JONES THOMBLISON LLP , CHARTERED ACCOUNTANTS

3515 Mainway
Burlington, ON L7M 1A9

Ph: (905) 319-3515
Fax: (905) 332-7712
Email: steve@jtca.ca
jay@jtca.ca

Dear Clients/Friends:

This is a quarterly newsletter which we send to clients, referral sources and friends. The information is meant to be educational and application of the concepts should be on an individual basis. Please do not hesitate to contact us should you require further clarification of any item.

In this edition:

TAX TICKLERS... some quick points to consider...

- **Timing and amounts** of various **payments and benefits**, such as the Canada Child Benefit, can be obtained by calling the **CRA's TIPS line** at 1-800-267-6999.
- In the summer of 2016, CRA commenced a **project** to examine **taxpayers holding expensive properties** in Vancouver where only **low amounts of income** were reported. The goal of the project was to identify unreported worldwide income, **property "flipping"**, underreporting of capital gains on sales, and underreporting GST on sales of new homes.
- For the 2015 and subsequent tax years, **envelopes for church offerings** used as source documents should be retained for at least six years after the end of the year to which it relates.
- The CRA **Serving You Better** consultation campaign for small and medium-sized business has just kicked off. Have your say by **submitting feedback** to www.cra-engage-arc.ca/en.

CANADIAN INDUSTRY STATISTICS: How Do I Compare?

The Government of Canada provides **analysis** and **detailed information** on **economic indicators** using the most recent data from **Statistics Canada** on the website, **www.ic.gc.ca/eic/site/cis-sic.nsf/eng/home**. This website can help **small to medium sized businesses** understand the dynamics of their industries. Users can focus on a **single industry over time** or **compare one industry against another**.

Data is segregated based on the North American Industry Classification System **(NAICS) code**. Within each specific NAICS code is detailed **financial performance data**. Such data includes, for example, **average gross margins**, detailed **breakdowns of expenses** (e.g. repairs and maintenance, labour, professional and business fees) as a percentage of revenues, and **certain financial ratios** (e.g. current ratio, return on total assets).

Action Item: Consider using this site to compare your costs as a percentage of revenues to other Canadian companies in your industry.

Tax Tips & Traps

BENEFITS PAID TO SHAREHOLDER EMPLOYEES: Taxable?

The CRA is aware that owner-managers have an **incentive to receive benefits deductible** by their corporation which are **non-taxable to the owner**. In essence, this can be perceived as a method to extract profits out of a corporation without paying tax on it. As such, CRA is particularly vigilant to ensure that these benefits comply with the Income Tax Act and do not confer **unfair advantages on owners**.

To start off, it must be established whether the **benefits or allowances** have been **conferred** on the individual in their **capacity as an employee or** in their capacity as a **shareholder**. Unless the particular facts establish otherwise, **CRA presumes** that an employee-shareholder receives a benefit or an allowance in their **capacity as a shareholder** (assuming the individual can significantly influence business policy). This presumption **may not apply if**:

- the benefit or allowance is **available to all employees** of the corporation; or
- all of the employees are shareholders or individuals related to a shareholder, and the benefit or allowance is **comparable** (in nature and amount) to benefits and allowances generally offered to non-shareholder employees of **similar-sized businesses**, who perform **similar services** and have **similar responsibilities**.

If the benefit or allowance is received in their **capacity as an employee**, the federal income tax treatment is the **same as** for an **unrelated employee**. This means that the benefit is generally **deductible to the corporation and, under certain special circumstances, not taxable to the employee**.

Where an employee-shareholder receives a benefit or an allowance in their **capacity as a shareholder**, the value of the benefit or allowance is **included in the shareholder's income** and **may not be deductible** to the company.

Action Item: When commencing the provision of non-taxable benefits, consider whether they will also be offered to non-shareholder employees. If not, they may be taxable to the shareholder employee.

MUTUAL FUNDS: Corporate Class and Switch Funds

Mutual fund corporations have often been structured to permit changing funds within the group on a tax-free basis. These are commonly referred to as **"switch funds"** or **"corporate-class funds"**, and have become popular due to the ability to defer accumulated capital gains. Essentially, investors can **switch funds without realizing dispositions** and the related taxable capital gains.

However, **new legislation** has been proposed to **end these deferrals commencing** with exchanges on or after **January 1, 2017**.

Some exceptions exist, including switching between different series in the same class of shares representing the same underlying fund (for example, due to different commission or fee terms) and transactions where the underlying investment is unchanged, but shares are reorganized for other bona fide reasons (for example, changing voting rights or amalgamating funds).

Action Item: Consider rebalancing switch fund portfolios by December 31, 2016.

TRANSFERRING PROPERTY TO A FAMILY MEMBER: Taxable Transaction?

When transferring the **legal title** of a property to a family member, a disposition for tax purposes may not necessarily occur. The taxable event would **occur** when a **"beneficial ownership"** change happens. Usually, a beneficial change and legal change are one in the same, but not always.

In a June 14, 2016 **Technical Interpretation**, CRA examined the situation where a married couple **transferred the title to a property and mortgage** into a parent's name because they **no longer qualified to refinance** the original mortgage. Once their financial position improved, they **transferred the title back**. The original taxpayers continued to **make all mortgage** payments and other house costs. They also **continued to live** in the dwelling throughout the legal transitions.

The CRA opined that despite the legal ownership changes, **no beneficial ownership change occurred**. Therefore, there was **no taxable disposition**.

Action Item: Since the taxability of such a transaction is a matter of interpretation, caution should be taken when relying on such a position. Discuss your fact pattern with a professional and be sure to document appropriate support.

TEACHERS: This Credit Is for You!

The **Eligible Educator School Supply Tax Credit**, worth **15%** on up to **$1,000** of eligible supply expenses, has now become law. To mark the occasion, CRA has published a Question and Answer providing commentary on this new

refundable tax credit available in **2016** and subsequent years. The credit is also referred to as the Teacher and Early Childhood Educator School Supply Tax Credit.

Who Qualifies?

The new tax credit can only be claimed by an **eligible teacher or early childhood educator employed** at an **elementary** or **secondary** school or a **regulated child care facility**. The employee must either:

- hold a **teacher's certificate** that is valid in the province or territory in which they are employed (eligible teacher); or
- hold a **certificate or diploma** in **early childhood education** that is recognized in the province or territory in which the individual is employed (eligible early childhood educator).

What Expenditures Qualify?

An **eligible supply expense** is an amount paid in the year for supplies used or consumed in the school or regulated child care facility in the performance of the taxpayer's employment. Supplies include:

- **consumable goods** such as construction paper, flashcards, items for science experiments, art supplies, and stationary items; and
- **durable goods limited** to games, puzzles, books, containers and educational support software. Computers, tablets and rugs (for kids to sit on) are provided as examples of expenses which are not eligible.

The expense must **not be reimbursable**, nor subject to an allowance or other form of assistance. As well, the credit cannot be claimed for an expense which is **deducted** by any person for the year. The credit is available for the **year in which it was purchased** rather than when it was used.

Documentation Requirements

CRA may ask taxpayers to provide **certification from their employer** attesting to the eligible supplies expense. The certification should be a statement signed by the individual's employer that attests that the supplies were **used for the purpose of teaching or facilitating** students' learning, directly consumed in an appropriate facility in the performance of the individual's employment duties, and amounts paid were **not reimbursable** or otherwise deducted in income calculation. Employers providing this certification **should not** also **provide** a T2200, Declaration of Conditions of Employment, in relation to those supplies.

Taxpayers should **request** the **certification** from their employer in a timely manner and **keep it** in their files, along **with** their **receipts** for the supplies.

Action Item: Eligible Teachers and Educators – Keep receipts from the purchase of eligible supplies in the year.

CHARITIES: Ineligible Individuals Can Get Your Organization De-Registered

CRA holds the authority to suspend receipting privileges and **refuse** or **revoke the registration** of a registered charitable organization when an "**ineligible individual** is a **board member** or **controls or manages** the organization".

On March 17, 2016 CRA Guide CG-024, **Ineligible Individuals**, was updated. It provides 29 pages of description and implications of having ineligible individuals on **boards and in management positions**.

Generally, an **individual is ineligible** if he/she:

- has been **convicted** of an offence:
  - related to financial dishonesty; or
  - relevant to the operation of the organization; or
- was **connected** to an **organization** whose **registration was revoked** for a serious breach of the requirements for registration. Relevant connections could include:
  - a director, trustee, officer, or like official;
  - an individual in a position of management or control; or
  - a promoter of a tax shelter, and participating in that tax shelter caused the revocation of an organization's registration.

Individuals who **manage** a registered **organization**, directly or indirectly, include anyone who does one or more of the following:

- performs managerial (rather than only operational) duties;
- hires, disciplines and dismisses employees;
- prepares budgets within the organization; or
- varies staff assignments.

Individuals who have **influence** or the **power** to do one or more of the following would be **considered to have control**:

- change the board of directors or reverse its decisions;
- make alternative decisions concerning the actions of the organization;
- directly or indirectly end the organization; or
- appropriate the organization's assets.

Action Item: Review your charity's current leadership for possible ineligible individuals. Also consider adjusting recruitment and engagement processes to detect such individuals.

REGISTERED EDUCATION SAVINGS PLAN (RESP): Distribution of Funds

Amounts paid out of an RESP may be **taxable**, **non-taxable**, or may **trigger a repayment of Government support**. The taxation status of a receipt depends on whether it is considered an Educational Assistance Payment, a Refund of Contributions, or an Accumulated Income Payment.

Educational Assistance Payment (EAP) – An EAP is a **taxable amount** paid to a **beneficiary (a student)** from an RESP to help finance the cost of post-secondary education. An EAP consists of the **Canada Education Savings Grant, the Canada Learning Bond**, amounts paid under a provincial education savings program, and the **earnings on the money saved** in the RESP. The student includes the EAPs as income on their income tax return for the year the student receives them.

Refund of Contributions – The promoter can return contributions **tax-free** to the subscriber or beneficiary when the contract ends, or, at any time before. These payments are **not considered income** to the recipient. That said, a refund of contributions may, in some cases, **trigger a repayment of Government support**.

Accumulated Income Payments (AIP) – An **AIP** is an amount **paid to the subscriber** that relates to the **income earned in an RESP**. An AIP **does not generally include**: EAPs; payments to a designated educational institution in Canada; the refund of contributions to the subscriber or to the beneficiary; transfers to another RESP; or repayments under the Canada Education Savings Act or under a designated provincial program. An AIP is **included in the income** of the **subscriber** and is generally subject to an **additional 20% tax rate**, except where the amount is eligible for a rollover to another registered plan.

Action Item: Consider the financial consequences, tax or otherwise, on withdrawing funds from an RESP.

PRINCIPAL RESIDENCE EXEMPTION

The principal residence exemption (PRE) is an income tax benefit that generally provides taxpayers an exemption from tax on the capital gain realised when selling the property that is their principal residence. Previously, the CRA has not required any reporting related to the sale of a principal residence if the property was the taxpayer's principal residence for every year owned. **Starting with the 2016 tax year**, taxpayers will be required to **report basic information (date of acquisition, proceeds of disposition and a description/address of the property)** on their income tax return in the year they sell a principal residence and are claiming the full principal residence exemption**. If you sold or are planning to sell your principal residence, be sure to have this information available at tax time.**

If you also own a recreational property we may complete a form T2091 for the sale of your principal residence to allow some of the PRE to be claimed on the eventual sale of the recreational property. If this is your situation please discuss further with us.

DOCUMENTS REQUIRED TO CLAIM A U.S. FOREIGN TAX CREDIT:

Prior to the summer of 2015, CRA often accepted copies of the **U.S. tax returns**, as support to claim a U.S. Foreign Tax Credit (FTC). The **"Federal Account Transcript"** was selected as alternative evidence the return provided to CRA was filed and assessed as filed.

Some practitioners report that **obtaining "transcripts"** from the Federal Government, and State Governments in particular, can be onerous, often requiring a request from the client rather than a representative.

Form T2209 Federal Foreign Tax Credits sets out the documents required to support foreign tax credit claims, including **federal, state and municipal tax returns** with all associated schedules and forms, a copy of the **federal account transcript** and an **account statement** or similar document from **state and/or municipal tax authorities**.

CRA recently **changed** its requirements, to accept **proof of payments** made **or refunds** received in lieu of a notice of assessment, transcript, statement or other document from the applicable foreign tax authority (FTA), **provided all of the following information** is clearly indicated:

- that the **payment** was **made to** or received from the **FTA**;
- the **amount** of the payment or refund;
- the **tax year** to which the payment or refund relates; and
- the **date of payment** of receipt.

Action Item: Request these documents before a CRA pre- or post-assessing review letter is received to expedite the FTC Claim.

To get a Federal transcript from the IRS, go to: www.irs.gov/individuals/get-transcri