foreign investments had to be reported on the form, segregated by type, such as foreign shares or indebtedness, along with the total income reported from the
investments and the foreign source where the investments were located. For 2013 and subsequent years, you now have to provide the following additional information:

- whether the filing is an amended return;
- the country where each property is located;
- the maximum cost of each property held during the year, as well as its cost at year-end;
- any gain/loss recognized on a disposition of the property;
- the amount of foreign income earned on each property during the year;
- whether foreign income you have received has been reported on a T3 or T5 tax slip from a Canadian issuer in respect of a specified foreign property (for 2013 only);
- the name of the bank or other entity holding funds outside of Canada;
- where the form is prepared by a partnership, the nature of the partners (individuals, trusts, or corporations) must be disclosed;
- if you hold foreign shares, the name of the corporation issuing the shares;
- a description of any indebtedness owed to you by a non-resident;
- where an interest is held in a non-resident trust, the name of the trust and the amount of income and capital distributions received (if any) during the year;
- a description of all real property you hold outside of Canada (except for personal use property and real estate used in an active business); and
- a description of all other specified foreign properties held outside of Canada.

However, instead of the above, there is a streamlined reporting option available for specified foreign properties held in accounts with Canadian registered securities dealers and/or Canadian trust companies. With this streamlined method, detailed reporting for each specified foreign property is not required. Instead, these foreign properties can be aggregated and reported on a country-by-country basis, or aggregate totals can be reported for each particular account, as long as they are reported on a country-by-country basis. Fair market values at year end would be reported instead of cost, along with the highest
month-end fair market value for the year. A similar "transitional method" was available for 2013 reporting only.

This foreign reporting requirement applies to corporations, partnerships, as well as individuals.

The amount of information required to be reported on this new form could be significant, and in some cases, the information won’t be readily available. You should contact your tax adviser if you think you may own foreign property that would require disclosure under these rules.

**Tax tip**

Does your portfolio include specified foreign investments? If so, then it’s time to consult your tax adviser to review your filing requirements. In some cases, the information you’re required to report won’t be readily available and you’ll need time to accumulate it.

157 Alternative minimum tax (AMT)

The purpose of the alternative minimum tax (AMT) is to restrict the tax benefits derived from various tax preference items, such as approved tax shelters, capital gains, investment tax credits and certain losses. It either imposes an overall limit on the total of these identified deductions, credits and exclusions or reduces the tax savings derived from these items.

You should not have to pay AMT unless your tax preference holdings exceed a $40,000 exemption. Even then, depending on your circumstances, the total of such items may significantly exceed this limit before AMT is triggered. In many cases, no AMT will be due. Additionally, it doesn’t apply in the year of death.

If your AMT exceeds the amount of your regular federal taxes payable, the AMT becomes the amount of federal tax used to determine your tax liability. You can also be subject to provincial AMT. You can recover AMT paid in future years when your regular tax liability exceeds your AMT for that year. The carry-forward period is up to seven years.
Section 4 – Everyone

158 Understand the rules before you act
Are you considering a financial transaction that is not part of your ordinary routine? If so, it’s important to understand the tax rules that apply to your proposed action. In most cases, the opportunities available to save or defer income taxes arise at the preliminary stage, before you’ve completed the transaction. The preliminary stage is also the best time to evaluate and plan for the impact of GST/HST/QST and other types of taxes on the proposed transaction. If you wait until you have completed the arrangement to have your tax adviser review the situation, it’s usually too late. The best way to benefit from the rules is to conduct your tax planning well in advance.

159 The CRA’s policy and what’s really law
In most cases, amendments to the Income Tax Act are presented to the House of Commons as part of a budget. The Department of Finance, under the direction of the Minister of Finance, prepares these amendments. After an amendment becomes law, the Canada Revenue Agency (CRA) administers it.

Over the years, due to the uncertainty in many areas of tax law, the CRA has developed a number of administrative rules in an effort to deal with practical problems that arise. In some cases, the administrative rules may not even agree with the law.

In tax planning, you should know whether your plan complies with the tax law or depends on the agency’s stated policy. The CRA is not bound by its stated policy, and the courts do not necessarily consider this policy in making their decisions.

160 T3s, T4s, T5s and other information slips
Any employment, pension and most investment income you receive in 2014 is reported on information slips prepared by the person or organization that paid you. In general, these slips must be mailed to you by
February 28, 2015. If you’re a beneficiary of a trust, (this would include ownership in units of a mutual fund trust), your T3 information slip could be delayed until the end of March, depending on the year-end of the trust. Partnerships in which all members are individuals are required to file a partnership information return and issue the required information slips to the partners by March 31, 2015 (see topic 2).

Public trusts and public partnerships are required to disclose distributions or allocations of capital and income for public mutual fund trust units and public limited partnership units within 60 days after the calendar year-end via a Web site maintained by CDS Innovations Inc. This information is particularly useful for investors since in many instances distributions received by the investor will be a combination of income allocations and returns of capital. Furthermore, any income allocations will need to be broken down by income source which would also include allocations of capital gains or losses. CDS Innovations Inc.’s Mutual Fund and Limited Partnership Tax Breakdown Posting service can be found at http://www.cdsinnovations.ca/applications/taxforms/taxforms.nsf/Splash?Openpage.

If you are enrolled in the CRA’s My Account service (see topic 163), you will be able to view T4s, T4As, T4A(P)s, T4A(OAS)s and T4Es issued to you that have been received by the CRA. The My Account service also allows you to view several other important balances and carryover amounts that may be needed in preparing your tax return.

Regardless of whether you receive the appropriate slip, you must declare all your income. Be sure to check the amounts reported on the slips to ensure that they are correct, as mistakes on these documents are not uncommon. If there’s an error, you can obtain an amended slip.

If you’re filing your return electronically (see topic 161), all information slips and other supporting documentation,

---

31 Since this date falls on a Saturday, the deadline is administratively extended to Monday, March 2, 2015.
such as charitable donation receipts, must be retained in case the CRA requests confirmation of the amount claimed. Your return may be reassessed if you cannot provide a copy of the relevant slip.

Businesses and organizations that prepare these slips are required to electronically file them with the CRA if the number of slips filed for a particular information return is more than 50. Penalties will be assessed for not e-filing information slips when required.

161 EFILE and NETFILE

EFILE for individuals

Electronic filing (EFILE) allows registered tax professionals to electronically send your personal income tax return directly to the CRA. Since the returns are received and verified almost instantly, refunds can often be issued within a couple of weeks of submitting your return. Although almost all Canadians are eligible to use this system, there are certain returns that cannot be EFILED, such as returns for non-residents and certain deemed residents, taxpayers who have an address outside of Canada, and taxpayers who have to pay income tax to more than one province or territory.

NETFILE

You may also be able to file your personal income tax return directly with the CRA via the internet using their NETFILE service. If you qualify for NETFILE, you will need to prepare your return using one of the tax preparation software programs or web applications certified by the CRA for NETFILE. Once you are ready to file your return, you will need to provide your social insurance number and date of birth for identification purposes. Detailed information on the NETFILE service, including a list of certified software programs, can be found on the CRA’s Web site. NETFILE does not require that you file the supporting documentation used to prepare the return, unless requested to do so.

Electronic filing of GST/HST returns

Refer to topic 46 for information on the electronic filing of GST/HST returns.
Internet filing for T3s, T4s, T5s and other information returns
As noted in topic 160, businesses can now file several different information returns over the Internet. The option to Internet-file is available to those businesses that file up to 50 slips and use authorized tax preparation software. Businesses that file more than 50 slips related to a particular type of information return are required to file electronically.

Corporation Internet filing
This filing option allows corporations to use a six-character alphanumeric Web Access Code (WAC) to file their corporate income tax returns directly to the CRA through the Internet. In prior years, the WAC was provided in a letter from the CRA; however, the CRA has discontinued the use of these letters. If you cannot remember your WAC, you can call the CRA Helpdesk at 1-877-322-7849 or use their WAC online service to obtain the WAC assigned to your business. Instead of using a WAC to file returns, tax professionals who file corporate income tax returns for their clients can register and transmit using an EFILE online number and password.

Certain corporations must file their returns in electronic format (mainly, most corporations with annual gross revenues in excess of $1 million). Also, starting in 2013, tax preparers who prepare more than 10 T2 corporation income tax returns are required to file them electronically.

To ensure compliance with the mandatory electronic filing changes, penalties have been introduced for filing a corporate tax return in an incorrect format. If you are required to file your corporation’s tax return electronically and fail to do so, you may be assessed a $1,000 penalty. Tax preparers who are required to file electronically but do not comply, may be charged a penalty of $100 for each T2 corporation return that is paper-filed.

162 Registering for online access to your CRA account
The CRA provides online account access for registered users through one of three portals: “My Account,” “My Business Account” and “Represent A Client.” Topic 163 provides a listing of some of the available services for My Account and
My Business Account users. Similarly, topic 164 lists some of the services available to authorized representatives accessing tax accounts through Represent A Client.

Regardless of which portal is used, the individual seeking access must first register with the CRA in order to obtain online access credentials, as more fully explained under the heading “Individual registration.” In addition, individuals wishing to act as authorized representatives and to use the Represent A Client portal to access the account of another individual or a business not owned by them also need to obtain a RepID, as more fully covered under the heading “Representative registration.”

Although this initial registration process appears quite complex, it achieves the following security-related objectives:

- It confirms the identity of the individual.
- It confirms that the individual has authorization to access the individual or business account.

**Individual registration**

Anyone wishing to access their personal account, the accounts of a business they own or the individual or business accounts of other taxpayers must register with the CRA, at which time they will have the choice of obtaining a CRA user ID or using their existing online banking credentials (provided they bank with one of the CRA’s Sign-in Partners). Currently, those partners only include BMO Financial Group, TD Banking Group and Scotiabank, but more are likely to sign on in the future. An individual can have multiple CRA user IDs, as well as using their banking credentials. This might be useful, for example, where they want to maintain separate log-in credentials for their personal and business accounts or a separate set of credentials when accessing accounts as an authorized representative.

**Registration is a three-step process:**

(1) Confirm identity (and link to sign-in credentials): Where the individual wishes to obtain access to their personal tax account or the business accounts where they are the business owner, they will need to provide their SIN, their date of birth,
their current postal code and an amount from a random line on either their current or previous year’s tax return (and the BN of the business, if applicable). Where the individual is only registering to be able to act as a representative, they will need to provide the eight-character access code from their most recent personal Notice of Assessment and their current postal code.

(2) Initial access setup: Individuals have the option of creating a CRA user ID and password or using their existing online banking credentials (limited to the Sign-in Partners noted above).

(3) Validation for CRA user ID only: Once the entered information is confirmed, the CRA will send a Security Code by mail to the individual. The Security Code must be entered on the first log-in to validate the user ID or banking credentials and provide access.

Representative registration
Individuals are considered representatives in relation to the personal tax accounts of other individuals or business tax accounts where they are not one of the owners of the business. This means that in addition to individuals traditionally defined as representatives, such as third-party tax preparation providers, employees of a business can also be considered a representative.

After registering as a representative, the individual will receive a unique seven-character RepID that they must provide to any individual or business that they wish to represent. The individual or business owner enters the RepID in the appropriate area in their online account to authorize the representative or on a third-party authorization form that is filed with the CRA (Form T1013).

Where the representative is a business itself, it registers using its BN, which becomes its RepID. In turn, employees of the representative must then obtain individual RepIDs that they will provide to the firm to link to the firm’s BN.
163 My Account and My Business Account

The number of services available using My Account and My Business Account continue to grow as the CRA focuses on modernizing its systems and reducing its costs. In many cases, it is now possible to file returns electronically through one of the two portals. More recently, the CRA announced that an individual or business can choose the digital mailboxes within My Account and My Business Account as the primary delivery method of all correspondence with the CRA. This would include Notices of Assessment and Reassessment, announcement of upcoming audits, etc. In addition, you would be able to respond to any information requests as well.

My Account

My Account provides access to an individual’s income tax account, including carryover balances, credits, etc. Furthermore, depending on the access level, My Account can be used to not only review information, but also to make changes to certain information or tax return filings (see topic 164 for access level information).

My Business Account

Many businesses deal with more than one program administered by the CRA, and in some cases, may have more than one account within a program. For instance, many businesses have more than one payroll account or more than one division requiring them to set up one or more GST/HST accounts. In order to track multiple accounts within multiple programs all related to the same business, the CRA assigns a nine-digit business number to the business to be used across all programs and that remains the same regardless of the number of program accounts. Different programs and program accounts using the same business number are identified by the addition of a six-character suffix to the business number. The first two alpha characters identify the program (for example, RC for corporate income tax, RT for GST/HST and RP for payroll) and the remaining four numerals identify the account (for instance, RP0001 and RP0002 are payroll accounts 1 and 2, respectively).
This system means that a business has access to all of its accounts in most of CRA’s separate programs through My Business Account. It also allows the business to authorize different representatives for different program accounts.

164 Represent A Client

Represent A Client allows individuals and businesses to establish a link between their My Account or My Business Account and an employee of the business or a third party, thereby authorizing the representative to access the account. Both My Account and My Business Account are based on the concept of “See It Online” or “Do It Online,” which also underpins the access levels that can be granted to representatives.

See It Online

One of the main purposes of these programs is to give individuals access to tax-related information and amounts maintained by the CRA. Examples of information would include carryover balances for losses, RRSP contribution room, notices of assessments from prior years, instalment balances and account balances, entitlements to credits, and so forth. Where access is provided under the “See It Online” concept, the representative is only able to view the account information and cannot initiate any changes to the information or submit new information.

Do It Online

A number of actions can be initiated through My Account or My Business Account. Examples include the electronic filing of information returns, changing banking information, initiating a formal objection to an assessment, providing materials requested by the auditor and so on. An authorized representative must be granted a certain level of access in order to “do it online.”

As a result, you can authorize representatives for Level 1 access (“See It Online”) or Level 2 access (“Do It Online”).

Additional details regarding My Account, My Business Account and Represent A Client can be found on the CRA’s Web site.
165 Notice of assessment and your return
Shortly after you file your 2014 return, you should receive a Notice of Assessment from the CRA. When you receive it, compare it to the taxes payable as reported on your return. If there’s any discrepancy, try to determine the reason.

If you don’t understand why the amounts are different or you disagree with the assessment, consult your tax adviser or ask the CRA to provide further details. Do not automatically assume you made the error. The assessment may be based on a misunderstanding of the facts, or it may be due to a processing error.

The CRA will generally reassess returns if the adjustment relates to a calculation error or a misunderstanding of the facts. If your dispute is based on a different interpretation of the law, you may have to file a Notice of Objection.

Individual taxpayers can initiate the appeal process by outlining the objection on Form T400A or by setting out the facts and reasons for their objection in a letter to the chief of appeals at their local district taxation office.

Generally, a Notice of Objection must be filed within 90 days of the mailing date of the Notice of Assessment. However, individuals and testamentary trusts have until one year from either the filing due date of the return or 90 days after the day of mailing the Notice of Assessment, whichever is later. Consult your tax adviser if you believe a reassessment or an objection is warranted.

166 Taxpayer relief provisions
The CRA has rules to improve the fairness of the tax system when personal misfortune or circumstances beyond your control make you unable to meet your filing or payment deadlines or comply with certain rules. For example, interest and penalties may be waived if you can show that you were prevented from filing on time due to extraordinary circumstances such as illness, death, or natural disaster. Penalties and interest may also be waived if they arose primarily because of actions of the CRA, such as disruption in services or erroneous information from the tax department in the
form of incorrect written answers, errors in published
information, or undue delays in resolving an objection or an
appeal or in completing an audit. Interest may also be waived
in whole or in part if a taxpayer is unable to pay due to
financial hardship. Penalties will not generally be waived
due to financial hardship.

Individuals and testamentary trusts can also use these rules
to apply for a refund for any taxation year that ends in the
10 preceding calendar years, which includes years which
would otherwise be statute-barred. For example, you may
find that you failed to claim the disability tax credit (see
topic 80) in previous years even though you were entitled
to do so. Other provisions permit you to amend, revoke
or late-file certain prescribed tax elections.

To request this relief, you must either write a letter to
the CRA or complete and file Form RC4288, “Request
for Taxpayer Relief,” with the CRA, indicating why you
think the taxpayer relief provisions should apply to your
particular situation. You’ll have to submit receipts or other
backup information to support your claim. Relief is not
automatic, and the rules are not intended to permit retroactive
tax planning. Your tax adviser can assist you in determining
whether you’re likely to qualify, as well as in making
the application.

167 The CRA’s collection procedures
If you cannot afford to pay your taxes owing, you should
still file your return on time. Filing late can incur significant
penalties and interest (see topic 171).

In most cases, the CRA cannot begin legal proceedings to
collect until 90 days after the day on which the Notice of
Assessment was mailed. There are further delays if you
file a Notice of Objection or otherwise indicate that you’re
objecting to the assessment. Nevertheless, interest is
charged that compounds daily to the date of payment.

The CRA will make every effort to contact you before
beginning formal legal proceedings, but it would be
prudent for you to contact the CRA if you’re unable to
pay the full amount. Depending on your circumstances, a schedule of payments over a period of time will normally be accepted. If you don’t pay, the CRA has the power to seize funds from your bank account or require your employer to pay a portion of your salary directly toward your taxes owing.

Limitation period for collection of tax debts
There is a 10-year limitation period for the collection of income tax debts. For all federal tax debts and any other amounts that became payable before March 4, 2004, but remained unpaid at that date, this 10-year limitation period commenced on March 4, 2004. For debts that become payable after this date, the limitation period is 10 years.

168 Income tax refunds
You’re eligible for an income tax refund if the amount of income taxes withheld from you or paid by you during the year exceeds the actual taxes you owe. Although you may look forward to receiving a tax refund, it is not always good planning to get one. If you get a refund, that means the government has been holding your money and not paying you interest on it for many months.

Tax tip
If you expect to receive a refund after filing your return—for example, for support payments or other deductions—you can apply to the CRA to obtain permission to have your source withholdings reduced. In some cases, the TD1 form you file with your employer can be amended to provide for the reduced withholdings.

Although you won’t be penalized for filing a return late when you’re owed a refund, interest doesn’t begin to accrue on the refund amount until you file the return. For individual tax returns, interest on tax refunds doesn’t start to accrue until 30 days after the balance-due date (April 30) or 30 days after the actual filing date or the date the overpayment arose, whichever is later.
If you have made an error and you actually owe money, late-filing penalties and interest will apply on the balance owing. Therefore, regardless of whether you owe money or are receiving a refund, you should always file your return on time.

169 Income tax instalments

Instalments for individuals

You may be required to prepay your tax through quarterly instalments (due on March 15, June 15, Sept 15 and Dec 15). Instalments are required if the difference between your combined federal and provincial tax and the amount of tax actually withheld at source was greater than $3,000 in 2012 or 2013 and will be greater than $3,000 in 2014. This last test requires an estimate in advance of the actual calculation of 2014 tax.

You can choose from three options to calculate the amount of your instalment. Under the first two options, you can base your instalments on your 2013 tax or on your estimate of your 2014 tax. If you choose the latter option, be careful. Underestimating your 2014 tax means the CRA will charge you interest based on the higher instalment required.

With the third option, the CRA calculates the amount of your instalment and sends you the calculation as a reminder. The total for the year will equal your prior year instalment base. The major advantage in paying the amounts shown on the CRA notices is that you won’t be charged any instalment interest if you pay on time. The CRA sends the instalment reminders in batches of two—in February for the March and June instalments, and in August for the September and December instalments.

Failing to remit the instalments on time can be costly. The CRA charges interest on the deficient amounts as if you owed the money and, if this interest charge adds up to more than $1,000, an additional charge is added. This can become quite expensive and should be avoided if possible.
Tax tip

If you discover during the year that you should have been making higher instalments, it’s possible to catch up because the CRA will credit interest on overpayments and apply that against interest deficiencies.

You can now use a pre-authorized payment plan to make your quarterly personal instalments. To do this, complete Form T1162A, attach a cheque marked “void” and return it to the CRA. This will authorize the CRA to automatically debit your bank account for a predetermined amount on a specified date.

Instalments for corporations

In general, your corporation is not required to make instalments if its total tax liability for the current or preceding taxation year is $3,000 or less. In this case, the amount owing is paid on the balance-due day for the taxation year.

Again, there are three options for determining the monthly instalment amount. Under the first two options, you can base your corporation’s instalments on its “instalment base” for the immediately preceding year or on your estimate of its tax liability for the current year. If you choose the latter option, be careful. If you underestimate the amounts, the CRA will charge non-deductible interest on the underpayments.

Under the third option, the first two instalments can be calculated as 1/12 of the corporation’s instalment base for its second-last taxation year, and the next 10 instalments can be based on the corporation’s instalment base for the immediately preceding taxation year after deducting the first two instalments.

Each instalment is due on the last day of each month of the taxation year.

A Canadian-controlled private corporation that meets all of the following criteria will be able to make quarterly instalments:
• The taxable income of the corporation and all associated corporations for either the current or previous year does not exceed the amount that qualifies for the small business deduction (see topic 24).
• The corporation qualified for the small business deduction in either the current or previous year.
• The taxable capital employed in Canada of the corporation and all associated corporations does not exceed $10 million in either the current or previous year.
• The corporation has no compliance irregularities during the preceding 12 months.

As above, there are three similar methods for determining the quarterly instalment amounts. Each instalment will be due on the last day of each quarter of the corporation’s taxation year.

There are special rules in situations where a corporation has undergone a corporate reorganization or where the instalment base year was less than 365 days.

170 Books and records
Individual taxpayers should keep their tax records for at least four years—approximately the period during which the CRA can reassess a return—and preferably longer.

If you operate a business, you must keep your business records for a minimum of six years from the end of the last tax year to which they relate. For non-incorporated businesses, permanent books and records must be kept for six years after the last day of the taxation year in which the business ceased. For corporations, permanent records must be kept for two years after dissolution. Permanent books and records include the general ledger and special contracts and agreements, as well as all incorporation documentation. If a return is filed late, the books and records must be kept for six years from the day the return is filed.

Note that the minimum retention period is generally determined by the last tax year for which a record may be required for purposes of the Income Tax Act, not the year in which the transaction occurred and the record was
created. For example, records supporting the acquisition and capital cost of investments and other capital property should be maintained until the day that is six years from the end of the last tax year in which such an acquisition could enter into any calculation for income tax purposes.

Books and records can only be destroyed at an earlier time if you obtain written permission from the CRA.

### 171 Be aware of penalties and interest

The concept of increased penalties for repeat offenders is now firmly entrenched in the Income Tax Act.

The penalty for filing a return late is 5% of the unpaid taxes plus an additional 1% for each complete month the return is late, up to a maximum of 12 months—a maximum penalty of 17%.

Additionally, if you’ve been assessed this penalty for any of the three previous years and the CRA issues a demand to file the current year’s return, the penalty for a repeat offence will be 10% of the unpaid taxes plus an additional 2% per month for a period up to 20 months—a maximum penalty of 50%. Similarly, if you fail to report an amount for a given year and then fail to report another amount in any of the three subsequent years, a special penalty will apply which is equal to 10% of the amount you failed to report for the second time.

And don’t forget the interest that can be assessed for failing to remit the appropriate amount of income tax instalments (see topic 169).

There is also a penalty for late filing information returns even though no taxes are owing. The amount of the daily penalty (to a maximum of 100 days) is based on the number of slips of a particular type that are late-filed.

To reduce the amount of late filing penalties when the number of slips of a certain type that are filed late are 10 or less, the CRA has introduced an administrative policy for certain types of information returns (T4, T4A, T4E, T5, NR4).
For example, there is a $100 flat penalty when one to five slips of a certain type are filed late by a taxpayer. When six to 10 slips are filed late, the penalty is $5 per day, subject to a $100 minimum and a $500 maximum. But when more than 10 slips are filed late by a taxpayer, the penalty is equal to the legislated amount of $10 per day, subject to a $100 minimum and $1,000 maximum, increasing to $75 per day where over 10,000 slips are late filed. Information returns subject to the legislated penalties (i.e., not subject to the administrative relief) include foreign reporting forms (T106, T1134, T1141, T1142 and T1135) and non-profit organization returns (T1044). Generally, the CRA’s administrative policy is to charge the penalty in all cases, even for first-time late filers.

There are also penalties for failing to provide your SIN (social insurance number) or your BN (business number) or for failing to include the SIN or BN on an information slip you have prepared. Partnerships and tax shelters are also subject to penalties for failure to file the required information returns.

**Even bigger penalties**

If you knowingly, or in circumstances amounting to gross negligence, make false statements or omit information from a return, a penalty may be imposed that is equal to whichever is the greater of $100 or 50% of the tax avoided or benefit improperly claimed. And if the CRA finds that a false statement or omission amounts to tax evasion, a fine of 50% to 200% of the tax evaded may be imposed.

The interest rate charged on amounts owing to the CRA is 2% higher than the rate the CRA pays on refunds to non-corporate taxpayers (4% higher than the rate for corporate tax refunds). The increased rate applies to all amounts owing to the CRA, including unpaid taxes, instalments and source deductions.

**Voluntary disclosures**

It is the CRA’s policy not to impose penalties when a voluntary disclosure is made. If a taxpayer has never filed tax returns and the returns are then voluntarily filed, the
taxpayer will be required to pay only the tax owing—with interest—on the reported incomes. If a taxpayer has given incomplete information in a return and subsequently submits the missing information, the taxpayer will be required to pay only the tax owing on the adjusted income, with interest.

To make a voluntary disclosure, you have to initiate the process. A disclosure is not considered voluntary if it arises when the CRA has begun an audit or a request for information has been issued. Contact your tax adviser regarding initial contact with the tax department and the information to be provided.

Ministerial discretion to waive interest and penalties
In some cases, interest and penalties may have arisen through no fault of your own. To deal with such inequities, there are rules that give the minister the discretion to waive or cancel interest or penalties (see topic 166).

Tax preparer penalty
For returns of income for the 2012 and subsequent taxation years that are filed after 2012, a “tax preparer” will be required to file T1 and T2 returns electronically. For this purpose, a “tax preparer” is defined as a person or partnership who, in the year, is paid to prepare more than 10 T2s or more than 10 T1s. A tax preparer who fails to file in the appropriate manner will be subject to a penalty equal to $25 for each failure to file a T1 in electronic format and $100 for each failure to file a T2 in electronic format.

This new requirement is subject to the following exceptions:
• A tax preparer may file in a calendar year by other means up to 10 T2s and 10 T1s;
• A tax preparer will not have to file electronically if the application to file electronically has been denied or revoked for the year;
• The CRA may specify that certain returns cannot be filed electronically; and
• Certain types of corporate returns will not be required to be filed electronically.
Civil penalties for misrepresentation by third parties
It’s not only taxpayers who have to deal with the prospect of penalties—tax preparers and other third parties can be subject to two different penalties: one for advising or participating in a false filing (preparer penalty) and the other for participation in a tax shelter or other tax-planning arrangement that includes a false statement or omission that may be used for tax purposes by another person (planner penalty).

Reporting requirements for certain tax avoidance transactions
As if all of the above isn’t enough, recently enacted legislation requires taxpayers and their advisers or promoters to report certain tax avoidance transactions to the CRA. If the required information return is not filed as and when required, each person who is required to file will be liable to pay a penalty and the CRA will deny the tax benefit resulting from the transaction. If the taxpayer still wants to claim the tax benefit, the taxpayer is required to file the required information return with the CRA, as well as pay the late-filing penalty.

The reporting requirement applies to certain avoidance transactions entered into after 2010, as well as avoidance transactions that are part of a series of transactions commenced before 2011 and completed after 2010. Where applicable, an information return, Form RC312 “Reportable Transaction Information Return,” is due on or before June 30 of the calendar year following the calendar year in which the transaction first became a reportable transaction (subject to transitional rules for transactions arising in 2011 or 2012).
Active business
Includes any business, as well as an adventure or concern in the nature of trade, but excludes: (i) a business that derives its income from property (including interest, dividends, royalties and rent) and has less than six full-time employees; and (ii) a business that provides personal services through a corporation, has fewer than six full-time employees and where, were it not for the presence of the corporation, the individuals providing the services would be considered employees or officers of the entity using those services.

Active business income (ABI)
Uses corporate income as the benchmark for calculating certain tax credits. It includes income derived from an active business (including incidental income from its active business, such as interest earned on customers’ delinquent receivables) and specifically excludes income derived from property such as capital gains, interest, dividends, royalties and rent.

Affiliated
A relationship that exists between persons for purposes of determining whether certain stop-loss rules apply. For example, individuals are affiliated with themselves and their spouse or common-law partner (but not with their children). They are also affiliated with a corporation that they and/or another affiliated person control.

Amortization
See Depreciation. The term “amortization” is also used to describe the systematic repayment of a debt’s principal and interest.

Annuity
A form of investment that yields a sequence of periodic, usually equal, payments made at equal intervals of time (e.g., $1,200 every month). In return for a single payment to the provider, the annuitant receives a series of payments for a specific term that can begin immediately or be deferred into the future. Annuities can have a variety of options associated with them.
**Arm’s-length**
“At arm’s-length” indicates that the parties to a transaction are unrelated and have separate interests in entering the transaction. A “non-arm’s-length” transaction would be one between related parties or between parties with a common interest acting in concert.

**Beneficiary**
A person for whom a trust is created and who receives, or may become entitled to receive, benefits under a will, insurance policy, retirement plan, annuity, trust or other contract.

**Calendar year**
The period between January 1 and December 31 of any given year.

**Capital asset**
An asset intended to be used on a continuing basis by a business in its daily operations for production or supply of goods and services, for rental to others or for administrative purposes. It is not an asset intended for sale in the ordinary course of business, such as an inventory item. A depreciable asset is an example of a capital asset.

**Carry-forward**
A carry-forward arises when a loss or tax credit is not fully utilized in the current period and, as a result, the unused portion may be used in a future period. For example, a loss carry-forward arises when a taxpayer has incurred a loss in the current period and cannot use it to offset income from a previous period. The loss can be carried forward to offset future income.

**Common-law partner**
A person of the opposite or the same sex who has either cohabited with you for at least one year in a conjugal relationship or is the parent of your child.

**Depreciation**
An accounting procedure that aims to distribute the cost of tangible capital assets, less any expected salvage value, over the estimated useful life of the asset in a rational and
systematic manner. The depreciation for a period is the portion of the total cost allocated to that period.

**Fair market value (FMV)**
The highest price that can be obtained for the sale of an asset between informed parties who deal at arm’s-length and are under no compulsion to act.

**Fiscal year-end**
The point in time that a business has chosen to account for its profits and losses. Generally, a corporation may choose any date in the year, but special rules exist for individuals and partnerships. Once a business establishes a fiscal year-end date, it cannot be changed for tax purposes without the CRA’s approval.

**Flow-through share**
A form of investment specifically related to the resource industry. Unlike a typical share, certain expenditures incurred by the corporation can be renounced by the corporation and “flowed through” to the shareholders. The shareholders can then deduct these items on their own tax returns.

**Goodwill**
An intangible asset that represents the superior earning power of a business. Generally, the value assigned to the goodwill of a business is the fair market value of the business as a whole, less the fair market value of the net tangible assets and identifiable intangible assets that comprise the business.

**Holding company**
A corporation whose principal purpose is to hold investment assets, such as shares in other companies and portfolio investments.

**Information returns**
Forms or documents containing tax-related information about individuals, corporations, trusts or other entities that the CRA requires them to file so it can administer the provisions of the Income Tax Act.
Joint venture
An economic activity resulting from a contractual arrangement whereby two or more entities jointly control an economic activity. Unlike other investments, none of the venturers can exercise unilateral control over the joint venture, regardless of the ownership interest any of them might hold. A joint venture has no legal status itself. The venturers may own property in common, but each has a direct share in the property.

Limited partnership
In a limited partnership, the limited partners have limited liability. This is a similar responsibility to that of shareholders of a corporation and means that liability is restricted to the amount invested in the partnership. There must be at least one general partner who is fully liable for the debts of the partnership. The general and limited partners share the profits of the partnership in accordance with the terms of a partnership agreement.

Marginal tax rate
The income tax rates that apply to each dollar of additional income at different levels of taxable income. As an individual’s income level rises, his or her marginal tax rate also rises.

Non-refundable tax credit
A tax credit earned during the year that is applied to reduce income tax payable for that year but is limited to reducing taxes to a nil balance. If there is an unused portion of the tax credit after reducing taxes to a nil balance, it cannot be used to create a refund. The basic personal credit is an example of a non-refundable tax credit.

Non-resident
The determination of whether a person is a non-resident is a question of fact based on residential ties with another country or the amount of time away from Canada.

Partnership
An arrangement between persons carrying on a common business to earn a profit. It can be formed by a group of individuals, by corporations or by a combination thereof. The partners share the net profits and not the gross returns.
of a business. A partnership can be formed by verbal or written agreement and is governed by provincial law.

**Probate**
A fee that has to be paid to probate a will. The fee varies from province to province, but it is essentially levied on the fair market value of an individual’s estate that passes through his or her will on death. Assets passing outside the will—for example, by right of survivorship or direct beneficiary designation—are not subject to probate.

**Recapture**
An income item created when the balance of the undepreciated capital cost (UCC) of a class of depreciable assets becomes negative. This can occur when the proceeds of the disposition of a capital asset (which is limited to the original cost of the asset) is applied to reduce the UCC of the class and results in a negative balance. In essence, a capital cost allowance (CCA) had been recorded in excess of the asset’s remaining economic value. On the sale of the assets of that class, a portion of the previous CCA is recovered.

**Renunciation**
The process of foregoing, or giving up, a particular benefit in a formal manner. Certain tax credits or deductions can be renounced in favour of an alternative treatment.

**Reserve**
Generally, an income amount that relates to a future period and therefore can be set aside and included in income for that period. A reserve is excluded from the current period’s income and included in the next period’s income. A new reserve would be established in the next period, if applicable.

**Resident**
The determination of whether a person is a resident of Canada is a question of fact. The factors considered are residential ties with Canada, length of time in Canada, object, intention and continuity with respect to stays in Canada.

**Retained earnings**
The total net after-tax income of a corporation, minus
distributions of dividends to shareholders that have accumulated since incorporation.

**Share capital**
Basically, the owner’s investment in a corporation, represented by common and preferred shares. A monetary value is assigned to shares when they are first issued from a corporation’s treasury.

**Small-business limit**
The amount of corporate income that qualifies for the low rate of tax. The federal small-business limit is currently $500,000. This limit is shared between associated corporations.

**Spouse**
The person to whom you are legally married.

**Superannuation**
The term “superannuation” is synonymous with a pension benefit and includes any amount received out of a pension fund or pension plan. Some examples of items that would be considered a superannuation payment would be Old Age Security payments, Canada Pension Plan payments and payments from a privately established pension plan.

**Testamentary trust**
A trust created as a consequence of the death of an individual.

**Trust**
An entity in which a person (a trustee) acting on behalf of a trust holds property for the benefit of one or more other people (beneficiaries). A trust can be created at any time (inter vivos or testamentary) and is taxed as a separate taxpayer.

**Trustee**
A person who, alone or with other trustees, administers the operation of a trust and makes various decisions with respect to the trust—for example, when and how much trust income and/or capital to distribute to the trust’s beneficiaries—based on the terms of the trust document.

**Write-off**
A deduction used to reduce net income for tax purposes.
## Locations

<table>
<thead>
<tr>
<th>Province</th>
<th>City</th>
<th>Telephone</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>British Columbia</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kelowna, BC</td>
<td>T +1 250 712 6800</td>
<td></td>
</tr>
<tr>
<td>Langley, BC</td>
<td>T +1 604 455 2600</td>
<td></td>
</tr>
<tr>
<td>Vancouver, BC</td>
<td>T +1 604 687 2711</td>
<td></td>
</tr>
<tr>
<td>Victoria, BC</td>
<td>T +1 250 383 4191</td>
<td></td>
</tr>
<tr>
<td><strong>Alberta</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Calgary, AB</td>
<td>T +1 403 260 2500</td>
<td></td>
</tr>
<tr>
<td>Camrose, AB</td>
<td>T +1 780 672 9217</td>
<td></td>
</tr>
<tr>
<td>Edmonton, AB</td>
<td>T +1 780 422 7114</td>
<td></td>
</tr>
<tr>
<td>Wetaskiwin, AB</td>
<td>T +1 780 352 1679</td>
<td></td>
</tr>
<tr>
<td><strong>Manitoba</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Winnipeg, MB</td>
<td>T +1 204 944 0100</td>
<td></td>
</tr>
<tr>
<td><strong>Ontario</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Barrie, ON</td>
<td>T +1 705 728 3397</td>
<td></td>
</tr>
<tr>
<td>Beamsville, ON</td>
<td>T +1 905 563 4528</td>
<td></td>
</tr>
<tr>
<td>Burlington, ON</td>
<td>T +1 289 313 0300</td>
<td></td>
</tr>
<tr>
<td><strong>Ontario</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Barrie, ON</td>
<td>T +1 705 728 3397</td>
<td></td>
</tr>
<tr>
<td>Beamsville, ON</td>
<td>T +1 905 563 4528</td>
<td></td>
</tr>
<tr>
<td>Burlington, ON</td>
<td>T +1 289 313 0300</td>
<td></td>
</tr>
<tr>
<td><strong>Fort Erie</strong></td>
<td>T +1 905 871 6620</td>
<td></td>
</tr>
<tr>
<td><strong>Georgetown</strong></td>
<td>T +1 905 877 5155</td>
<td></td>
</tr>
<tr>
<td><strong>Hamilton</strong></td>
<td>T +1 905 523 7732</td>
<td></td>
</tr>
<tr>
<td><strong>London</strong></td>
<td>T +1 519 672 2930</td>
<td></td>
</tr>
<tr>
<td><strong>Markham</strong></td>
<td>T +1 416 366 0100</td>
<td></td>
</tr>
<tr>
<td><strong>Mississauga</strong></td>
<td>T +1 416 366 0100</td>
<td></td>
</tr>
<tr>
<td><strong>National Toronto</strong></td>
<td>T +1 416 366 4240</td>
<td></td>
</tr>
<tr>
<td><strong>New Liskeard</strong></td>
<td>T +1 705 647 8100</td>
<td></td>
</tr>
<tr>
<td><strong>Niagara Falls</strong></td>
<td>T +1 905 358 5729</td>
<td></td>
</tr>
<tr>
<td><strong>North Bay</strong></td>
<td>T +1 705 472 6500</td>
<td></td>
</tr>
<tr>
<td><strong>Orillia</strong></td>
<td>T +1 705 326 7605</td>
<td></td>
</tr>
<tr>
<td><strong>Port Colborne</strong></td>
<td>T +1 905 834 3651</td>
<td></td>
</tr>
<tr>
<td><strong>St. Catharines</strong></td>
<td>T +1 905 682 8363</td>
<td></td>
</tr>
<tr>
<td><strong>Thunder Bay</strong></td>
<td>T +1 807 345 6571</td>
<td></td>
</tr>
</tbody>
</table>
Locations

**Abbreviations**

<table>
<thead>
<tr>
<th>Location</th>
<th>Phone</th>
</tr>
</thead>
<tbody>
<tr>
<td>Toronto, ON</td>
<td>T +1 416 366 0100</td>
</tr>
<tr>
<td>New Brunswick</td>
<td></td>
</tr>
<tr>
<td>Bathurst, NB</td>
<td>T +1 506 546 6616</td>
</tr>
<tr>
<td>Fredericton, NB</td>
<td>T +1 506 458 8200</td>
</tr>
<tr>
<td>Grand Falls, NB</td>
<td>T +1 506 473 5068</td>
</tr>
<tr>
<td>Miramichi, NB</td>
<td>T +1 506 622 0637</td>
</tr>
<tr>
<td>Moncton, NB</td>
<td>T +1 506 857 0100</td>
</tr>
<tr>
<td>Perth-Andover, NB</td>
<td>T +1 506 273 2276</td>
</tr>
<tr>
<td>Saint John, NB</td>
<td>T +1 506 634 2900</td>
</tr>
<tr>
<td>Woodstock</td>
<td>T +1 506 324 8040</td>
</tr>
<tr>
<td>Nova Scotia</td>
<td></td>
</tr>
<tr>
<td>Antigonish, NS</td>
<td>T +1 902 863 4587</td>
</tr>
<tr>
<td>Bridgewater, NS</td>
<td>T +1 902 543 8115</td>
</tr>
<tr>
<td>Digby, NS</td>
<td>T +1 902 245 2553</td>
</tr>
<tr>
<td>Halifax, NS</td>
<td>T +1 902 421 1734</td>
</tr>
<tr>
<td>Kentville, NS</td>
<td>T +1 902 678 7307</td>
</tr>
<tr>
<td>New Glasgow, NS</td>
<td>T +1 902 752 8393</td>
</tr>
<tr>
<td>Port Hawkesbury, NS</td>
<td>T +1 902 625 5383</td>
</tr>
<tr>
<td>Sydney, NS</td>
<td>T +1 902 562 5581</td>
</tr>
<tr>
<td>Truro, NS</td>
<td>T +1 902 893 1150</td>
</tr>
<tr>
<td>Yarmouth, NS</td>
<td>T +1 902 742 7842</td>
</tr>
<tr>
<td>Prince Edward Island</td>
<td>T +1 902 892 6547</td>
</tr>
<tr>
<td>Charlottetown, PE</td>
<td>T +1 902 838 4121</td>
</tr>
<tr>
<td>Montague, PE</td>
<td>T +1 902 436 9155</td>
</tr>
<tr>
<td>Summerside, PE</td>
<td></td>
</tr>
<tr>
<td>Newfoundland and Labrador</td>
<td>T +1 709 634 4382</td>
</tr>
<tr>
<td>Corner Brook, NL</td>
<td>T +1 709 651 4100</td>
</tr>
<tr>
<td>Gander</td>
<td>T +1 709 896 2961</td>
</tr>
<tr>
<td>Happy Valley-Goose Bay</td>
<td>T +1 709 489 6622</td>
</tr>
</tbody>
</table>
Locations

Marystown, NL
T +1 709 279 2300

St. John’s, NL
T +1 709 778 8800
Index

A
Active business income ............................................. 35, 37, 224
Adoption .................................................................. 115, 125
Allowable business investment loss (ABIL) .......... 186, 187, 188, 191
Alimony and maintenance .............................................. 107
  Registration of agreements .................................. 108
  Third-party payments ........................................ 109
Alter-ego .................................................................. 173
Alternative minimum tax (AMT) .............................. 194, 203, 207
Apprenticeship job creation tax credit ......................... 33
Affiliated ................................................................ 190, 224
Artists ..................................................................... 135
Associated ................................................................ 38
Attendant care .......................................................... 117, 118, 125
  Retirement home .................................................. 125
Automobile .............................................................. 47, 48, 74
  Allowances .......................................................... 51, 77
  Capital cost allowance ........................................ 19, 75
  Expenses ........................................................... 49, 51
  GST/HST and automobiles .................................. 74
Logbook ................................................................... 48
Operating costs ...................................................... 48, 49, 75
Parking .................................................................... 49, 50, 51
Salespersons ........................................................... 25, 37
Standby charge ....................................................... 47, 48, 49, 75
Taxable benefits ...................................................... 47, 48

B
Beneficiary ................................................................. 225
  RDSP ................................................................. 147, 148, 149, 150
  RRSP ................................................................. 96, 150
  Trust ................................................................. 179, 204, 209
Bonuses ................................................................... 39, 40
Books and records ..................................................... 219
Business loss ............................................................. 23, 32, 85, 191
Business income ...................................................... 18, 22, 23, 34, 85, 107, 111, 183

C
Canada Child Tax Benefit (CCTB) ......................... 132, 134, 176
Index

Shared custody arrangements ............................................ 134
Canada Disability Savings Bonds and Grants. 147, 148, 149, 150
Canada Education Savings Grant (CESG)............................ 146
Canada Employment Credit ............................................. 129
Canada Pension Plan ...................................................... 28, 129, 176
Contributions .................................................................. 28
Splitting benefits with spouse ........................................... 104, 106, 151
Canadian residents working in the United States ................. 159
Capital cost allowance (CCA) .......................................... 19
Automobile .................................................................. 19, 75
Classes .......................................................... Table 6
Rental property ............................................................ 181, 182
Capital dividend .............................................................. 191
Capital gain ...................................................................... 183
Capital gains deduction ................................................. 186, 187, 188
ABIL ....................................................................... 186, 187, 188
CNIL ....................................................................... 186, 187, 188
Farming property .......................................................... 187
Fishing property ......................................................... 188
Qualified small business corporation share ...................... 186, 187
Deferral for investment in small businesses ...................... 189
Identical properties ........................................................ 184
Personal-use capital property ........................................ 141
Principal Residence ....................................................... 140
Reserve ..................................................................... 182, 189
Capital loss ...................................................................... 190
ABIL ....................................................................... 191
Personal-use capital property ........................................ 141
Stop loss rules .............................................................. 190
Capital tax ...................................................................... 38
Caregivers .................................................................... 116
Charitable donations .................................................... 118, 119, 120, 121, 122, 174
Childcare expenses ....................................................... 106, 107
Investment tax credit for childcare .................................. 33
Children's arts costs ...................................................... 132
Children's fitness costs .................................................. 131, 132
Child support ............................................................... 107, 108, 109, 110, 154
Clearance certificate ..................................................... 161, 162, 175
Clergy ....................................................................... 138
Collections .................................................................... 215
Limitation period ........................................................... 216
Index

Common-law couples—taxation .................................................. 134
Conferences and conventions .................................................. 28
Contractors ........................................................................... 60, 61, 139
Cumulative net investment loss (CNIL) .................................. 199

D
Deceased taxpayers ................................................................... 175
  Capital properties ............................................................... 180
  CCTB and UCCB .............................................................. 176
  CPP and OAS ................................................................. 176
  Executor’s responsibilities .............................................. 175
  Filing obligations of legal representative ............................ 177
  Funeral expenses ................................................................ 180
  GST/HST credit ................................................................ 176
  Instalments ....................................................................... 176
  Rights or things .................................................................. 178, 179
  RRSPs and RRIFs ............................................................. 97
Deferred Profit Sharing Plan (DPSP) ................................. 86, 91, 98, 100, 128
Depreciation ........................................................................... 19
  Available-for-use ............................................................ 21
  Half-year ........................................................................ 21
Directors’ fees ....................................................................... 40
Disability supports deduction ............................................... 125
Disabled persons ................................................................. 93, 94, 125, 130, 131, 132, 147
Discounts (employees) ............................................................ 45
Dividend income ..................................................................... 191
  Capital dividend ............................................................. 191
  Eligible dividend ........................................................... 192, 193, 194
  Foreign source ............................................................... 194, 205
  Gross-up and tax credit .................................................. 192
  Regular dividend ........................................................... 191
  Transfer between spouses ............................................... 195
Divorce ................................................................................... 107, 109
  Deductibility of legal fees ................................................ 109, 110
Dues .................................................................................... 25, 26, 46

E
Earned income (RRSP) ...................................................... 40, 82, 85, 86, 88, 90, 95
EFILE210
Eligible capital property ....................................................... 22, 154
Index

Amortization ................................................................. 22
Eligible dividends .......................................................... 192, 193, 194
Designation ................................................................. 193, 194
General rate income pool (GRIP) ................................. 192, 193
Low rate income pool (LRIP) ..................................... 193
Emergency volunteers .................................................. 139
Employee benefit plan ............................................... 158
Employee loans .......................................................... 43, 46
Employment insurance (EI) ........................................ 19
Contributions ............................................................ Table 8
Family members .......................................................... 19
Entertainers ................................................................. 135
Estate freeze/refreeze ............................................... 170

F
Fairness measures .......................................................... 214
Family caregiver credit ............................................... 116
Farming ......................................................................... 61, 62, 63, 64, 65
Capital gains deduction ............................................... 187
Intergenerational transfers ......................................... 64
Losses ........................................................................ 32, 63
Qualified farm property ........................................... 64, 187
Restricted farm losses .................................................. 64
Family trusts ................................................................. 153, 203
Filing a tax return .......................................................... 82
Filing deadline SR&ED return ..................................... 59
Filing deadline final return ......................................... 178
Fines and penalties ....................................................... 31
Fishing ......................................................................... 188, 189
Capital gains deduction ............................................... 188, 189
Qualified fishing property ........................................... 188, 189
Flow-through shares .................................................. 16, 202, 226
Foreign tax credit ..................................................... 160, 161, 166, 205
Foreign investments ................................................ 205, 206
Reporting requirements ........................................... 205, 206
Foreign pensions ....................................................... 156
Foreign spinoffs .......................................................... 194
Forestry operations .................................................... 61, 63
Index

G
Gifts and awards ............................................................... 43, 44
Golf ........................................................................... 25, 26, 121
GST/HST .............................................................................. 67
   Automobiles ............................................................... 74, 75, 76, 77
   Credit for individuals ....................................................... 83, 84
   Employee reimbursements .............................................. 72
   Employee or partner rebate ............................................. 76
   Home office ........................................................................ 24, 25
   Input tax credits ............................................................... 70, 71, 72, 73
   Large businesses ............................................................. 69, 71, 72, 78
   New businesses ................................................................... 69
   Real property ....................................................................... 78
   Registration, collection and remittance .......................... 68, 69
   Reporting periods ............................................................. 69
   Sale of a business ............................................................. 79
   Streamlined accounting ..................................................... 73, 74

H
Health and dental insurance premiums ............................. 30, 123
Holding companies ............................................................ 198, 199, 226
Home Buyer’s Plan ............................................................. 92, 93
Home office ........................................................................ 22, 23, 24, 25
   Employee ........................................................................ 24
   Self-employed .................................................................. 23
   GST/HST ......................................................................... 24, 25

I
Income splitting ................................................................. 103, 143, 144, 151, 152, 153
Income tax instalments .................................................... 176, 217, 218
Income trust ......................................................................... 197
Incorporation ......................................................................... 34
Incorporation of professionals ............................................. 35
Individual pension plan (IPP) ..................................................... 100, 101, 102
Information slips ................................................................. 61, 209, 210, 213
Instalments ........................................................................... 176, 217, 218
   Individuals ........................................................................ 217
   Corporations ........................................................................ 218
Insurance ........................................................................... 30, 31
Index

Health and dental .................................................................30
Life ................................................................................31
Interest ........................................................128, 195, 200, 220
Expense ...............................................................200, 201, 202
Income ................................................................195, 196
Student loans ...............................................................128
Internet filing .................................................................211
Corporations .................................................................211
Inventory ...............................................................31, 32, 63
Investment tax credit .........................................................33, 57
Childcare spaces ...............................................................33
SR&ED ................................................................57, Table 5

J
Joint-partner .........................................................................173

K
Kiddie tax .....................................................................144, 153

L
Leasing ......................................................................21, 49, 50
Legal expenses ...........................................................109, 110, 126
Life Income Fund (LIF) .......................................................99
Lifelong Learning Plan ..........................................................93
Life insurance ...............................................................31, 60, 171, 172
Limited partnerships .....................................................15, 202, 203, 227
At risk rules ...................................................................203
Listed personal property ......................................................142
Loans ........................................................................41, 42, 43, 46, 91, 142
Employee .......................................................................46
Excepted ........................................................................42, 43
Family members .........................................................142, 143, 144, 145
RRSPs ...........................................................................91
Shareholder .....................................................................41
Logbook – Automobile ...........................................................48
Loss ........................................................................32, 190, 191, 199
Allowable business investment loss (ABIL) .............. 191
Business ........................................................................32
Capital ...........................................................................190
Cumulative net investment loss (CNIL) ...................... 199
Index

Farm ................................................................. 63, 64
Lottery winnings ..................................................... 154
Lump-sum payments–retroactive .......................... 153

M
Meals and entertainment (M&E) .............................. 26, 27, 28
  GST/HST ................................................................. 27
  Long-haul truck drivers ...................................... 27
Mineral exploration tax credit ................................. 202
Moving expenses .................................................... 45, 111, 112
Musicians ................................................................. 135
Mutual funds ............................................................ 196, 197
My account .............................................................. 213
My business account .............................................. 213

N
NETFILE ................................................................. 70, 210, 211
Notice of assessment/reassessment .................... 212, 213
Notice of objection ................................................. 212, 213
National child benefit .......................................... 133, 147
Non-competition payments .................................. 154, 155
Non-residents ......................................................... 66, 67, 160, 161, 162, 163, 164
  Interest payments .................................................. 66
  Requirement to file a tax return .......................... 81, 160, 163
  Services rendered in Canada ............................... 66
  Taxable Canadian property ................................. 160, 161, 162
  Tax obligations ....................................................... 160
Northern residents deduction ............................... 137

O
Old Age Security (OAS) .......................................... 105, 176
  Clawback ................................................................. 104, 105
Operating loss ....................................................... 32
Overcontributions .................................................. 89, 90, 103, 145
  RESP ................................................................. 145
  RRSP ................................................................. 89, 90
  TFSA ................................................................. 103
Overtime ................................................................. 45
Index

P

Parking ......................................................................49, 50, 51
Partnerships ............................................15, 16, 181, 210, 228
    Corporate partners.........................................................16
    Limited........................................................................203, 227
Partnership deferral ................................................................16
Passenger vehicle ................................................................74, 75
Past service pension adjustment (PSPA) ........................................87, 88
Penalties ........................................................................220, 221, 222, 223
    Civil penalties for misrepresentation by third parties ......223
    Failure to file................................................................169, 221, 222
    Gross negligence..........................................................221
    Insufficient instalments.................................................220
    Late-filed information return ..................................220, 221
    Late-filed tax return .......................................................220
    Ministerial discretion to waive ........................................222
    Repeat offense .............................................................220
    Tax preparer ................................................................222, 223
Pension adjustment (PA) ..............................................87, 88, 98
Pension income splitting ............................................103, 104
Pooled Registered Pension Plan (PRPP) ..................................100
Planned giving ................................................................174
Post-secondary ................................................................113, 127, 128
Principal residence ................................................139, 140, 141
    Designation ..................................................................140
    Rental of home .............................................................141
Private health services plan .............................................30, 45
Probate fees ..................................................................173, 174, 228
Professional and union dues ..............................................44, 85
Public transit passes .........................................................130

Q

Qualified farm property ...................................................64, 187
Qualified fishing property .......................................................188
Qualified small business corporation ..............................186, 187

R

Racehorses ........................................................................62
Real Estate Investment Trust (REIT) ........................................197
Refund ................................................................. 19, 57, 70, 82, 216
Employment insurance ............................................... 19
GST/HST (input tax credit) ......................................... 70
Income tax .................................................................. 82, 216
Investment tax credit .................................................. 57, 58
Registered Disability Savings Plan (RDSP) ........ 147, 148, 149, 150
  Canada Disability Savings Bond (CDSB) ....... 148, 149, 150
  Canada Disability Savings Grant (CDSG) ... 147, 148, 149, 150
  Rollover to RRSP or RRIF ........................................ 150
Registered Education Savings Plan (RESP) .... 145, 146, 147
  Canada Education Savings Grant (CESG) ....... 146
  Canada Learning Bond (CLB) ................................ 147
Contributions .......................................................... 145
  Transfer to RRSP ..................................................... 146
Registered Pension Plan (RPP) ......................... 86, 87, 98, 99
  Defined benefit ....................................................... 98
  Defined contribution ............................................. 99
Registered Retirement Income Fund (RRIF) .... 94, 95
Registered Retirement Savings Plans (RRSP) .... 84 to 101
  Administration fee .................................................. 89
  Age limits .............................................................. 88
  Carry-forward ....................................................... 90
  Contribution limits ................................................ 85, 86, 88
  Death .................................................................... 96
  Investment in CCPC shares .................................. 87
  Loans to acquire .................................................... 91
  Overcontributions ................................................ 89
  Past service contributions .................................. 98, 99, 101
  Past service pension adjustment ..................... 87
  Pension adjustment ............................................... 87
  Pension adjustment reversal .............................. 87
  Retiring allowance ............................................... 90
  Self-directed ........................................................ 86
  Spousal ................................................................. 85
  Withdrawals to fund home purchase ................ 92, 93
  Withdrawals to finance education ..................... 93
Remote work site .................................................... 48
Rental properties ...................................................... 181, 182, 183
  Joint owner or partner ........................................... 181
  Depreciation .......................................................... 182
  Sale of property ...................................................... 182, 183
Index

Reporting tax avoidance transactions.................................223
Represent a client .................................................................214
Research grants ...............................................................112, 113
Residence ...................................................................155, 156, 157, 158, 159
    Becoming a Canadian resident ...................................155, 156
    Ceasing to be a Canadian resident ..............................156, 157, 158
    Residency defined ......................................................158, 159
Resource sector ................................................................202
Restricted Life Income Fund (RLIF) ..................................99
Retirement compensation arrangement..........................158
Retroactive payments .........................................................153
Rights or things ..............................................................178, 179

S

Salary deferral arrangements ....................................................40
Scholarships ......................................................................113
Scientific Research and Experimental Development (SR&ED) ......55, 56, 57, 58, 59
    Investment tax credits .................................................57
Segregated funds ................................................................197
Self-employed ..............................................................15, 23, 29, 30, 31, 35, 51, 68
Separation .......................................................................108, 109, 110
    Deductibility of legal fees ..........................................109, 110
Shareholder agreements ......................................................60
Shareholder loans ..............................................................41, 42, 43
Small business deduction ....................................................35, 36, 37
Social events for employees ...............................................43
Sports club .....................................................................46
Spouse ............................................................................229
    Dividends ....................................................................195
    RRSP ..........................................................................85
    Splitting CPP benefits .................................................151
    Transfers (inter vivos) ....................................................91, 142, 143
    Transfers (on death) ......................................................180
    Travel expenses ..........................................................46
    Unused credits ..............................................................129
Stock options .................................................................52, 53, 54
    CCPC .......................................................................53, 54
    Decline in value ..........................................................54
    Public company ..........................................................54
Succession and estate planning .............................................. 169 to 175
Support payments ............................................................... 108, 109, 110, 216

T

Taxable benefits ............................................................. 43, 44, 45, 46, 47, 52
  Christmas parties and special events .................................. 43
  Employee loans ............................................................. 46, 47
  Employer-paid professional membership fees ................... 44
  Non-cash gifts and awards ............................................... 43
  Non-taxable .................................................................... 45
  Personal use of company vehicle ...................................... 47, 48, 49
  Stock options ............................................................... 52, 53, 54, 55
Taxable Canadian property ............................................... 160, 161, 162
Tax credits – personal ..................................................... 113 to 132
  Adoption ....................................................................... 125
  Age ............................................................................. 116
  Basic personal ............................................................. 114
  Caregiver ..................................................................... 116
  Charitable donations ...................................................... 118, 119, 120, 121
    Donating property ...................................................... 119
    Receipting guidelines .................................................. 121
    US charitable organizations ........................................ 118
  Child under 18 years ..................................................... 115
  Children’s arts ............................................................... 132
  Children’s fitness ......................................................... 131
  Disability ....................................................................... 117
  Education ....................................................................... 127
  Eligible dependant ........................................................ 114
  Employment .................................................................... 129
  First-time home buyer .................................................. 129
  Infirm dependant .......................................................... 115, 116
  Medical expenses ......................................................... 122, 123, 124
    Dependents other than spouse or common-law partner .. 123
    Minor children ................................................................ 124
    Refundable medical expense credit ................................ 124
  Pension income ............................................................ 128
  Political donations ......................................................... 122
  Public transit ................................................................. 130
  Spouse or common-law partner ...................................... 114
  Student loan interest ...................................................... 128
Tax credit versus tax deduction ........................................... 113, 114
Textbook ............................................................................. 127
Tuition fees .......................................................................... 126
Tax-free savings account (TFSA) ................................... 90, 102, 103, 106, 163
Taxpayer relief – fairness provisions .................................... 214, 215
Tax shelters ........................................................................... 21, 121, 121, 199, 202, 203, 221
TELEFILE ........................................................................... 210, 211
Temporary assignments outside Canada............................. 158
Third party penalties .............................................................. 223
Tools ...................................................................................... 21, 135, 136, 137
Apprentice mechanic deduction ........................................... 135
Tradespersons ......................................................................... 136
Transfers ................................................................................ 129, 142, 143, 144
Unused credits from spouse or common-law partner ............ 129
Capital property to spouse or common-law partner ............. 142, 143
Capital property to other family members ........................... 144
Transfer pricing ...................................................................... 65
Trusts .................................................................................... 153, 173, 197, 203, 204

US citizens resident in Canada .............................................. 162
US estate tax .......................................................................... 167
US financial reporting requirements ...................................... 169
US real estate ......................................................................... 165, 166
Selling US property ................................................................ 166
US residency regulations ......................................................... 167
US Social Security ................................................................... 164
Uniforms .................................................................................. 45
Universal Child Care Benefit (UCCB) .................................... 133, 176

Voluntary disclosure ............................................................... 222
Volunteer firefighters ............................................................. 139

Wage-loss replacement plans .................................................. 31, 44
Wills ...................................................................................... 175, 176
Withholding tax .................................................................... 66, 67, 161, 165, 166, 167, 205
Interest payments to non-residents ....................................... 66, 67
Income from US sources ....................................................... 165, 166, 167
Working income tax benefit .................................................. 81, 130
Workers’ Compensation benefits .......................................... 154
Workspace in home ........................................................... 23, 24

Year-end .............................................................................. 226