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MTI NEWSLETTER - TAX TIPS & TRAPS

We would like to take this opportunity to wish you and your family a safe and happy holiday season.

Our office will be closed for the holidays starting December 24th and will re-open on January 3rd, 2017.

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 kicked off. Have your say by submitting feedback to www.cra-engage-arc.ca/en.

IN THIS EDITION

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.

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.

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

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

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.

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.

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.

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?

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.

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.

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

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.

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 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.