Principles of taxation final notes essay sample

Economics, Tax

Capital property: depreciable property and any other property the disposal of which would result in a capital gain

Capital gains = proceeds – ACB

Taxable capital gain = capital loss and gain are taxed at a rate of ½

Capital losses are denied: depreciable property, personal use property, deemed dispositions (to the extend they exceed capital gains

Disposition of Identical Properties (shares)

Post V day pool (pre 1972) (real estate property

Median rule: ACB is the middle about of

1) Proceeds of disposition

2) V Day value

3) Cost (FIFO basis)

VDay Method: available only to individual taxpayers (election must be made accrued gains not taxed

V day method is used, no need to compute average cost of pre VDay property

Superficial Losses

Property is sold at a loss but the property was acquired or reacquired within 30 days from the date of sale by the taxpayer or an affiliated person (spouse, or corporation controlled by tax payer

The loss is denied and added back to the ACB of the reaquired property

Personal Use property

- Cars, furniture, clothes
- 1000 floor rule to proceeds and acb
- Capital gain is taxed, capital loss denied

Listed Personal Property

- Coins, stamps, jewellery, paintains, drawings, sculptures, and rare books
- 1000 floor rule applies
- Losses can be only applied against gains from LLP
- Can be carried back 3 years and forward 7 years

Reserve on Capital gain is computed as the lesser of:

1) Outstanding proceeds x capital gain

Total proceeds

2) 1/5 of the gain x (4-#preceding years)

At least 20% of the gain is taken into income each year, capital gain is fully recognized no later than the 5th year after the disposition

On the disposition of shares in a QUALIFYING SMALL BUSINESS CORP, a 10 yr deferral is available

Deferred gain is computed as:

CG x lesser of: 1) cost of replacement shares or 2) proceeds of disposition

Proceeds of Disposition

ACB of reinvested shares: amount reinvested – deferred gain = shares of new company

Principal Residence

If you have more than 1 residence, when allocated years of designation to determine exempt portion of gain consider: which property has the greatest accrued gain and time from for disposition

Exempt portion of the gain is computed as:

1 + # of years of designation x CG

# of years owned (the +1 factor takes care of the year a residence is sold and another purchased, since you can only designate one principal residence per year

Non Arms Length Transfers/Sales (Attribution Rules

For Non-Depreciable Property S69

TransferVendor Purchaser

Greater than FMVNo adj. to proceeds ACB = FMV

Less than FMVProceeds = FMVACB = $ Paid

GIFT Proceeds = FMVACB = FMV

Spousal transfers (when a spouse transfers property to the other spouse, the transferor is deemed to have disposed of the property at: 1) Its ACB for non-depreciable property

2) Its UCC for dep. Property is the asset is one of many assets in the class than the Deemed Proceeds of Disposition is computed as: UCC of class x FMV of asset transferred

FVM of all assets in the class

** if the transferor did not elect of of S73(1), it is not considered a sale, there are not capital gains Transferee: ACB or UCC will flow through the transferee unless transferor receives FMV and elects out of S73(1)

Tax Consequences if the taxpayer elects out of S73(1)

1) If the taxpayer receives FMV consideration:

• This would be considered an actual disposition, reported as capital gain realized at date of transfer • Any capital gain realized when the disposition takes place is not attributed back, nor is any income • If debt is taken back as consideration, it must bear interest at the prescribed rate and interest must be paid within 30 days after year end

2) FMV consideration is not received:

• Capital gain is reported by the transferor at date of transfer based on the FMV at that date • Property income and any CG is attributed back

• Second generation income is NOT attributed back • Rules of S69 apply is the consideration received is less or greater than FMV

Transfers to Minors (dependent)

• Property income is attributed back (but not capital gains) until child reaches 18 • Attribution applies to substituted property (second generation income) • If FMV was received, attribution does not apply

• Reasonable gifts made without concern of attribution rules

***Attribution does not apply if the asset is transferred to a family member not a spouse or minor child of taxpayer

Split Income “ The Kiddy Tax” (29% tax on child under 18. No deductions or credits allowed

Depreciable Property

Where the ACB of the vendor is > than price paid by purchaser 1) ACB to the purchaser is equal to the sellers ACB

2) If the price paid is < the UCC of the vendor, the purchaser’s UCC is equal to the seller’s UCC 3) If the price paid is > the UCC of the vendor, the purchaser’s UCC will be equal to the price paid

Computation of Taxable Income for Individuals (Division C Employee stock option deduction (½ of the stock option benefit • If the shares are gifted to charitable organization, the stock option deduction is 100% • Gifts through stock option (entitled to an additional 50%, so no stock option benefit is actually taxed

Home Relocation Loan Deduction (lesser of:

a) Amount of net taxable benefit

b) 250 x prescribed rate

** Deduction is available for no more than five years

Deduction for certain payments:

• Workman’s compensation payments

• Social assistance payments

• Employment income from a prescribed international organization

Capital Gains deduction (CCPC with over 90% assets in ABI

• Up to $750K

• Cannot exceed FMV

Losses carried forward

• Non Capital Losses: Net losses from non-capital sources + stock option deduction + home relocation deduction + exempt items = Non capital loss of the year • May be used against any source of income

Net Capital Losses: can only be used against taxable capital gains • From the disposal of capital assets, allowable capital loss of the year exceeding taxable capital gains of the year • In the year of death, can be used against any income

Computation of Tax Payable for Individuals

Registered Retirement Savings Plan; deduction if the lesser of:

• Actual contributions

• 18% prior year's income less pension adjustment of previous years plus previous years' unused room • $22 970 less pension adjustment of previous years plus previous years' unused room

Registered Pension Plan:

• Contributions

• 18% of this year's income less pension adjustment of previous years plus previous years' unused room • 22 450

Corporate Taxation

Net Income:

ADD:

• Accounting income tax expense

• Accounting depreciation

• Recapture of CCA

• Tax reserves deducted in the prior year

• Accounting Losses

• Accounting warranty expenses

• Foreign tax paid

• Taxable capital gains

• Interest and penalties paid for income tax purposes

• Non-deductible automobile costs

• ½ meals and entertainment

- Equity loss
- Club dues and recreational facilities
- Accounting reserves
- Charitable contributions
- Accounting Write-downs

Eligible Dividends = gross up 1. 38, tax credit 66 2/3

Non Eligible Dividends = gross up 1. 25, tax credit 6/11

Computation of Non Capital loss = Net Income = Dividends – Charitable donations (75% NI) – Capital Losses

Administration & Enforcement

Filing of tax returns (an individual is required to file by April 30th the following year, trust must file 90 days from YR, corporation must file 6 months from YE

Employer Withholdings (Late penalties: 3% 3 days late, 5% 4/5 days late, 7% 6/7 days late, 10% 8 or more days late. Double penalty is knowingly withheld

Installments for Individuals: an individual will be required to make quarterly payments if the difference between the tax payable and amounts withheld at source is greater than $3000 in both the current year and either of the two preceding years. Interest on late installments

Installments for corporations: 2 months after YE to pay interest

Foreign Reporting Requirements: taxpayers and partnerships are required to file if certain property ids help outside Canada with a cost more than $100K. Failure to do so = $500/m up to 24 months. Doubled if demand is served

Refund of interest: Interest is paid at the prescribed rate from the latest of:

1. Date overpayment arose

2. Individuals = 30 days following the day the return was or would have been due 3. Individuals = the day the return is filed

4. Corporations = 120 after the end of the filing date

Interest and Penalties (Late filing penalty = 5% + 1%/month for up to 12 months. If taxpayer has already been assessed, 10% and 2%/month up to 20 months. Interest is compounded and non deductible

Failure to report income: 10% penalty for 2nd occurrence within 3 years

Gross negligence = 50% tax liability

Criminal offense: $100/$25 000 fine and 12 month prison

Criminal offence: 50%/200% tax and 2 year prison

Books and reports (maintain for 6 years

Assessment and Reassessment(reassess within 3 years, 6/7 years (public) if theres a loss carry back

Adjustment: Send letter to CRA, online services, filing a form

Collection of taxes: CRA can (seize and sell assets, require debtor to make payments directly to CRA, immediate payment if leaving Canada. CRA cannot legally collect after

Objection and Appeals:

• File a notice of objection from the later of: 90 days or 1 year from the date the return was filed for a trust • CRA's response must be within 90 days

1. Informal Procedure

▪ Tax at issue is no more than $12K or income item is no more than $24K ▪ Individual can represent himself or by a 3rd party ▪ Corp must be represented by counsel

▪ CRA must reply within 45 days after notice of appeal (otherwise taxpayer wins ▪ Case is heard within 90 days, decision rendered within 60 days ▪ Completed within 7 months

2. Formal Procedure

▪ Represented by counsel

▪ 50% successful, judge can order the Minister to pay all or part of the costs

▪ Motion for a judge can be applied 75 days after case has been heard ▪ If case not heard one year from the time it was appealed, case may be dismissed ▪ Taypayer must appeal the tax court decision to the federal court of appeal within 30 days

General Anti Avoidance Rules (GAAR)

• 3 requirements: tax benefit, avoidance transaction, must be abusive tax avoidance. Burden is on taxpayer to refute 1 and 2 and CRA must establish 3

Fairness Package: allows taxpayer to claim deductions, requesting late/amended elections, request reductions or cancellation of interest

Deduct:

- Allowable capital losses
- CCA
- CEC
- Terminal losses
- Current year tax reserves
- Equity income
- Accounting gains
- Warranties paid
- Foreign non-business tax deduction
- Allowable business investment losses

NET INCOME FOR TAX PURPOSES

Less Division C Deductions:

- Dividends received
- Charitable Donations
- Losses carried forwards

TAXABLE INCOME FOR CORPORATIONS