

TAX UPDATE

NEWSLETTER SEPTEMBER 2018

Welcome to the Tax Update Newsletter, a summary of the most recent tax developments that affect business owners and individuals.

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IN THIS EDITION:

DONATION RECEIPTS: How Complete Is Complete	1
PERSONAL USE OF BUSINESS AIRCRAFT: How Big of a Taxable Benefit Is It?	2
SUBSIDIZED MEALS: Are They a Taxable Benefit?	3
EMPLOYER-SPONSORED SOCIAL EVENTS: After the Party	3
DIRECTORS: Can They Be Liable for Corporate Income Taxes?	4
INTEREST ON DELINQUENT ACCOUNTS Proper Disclosure on Legal Documents	5
INTEREST DEDUCTIBILITY: Returns of Capital	5
INPUT TAX CREDITS: Making Timely Claims	5

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DONATION RECEIPTS: How Complete Is Complete?

Charities should ensure that any donation receipts issued are fully compliant with the tax rules. Failure to do so may result in the donor being denied a charitable donation if reviewed by CRA. This could cause operational and goodwill problems for the charity.

Receipts for cash gifts must have the following:

- a statement that it is an official receipt for income tax purposes;
- the name and address of the charity as on file with CRA;
- a unique serial number;
- the registration number issued by CRA;
- the location (city, town, municipality) where the receipt was issued;
- the date or year the gift was received and the date the receipt was issued;
- the full name, including middle initial, and address of the donor;
- the amount of the gift;
- the amount and description of any advantage received by the donor;
- the eligible amount of the gift;
- the signature of an individual authorized by the charity to acknowledge gifts; and
- the name and website address of CRA.



DONATION RECEIPTS: How Complete Is Complete? *continued from page 1*

Receipts for non-cash gifts must also include:

- the date the gift was received (if not already included);
- a brief description of the gift received by the charity; and
- the name and address of the appraiser (if the gift was appraised).

The amount of a non-cash gift must be the fair market value of the gift at the time the gift was made.

Effective March 31, 2019, charities and qualified donees must include the new website address of CRA, www.canada.ca/charities-giving on all donation receipts. This follows the move of various old Federal Government websites to the new official www.canada.ca website.

Action Item: If you are involved with a charity, ensure properly completed donation receipts are being distributed.

PERSONAL USE OF BUSINESS AIRCRAFT: How Big of a Taxable Benefit Is It?

A CRA communication dated March 7, 2018 provided updated commentary on taxable benefits arising from the personal use of a business aircraft.

CRA categorized the types of flights into three groups, as follows:

Mixed-use flights – If a shareholder or employee takes a flight which has a clear business purpose, they would not generally be subject to a taxable benefit. An individual's purpose is a question of fact. If others take the same flight (such as a non-employee spouse or child) for purely personal purposes, the taxable benefit would be equal to the highest priced ticket available for an equivalent commercial flight available in the open market for the accompanying individual(s).

Full personal use flights – Where there is no business purpose to the flight, the shareholders or employees will be considered to have received a taxable benefit equal to the price of a charter on an equivalent aircraft for an equivalent flight in the open market

(split amongst relevant individuals on the flight). Limited exceptions may apply where an open market charter is not a viable option.

Full personal use by non-arm's length persons – For shareholders or employees who do not act at arm's length with the business (such as an owner who controls the business), where the aircraft is used primarily for personal purposes relative to the aircraft's total use, the taxable benefit will equal their portion of the aircraft's operating costs plus an available-for-use amount. The available-for-use amount is computed as the original cost multiplied by the prescribed interest rate for the percentage of personal usage. The available-for-use amount on leased aircrafts is based on the monthly leasing costs of the actual usage multiplied by the proportion of personal usage.

Taxable benefits in respect of passengers that are non-employee family members or friends would be assessed on the shareholder or employee.

TAX TICKLERS

A large amendment to a T4 slip may trigger a payroll audit. Ensure that T4 slips are as accurate as possible at the outset.

CRA may request taxpayer information from third-parties.

A recent project using third-party data identified \$86 million of unreported income and attracted over \$19 million in additional taxes. CRA stated additional projects began in late 2017.

A recent poll found that 51% of Canadians have no will, and only 35% have one that is up to date. Quebec and B.C. lead the provinces (58% and 54% respectively), with the less than 50% in all other provinces.

Action Item: If employees are using a business aircraft for personal use, attention should be paid to whether employment benefits are being properly calculated and reported.

SUBSIDIZED MEALS: Are They a Taxable Benefit?

Do you have an employee dining room or cafeteria? In a March 21, 2018 Technical Interpretation, CRA stated that they do not consider meals subsidized by the employer to be a taxable benefit provided the employee pays a reasonable charge. This charge should be sufficient to cover the cost of the food, its preparation and service.

Where the charge is less than the cost, the difference would be considered a taxable benefit and should be included on the employee's T4. It is also important to note that the taxable benefit would be pensionable (CPP remittance required), but not insurable (no EI remittance required).

Action Item: Due to the tax cost to the employee, in addition to the administrative tracking costs, one should consider having employees pay at least a reasonable amount for meals provided.



EMPLOYER-SPONSORED SOCIAL EVENTS: After the Party

In an April 9, 2018 French Technical Interpretation, CRA clarified their position on taxable benefits arising from employer-sponsored social events, such as a holiday party or other event.

Where the cost of the social event does not exceed \$150/person (previously the limit was

\$100), excluding incidentals such as transportation, taxi fares and accommodations, there would be no taxable benefit to employees. CRA indicated that the cost should be computed per person who attended, and not per person invited.

If the cost exceeds \$150/person, the entire amount, including

the additional cost, is a taxable benefit to the employee. In these cases, only employees attending the function would be subject to the taxable benefit.

Action Item: Ensure the cost of employer-sponsored events do not exceed this threshold to avoid a surprise tax cost for employees.

DIRECTORS: Can They Be Liable for Corporate Income Taxes?

A December 11, 2017 Tax Court of Canada case examined whether a taxpayer was liable for unpaid income taxes of the corporation of which he was a director. CRA's assessment was based on the assertion that the taxpayer was a legal representative of the corporation and had distributed assets of the corporation without having first obtained a clearance certificate from CRA.

the time the certificate was issued. Legal representatives that fail to get a clearance certificate before distributing property may be liable for any unpaid amounts, up to the value of the property distributed.

Taxpayer wins

The Court examined whether the taxpayer was a legal representative and personally liable for the corporation's unpaid taxes. The definition of a legal representative does not specifically include directors, despite naming many other persons (e.g. a receiver, a liquidator, a trustee, and an executor). While a director could

result in the director being a "legal representative".

A director could become a legal representative where:

1. additional powers beyond directorship have been legally granted or, if not legally granted, were available and assumed;
2. these additional powers allowed the legal representative to legally and factually dissolve (wind-up) and liquidate the corporation; and
3. by virtue of these powers, the director liquidated the assets of the corporation.



In this case, no such legal powers had been conferred or exercised. The taxpayer was not considered to be the corporation's legal representative. Also, the corporation had not been dissolved. As such, the taxpayer was not personally liable for unpaid corporate income taxes.

Action Item: If you are a director and legal representative of a corporation, ensure that you are properly protected if distributing assets.

A clearance certificate essentially confirms that the corporation has paid all amounts of tax, interest and penalties it owed to CRA at

become a receiver or liquidator for a corporation, carrying out the usual activities of a director, such as declaring dividends, would not

INTEREST DEDUCTIBILITY: Returns of Capital

In an April 20, 2018 Tax Court of Canada case, at issue was whether the taxpayer could deduct interest incurred in 2013, 2014 and 2015 related to \$300,000 borrowed in 2007 to purchase mutual funds. From 2007-2015, the taxpayer received a return of capital from the funds, totalling \$196,850 over the period. A return of capital is essentially a return of the taxpayer's original investment. The taxpayer used some proceeds to reduce the loan principal, but the majority was used for personal purposes.

Taxpayer loses

The Court examined whether there was a sufficiently direct link between the borrowed money and its current use in respect of gaining or producing income from the investments.

As much of the returned capital was used for personal purposes, there was no longer a direct link to the income earning purpose. The Court upheld CRA's denial of interest expense.

Action Item: Where funds are borrowed to invest, one may need to track any return of capital which is not reinvested to determine interest deductibility.

INPUT TAX CREDITS: Making Timely Claims

In a May 31, 2018 Tax Court of Canada case, the taxpayer claimed ITCs (arising from the December 2008 quarter-end) which were previously disallowed when claimed by a related party. Within 30 days of that decision, the taxpayer claimed the ITCs on their return for the quarter ending September 30, 2015.

Taxpayer loses

ITCs must be claimed within four years after the end of the reporting

period in which they arise. It was not relevant that the related party had attempted to claim the ITCs within that period. Failure to make the claim on a return filed within four years of the end of the appropriate period was fatal to the claim.

Action Item: Ensure you are claiming your input tax credits in a timely fashion or risk losing them altogether.

INTEREST ON DELINQUENT ACCOUNTS: Proper Disclosure on Legal Documents

In a November 10, 2017 Alberta Court of Queen's Bench case, the amount of a creditor's claim was challenged after an uncontested default judgment. The claim included interest calculated at 1% per month as stated in the contract. However, where a rate is not stated in per annum terms, the legal maximum is capped at 5% annually under the Canada Interest Act. Therefore, the interest payable was legally capped at 5% per year, rather than the 1% per month specified by the contract.

Action Item: If stating interest rates in legal contracts, ensure to also state them in per annum terms.

