

Chapter One Test Item File Solutions

TIF Solution One - 1

1. The other sources of federal revenues that are shown in Figure 1-1 of the text are:
 - Corporate income taxes.
 - Non-resident income taxes.
 - GST.
 - Customs and import duties.
 - Other excise taxes.
 - EI premiums.
2. In the *Income Tax Act*, the term "person" can refer to an individual, a corporation, or a trust.
3. Provincial income taxes on individuals are calculated by applying a provincial rate schedule to the same Taxable Income figure that is used to calculate the federal income tax for individuals. Provincial credits are then applied to the resulting figure. The provincial brackets may differ from the federal brackets. In addition, provincial credits may be different than the federal credits.
4. There are many examples that could be used here. The text divides them into resource allocation (e.g., public health care), distribution effects (e.g., federal GST credit), stabilization effects (e.g., deficit reduction), and fiscal federalism (e.g., allocations to various levels of government).
5. Examples provided in the text are as follows:
 - Tax revenues are used to provide public goods and services.
 - Excise taxes are used to discourage the consumption of alcohol and tobacco products.

There are, of course, many other examples that could be cited.
6. The child benefit system is designed to assist families with children. It would appear that the government is encouraging people to have children. The fact that the benefits are reduced as income increases suggests that it is also designed to assist lower income families care for these children.
7. There are a number of possibilities here. They include:
 - Progressive rates increase the complexity of the system.
 - Progressive rates are unfair to individuals with highly variable income streams.
 - Progressive rates are unfair to single income family units.
 - Progressive rates lead to pressure for various types of tax concessions.
 - Progressive rates discourage high income individuals from making additional efforts.
 - Progressive rates encourage tax evasion.
8. While the sales tax rate is the same for all individuals without regard to their income level, lower income individuals normally spend a higher percentage of their total income. Since the sales tax is levied on the amounts spent, this means that the sales tax paid by lower income individuals represents a larger percentage of their income. As a consequence, they are generally considered to be regressive in nature.
9. Horizontal equity is achieved when taxpayers in similar economic circumstances are subject to similar levels of taxation. Vertical equity is achieved when taxpayers in different economic circumstances are subject to taxes in a different manner.

10. The reasons that are listed in the text are as follows:

- It is less costly to administer tax expenditures than it is to administer government funding programs.
- More decisions are left to the private sector so that funds may be allocated more efficiently.
- Tax expenditures reduce the visibility of certain government actions. This is particularly beneficial if some social stigma is attached to the programs. For example, a child tax benefit system is more acceptable than increasing social assistance payments.
- Tax expenditures reduce the progressivity of the tax system. As many of the tax expenditures, such as tax shelters, are more available to higher income taxpayers, they serve to reduce effective tax rates in the higher rate brackets.

11. This situation reflects the fact that when a new Section is added, it has been more convenient to attach a decimal designation to the new Section, as opposed to renumbering all of the Sections that follow the new Section. As an example, over several years, the Department of Finance has added five new Sections after Section 12. They have been numbered Section 12.1 through Section 12.5. If they had used whole numbers for these new Sections, it would have been necessary to renumber all of the remaining Sections in the Act each time a new Section was added.

12. The purposes of these treaties are as follows:

- They attempt to avoid double taxation of taxpayers who may have reason to pay taxes in more than one jurisdiction.
- They try to prevent international evasion of taxes.

13. The required four items can be selected from the following:

- CRA Web Site
- Interpretation Bulletins
- Income Tax Folios
- Information Circulars
- Income Tax Technical News
- CRA News Releases, Tax Tips, and Fact Sheets
- CRA Guides
- CRA Pamphlets
- Advance Income Tax Rulings
- Technical Interpretations

14. For individuals and inter vivos trusts, the taxation year is equal to the calendar year. In contrast, corporations can always use a fiscal period. A fiscal period can end on any date, with the only constraint being that it cannot exceed 53 weeks for a corporation. With respect to testamentary trusts, prior to 2016, like corporations, they could always use a non-calendar fiscal year. In 2016 and subsequent years, their use of non-calendar fiscal periods is significantly restricted (see Chapter 19).

15. The circumstances that would result in a non-resident person having to pay income taxes in Canada are as follows:

- The non-resident person earns employment income in Canada.
- The non-resident person carried on a business in Canada.
- The non-resident person has a gain on the disposal of a taxable Canadian property.

16. As stated in the text, residence is the cornerstone of Canadian income taxation. If a person is considered a resident of Canada in a given year, that person will be subject to Canadian income tax for that year on all sources of income. Alternatively, if the person is a non-resident, Canadian Part I tax will only apply to Canadian employment income, Canadian business income, and gains on the disposition of Taxable Canadian Property.
17. As stated in S5-F1-C1, the primary factors that will be considered by the CRA are as follows:
- Whether the individual is continuing to maintain a dwelling in Canada.
 - Whether the spouse or common-law partner of the individual remains in Canada.
 - Whether the individual has dependants who remain in Canada.
18. The main factors here would be:
- Does the individual have a dwelling in Canada?
 - Does the individual's spouse or common-law partner live in Canada?
 - Do the dependants of the individual live in Canada?

Other factors that could be mentioned include:

- Owning personal property in Canada (such as furniture, clothing, automobiles, and recreational vehicles).
- Social ties with Canada (such as memberships in Canadian recreational and religious organizations).
- Economic ties with Canada (such as employment with a Canadian employer and active involvement in a Canadian business, and Canadian bank accounts, retirement savings plans, credit cards, and securities accounts).
- Hospitalization and medical insurance coverage from a province or territory of Canada.
- A driver's license from a province or territory of Canada.
- A vehicle registered in a province or territory of Canada.
- A seasonal dwelling place in Canada or a leased dwelling place.
- Holding a Canadian passport.
- Membership in Canadian unions or professional organizations.

19. As noted in the text, S5-F1-C1 identifies the following factors:

Intent The issue here is whether the individual intended to permanently sever residential ties with Canada. If, for example, the individual has a contract for employment, if and when he returns to Canada, this could be viewed as evidence that he did not intend to permanently depart. Another factor would be whether the individual complied with the rules related to permanent departures (i.e., as noted in Chapter 8, there is a deemed disposition of an individual's property at the time of departure from Canada, resulting in the need to pay taxes on any gains).

Frequency Of Visits If the individual continues to visit Canada on a regular and continuing basis, particularly if other secondary residential ties are present, this would suggest that he did not intend to permanently depart from Canada.

Residential Ties Outside Of Canada A further consideration is whether or not the individual establishes residential ties in another country. If someone leaves Canada and travels for an extensive period of time without settling in any one location, it will be considered as evidence that he has not permanently departed from Canada.

20. A Canadian resident normally becomes a non-resident on the latest of the following days:
- on leaving Canada,
 - when a spouse and/or dependants leave Canada, and
 - on becoming a resident of another country.

21. As a sojourner, Jane would be assessed Canadian income taxes on her world wide income for the entire year. As she would not be considered a resident of a province, she would be assessed an additional federal income tax of 48 percent of her basic federal tax otherwise payable.

In contrast, Jack would only be assessed Canadian income taxes on his world wide income for the 210 day period prior to his departure from Canada. In addition, he would be assessed provincial income tax in the province of Manitoba for this 210 day period.

22. The required three items could be selected from the following:

Permanent Home If the individual has a permanent home available in only one country, the individual will be considered a resident of that country. A permanent home means a dwelling, rented or purchased, that is continuously available at all times. For this purpose, a home that would only be used for a short duration would not be considered a permanent home.

Centre of Vital Interests If the individual has permanent homes in both countries, or in neither, then this test looks to the country in which the individual's personal and economic relations are greatest. Such relations are virtually identical to the ties that are examined when determining factual residence for individuals.

Habitual Abode If the first two tests do not yield a determination, then the country where the individual spends more time will be considered the country of residence.

Citizenship If the tie-breaker rules still fail to resolve the issue, then the individual will be considered a resident of the country where the individual is a citizen.

Competent Authority If none of the preceding tests resolve the question of residency then, as a last resort, the so-called "competent authority procedures" are used. Without describing them in detail, these procedures are aimed at opening a dialogue between the two countries for the purpose of resolving the conflict.

23. If an enterprise is incorporated in Canada after April 26, 1965, it will always be considered resident in Canada. However, if it is incorporated in Canada prior to April 27, 1965, it will only be considered resident in Canada in those situations where it either:
- carried on business in Canada at any time after that date; or
 - was resident in Canada at any time after that date (as measured by the location of the mind and management of the corporation).
24. Limon Inc. is a U.S. resident because it was incorporated in that country. It is also a Canadian resident under the mind and management test. In such dual residency cases, the tie-breaker rule in the Canada/U.S. tax treaty indicates that the taxes will be assessed in the country of incorporation. That means that Limon Inc. would be subject to U.S. income taxes.
25. The components of Net Income For Tax Purposes are employment income, business and property income, net taxable capital gains, other sources of income, and other deductions from income.
26. The phrase "the amount, if any" is used throughout the *Income Tax Act* to indicate that only positive amounts should be considered. In the context of ITA 3(b), the requirement that negative amounts be ignored, in effect, prevents the deduction of current year allowable capital losses in excess of current year taxable capital gains in the determination of Net Income For Tax Purposes.

27. Tax avoidance is a form of tax planning in which the taxpayer, through means that are within the boundaries of tax legislation, arranges his affairs in a manner that allows him to receive benefits without the payment of taxes. Tax planning to achieve tax deferral involves either the delayed recognition of income, or the accelerated recognition of deductions. The payment of tax is delayed, as opposed to permanently avoided.
28. Income splitting involves efforts to share the total income accruing to an individual with family members or other related parties. It will only benefit a taxpayer who is in a high tax bracket in those circumstances where there are family members or other related parties who are in lower tax brackets.
29. The basic type of tax planning that is involved in Registered Retirement Savings Plans is tax deferral — a tax savings results from making contributions that will have to be paid back at a later point in time. There may also be an element of avoidance in that, after retirement, an individual may be in a lower tax bracket than he was during his working years. If this is the case, there will be an absolute reduction in taxes. (This assumes that the basic rate structure is unchanged.)
30. The basic goals of tax planning can be summarized as follows:
- Tax avoidance - To permanently avoid the payment of some amount of tax.
 - Tax deferral - To delay the recognition of certain types of income or accelerate the timing of certain deductions.
 - Income splitting - To have a family or other related group's aggregate taxable income allocated as evenly as possible among the members of the group.

He should contribute the \$5,000 to the spousal RRSP. By contributing to an RRSP he will be deferring taxes. By contributing to a spousal RRSP he is also income splitting and there may be possible tax avoidance if his spouse is taxed at a lower rate when the funds become taxable to her.

TIF Solution One - 2

1. True. A value added tax is a tax levied on the increase in value of a commodity or service that has been created by the taxpayer's stage of the production or distribution cycle.
2. False. Only individuals, corporations, and trusts are taxable entities for income tax purposes.
3. True. Partnerships engaged in commercial activity are taxable entities for GST purposes.
4. False. In general, provincial taxes are based on a specified percentage of federal taxable income.
5. False. The federal government collects taxes for Ontario.
6. True. Even if the rate is the same on all transactions, it will be a higher rate on the taxable income of lower income individuals because they spend a larger percentage of their income.
7. False. Progressive rates discourage both employment and investment, thereby limiting economic growth.
8. True. Tax expenditures are less costly to administer than direct funding programs.
9. True. Part I of the *Income Tax Act* is the largest and the most important part.
10. False. The citation ITA 61(4)(b)(ii) would be read Section 61, Subsection 4, Paragraph b, Subparagraph ii.
11. True. While individuals and inter vivos and most testamentary trusts must use a calendar taxation year, other taxpayers, corporations and testamentary trusts that have been designated as graduated rate estates, can choose to use this period as their taxation year.
12. False. The provisions of the international treaty will prevail.
13. True. An income tax is payable for each taxation year on the Taxable Income of every person resident in Canada at any time in the year.
14. False. Canadian income taxes are assessed on residents of Canada.
15. False. S5-F1-C1 makes it clear that the length of the period of time during which the individual is absent from Canada is not a determining factor with respect to residency.
16. False. Such part year residents will only be taxed on their world side income for the portion of the year prior to their moving to Canada.
17. True.
18. False. Whether the individual continues to maintain social ties is not one of the three most significant factors.
19. False. The length of the period of absence from Canada is not considered a factor in determining residency retention.

20. True. A part year resident for the current year is an individual who either establishes residency in Canada during the current year or, alternatively, terminates residency in Canada during the current year.
21. False. The 183 days do not have to be consecutive.

TIF Solution One - 3

Canadian Tax System

1. C. Head Tax
2. C. Walters and Walters, a group of CPAs operating as a partnership.
3. D. All of the above could be required to file a GST return.
4. A. Personal income tax
5. D. Each province can establish rules for determining the Taxable Income of individuals.
6. C. Individuals, trusts and corporations
7. B. Provincial, federal, and international

Tax Policy Concepts

8. B. Extremely high rates of tax will always encourage individuals to work harder so that they will have more after tax income.
9. C. Ensure fairness in the allocation of resources to different levels of government.
10. B. A progressive rate system provides greater stability in the context of changing economic conditions.
11. B. A regressive tax is one which results in lower effective tax rates for higher income taxpayers.
12. A. It is more costly to administer tax expenditures as opposed to program spending.
13. B. Inelasticity.
14. C. Simplicity.
15. A. Neutrality.
16. D. Horizontal equity.

Income Tax Reference Materials

17. D. The *Income Tax Act* is the most important source of information for dealing with matters related to the federal income tax.
18. D. All Parts of the *Income Tax Act* contain at least one Section.
19. B. Income Tax Folios.
20. C. Dominion Tax Cases.
21. C. Unreported revenues from business transactions.
22. B. The Income Tax Regulations.
23. D. When there is a conflict between the Canadian *Income Tax Act* and an international agreement, the terms of the Canadian *Income Tax Act* prevail.

Liability For Tax

24. B. Corporations must use the calendar year as their taxation year.
25. A. is a resident of Canada.
26. D. Bunly Im, a resident of the United States who earns interest income in Canada.
27. C. Rental income earned in Canada

Residence

Residence Of Individuals

28. C. The individual has become a resident of another country.
29. D. She did not leave taxable Canadian property in Canada.
30. C. An individual who immigrates to Canada during the year is a resident of Canada for tax purposes for the full calendar year.
31. B. Bob, Charles, and Dick.
32. A. To be a resident for tax purposes, an individual must be a Canadian citizen.
33. A. The country in which the individual earns business income.

34. C. Jamal is considered a non-resident of Canada.
35. A. Ravi is a citizen of India, where he was born and lived until moving to Canada on March 1 of the current year. He was transferred by his employer to its Canadian head office.
36. B. A non-resident
37. D. A part-year resident

Residence Of Corporations

38. D. Exeter Ltd. was incorporated in Alberta in 1956. However, it has never carried on business in Canada and its management has always been located in Montana.

Residence Of Corporations And Individuals

39. B. A corporation that was incorporated in North Dakota but carries on all of its business in southern Manitoba.
40. B. Karen Cotin, a computer programmer, had been employed by ABC Systems Ltd. in Toronto. In 2016, she accepted a minimum two-year contract with CS Services Inc. in London, England. Her position with CS Services Inc. started October 1, 2016. Before moving to England, where she will join her fiancé, Karen terminated the lease on her apartment in Toronto and sold her car. It appears Karen has severed all ties with Canada.

Alternative Concepts Of Income

41. C. Net Income For Tax Purposes requires that costs be matched with revenues.
42. B. Net income is determined by adding together several different types of income which are added together based on an ordering rule.

Calculation Of Net Income For Tax Purposes

43. D. If a business loss exceeds all other positive sources of income, Net Income For Tax Purposes is equal to nil.
44. C. Business losses can be netted against employment income in determining the positive amounts to be included under ITA 3(a) and 3(b).
45. C. \$45,000
46. B. \$ 22,000 (\$34,000 + \$4,000 - \$2,000 - \$14,000)
47. B. Nil, with a business loss that can be used in either the previous 3 years or in the next 20 future years of \$12,000 (34,000 + 6,000 + 4,000 - 2,000 - 54,000)

48. B. That the current year allowable capital losses can only be deducted to the extent that there are taxable capital gains during the current year.
49. D. $\$32,000 [\$45,000 + (1/2)(\$20,000 - \$12,000) - \$3,000 - \$14,000]$

Net Income To Taxable Income

50. B. A deduction for the extra costs related to living in prescribed areas of the Canadian north.
51. D. The excess of allowable capital losses over taxable capital gains for the year.

Tax Planning

52. C. Accelerated depreciation (CCA) on rental properties.
53. D. Tax avoidance.
54. B. Tax deferral.
55. C. Making use of the lifetime capital gains deduction.

TIF Solution One - 4

Exam Exercise One - 1 Solution (Taxable Entities For Income Tax Purposes)

Sally Forbes, the Forbes family trust, and Forbes Enterprises Ltd. could be required to file income tax returns. Forbes Boutique, Forbes and Delaney, and the Forbes Foundation are not taxable entities for income tax purposes.

Exam Exercise One - 2 Solution (Taxable Entities For GST Purposes)

Under the GST legislation, all of the listed entities could be required to file a GST return. Where only individuals, corporations and trusts can be required to file an income tax return, the definition of a person (i.e., taxable entity) is much broader for GST purposes. As is explained in detail in Chapter 21, whether an entity is required to file a GST return is dependent on the level of commercial activity.

Exam Exercise One - 3 Solution (Federal And Provincial Taxes Payable)

Federal Tax Payable [(15%)(37,500)]	\$5,625
Provincial Tax Payable [(8.2%)(37,500)]	3,075
<u>Total Tax Payable [(15% + 8.2%)(37,500)]</u>	<u>\$8,700</u>

Exam Exercise One - 4 Solution (Federal And Provincial Taxes Payable)

Federal Tax Payable [(15%)(26,700)]	\$4,005
Provincial Tax Payable [(10%)(26,700)]	2,670
<u>Total Tax Payable [(15% + 10%)(26,700)]</u>	<u>\$6,675</u>

Exam Exercise One - 5 Solution (Regressive Taxes)

Samantha's HST paid totals \$28,080 [(13%)(216,000)]. Based on her Taxable Income of \$625,000, this would represent an effective rate of 4.5 percent ($\$28,080 \div \$625,000$).

Martha's HST paid totals \$2,782 [(13%)(21,400)]. On her Taxable Income of \$12,000, this would be an effective rate of 23.2 percent ($\$2,782 \div \$12,000$).

Exam Exercise One - 6 Solution (Regressive Taxes)

Veronica's HST paid totals \$21,060 [(13%)(162,000)]. Based on her Taxable Income of \$843,000, this would represent an effective rate of 2.5 percent ($\$21,060 \div \$843,000$).

Her sister's HST paid totals \$4,680 [(13%)(36,000)]. On her Taxable Income of \$8,000, this would be an effective rate of 58.5 percent ($\$4,680 \div \$8,000$).

Exam Exercise Solution One - 7 (Non-Resident Liability For Tax)

She is not correct. Under ITA 2(3) she would be subject to Canadian taxes on employment income earned in Canada, but not on her U.S. employment income.

Exam Exercise One - 8 Solution (Non-Resident Liability For Tax)

He is not correct. Under ITA 2(3) he would be subject to Canadian taxes on the gain resulting from a disposition of Taxable Canadian Property.

Exam Exercise Solution One - 9 (Residential Ties)

While the situation is not completely clear, it is likely that the CRA would conclude that Mr. Resner is no longer a Canadian resident. By retaining his residence, he has maintained one of the primary residential ties. However, the fact that he was not able to sell the property, accompanied by the long-term lease to a third party, would probably be sufficient evidence that this is not a significant residential tie. The retention of his membership in the Chartered Professional Accountants Association Of Alberta would be viewed as a secondary residential tie. However, it is unlikely that this tie would be sufficient to cause Mr. Resner to be viewed as a Canadian resident.

Exam Exercise Solution One - 10 (Temporary Absences)

Mary did, in fact, sever most of her residential ties with Canada. This would suggest that she would not be considered a Canadian resident during the two years she worked in New York City. However, the fact that she returned frequently to visit her boyfriend might lead the CRA to assess her on the basis of being a Canadian resident during this period, but it is not clear that such an assessment would be successful.

Exam Exercise Solution One - 11 (Temporary Absences)

While John severed the great majority of his residential ties with Canada, two factors would suggest that the CRA would likely view him as a Canadian resident during the 18 months that he is absent from the country:

- His frequent visits to spend time with his dog.
- Perhaps more importantly, the fact that he claimed a Canadian address to maintain access to the Ontario health care system would be viewed as a very significant factor.

While the answer is not clear cut, our opinion would be that these factors would lead to the conclusion he maintained his Canadian residency. Given the fact that he appears to be defrauding the Ontario health care system, he might be wise to avoid disputing his continued residency.

Exam Exercise Solution One - 12 (Part Year Residence)

Melissa would be taxed on her worldwide income for the part of the year that she was resident in Canada. This would be the period January 1 through July 1, the date that her husband and children fly to the U.S. July 1 would be the latest of: the date that Melissa leaves Canada (March 15), the date that Melissa establishes U.S. residency (March 15), and the date that her husband and children depart Canada (July 1). It is unlikely that the fact that her house was not sold until a later date would influence her residence status.

Exam Exercise Solution One - 13 (Part Year Residence)

For residency purposes, an individual is considered to have ceased being a resident of Canada at the latest of three dates:

1. The date the individual leaves Canada.
2. The date the individual's family leaves Canada.
3. The date the individual establishes residency in another country.

In Barton's case the latest of the dates would be July 1, 2018, the date on which he receives the required residency documents. Given this, Barton would be considered a Canadian resident for the entire 2017 taxation year. In addition, he would be a part year resident for the period January 1, 2018 through June 30, 2018.

Exam Exercise Solution One - 14 (Individual Residency)

Under ITA 250(1)(c)(i), Mrs. Sothor would be a deemed Canadian resident because of her position as a Canadian ambassador and the fact that she was a Canadian resident at the time she was appointed to this post. As her husband is exempt from Tanzanian taxation due to his relationship to a deemed resident, he is a deemed resident of Canada under ITA 250(1)(g). Of her two children, the younger son would be a deemed resident under ITA 250(1)(f) as he is a Canadian ambassador's dependent child. However, the older son would not be a deemed resident because his income exceeds the base for the basic personal tax credit for 2017 of \$11,635 and he would therefore not be considered a dependant.

Exam Exercise Solution One - 15 (Individual Residency)

While Ms. Washton is the child of a Canadian High Commissioner, it appears that she is no longer a dependant of this individual. It would also appear that she has income in excess of the base for the basic personal tax credit for 2017 of \$11,635. As a consequence, she would not be considered a deemed resident under ITA 250(1).

Exam Exercise Solution One - 16 (Corporate Residency)

As the Company was incorporated in Canada after April 26, 1965, it would be deemed to be a Canadian resident under ITA 250(4). While the problem does not provide enough information to determine this, it is possible that the Company has dual residency with the country or countries where it does business. This could result in the application of one or more international tax treaties. Note that, in general, where a corporation does business is not relevant to the residency decision.

Exam Exercise Solution One - 17 (Corporate Residency)

As Wolfhowl Ltd. was incorporated in Canada prior to April 27, 1965, it will only be considered to be a Canadian resident if it has carried on business in Canada or become a Canadian resident subsequent to April 26, 1965. As the director's meetings were held in Canada until 1971, this would suggest that the "mind and management" of the Company was in Canada during this period. This would make the Company a Canadian resident subsequent to April 26, 1965. However, as the mind and management of the corporation is in the United States, it would also be considered a resident of that country. In such dual residency situations, the Canada/U.S. tax treaty tie breaker rules indicate the Company will be considered a resident of the country of incorporation, which in this case would be Canada.

Exam Exercise Solution One - 18 (Corporate Residency)

While Acton Enterprises was not incorporated in Canada, it would appear that the "mind and management" of the Company is now located in Canada. This means that the Company would be considered a Canadian resident for the 2017 taxation year. However, as it was incorporated in the U.S., it would also be considered a resident of that country. In such dual residency situations, the tie breaker rules indicate the residence would be based on the country of incorporation. This would mean that Acton Enterprises would not be a Canadian resident during 2017.

Exam Exercise Solution One - 19 (Net Income For Tax Purposes)

Ms. Nexus' Net Income For Tax Purposes would be calculated as follows:

Income Under ITA 3(a):		
Net Employment Income	\$66,000	
Interest Income	<u>10,250</u>	\$76,250
Income Under ITA 3(b):		
Taxable Capital Gains	\$13,500	
Allowable Capital Loss	<u>(24,000)</u>	Nil
Balance From ITA 3(a) And (b)		\$76,250
ITA 3(c) Deductions:		
Spousal Support		(14,000)
RRSP Contributions		<u>(3,000)</u>
Balance From ITA 3(c)		\$59,250
Deductions Under ITA 3(d):		
Net Rental Losses		(6,750)
Business Loss		<u>(28,000)</u>
Net Income For Tax Purposes		<u>\$24,500</u>

She has an unused allowable capital loss carry over of \$10,500 (\$24,000 - \$13,500).

Exam Exercise One - 20 Solution (Net Income For Tax Purposes)

Mr. Nicastro's Net Income For Tax Purposes would be calculated as follows:

Income Under ITA 3(a):		
Net Employment Income	\$45,000	
Interest Income	<u>4,500</u>	\$49,500
Income Under ITA 3(b):		
Taxable Capital Gains	\$13,500	
Allowable Capital Loss	<u>(18,200)</u>	Nil
Balance From ITA 3(a) And (b)		\$49,500
ITA 3(c) Deductions:		
Spousal Support		(24,000)
Balance From ITA 3(c)		\$25,500
Deductions Under ITA 3(d):		
Business Loss		(23,000)
Net Rental Loss		<u>(14,500)</u>
Net Income For Tax Purposes		<u>Nil</u>

At the end of this year, Mr. Nicastro would have an unused allowable capital loss carry over of \$4,700 (\$13,500 - \$18,200). In addition, he would have a non-capital loss carry over of \$12,000 (\$25,500 - \$23,000 - \$14,500).

Exam Exercise Solution One - 21 (Tax Planning)

This transaction clearly involves tax deferral, in that the contribution will be deductible and the earnings on the contribution will accumulate on a tax free basis. However, all of these amounts will be taxable when they are withdrawn from the plan. There may also be tax avoidance. This will happen if Mr. Bronson is taxed at a lower rate when the funds become taxable.

Exam Exercise One - 22 Solution (Tax Planning)

This transaction involves tax avoidance. Ms. Bloom can receive this benefit from her employer without being assessed a taxable benefit. Extra salary would be taxable.

Exam Exercise Solution One - 23 (Tax Planning)

Natasha is involved in income splitting, tax deferral, and possibly tax avoidance. She is getting the deduction from Taxable Income now and her spouse will be taxed on the income in the future. The tax deferral occurs as the contribution is currently deductible and the earnings on the contribution will accumulate on a tax free basis. However, all of these amounts will be taxable when they are withdrawn from the plan. Tax avoidance will occur if John is taxed at a lower rate than is currently applicable to Natasha when the funds become taxable to him.

Exam Exercise One - 24 Solution (Tax Planning)

Contributions to a registered pension are deductible in the year in which they are made. They are not taxed until retirement benefits are received under the terms of the plan. This involves tax deferral and, if Ms. Jones is taxed at a lower rate after she retires, tax avoidance has also been accomplished.

Exam Exercise Solution One - 25 (Tax Planning)

This transaction involves income splitting. It would appear that her daughter is in a lower tax bracket than Mrs. Theil. This means that the income on the Canada Savings Bonds will be taxed at a lower rate than would be the case if the bonds remained in Mrs. Theil's hands.

Exam Exercise One - 26 Solution (Tax Planning)

This transaction involves income splitting. As Norman's son is over 18 years of age, the dividends will be taxed in his name and not attributed back to his father. Provided he is in a lower tax bracket than Norman, this will reduce the family's overall tax burden.

TIF Solution One - 5A

The correct definitions for each of the listed key terms are as follows:

- A. 1
- B. 8
- C. 9
- D. 3
- E. 5
- F. 2
- G. 6
- H. 7

The two unused definitions are as follows:

Income Tax Folios = 4

Progressive Tax System = 10

TIF Solution One - 5B

For some terms there is both a 100 percent correct answer and an answer that is close. We have indicated the "close answer" in brackets.

The correct definitions for each of the listed key terms are as follows:

- A. 1 (not 12)
- B. 10
- C. 13
- D. 4 (not 7)
- E. 6 (not 11)
- F. 3 (not 14 which is also an unused definition)
- G. 8
- H. 9 (not 2)

The two unused definitions are as follows:

Income Tax Folios = 5

Progressive Tax System = 14

TIF Solution One - 6

Note The descriptions of these tax measures are significantly simplified. The objective of this problem is to present the basic ideas so they can be understood by students at this introductory level, while still providing a basis for discussion. It is obvious that there is no definitive solution to this problem. The analysis provided below is intended to be no more than suggestive of possible points that could be made. There are, of course, many alternative solutions.

Increase In The Maximum Tax Rate

Possible comments here would be as follows:

Adequacy As this increase was accompanied by a reduction in the second tax bracket from 22.0 percent to 20.5 percent, as well as a number of new spending initiatives, the government felt that this increase was necessary in order to provide compensating revenues.

International Competitiveness The fact that, in most provinces, the maximum tax rate on individuals is over 50 percent makes Canada less competitive with many other jurisdictions. In particular, in the United States, maximum tax rates on individuals are generally much lower.

Repeal Of The Family Tax Cut

Possible comments here would be as follows:

Simplicity And Ease Of Compliance This was an extremely complex provision that few individuals, other than those working as tax professionals really understood. Elimination of the provision reduces the complexity of the Canadian tax system.

Equity Or Fairness The family tax cut was widely criticized for providing most of its benefits to middle and upper income Canadians. Lower income individuals rarely benefitted from its provisions. It can be argued that the elimination of the family tax cut improves the fairness of the system.

Reduction In Contributions To Tax Free Savings Accounts

Possible comments here would be as follows:

Adequacy The reduction in the 22 percent tax bracket to 20.5 percent and several new and expensive programs have increased the government's need for additional revenues. Reducing this limit on the amount of investment income that can be earned tax free will increase revenues.

Balance Between Sectors As this provision is only available to individuals, the ability to earn tax free investment income reduces taxes for this group of taxpayers. A reduction in the maximum contribution has the effect of increasing taxes for the group. This serves to increase the already heavy tax burden on this group of taxpayers.

Small Business Tax Rate

Possible comments here would be as follows:

Certainty By clearly indicating that the small business tax rate will remain at 10.5 percent for the foreseeable future, certainty is increased for this group of taxpayers.

Neutrality The small business tax rate is designed to assist a specific group of taxpayers. The fact that the scheduled reductions in this rate have been cancelled is an unfavourable event for this group.

Early Child Educator School Supply Tax Credit

Possible comments here would be as follows:

Simplicity And Ease Of Compliance The large number of existing tax credits and the fact that new ones are added nearly every year, has greatly increased the complexity of the Canadian tax system. Another addition will exacerbate this problem. Additional complexity is also created by issues such as defining eligible supplies and determining who qualifies for the credit.

Neutrality This credit results in a benefit related to the costs associated with being a particular type of employee. It is not neutral in that it does not provide similar benefits for the costs associated with other types of employment (e.g., construction workers cannot deduct the cost of protective clothing).

TIF Solution One - 7

If this problem is used on an examination, great flexibility will be required in marking the student's responses. There is obviously no one solution to this problem and, given this, marks will have to be allocated on the basis of the reasonableness of the student's answers.

We would also note that we do not present the following as a comprehensive solution. It simply reflects some of the points that could be made with respect to the alternatives that are described in the text. The list of characteristics is as follows:

- Equity Or Fairness
- Neutrality
- Adequacy
- Elasticity
- Flexibility
- Simplicity And Ease Of Compliance
- Certainty
- Balance Between Sectors
- International (Provincial in this case) Competitiveness

Alternative 1

The following comments could be made with respect to this alternative:

Adequacy The introduction of a provincial sales tax (PST) could provide adequate revenues to solve the deficit problem.

Neutrality Whether a sales tax would be neutral would depend on its application. If it applied to all goods and services, it could be considered neutral. However, if it provides exemptions for certain types of goods and services (an exemption for basic food products), it would influence the allocation of resources.

Fairness As noted in the text, sales taxes of any type are regressive and this can be viewed as unfair to lower income individuals.

Certainty Sales taxes make it clear to individual taxpayers the amounts that will have to be paid. However, certainty can be compromised if the application of the sales tax involves numerous exemptions.

Ease Of Compliance Here again, it depends on how the tax is applied. If it applies to all goods and services, compliance is not too difficult. However, compliance could become very complex if various types of exemptions are available. Also increasing complexity would be variances between the application of this tax and the application of the federal GST.

Alternative 2

The following comments could be made with respect to this alternative:

Adequacy, Neutrality, Fairness, And Certainty The comments on alternative 1 would be applicable here.

Ease Of Compliance The major advantage of this Alternative over Alternative 1 is ease of compliance. When there is a separate PST, taxpayers will have to file both a GST return and a PST return. Note, however, when a province chooses to apply HST to different items than those covered by the GST legislation, compliance is made more difficult.

Alternative 3

The following comments could be made with respect to this alternative:

Adequacy Cuts in expenditures can provide for the required deficit reduction.

Ease Of Compliance As the subject of the cuts have little choice in the matter, compliance is not an issue. However, implementation could present many problems for targeted organizations, particularly if the cuts are not anticipated.

Fairness This alternative is targeted at the needs of students. This could be viewed as favouring older individuals who are not participating in educational programs and/or do not have children involved in educational programs.

Provincial Competitiveness University students have considerable mobility and could decide to search for positions in the universities of other provinces. However, they may be faced with higher out-of-province tuition, as well as the costs of living away from home. With respect to families with children in elementary or high school, a decline in the quality of schools could discourage immigration to the Province.

Alternative 4

The following comments could be made with respect to this alternative:

Adequacy And Ease Of Compliance The comments on Alternative 3 would be applicable here.

Fairness The impact of this change would be broadly based. However, it could be viewed as being unfair to those individuals with health problems. It is likely that the impact of cuts in health care would be felt most by older individuals. There is an additional fairness question in terms of whether the current health care system is adequately funded. If it is not, then the proposed cuts could be unfair to everyone with health problems.

Alternative 5

The following comments could be made with respect to this alternative:

Adequacy It is likely that the introduction of progressive rates on individuals would assist with deficit reduction. Note, however, that an offsetting factor could be that individuals are less willing to work more when the result will be a higher rate of tax.

Ease Of Compliance As discussed in the text, progressive rates add complexity and encourage evasion.

Fairness Most analysts view progressive rates as being fair in that individuals with higher income will have higher rates. The basis for this argument is ability to pay.

Alternative 6

The following comments could be made with respect to this alternative:

Adequacy Increases in corporate tax rates could contribute to deficit reduction.

Ease Of Compliance Given that corporate income tax is already in place, an increase in rates would not add to compliance issues.

Balance Between Sectors This change would result in heavier reliance on the corporate income tax, as compared to the amounts resulting from the application of the individual income tax. Without knowing the current balance between these two sectors, it is difficult to comment on this change.

Provincial Competitiveness If the increase in the corporate tax rate results in a rate that is higher than other provinces, the result could be some loss of corporate business in Alsaskatoba.

Alternative 7

The following comments could be made with respect to this alternative:

Adequacy Provided this fee did not discourage immigration to Alsaskatoba, this fee could help reduce the deficit.

Fairness There is an argument, based on the fact that new immigrants use provincial resources, (e.g. health care for example), that such a tax would be fair to the current residents of Alsaskatoba.

Provincial Competitiveness This fee will clearly discourage immigration, making it more difficult to attract individuals from other provinces.

There are, of course, many other comments that could be made on all of these alternatives. We would also note that there is another issue with respect to all of these alternatives. This is the question of political acceptability. If the residents of Alsaskatoba have never had a sales tax, this alternative may not be acceptable, without regard to other considerations.

TIF Solution One - 8

Mr. Morris would fall under the part year resident rules and would only be assessed for Canadian taxes on worldwide income during the portion of the year prior to his ceasing to be a resident of Canada.

By selling his house, disposing of other personal property, and resigning from various social and professional clubs, Mr. Morris appears to have done most of the things that would be required to establish that he had made a clean break from Canada as of April 1. However, S5-F1-C1 indicates that, in general, the CRA will view an individual as becoming a non-resident on the latest of three dates:

- The date the individual leaves Canada.
- The date the individual's spouse or common-law partner and dependants leave Canada.
- The date the individual becomes a resident of another country.

Because of the continued presence in Canada of the spouse and dependent children of Mr. Morris, he would be considered a resident of Canada until June 30, the latest of the relevant dates.

In terms of tax consequences, he would be subject to Canadian taxes on his salary until March 31. He would then be subject to U.S. taxes on income earned in that country after March 31. However, he would also be liable for Canadian taxes during the period April 1 through June 30. While he would be eligible for a tax credit for U.S. taxes paid on this income, the fact that Canadian taxes are generally higher than those in the U.S. would probably result in a liability for Canadian taxes during this period until his family departs from Canada.

TIF Solution One - 9

Case A

As Mr. Plesser became a Canadian resident on July 1 of the current year, he would be subject to Canadian Part I tax on his worldwide income for the part of a year subsequent to that date. This would include all of his employment income, as well as one-half (£5,500) of his U.K. interest.

Case B

Members of the Canadian armed forces are deemed to be Canadian residents without regard to where they actually live. As Mrs. Jurgens is exempt from German taxation due to her relationship to a deemed resident, she is a deemed resident and will be subject to Canadian taxation on her employment income.

Case C

While Ms. Mennan has a small Canadian savings account, it is unlikely that the CRA would consider this a sufficient tie with Canada to view her as a resident. She would be considered a non-resident.

With respect to the interest she received, Part XIII would not be applicable because it is an arm's length payment and does not involve participating debt. In addition, as was noted in Case C, the Canada/U.S. tax treaty has a provision which does not allow either country to assess taxes on interest paid to residents of the other country.

TIF Solution One - 10

Canada/U.S. Tax Treaty Tie Breaker Rule

In cases of dual residency for corporations, where a corporation could be considered a resident of both countries, the Canada/U.S. tax treaty indicates that the corporation will be deemed to be a resident only in the country in which it is incorporated.

Case A

While Bonix is no longer operating in Canada, it was incorporated here and it is deemed a Canadian resident. However, as the mind and management of the Company are currently in the United States, the Company is also a resident of the U.S. Using the tie breaker rule, Bonix will be considered a resident of Canada.

Case B

Dorad Inc. was not incorporated in Canada and its mind and management are not currently located here. Therefore, Dorad would not be considered a resident of Canada.

Case C

The mind and management of Upton Inc. are in Canada and this suggests that the Company is a resident of Canada. However, as Upton Inc. was incorporated in the U.S., it is also a resident of the U.S. Using the tie breaker rule, the Upton Inc. will be considered a resident of the U.S. and a non-resident of Canada.

Case D

Carlin Inc. was incorporated in Canada which means Carlin is a deemed resident of Canada. However, because the mind and management of the Company are in the United States, it is also a resident of the U.S. Using the tie breaker rule, Carlin Inc. will be considered a resident of Canada.

TIF Solution One - 11

Case A

Mr. Salazar is not a resident of Canada. Commuting across the border for employment purposes is not considered sojourning (S5-F1-C1). However, unless he is exempted by the Canada/U.S. tax treaty, he would be subject to Canadian taxation on the employment income which he earns in Windsor.

With respect to the treaty exemption, his employment income exceeds \$10,000 and he is physically present in Canada for more than 183 days in the year. Given these facts, he would not qualify for the treaty exemption.

Case B

The information suggests that Mr. Wills made a clean break with Canada on September 1 of the current year. As a consequence, he would be considered a Canadian resident for the portion of the current year prior to his departure and would be taxed on his worldwide income for this period. For the portion of the year subsequent to his departure, he would no longer be considered a Canadian resident.

Case C

Joan Brothers would be deemed to be a Canadian resident under ITA 250(1)(f) because she is a dependent child of an officer or servant of Canada who is deemed to be a resident of Canada under ITA 250(1)(c)(i).

Case D

Brogan Inc. was not incorporated in Canada and its mind and management are not currently within Canada. As a result, the Company is not a Canadian resident and none of its income would be subject to Canadian taxes.

Case E

Mercer Ltd. was incorporated prior to April 27, 1965 and, if it had not resided in or done business in Canada subsequent to that date, it would not be considered a resident of Canada. However, the fact that directors meetings were held in Canada until May, 1994 makes it a Canadian resident. As the mind and management are now in the U.S., it would also be considered a resident of that country.

In cases of dual residency for corporations, where a corporation could be considered a resident of both countries, the Canada/U.S. tax treaty indicates that the corporation will be deemed to be a resident only in the country in which it is incorporated. Mercer Ltd. would be a resident of Canada and its worldwide income would be subject to tax in Canada.

Case F

The Booker Manufacturing Company would be considered resident in Canada because of the location of its mind and management. However, as Booker was incorporated in the U.S., it would also be considered a resident of that country. In cases of dual residency for corporations, where a corporation could be considered a resident of both countries, the Canada/U.S. tax treaty indicates that the corporation will be deemed to be a resident only in the country in which it is incorporated. As a result, the Company is not a Canadian resident and none of its income would be subject to Canadian taxes.

TIF Solution One - 12

Part A

As she is exempt from taxation in Indonesia because she is related to a deemed resident, Dorothy would be a deemed resident of Canada for income tax purposes during the current year under ITA 250(1)(g).

Part B

As she is present in Canada on a temporary basis for more than 183 days per year, she would be considered a sojourner. Under ITA 250(1)(a), this would make her a Canadian resident for income tax purposes for all of the current year.

Part C

Because he has an employment contract that requires him to return to Canada, he will be a Canadian resident for income tax purposes during the current year. Although he has severed his ties with Canada, the requirement to return would show that he does not intend to permanently leave Canada.

Part D

Millicent would be a Canadian resident for income tax purposes during the current year. An individual is not considered to have departed from Canada until the latest of the departure date, the date of departure for their spouse and children, and the date on which residence is established in a different country. As her family is staying in Canada and Millicent will not be establishing residency in another country, she will remain a Canadian resident during her trip.

Part E

ITA 250(4)(c) indicates that a corporation is resident in Canada if it was incorporated in Canada prior to April 27, 1965 and carried on business, or was resident in Canada, in any year ending after April 26, 1965. However, as the mind and the management of the company is in the U.S., it is also a resident of that country. In cases of dual residency for corporations, where a corporation could be considered a resident of both countries, the Canada/U.S. tax treaty indicates that the corporation will be deemed to be a resident only in the country in which it is incorporated. Given this, Berkley Management would be a resident of Canada.

Part F

The company was not incorporated in Canada and the mind and management of the company is not in Canada. Lorris Ltd. is not a resident of Canada.

TIF Solution One - 13

Case A

The Case A solution would be calculated as follows:

Income Under ITA 3(a):		
Employment Income	\$17,000	
Net Rental Income	<u>8,500</u>	\$25,500
Income Under ITA 3(b):		
Taxable Capital Gains	\$17,400	
Allowable Capital Losses	<u>(19,200)</u>	Nil
Balance From ITA 3(a) And (b)		\$25,500
Subdivision e Deductions		<u>(6,300)</u>
Balance From ITA 3(c)		\$19,200
Deduction Under ITA 3(d):		
Business Loss		<u>(12,300)</u>
Net Income For Tax Purposes (Division B Income)		<u>\$ 6,900</u>

In this Case, Ms. Burke has an unused allowable capital loss carryover of \$1,800 (\$17,400 - \$19,200). The lottery winnings are not subject to tax.

Case B

The Case B solution would be calculated as follows:

Income Under ITA 3(a):		
Employment Income	\$42,100	
Interest Income	<u>8,200</u>	\$50,300
Income Under ITA 3(b):		
Taxable Capital Gains	\$22,400	
Allowable Capital Losses	<u>(19,200)</u>	3,200
Balance From ITA 3(a) And (b)		\$53,500
Subdivision e Deductions		<u>(4,200)</u>
Balance From ITA 3(c)		\$49,300
Deduction Under ITA 3(d):		
Unincorporated Business Loss		<u>(51,000)</u>
Net Income For Tax Purposes (Division B Income)		<u>Nil</u>

In this Case, Ms. Burke's Net Income For Tax Purposes (Division B income) is nil. There would be an unused business loss carry over of \$1,700 (\$49,300 - \$51,000).

TIF Solution One - 14

Case A

The Case A solution would be calculated as follows:

Income Under ITA 3(a):		
Employment Income	\$126,100	
Business Income	<u>14,100</u>	\$140,200
Income Under ITA 3(b):		
Taxable Capital Gains		
[(1/2)(\$56,400)]	\$28,200	
Allowable Capital Losses		
[(1/2)(\$72,300)]	(36,150)	Nil
Balance From ITA 3(a) And (b)		\$140,200
Spousal Support Payments [(12)(\$600)]		(7,200)
Balance From ITA 3(c)		\$133,000
Deduction Under ITA 3(d):		
Net Rental Loss		(4,600)
Net Income For Tax Purposes (Division B Income)		<u>\$128,400</u>

In this Case, Carl has an unused allowable capital loss carry over of \$7,950 (\$28,200 - \$36,150). The lottery winnings would not be included in income.

Case B

The Case B solution would be calculated as follows:

Income Under ITA 3(a):		
Employment Income	\$89,000	
Interest Income	3,100	
Net Rental Income	<u>8,600</u>	\$100,700
Income Under ITA 3(b):		
Taxable Capital Gains		
[(1/2)(\$46,200)]	\$23,100	
Allowable Capital Losses		
[(1/2)(\$26,300)]	(13,150)	9,950
Balance From ITA 3(a) And (b)		\$110,650
Deductible RRSP Contribution		(8,600)
Balance From ITA 3(c)		\$102,050
Deduction Under ITA 3(d):		
Unincorporated Business Loss		(187,400)
Net Income For Tax Purposes (Division B Income)		<u>Nil</u>

In this Case, Carl has an unused business loss carry over of \$85,350 (\$102,050 - \$187,400).

TIF Solution One - 15

Case A

The Case A solution would be calculated as follows:

Income Under ITA 3(a):		
Employment Income	\$34,000	
Income From Property	<u>21,000</u>	\$55,000
Income Under ITA 3(b):		
Taxable Capital Gains	\$42,000	
Allowable Capital Losses	<u>(57,000)</u>	Nil
Balance From ITA 3(a) and (b)		\$55,000
Subdivision e Deductions		<u>(5,500)</u>
Balance From ITA 3(c)		\$49,500
Deduction Under ITA 3(d):		
Business Loss		<u>(36,000)</u>
Net Income For Tax Purposes (Division B Income)		<u>\$13,500</u>

Miss Bain would have a carry over of unused allowable capital losses in the amount of \$15,000 (\$57,000 - \$42,000).

Case B

The Case B solution would be calculated as follows:

Income Under ITA 3(a):		
Employment Income	\$18,500	
Income From Property	<u>12,000</u>	\$30,500
Income Under ITA 3(b):		
Taxable Capital Gains	\$ 9,000	
Allowable Capital Losses	<u>(12,000)</u>	Nil
Balance From ITA 3(a) and (b)		\$30,500
Subdivision e Deductions		<u>(10,500)</u>
Balance From ITA 3(c)		\$20,000
Deduction Under ITA 3(d):		
Business Loss		<u>(28,200)</u>
Net Income For Tax Purposes (Division B Income)		<u>Nil</u>

As Miss Bain's business loss exceeds the balance from ITA 3(c), her Net Income For Tax Purposes (Division B income) is nil. This means there would be a carry over of unused business losses in the amount of \$8,200 (\$28,200 - \$20,000) and of unused allowable capital losses in the amount of \$3,000 (\$12,000 - \$9,000).

TIF Solution One - 16

Case 1

The Case 1 solution would be calculated as follows:

Income Under ITA 3(a):		
Net Employment Income	\$82,438	
Interest Income	<u>3,521</u>	\$85,959
Income Under ITA 3(b):		
Taxable Capital Gains	\$16,346	
Allowable Capital Losses	<u>(3,478)</u>	12,868
Balance From ITA 3(a) And (b)		\$98,827
RRSP Contribution		<u>(6,420)</u>
Balance From ITA 3(c) And Net Income For Tax Purposes		<u>\$92,407</u>

In this Case, Mr. Bowman has no loss carry overs at the end of the year.

Case 2

The Case 2 solution would be calculated as follows:

Income Under ITA 3(a):		
Net Business Income		\$56,782
Income Under ITA 3(b):		
Taxable Capital Gains	\$3,426	
Allowable Capital Loss	<u>(4,560)</u>	Nil
Balance From ITA 3(a) And (b)		\$56,782
Spousal Support Payments		<u>(18,000)</u>
Balance From ITA 3(c)		\$38,782
Deduction Under ITA 3(d):		
Net Rental Loss		<u>(6,742)</u>
Net Income For Tax Purposes (Division B Income)		<u>\$32,040</u>

In this Case, Mr. Bowman has a carry over of \$1,134 (\$4,560 - \$3,426) in unused allowable capital losses.

Case 3

The Case 3 solution would be calculated as follows:

Income Under ITA 3(a):		
Net Employment Income		\$36,582
Income Under ITA 3(b):		
Taxable Capital Gains [(1/2)(\$8,426)]	\$4,213	
Allowable Capital Losses [(1/2)(\$6,220)]	<u>(3,110)</u>	1,103
Balance From ITA 3(a) and (b)		\$37,685
Child Care Costs		<u>(2,860)</u>
Balance From ITA 3(c)		\$34,825
Deduction Under ITA 3(d):		
Net Business Loss		<u>(47,384)</u>
Net Income For Tax Purposes (Division B Income)		<u>Nil</u>

In this Case, Mr. Bowman would have a business loss carry over in the amount of \$12,559 (\$47,384 - \$34,825).

Case 4

The Case 4 solution would be calculated as follows:

Income Under ITA 3(a):		
Interest Income	\$ 4,850	
Net Business Income	<u>35,682</u>	\$40,532
Income Under ITA 3(b):		
Taxable Capital Gains [(1/2)(\$8,460)]	\$4,230	
Allowable Capital Losses		
[(1/2)(\$18,462)]	(9,231)	Nil
Balance From ITA 3(a) And (b)		\$40,532
Moving Expenses		(5,643)
Balance From ITA 3(c)		\$34,889
Deduction Under ITA 3(d):		
Net Rental Loss		(51,462)
Net Income For Tax Purposes (Division B Income)		Nil

Mr. Bowman would have a rental loss carry over in the amount of \$16,573 (\$51,462 - \$34,889) and unused allowable capital losses in the amount of \$5,001 (\$9,231 - \$4,230).

Chapter Two Test Item File Solutions

TIF Solution Two - 1

1. For an employer to grant this request, the reason for the reduction must be documented in a reasonable fashion and it must be recurring. While there are other examples, the one mentioned in the text involves an individual with deductible spousal support payments.
2. While there are other possibilities, the ones that are mentioned in the text are:
 - Normal withholding is based on rates in a low tax rate province, but the individual resides in a high tax rate province (e.g., the individual works in Alberta, but lives in Saskatchewan).
 - An individual receives large amounts of taxable spousal support payments that are not subject to withholding.
3. Individuals are required to make instalment payments if their net tax owing is greater than \$3,000 (\$1,800 in Quebec) in the current year and in either of the two preceding years. An alternative approach would be to indicate when instalments are not required. The statement here would be that instalments are not required when the net tax owing for the current year, or for each of the two preceding years is \$3,000 or less.
4. An individual can choose from three different methods in determining their instalment payments:

Method 1 The instalments could be based on one-quarter of the estimated net tax owing for the current year.

Method 2 The instalments could be based on one-quarter of the net tax owing for the previous year.

Method 3 The first two instalments could be based on one-quarter of the net tax owing for the second previous year, with the third and fourth instalments based on one-half of the net tax owing for the previous year, less the sum of the first two instalments paid.
5. The CRA's instalment reminder results in total instalment payments equal to the net tax owing in the previous taxation year. If the estimated net tax owing for the current year is less, lower instalments could be paid using the estimated current year net tax owing as the base.
6. If the client has debt on which he is paying non-deductible interest (e.g., interest on non-business credit cards), you should determine the applicable rates. If he is paying at a rate in excess of the rate he will be charged on deficient instalments (i.e., the prescribed rate plus 4 percent), he might consider paying down the debt in lieu of making instalment payments. Alternatively, if the rate that he is paying on the personal debt is lower, he should make an effort to pay his instalments. The excess penalty under ITA 163.1 would also have to be taken into consideration if the instalment payments are large.
7. Interest on later instalments is calculated using the highest prescribed rate (the regular rate plus 4 percentage points) applied for the period from the date the instalment is due until the balance due date for the total tax payable.
8. She should file the return on the due date, regardless of whether she has the funds to pay the balance owing. Whether or not she files, she will have to pay interest on the balance owing. However, if she delays filing until early July, she will not only have to pay the non-deductible interest, she will also be subject to an immediate penalty of 5 percent of the balance owing, plus an additional 1 percent per complete month for the period from April 30, for a total penalty of 7 percent.

If, within the last three years, there has been another late filing of her return, the penalty can double to an immediate 10 percent, plus 2 percent per month. The monthly penalty will be assessed for a maximum of 20 months.

9. Corporations are generally required to make either monthly or quarterly instalment payments throughout their taxation year. The only exception to this is when the estimated taxes payable for the current year, or the taxes payable in the preceding year, are \$3,000 or less.

10. A corporation that is not a small CCPC can choose from three different methods in determining their instalment payments:

Method 1 The instalments can be based on one-twelfth of the estimated taxes payable for the current taxation year.

Method 2 The instalments can be based on one-twelfth of the taxes payable for the previous taxation year.

Method 3 The first two instalments can be based on one-twelfth of the taxes payable for the second previous year. The remaining 10 instalments will then be based on the taxes payable for the previous taxation year reduced by the amounts paid in the first two instalments, with this amount divided by 10.

11. A corporation that is a small CCPC can choose from three different methods in determining their instalment payments.

Method 1 The instalments can be based on one-fourth of the estimated taxes payable for the current taxation year.

Method 2 The instalments can be based on one-fourth of the taxes payable for the previous taxation year.

Method 3 The first instalment can be based on one-fourth of the taxes payable for the second previous year. The remaining three instalments will then be based on the taxes payable for the previous taxation year reduced by the amount paid in the first instalment, with this amount divided by three.

12. Corporate tax returns must be filed within six months of the end of the corporation's taxation year. In contrast, the balance due date is either 2 months after the end of the corporation's taxation year (general rule) or 3 months after the end of the corporation's taxation year (qualifying CCPCs). As a consequence, payment is always required prior to the due date for filing the corporate tax return.

13. There are a number of situations that could be cited. The ones listed in the text are as follows:

- Reassessment can occur at any time if the taxpayer or person filing the return has made any misrepresentation that is attributable to neglect, carelessness or willful default, or has committed any fraud in filing the return or in supplying information under the *Income Tax Act*.
- Reassessment can occur at any time if the taxpayer has filed a waiver of the normal time limit. A taxpayer can revoke such a waiver at any time.
- Reassessment can occur outside the normal reassessment period if an individual or testamentary trust has requested a reduction in taxes, interest, or penalties. The ability to use this provision is limited to ten years after the particular year in question.
- Reassessment can occur beyond the normal reassessment period when reassessment within the normal period affects a balance outside of this period.

- Reassessment can occur outside the normal reassessment period in situations where the taxpayer is claiming certain specified deductions, such as a loss carry back for that year.

14. The general and informal procedures differ as follows:

- Under the informal procedures, the tax involved must be less than \$25,000, or the loss in question is less than \$50,000.
- Under the informal procedures, an individual can represent himself, or be represented by someone other than a lawyer (e.g., an accountant).
- Under the informal procedures, the taxpayer cannot be assessed court costs.
- Under the informal procedures, if the taxpayer loses, there is no appeal to a higher court.
- Informal procedures usually resolve a dispute much more quickly than the general procedures.

15. Tax evasion is described on the CRA web site as follows:

Tax evasion typically involves deliberately ignoring a specific part of the law. For example, those participating in tax evasion may under-report taxable receipts or claim expenses that are non-deductible or overstated. They might also attempt to evade taxes by wilfully refusing to comply with legislated reporting requirements.

A less clear description of tax avoidance is as follows:

When tax planning reduces taxes in a way that is inconsistent with the overall spirit of the law, the arrangements are referred to as **tax avoidance**. The Canada Revenue Agency's interpretation of the term "tax avoidance" includes all unacceptable and abusive tax planning. Aggressive tax planning refers to arrangements that "push the limits" of acceptable tax planning.

TIF Solution Two - 2

1. False. The deficiency must be recurring, not just for a particular year.
2. False. There are two filing due dates for individuals. April 30 or, for individuals earning business income, June 15. In addition, deceased taxpayers may have a different filing date.
3. True.
4. True.
5. False. The acceptable approach is to use one-quarter of the net tax owing for the current year.
6. False. The interest rate applicable on refunds to individuals is 2 percentage points less than the interest rate on amounts owing to the CRA.
7. False. There is no penalty for late payment of taxes. The penalty is for late filing of a return.
8. True.
9. False. Corporations, other than some CCPCs, must pay the balance of tax owing no later than two months after the end of their fiscal year.
10. True.
11. False. Deliberately ignoring a specific provision in the *Income Tax Act* is tax evasion, not tax avoidance.
12. True.
13. True.

TIF Solution Two - 3

Individual Filing Requirements

1. C. If an individual has no Taxable Income for the year, they do not have to file an income tax return
2. D. A self employed individual with a net business loss for the year does not have to file an income tax return for the year.
3. C. If an individual has disposed of a capital property during the year, they are required to file an income tax return, even if no tax is payable.
4. B. John must file a tax return on or before June 15, 2018.
5. B. April 30, 2018.
6. B. June 15, April 30.
7. E. Nil. The late filing penalty amounts to 5 percent of the tax that was unpaid at the filing due date. Since Ms. Deveco has paid more than her net tax owing by April 30, 2018, there are no penalties or interest.
8. A. The final tax return of individuals who die between January 1 and October 31 must be filed no later than April 30 of the following year. The 6-month filing extension provided by ITA 150(1)(b) only applies where an individual dies between November 1 of the year and April 30 of the following year.
9. D. June 15, 2018.
10. B. June 15, 2018, his regular filing date for his 2017 tax return.
11. C. August 1, 2018.
12. A. April 30, 2018

Individual Instalments

13. B. Charlotte Bronte, who realized capital gains of \$3,500 in 2016 and \$4,000 in 2017. With her only other income during the years 2015 through 2017 being \$5,000 in employment income, the net tax owing on the taxable one-half of the capital gains plus the employment income would be less than \$3,000.
A. is not correct. Although there is a requirement to pay instalments, the minimum instalment would be nil because the prior year's net tax owing was nil.

14. C. \$1,875 ($\$7,500 \div 4$).
15. B. \$3,750 ($\$15,000 \div 4$).
16. A. Jane White, who received a one-time bonus of \$60,000 last year and, because her employer had not deducted enough tax, found herself with net tax owing of \$8,200.
17. D. If Larry has as much income in 2018 as he had in 2017, he will have to pay instalments during 2018.
18. C. When net tax owing is over \$3,000 for the current year and one of the two prior years.
19. A. To pay the amounts provided by the CRA in their instalment reminder on or before the required dates. B is wrong as the estimate for the current year may be too low.

Interest And Penalties

20. A. Dora should pay off her credit card balance before making instalment payments.
21. B. The penalty for a first offence is 5% + 1% per full month late to a maximum of 12 months. Since the return was more than 19 months late, the maximum penalty is 17% of $\$15,500 = \$2,635$.
22. C. A taxpayer who has a balance owing files their tax return late, with the payment enclosed.

Corporate Filing Requirement

23. B. All corporations must file their income tax returns electronically. If their gross revenues are less than \$1,000,000, they can file a paper return.
24. E. Six months after the fiscal year end.
25. D. The return would be due on May 31, 2018, six months after the taxation year end.
26. D. The penalty would be 5 percent of the tax unpaid at the date the return was due to be filed, plus 1 percent per month for three months, a total of 8 percent. This amounts to $\$200 [(8\%)(\$2,500)]$.

27. D. Two months after the end of the fiscal year, or three months after the end of the fiscal year if the corporation is a small CCPC.

Corporate Instalments

28. C. Twelve payments of \$6,250 per month.
29. B. Its preceding year's taxes payable of \$13,200, divided by twelve months.
30. B. The only correct approach listed is to pay monthly instalments equal to 1/12th of the current year's estimated tax liability.
31. A. Monthly, based on the estimated tax for the current year.
32. A. Taxable income cannot exceed \$500,000 for the corporation and its associated corporations for the current taxation year and the two previous years.

Assessments And Appeals

33. B. April 30, 2019.
34. C. When a return has been reassessed once, no further reassessments are permitted.
35. B. The change is based on a successful appeal to the courts by another taxpayer.
36. E. For individuals, the notice of objection must be filed before the later of: 90 days from the date of the notice of assessment or reassessment, and one year from the filing due date for the return under assessment or reassessment.
37. C. Her notice of objection must be filed before the later of: 90 days from the date of the notice of assessment (July 18, 2018), and one year from the filing due date for the return (April 30, 2019).
38. D. It must be filed no later than 90 days after the date of the notice of assessment.
39. D. April 30, 2019.

Tax Planning

40. D. tax planning.

TIF Solution Two - 4

Exam Exercise Solution Two - 1 (Individual Due Dates)

While Mr. Brown's 2017 tax return does not have to be filed until June 15, 2018, his tax liability must be paid by April 30, 2018 in order to avoid the assessment of interest.

Exam Exercise Solution Two - 2 (Individual Due Dates)

While Ms. Farrel's 2017 tax return does not have to be filed until June 15, 2018, her tax liability must be paid by April 30, 2018 in order to avoid the assessment of interest.

Exam Exercise Solution Two - 3 (Deceased Taxpayer Due Date)

Mr. Klause's 2017 tax return must be filed by the later of six months after the date of his death and his normal filing date. Given that his income is from an unincorporated business, his normal filing date for the 2017 return would be June 15, 2018. However, the later date is September 1, 2018, six months after the date of his death.

Exam Exercise Solution Two - 4 (Deceased Taxpayer Due Date)

Ms. Klump's 2017 tax return must be filed by the later of six months after the date of her death and her normal filing date. Six months after her death would be June 1, 2018. However, because she has income from an incorporated business, her normal filing date would be June 15, 2018. Given this, the later date is June 15, 2018.

Exam Exercise Solution Two - 5 (Individual Instalments)

As the net tax owing for the current year and one of the two preceding years exceeds \$3,000, she is required to make instalment payments. The best alternative for instalment payments would be to use the current year estimate. This would result in required instalment payments of \$900 ($\$3,600 \div 4$) to be paid on March 15, June 15, September 15, and December 15. Note, however, that if the estimated taxes payable are below actual taxes payable for 2017, instalment interest may be charged.

Exam Exercise Solution Two - 6 (Individual Instalments)

The net tax owing amounts can be calculated as follows:

2015	\$11,000 (\$56,000 - \$45,000)
2016	\$2,800 (\$49,000 - \$46,200)
2017	\$20,000 (\$65,000 - \$45,000)

As the net tax owing exceeds \$3,000 in the current year and the second preceding year, instalments are required. The Instalment Reminder will have March 15 and June 15 instalments of \$2,750 each ($\$11,000 \div 4$). There would be no further instalments required for 2017 as his net tax owing for 2016 is only \$2,800 and he would already have paid \$5,500 [(2)(\$2,750)].

The best alternative for instalment payments would be to use the prior year option. This would result in required instalment payments of \$700 ($\$2,800 \div 4$) to be paid on March 15, June 15, September 15, and December 15.

Exam Exercise Solution Two - 7 (Individual Instalments)

The net tax owing amounts can be calculated as follows:

2015	\$5,000 (\$83,000 - \$78,000)
2016	Nil (\$76,000 - \$77,000). Note this is nil, not a negative amount.
2017	\$4,000 (\$63,000 - \$59,000)

As the net tax owing exceeds \$3,000 in the current year and the second preceding year, instalments are required. The three alternatives for calculating instalment payments are as follows:

- Based on the estimate for the current year, the instalments would be \$1,000 ($\$4,000 \div 4$).
- Based on the estimate for the preceding year, the instalments would be nil.
- Based on the second preceding year, the first two instalments would each be \$1,250 ($\$5,000 \div 4$). As the net tax owing for the previous year is nil, no further instalments would be required.

The best alternative would be to base the payments on the previous year, resulting in instalments of nil.

Exam Exercise Solution Two - 8 (Penalties And Interest For Individuals)

Given the size of her net tax owing, ITA 163.1 will not be applicable and there will be no penalties for late instalments. However, a penalty of 8 percent of taxes payable will be assessed for filing three complete months late (5 percent, plus 1 percent per month). If, in one of the three preceding taxation years she has also late filed, the penalty could be 16 percent (10 percent, plus 2 percent per month) if the CRA has already sent a request for the return.

Interest will be assessed on the deficient instalments, the balance owing on her filing date, and the penalty assessed for late filing. It will be assessed at the prescribed base rate plus 4 percent for the period May 1 through August 24, 2018.

Exam Exercise Solution Two - 9 (Penalties And Interest For Individuals)

A penalty of 9 percent of Tax Payable will be assessed for filing 4 complete months late (5 percent, plus 1 percent per month). There will be no interest on late instalments because, with the previous year's Tax Payable at nil, the required instalments were nil. This would also mean that the ITA 163.1 penalty could not apply.

Interest at the prescribed base rate plus 4 percent will be assessed on the balance owing on his filing date and the penalty assessed for late filing for the period May 1 through September 12, 2018.

**Exam Exercise Solution Two - 10
(Corporate Instalments - Regular And Small CCPC)**

Not Small CCPC The first two instalments would be based on the second preceding year and would be \$5,958.33 each ($\$71,500 \div 12$). The remaining 10 instalments would be based on the preceding year, less the \$11,916.66 paid in the first two instalments. The amount would be \$8,168.33 [$(\$93,600 - \$11,916.66) \div 10$]. The instalments would be due on the last day of each month in 2017.

Small CCPC In this case, the first instalment would be based on the second preceding year and would be \$17,875 ($\$71,500 \div 4$). The remaining 3 instalments would be based on the preceding year, less the \$17,875 paid for the first instalment. The amount would be \$25,241.67 [$(\$93,600 - \$17,875) \div 3$]. The instalments would be due on the last days of March, June, September, and December, 2017.

Note that when the initial instalment(s) are based on the second preceding year, the total amount of instalments will be the same as when all of the instalments are based on the first preceding year. However, using the second preceding year is preferable in that it provides some deferral of taxes.

Exam Exercise Solution Two - 11
(Corporate Instalments - Regular And Small CCPC)

Not Small CCPC The minimum instalments would be based on the estimated taxes payable for 2017. The amount would be \$4,358.33 ($\$52,300 \div 12$). The instalments would be due on the last day of each month in 2017. Note that, if the estimate for 2017 is too low, interest will be assessed on the deficiency.

Small CCPC In this case, all four instalments would be based on the estimated taxes payable for 2017. The amount would be \$13,075 ($\$52,300 \div 4$). The instalments would be due on the last days of March, June, September, and December, 2017.

Note that when the initial instalment(s) are based on the second preceding year, the total amount of instalments will be the same as when all of the instalments are based on the first preceding year. However, using the second preceding year is preferable in that it provides some deferral of taxes.

Exam Exercise Solution Two - 12
(Corporate Instalments - Regular And Small CCPC)

Not Small CCPC Minimum instalments would be based on the estimate for the current year. The monthly amount would be \$4,683.33 ($\$56,200 \div 12$). If the second previous year was used, the first two installments would be lower. However, as the remaining instalments would be based on the previous year's \$93,400, the total would be significantly larger. The instalments would be due on the last day of each month during the period October, 2016 through September, 2017. Note that, if the estimate for 2017 is too low, interest will be assessed on the deficiency.

Small CCPC Minimum instalments would be based on the estimate for the current year. The monthly amount would be \$14,050 ($\$56,200 \div 4$). The instalments would be due on the last day of December, 2016, March, 2017, June, 2017, and September, 2017.

Exam Exercise Solution Two - 13 (Corporate Due Dates - CCPC)

Grange Inc.'s tax return is due six months after its year end, on September 30, 2017. As it is a CCPC that claims the small business deduction, and its Taxable Income for the preceding taxation year did not exceed \$500,000, the final tax payment is due three months after the year end. This would be June 30, 2017.

Exam Exercise Solution Two - 14 (Corporate Due Dates)

Lawnco Inc.'s tax return is due six months after its year end, on July 31, 2017. As Lawnco is a public company that is not eligible for the small business deduction, the final tax payment is due two months after the year end, on March 31, 2017.

Exam Exercise Solution Two - 15 (Corporate Due Dates - CCPC)

Breyson's tax return is due six months after its year end of June 30, 2017. This would be December 31, 2017. As it is a CCPC that claims the small business deduction, and its Taxable Income for the preceding taxation year did not exceed \$500,000, its final tax payment is due three months after the year end on September 30, 2017.

Exam Exercise Solution Two - 16 (Notice of Objection)

A notice of objection must be filed by the later of:

- 90 days after the date on the Notice of Reassessment (September 30, 2019); or
- one year after the due date for filing the return that is being reassessed (April 30, 2019).

The later of these two dates is September 30, 2019.

Exam Exercise Solution Two - 17 (Notice of Objection)

A notice of objection must be filed by the later of:

- 90 days after the date on the Notice of Reassessment (June 6, 2019); or
- one year after the due date for filing the return that is being reassessed (June 15, 2019).

The later of these two dates is June 15, 2019.

TIF Solution Two - 5A

The correct definitions for each of the listed key terms are as follows:

A. 9

B. 4

C. 6

D. 3

E. 1

F. 7

G. 2

H. 5

The two unused definitions are as follows:

Assessment = 10

GAAR = 8

TIF Solution Two - 5B

For some terms there is both a 100 percent correct answer and an answer that is close. We have indicated the “close answer” in brackets.

The correct definitions for each of the listed key terms listed below.

- A. 12 (not 14)
- B. 5 (not 9)
- C. 7 (not 2)
- D. 4
- E. 1
- F. 8 (not 10)
- G. 3
- H. 6

The two unused definitions are as follows:

Assessment = 13

GAAR = 11

TIF Solution Two - 6

Part A - Case 1

Barry's net tax owing in each of the three years is as follows:

2015 = \$2,456 (\$14,256 - \$11,800)
2016 = \$1,626 (\$15,776 - \$14,150)
2017 = \$4,083 (\$16,483 - \$12,400) Estimated

While the net tax owing in the current year is expected to exceed \$3,000, it did not exceed \$3,000 in either of the two previous years. The payment of instalments is not required.

Part A - Case 2

Barry's net tax owing in each of the three years is as follows:

2015 = Nil (\$14,256 - \$14,920) Note that a negative number is not used here.
2016 = \$4,376 (\$15,776 - \$11,400)
2017 = \$3,257 (\$16,483 - \$13,226) Estimated

As his net tax owing is expected to exceed \$3,000 in 2017 and was more than \$3,000 in 2016, the payment of instalments is required.

Instalments under the three acceptable alternatives would be as follows:

Alternative 1 Using the estimated net tax owing for the current year would result in quarterly instalments of \$814.25 ($\$3,257 \div 4$), for a total amount of \$3,257.

Alternative 2 Using the net tax owing for the previous year would result in quarterly instalments of \$1,094 ($\$4,376 \div 4$), for a total amount of \$4,376.

Alternative 3 Using the net tax owing for the second previous year would result in the first two instalments being nil. The remaining two instalments would be \$2,188 ($\$4,376 \div 2$), a total of \$4,376.

The best choice would be Alternative 1. While the first two instalments are lower under Alternative 3, the total for the year under Alternative 3 is \$1,119 ($\$4,376 - \$3,257$) higher.

Part A - Case 3

Barry's net tax owing in each of the three years is as follows:

2015 = \$3,036 (\$14,256 - \$11,220)
2016 = \$2,501 (\$15,776 - \$13,275)
2017 = \$3,610 (\$16,483 - \$12,873) Estimated

As his net tax owing is expected to exceed \$3,000 in 2017 and was more than \$3,000 in 2015, the payment of instalments is required.

Instalments under the three acceptable alternatives would be as follows:

Alternative 1 Using the estimated net tax owing for the current year would result in quarterly instalments of \$902.50 ($\$3,610 \div 4$), for a total amount of \$3,610.

Alternative 2 Using the net tax owing for the previous year would result in quarterly instalments of \$625.25 ($\$2,501 \div 4$), for a total amount of \$2,501.

Alternative 3 Using the net tax owing for the second previous year would result in the first two instalments being \$759 ($\$3,036 \div 4$) each, a total of \$1,518. The remaining two instalments would be \$491.5 [$(\$2,501 - \$1,518) \div 2$], a total of \$983. When combined with the first two instalments, the total for the year would be \$2,501 ($\$1,518 + \983).

The best choice would be Alternative 2. While the total for the year under Alternative 3 is the same, the first two instalments are lower under Alternative 2, allowing for a small amount of tax deferral.

Part B

In Case Two and Case Three, the required instalments would be due on March 15, June 15, September 15, and December 15, 2017.

TIF Solution Two - 7

Need For Instalments

Instalments are required when an individual's "net tax owing" exceeds \$3,000 in the current year and in either of the two preceding years. In somewhat simplified terms, "net tax owing" is defined as the combined federal and provincial taxes payable, less amounts withheld under ITA 153. Mr. Grafton's net tax owing figures are as follows:

2015 = \$1,700 (\$31,500 - \$29,800)

2016 = \$8,400 (\$14,600 - \$6,200)

2017 = \$3,100 (\$27,400 - \$24,300) Estimated

As Mr. Grafton's net tax owing in 2017 (the current year) and his net tax owing in 2016 (one of the two preceding years) is greater than \$3,000, he is required to make instalment payments.

Amounts

If Mr. Grafton bases the first two quarterly payments on the 2015 net tax owing, they would only be \$425 each ($\$1,700 \div 4$). However, the payments for the last two quarters would be \$3,775 each $\{[\$8,400 - (2)(\$425)] \div 2\}$, resulting in total instalment payments of \$8,400.

A preferable alternative would be to base the payments on the net tax owing for 2017. These payments would be \$775 each ($\$3,100 \div 4$), for a total of \$3,100.

Payment Dates

The quarterly payments would be due on March 15, June 15, September 15, and December 15.

TIF Solution Two - 8

Case One

1. As the corporation's tax payable for both the current and the preceding year exceeds \$3,000, instalments are required. As the corporation is not a small CCPC, monthly instalments are required.
2. The three acceptable alternatives would be as follows:
 - Monthly instalments of \$9,435 ($\$113,220 \div 12$) based on the current year estimate.
 - Monthly instalments of \$10,185 ($\$122,220 \div 12$) based on the first preceding year.
 - Two monthly instalments of \$8,640 ($\$103,680 \div 12$) based on the second preceding year, followed by 10 monthly instalments of \$10,494 $\{[(\$122,220 - (2)(\$8,640)) \div 10]\}$, a total of \$122,220.
3. The best alternative in terms of minimum instalments would be 12 instalments of \$9,435, resulting in a total of \$113,220 of instalment payments.
The instalments would be due on the last day of each month, beginning in January, 2017.

Case Two

1. As the corporation's tax payable for both the current and the preceding year exceeds \$3,000, instalments are required. As the corporation is not a small CCPC, monthly instalments are required.
2. The three acceptable alternatives would be as follows:
 - Monthly instalments of \$9,435 ($\$113,220 \div 12$) based on the current year estimate.
 - Monthly instalments of \$9,210 ($\$110,520 \div 12$) based on the first preceding year.
 - Two monthly instalments of \$8,640 ($\$103,680 \div 12$) based on the second preceding year, followed by 10 monthly instalments of \$9,324 $\{[(\$110,520 - (2)(\$8,640)) \div 10]\}$, a total of \$110,520.
3. The best alternative would be two payments of \$8,640, followed by ten payments of \$9,324. While the total instalments are the same \$110,520 in both the second and third alternatives, the third alternative is preferable because the first two payments are lower. This provides a small amount of tax deferral.
The instalments would be due on the last day of each month, beginning in January, 2017.

Case Three

1. As the corporation's tax payable for both the current and the preceding year exceeds \$3,000, instalments are required. As the corporation is a small CCPC, instalments will be quarterly.
2. The three acceptable alternatives would be as follows:
 - Quarterly instalments of \$28,305 ($\$113,220 \div 4$) based on the current year estimate.
 - Quarterly instalments of \$30,555 ($\$122,220 \div 4$) based on the first preceding year.
 - One instalment of \$25,920 ($\$103,680 \div 4$) based on the second preceding year, followed by three instalments of \$32,100 $[(\$122,220 - \$25,920) \div 3]$, a total of \$122,220.
3. The best alternative in terms of minimum instalments would be four instalments of \$28,305, for total payments of \$113,220. The instalments are due on March 31, June 30, September 30, and December 31, 2017.

Case Four

1. As the corporation's tax payable for both the current and the preceding year exceeds \$3,000, instalments are required. As the corporation is a small CCPC, instalments will be quarterly.
2. The three acceptable alternatives would be as follows:
 - Quarterly instalments of \$28,305 ($\$113,220 \div 4$) based on the current year estimate.
 - Quarterly instalments of \$27,630 ($\$110,520 \div 4$) based on the first preceding year.
 - One instalment of \$25,920 ($\$103,680 \div 4$) based on the second preceding year, followed by three instalments of \$28,200 [$(\$110,520 - \$25,920) \div 3$], a total of \$110,520.
3. The best alternative would be one payment of \$25,920, followed by three payments of \$28,200. While the total instalments are the same \$110,520 in both the second and third alternatives, the third alternative is preferable because the first payment is lower. This provides a small amount of tax deferral.

The instalments are due on March 31, June 30, September 30, and December 31, 2017.

TIF Solution Two - 9

While there are alternatives in all Cases, the following answers represent the “minimum” instalments, as required in the problem.

Case One

Mr. Shivraj’s net tax owing in each of the three years is as follows:

2015 = \$2,300 (\$13,500 - \$11,200)
2016 = \$3,300 (\$16,200 - \$12,900)
2017 = \$3,300 (\$18,400 - \$15,100) Estimated

As his net tax owing is expected to exceed \$3,000 in 2017 and was more than \$3,000 in 2016, the payment of instalments is required.

Since the net tax owing is the same in the current year and the preceding year, the total instalments will equal \$3,300 under any of the alternatives. The best alternative would be to base the first two instalments on 2015. These would be \$575 ($\$2,300 \div 4$) each and would offer a small amount of deferral over the preceding year or current year alternatives. The remaining two instalments would each be \$1,075 [$(\$3,300 - (2)(\$575)) \div 2$] for a total of \$3,300.

They would be due on March 15, June 15, September 15, and December 15.

Case Two

Mr. Shivraj’s net tax owing in each of the three years is as follows:

2015 = \$4,300 (\$13,500 - \$9,200)
2016 = \$5,900 (\$16,200 - \$10,300)
2017 = \$3,500 (\$18,400 - \$14,900) Estimated

As his net tax owing is expected to exceed \$3,000 in 2017 and was more than \$3,000 in both the first and second preceding years, the payment of instalments is required.

Using the 2017 net tax owing would result in minimum instalment payments of \$875 ($\$3,500 \div 4$) for a total of \$3,500.

They would be due on March 15, June 15, September 15, and December 15.

Case Three

Mr. Shivraj’s net tax owing in each of the three years is as follows:

2015 = \$3,400 (\$13,500 - \$10,100)
2016 = Nil (\$16,200 - \$16,300) Note that a negative number is not used here.
2017 = \$3,700 (\$18,400 - \$14,700) Estimated

As his net tax owing is expected to exceed \$3,000 in 2017 and was more than \$3,000 in 2015, the payment of instalments is required.

Using the 2016 net tax owing would result in minimum instalment payments. Based on this year, the required quarterly instalments would be nil.

TIF Solution Two - 10

Case One

1. As the corporation's tax payable for both the current and the preceding year exceeds \$3,000, instalments are required. As the corporation is a small CCPC, instalments will be quarterly.
2. The three acceptable alternatives would be as follows:
 - Quarterly instalments of \$23,650 ($\$94,600 \div 4$) based on the current year estimate.
 - Quarterly instalments of \$25,350 ($\$101,400 \div 4$) based on the first preceding year.
 - One instalment of \$21,625 ($\$86,500 \div 4$) based on the second preceding year, followed by three instalments of \$26,591.67 [$(\$101,400 - \$21,625) \div 3$], a total of \$101,400.
3. The best alternative in terms of minimum instalments would be four instalments of \$23,650, for total payments of \$94,600. The instalments are due on March 31, June 30, September 30, and December 31, 2017.

Case Two

1. As the corporation's tax payable for both the current and the preceding year exceeds \$3,000, instalments are required. As the corporation is a small CCPC, instalments will be quarterly.
2. The three acceptable alternatives would be as follows:
 - Quarterly instalments of \$23,650 ($\$94,600 \div 4$) based on the current year estimate.
 - Quarterly instalments of \$23,025 ($\$92,100 \div 4$) based on the first preceding year.
 - One instalment of \$21,625 ($\$86,500 \div 4$) based on the second preceding year, followed by three instalments of \$23,491.67 [$(\$92,100 - \$21,625) \div 3$], a total of \$92,100.
3. The best alternative would be one payment of \$21,625, followed by three payments of \$23,491.67. While the total instalments are the same \$92,100 in both the second and third alternatives, the third alternative is preferable because the first payment is lower. This provides a small amount of tax deferral.
The instalments are due on March 31, June 30, September 30, and December 31, 2017.

Case Three

1. As the corporation's tax payable for both the current and the preceding year exceeds \$3,000, instalments are required. As the corporation is not a small CCPC, monthly instalments are required.
2. The three acceptable alternatives would be as follows:
 - Monthly instalments of \$7,883.33 ($\$94,600 \div 12$) based on the current year estimate.
 - Monthly instalments of \$8,450.00 ($\$101,400 \div 12$) based on the first preceding year.
 - Two monthly instalments of \$7,208.33 ($\$86,500 \div 12$) based on the second preceding year, followed by 10 monthly instalments of \$8,698.33 [$(\$101,400 - (2)(\$7,208.33)) \div 10$], a total of \$101,400.
3. The best alternative in terms of minimum instalments would be 12 instalments of \$7,883.33, resulting in a total of \$94,600 of instalment payments.
The instalments would be due on the last day of each month, beginning in January, 2017.

Case Four

1. As the corporation's tax payable for both the current and the preceding year exceeds \$3,000, instalments are required. As the corporation is not a small CCPC, monthly instalments are required.
2. The three acceptable alternatives would be as follows:
 - Monthly instalments of \$7,883.33 ($\$94,600 \div 12$) based on the current year estimate.
 - Monthly instalments of \$7,675 ($\$92,100 \div 12$) based on the first preceding year.
 - Two monthly instalments of \$7,208.33 ($\$86,500 \div 12$) based on the second preceding year, followed by 10 monthly instalments of \$7,768.33 $\{[(\$92,100 - (2)(\$7,208.33)) \div 10]\}$, a total of \$92,100.
3. The best alternative would be two payments of \$7,208.33, followed by ten payments of \$7,768.33. While the total instalments are the same \$92,100 in both the second and third alternatives, the third alternative is preferable because the first two payments are lower. This provides a small amount of tax deferral.

The instalments would be due on the last day of each month, beginning in January, 2017.

TIF Solution Two - 11

While there are alternatives in all Cases, the following answers represent the “minimum” instalments, as required in the problem.

In all three Cases, the current year alternative is the best, but you should note that if the estimated net tax owing is lower than the actual net tax owing, she may be charged interest on the insufficient instalments if the interest totals more than \$25.

Part A - Case One

Ms. Sloan's net tax owing in each of the three years is as follows:

2015 = \$500 (\$23,600 - \$23,100)
2016 = \$4,300 (\$25,400 - \$21,100)
2017 = \$3,900 (\$27,200 - \$23,300) Estimated

As her net tax owing is expected to exceed \$3,000 in 2017 and was more than \$3,000 in 2016, the payment of instalments is required.

Under the CRA approach, the first two instalments would be \$125 [(\$500 ÷ 4)] each, for a total of \$250. The remaining two instalments would be \$2,025 [(\$4,300 - \$250) ÷ 2], for a total of \$4,050. This would bring the total instalments for the year to \$4,300 (\$250 + \$4,050). A better solution would be to base the instalments on the estimated 2017 results. Each instalment would be \$975 (\$3,900 ÷ 4). The resulting total of \$3,900 would be less than the \$4,300 total under the CRA approach.

Part A - Case Two

Ms. Sloan's net tax owing in each of the three years is as follows:

2015 = Nil (\$23,600 - \$24,100)
2016 = \$6,800 (\$25,400 - \$18,600)
2017 = \$3,500 (\$27,200 - \$23,700) Estimated

As her net tax owing is expected to exceed \$3,000 in 2017 and was more than \$3,000 in 2016, the payment of instalments is required.

Under the CRA approach, no payment would be required for the first two instalments. However, the remaining two instalments would be \$3,400 each [(\$6,800 - Nil) ÷ 2], bringing the total for the year to \$6,800. A better solution would be to base the instalments on the estimated 2017 results. Each instalment would be \$875 (\$3,500 ÷ 4). The resulting total of \$3,500 would be less than the \$6,800 total under the CRA approach.

Part A - Case Three

Ms. Sloan's net tax owing in each of the three years is as follows:

2015 = \$4,500 (\$23,600 - \$19,100)
2016 = \$5,200 (\$25,400 - \$20,200)
2017 = \$2,900 (\$27,200 - \$24,300) Estimated

As her net tax owing is not expected to exceed \$3,000 in 2017, the payment of instalments is not required.

Part B

In Case One and Case Two, the required instalments would be due on March 15, June 15, September 15, and December 15.

TIF Solution Two - 12

Case One

1. As the corporation's tax payable for both the current and the preceding year exceeds \$3,000, instalments are required. As the corporation is not a small CCPC, monthly instalments are required.
2. The three acceptable alternatives would be as follows:
 - Monthly instalments of \$5,241.67 ($\$62,900 \div 12$) based on the current year estimate.
 - Monthly instalments of \$5,658.33 ($\$67,900 \div 12$) based on the first preceding year.
 - Two monthly instalments of \$4,800 ($\$57,600 \div 12$) based on the second preceding year, followed by 10 monthly instalments of \$5,830 $\{[(\$67,900 - (2)(\$4,800)) \div 10]\}$, a total of \$67,900.
3. The best alternative in terms of minimum instalments would be 12 instalments of \$5,241.67, resulting in a total of \$62,900 of instalment payments.

The instalments would be due on the last day of each month, beginning in January, 2017.

Case Two

1. As the corporation's tax payable for both the current and the preceding year exceeds \$3,000, instalments are required. As the corporation is not a small CCPC, monthly instalments are required.
2. The three acceptable alternatives would be as follows:
 - Monthly instalments of \$5,241.67 ($\$62,900 \div 12$) based on the current year estimate.
 - Monthly instalments of \$5,116.67 ($\$61,400 \div 12$) based on the first preceding year.
 - Two monthly instalments of \$4,800 ($\$57,600 \div 12$) based on the second preceding year, followed by 10 monthly instalments of \$5,180 $\{[(\$61,400 - (2)(\$4,800)) \div 10]\}$, a total of \$61,400.
3. The best alternative would be two payments of \$4,800, followed by ten payments of \$5,180. While the total instalments are the same \$61,400 in both the second and third alternatives, the third alternative is preferable because the first two payments are lower. This provides a small amount of tax deferral.

The instalments would be due on the last day of each month, beginning in January, 2017.

Case Three

1. As the corporation's tax payable for both the current and the preceding year exceeds \$3,000, instalments are required. As the corporation is a small CCPC, instalments will be quarterly.
2. The three acceptable alternatives would be as follows:
 - Quarterly instalments of \$15,725 ($\$62,900 \div 4$) based on the current year estimate.
 - Quarterly instalments of \$16,975 ($\$67,900 \div 4$) based on the first preceding year.
 - One instalment of \$14,400 ($\$57,600 \div 4$) based on the second preceding year, followed by three instalments of \$17,833.33 $\{[(\$67,900 - \$14,400) \div 3]\}$, a total of \$67,900.
3. The best alternative in terms of minimum instalments would be four instalments of \$15,725, for total payments of \$62,900. The instalments are due on March 31, June 30, September 30, and December 31, 2017.

Case Four

1. As the corporation's tax payable for both the current and the preceding year exceeds \$3,000, instalments are required. As the corporation is a small CCPC, instalments will be quarterly.
2. The three acceptable alternatives would be as follows:
 - Quarterly instalments of \$15,725 ($\$62,900 \div 4$) based on the current year estimate.
 - Quarterly instalments of \$15,350 ($\$61,400 \div 4$) based on the first preceding year.
 - One instalment of \$14,400 ($\$57,600 \div 4$) based on the second preceding year, followed by three instalments of \$15,667.67 [$(\$61,400 - \$14,400) \div 3$], a total of \$61,400.
3. The best alternative would be one payment of \$14,400, followed by three payments of \$15,667.67. While the total instalments are the same \$61,400 in both the second and third alternatives, the third alternative is preferable because the first payment is lower. This provides a small amount of tax deferral.

The instalments are due on March 31, June 30, September 30, and December 31, 2017.

TIF Solution Two - 13

Note To Instructor These Cases have been based on examples found in IC 01-1.

Case A

In view of the business that the taxpayer is in, there was nothing in the income statement that would have made the accountant question the validity of the information provided to him. Therefore, he could rely on the good faith reliance exception and would not be subject to the preparer penalty.

Case B

The prospectus prepared by the company contains a false statement (overstated fair market value of the software) that could be used for tax purposes. The company knew or would reasonably be expected to know, but for culpable conduct, that the fair market value of the software was a false statement. Since the company is engaged in an excluded activity, it cannot rely on the good faith reliance exception with respect to the valuation. The CRA would consider assessing the company with third-party civil penalties in the amount of \$2,000,000 (i.e., the gross entitlements). The CRA would also consider assessing the appraiser with third-party civil penalties. The amount of the penalty would be his gross entitlements from the valuation activity, which is \$75,000.

Case C

Although the tax return contains one or more false statements, the tax return preparer would be entitled to the good faith defense since he relied, in good faith, on information (the financial statements that were not obviously unreasonable) provided by another professional on behalf of the client. Therefore, he would not be subject to the preparer penalty.

The third-party penalties may be applied to the other accountant if he knew or would be expected to know, but for circumstances amounting to culpable conduct, that the financial statements contained false statements.

Case D

The accountant would not be subject to the penalties for participating or acquiescing in the understatement of a tax liability. The facts were highly suspect until the accountant asked questions to clear up the doubt in his mind that the client was not presenting him with implausible information. The response addressed the concern and was not inconsistent with the knowledge he possessed.

Case E

Since the tax return preparer e-filed the taxpayer's return without obtaining the charitable donation receipt, the CRA would consider assessing the tax return preparer with the preparer penalty. Given that the size of the donation is so disproportionate to the taxpayer's apparent resources as to defy credibility, to proceed unquestioningly in this situation would show wilful blindness and thus an indifference as to whether the ITA is complied with.

Case F

The issue here is whether the accountant is expected to know that GST is not payable on wages, interest expense, and zero-rated purchases. It is clear that the accountant should have known that no GST could be claimed on these items. Given this, in filing a claim that includes a GST refund on the preceding items, the accountant made a false statement, either knowingly, or in circumstances amounting to culpable conduct. Consequently, the CRA would consider assessing the accountant with the third-party civil penalty, specifically, the preparer penalty.