YOUR ACCOUNTANT

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In this edition:

This publication is a high-level summary of the most recent tax developments applicable to business owners, investors, and high net worth individuals. Enjoy!

TAX TICKLERS… some quick points to consider…

- The **tuition tax credit** has been **extended** to include courses at a post-secondary educational institution that are not at a post-secondary school level. This may include, for example, courses on basic literacy or numeracy, or learning a second language.
- **Medical expense claims** for **reproductive technologies** have been extended to include situations where the patient does not have a medical condition preventing conception. Claims will be allowed for 2007 and later years.
- Individuals can now **pay** their **individual taxes**, by cash or debit card, at **Canada Post**.
- Despite legal uncertainties, individuals may wish to **review their estate planning**, life insurance policies, and documents addressing Powers of Attorney and advanced directives, related to **physician assisted dying**.

EMPLOYEE DISCOUNTS ON MERCHANDISE: Change in CRA Policy

Historically, CRA has stated that an employee enjoying a discount on the purchase of merchandise from their employer is **only taxable** if a limited number of specified situations exist, such as where the employer makes a **special arrangement** with the employee or group of employees to buy the merchandise at a discount; the employee buys the merchandise for **less than** the **employer's cost**; or the employer makes a **reciprocal arrangement** with **another employer** so that the employees of one employer can buy merchandise from the other at a discount.

While the above guidance is still published in certain CRA documents, CRA has recently released updated guidance which appears to limit this administrative position. In CRA Folio S2-F3-C2, CRA noted that where an **employee receives a discount on merchandise** because of their employment, the **value** of the **discount** is generally a **taxable benefit**. This would apply regardless of whether the discount was provided by the employer or a third-party.

This updated guidance appears to be consistent with a number of Court decisions.

Action Item: Consider your business policy in respect of discounts on merchandise for employees in light of this updated administrative position.

DEATH BENEFITS: Tax-Free Employment Benefit

A death benefit is a payment received subsequent to the death of an employee, in **recognition** of the deceased **employee's services**. **Up to $10,000** can be received by the Estate or beneficiaries of the deceased as a death benefit on a **tax-free** basis. As an employment-related cost, this would generally be **deductible to the payer**.

A March 14, 2017 **Technical Interpretation**, addressed several questions related to these payments following the **death of an owner-manager**.

CRA noted that the determination of whether an individual is an employee is a **question of fact**. The fact that an owner-manager **received salaries** for several years but was **only** paid **dividends** in the **two years prior to death** would **not automatically mean that no death benefit** could be received. It would be **more difficult** to support an employment relationship where the individual **never received employment income** from the corporation.

The existence of a **formal commitment**, such as a contract or a Directors' Resolution, **prior to** the date of **death** is **not a requirement** for an amount to be a death benefit. Finally, a death benefit **could be paid out over time**, but the $10,000 **exclusion applies** only **once**, not once for each year.

Action Item: Consider this tax-free employment benefit.

RETIREMENT INCOME CALCULATOR: Ensure you are Financially Ready

The Canadian Retirement Income Calculator (https://www.canada.ca/en/services/benefits/publicpensions/cpp/retirement-income-calculator.html) provided by the Government of Canada **estimates retirement income** generated through a number of programs such as the **Canada Pension Plan**, **Old Age Security** pension, an individual's **employer's pension plan**, **RRSPs**, and **other sources** based on past and intended contributions.

When using this tool, individuals should have their CPP Statement of Contributions, financial information about their employer's pension, most recent RRSP statement, and any other information related to savings that will provide for ongoing monthly retirement income.

Action Item: Use this tool to help asses your financial readiness for retirement.

TAX CHANGES FOR PRIVATE CORPORATIONS

In our last newsletter we outlined the proposed changes that the Department of Finance released in July 2017. The consultation period ended 2 October 2017 and by 16 October 2017 the Department was releasing changes to the original proposals after concerns raised by small business owners and tax experts. These releases did not include revisions to the original draft legislation and therefore there remains some uncertainty until we receive the legislation.

The first such change announced was a reduction in the small business tax rate from the current rate of 10.5% to 10% effective 1 January 2018 and to 9% effective 1 January 2019. An offsetting increase to the taxation of non-eligible dividends will be implemented to maintain tax integration.

The second change announced was the Department, at this time, would not be moving forward with the proposed measures to limit access to the lifetime capital gain exemption. This was welcome news as many businesses were going to be forced into certain restructuring plans during 2018 or shareholders would have been entering into a transitional election to crystalize their lifetime capital gains exemptions in 2018. In many cases, costly valuations may have been required.

Thirdly, the Department will be proceeding with its measures to limit income sprinkling with family members to a reasonable amount. The Department did, however indicate that they intend to simplify their original proposals in determining what will be a reasonable dividend. It indicated that family members who meaningfully contribute to the business will not be impacted by these proposals. Meaningful contributions will be assessed through any combination of the following:

a. Labour contributions
b. Capital or equity contributions to the business
c. Assumption of financial risk of the business, such as co-signing a loan or other debt, and/or
d. Past contributions in respect to previous labour, capital or risks.

There will remain a certain degree of uncertainty of what will constitute a reasonable amount. We will have to wait and see how the draft legislation provides for this simplified process, however past experience has proven that this type of reasonable test will be open to interpretation and a source of potential CRA challenges. Income sprinkling measures will be effective for 2018.

Perhaps the most unanticipated announcement was the Departments intention to move forward on its measures to limit the tax deferral currently available by investing active business profits retained in the business in passive investments. Some changes to the original proposals were put forth. It appears that a grandfathering measure will be in place stating that investments already made by private corporations, including future income earned from such investments will be taxed under the current system. A further relief measure will be to allow for up to $50,000 of passive investment income to be earned each year in a corporation without any change to the taxation of this passive income. Draft legislation will be released in the 2018 Federal budget to determine how passive income above the $50,000 threshold will be taxed. It is anticipated that a detailed tracking system will need to be put in place to keep track of pre-budget assets and post-budget assets to ensure the correct taxation of the passive income earned.

Lastly, the Department has indicated that it will not be moving forward with measures relating to the conversion of income into capital gains. These measures were originally proposed to prevent individual taxpayers from using non-arm's length transactions to step-up the cost base of shares of their corporation. These measures would unintentionally have increased the taxation on intergenerational transfers. The Department will be reviewing the taxation of bona fide intergenerational transfers to ensure they are on a level playing field with transfers to unrelated parties.

VOLUNTARY DISCLOSURE PROGRAM: Proposed Tightening

The Voluntary Disclosure Program (VDP) provides taxpayers (individuals, corporations, partnerships, trusts, etc.) the opportunity to fix incorrect or incomplete previously filed tax returns (or returns that should have been filed) with a reduction to penalties and possibly interest.

CRA recently released fairly substantial proposed changes to the current program, **effective January 1, 2018**. The proposals are expected to be **finalized** in the **fall of 2017**.

The proposals will create **two tracks** for **income tax disclosures**.

General Program (GP)
The GP is similar to the **current VDP**. **Penalties** will be **waived**, subject to the usual ten-year limit, **criminal prosecution** will **not** be **considered** and **interest relief** will be **considered** for years preceding the most recent three years, with 50% of interest generally being waived. Interest for the most recent three years will not be waived.

Limited Program (LP)
The LP will be applicable for disclosures of **major non-compliance** and will provide **reduced relief**. **Examples** of situations where the LP would apply include where there are: **active efforts** to **avoid detection** through the use of offshore vehicles or other means; **large amounts** involved; **multiple years** of non-compliance; **sophisticated taxpayers** involved; **disclosures after CRA communications** such as official statements regarding its intended compliance focus, or following CRA campaigns or correspondence; and other circumstances where a high degree of **taxpayer culpability** contributed to the non-compliance.

Under the LP, **gross negligence penalties** will be **waived**, and **criminal prosecution** will **not** be **considered**. However, **all other penalties** will be **assessed**. **No interest relief** will be provided.

No Relief
In addition to current ineligible submissions, a number of situations will no longer be eligible for the VDP, including, for example where there is: income from **proceeds of crime**; a disclosure from a **corporation** with **gross revenue** in excess of **$250 million** in at least two of its last five years; and a disclosure related to **transfer pricing adjustments** or penalties.

Conditions for Valid Disclosure
The current requirements that any disclosure be **voluntary**, **complete**, involve a **penalty** or potential penalty, and include information **at least one year past due** will remain unchanged. Some further conditions, such as the requirement that the applicant pay the estimated taxes owing on application are proposed. Payment arrangements supported by adequate security may be accepted.

Action Item: If you have a disclosure which may be impacted by these proposed changes, ensure to submit your disclosure prior to the proposed changes effective date of January 1, 2018.

WITHHOLDINGS ON REMUNERATION TO NON-RESIDENT: Get your CRA Filings Correct

In a March 9, 2017 **Technical Interpretation**, CRA commented on the tax **filing** and **withholding requirements** related to a **non-resident individual providing services to a Canadian company**.

If an individual is **employed solely outside of Canada**, and is **not**, and has never been, a **resident of Canada**, **no withholdings** on payments are required. However, the corporation would generally be **required to file a T4** in respect of the non-resident individual's total remuneration. One exception to

this rule, would be where the total remuneration for the year is less than $500. This requirement to file a T4 is not conditional upon the payee being taxable in Canada.
CRA also opined that participation in meetings using the Internet or telephone from outside of Canada would not constitute performing the services in Canada.

Action Item: Ensure you are filing T4s in respect of non-resident employees providing services outside of Canada.

PROFESSIONALS' WORK IN PROGRESS EXCLUSION: Changes are coming

In the past, taxpayers in certain designated **professions** (i.e., accountants, dentists, lawyers, medical doctors, veterinarians and chiropractors) may have elected to **exclude** the value of **work in progress (WIP)** in computing their income for tax purposes. This essentially enabled these professionals to defer tax by permitting the costs associated with WIP to be expensed without including the matching revenues.

However, the 2017 Federal Budget proposed to **eliminate this election**, effective for the first tax year that begins after March 22, 2017. Transitional rules have been introduced to implement the change over two years. Once fully implemented, WIP, which is valued at the lower of cost or fair market value, will need to be included in income each year.
At present, many professionals either do not account for WIP in their financial accounts or account for WIP at its expected billing amount, using staff and partner billing rates rather than cost. These **professionals** will be **required to determine** the cost of their **WIP** in order to comply with these new provisions. There has been some **uncertainty** expressed regarding how the **cost of WIP** is properly **calculated**.

CRA has stated that the proposed changes are not expected to have any impact on bona fide contingency fee arrangements. That said, some practitioners have expressed concern that this concession has little or no basis in law.

Action Item: If you are in one of the industries impacted, and have not previously tracked the cost of your WIP, consider doing so. Also, budget for the possible additional tax liability over the next two years due to catching up the deferral of WIP.

ELECTRONIC T4 SLIPS: Now More Widely Available

CRA has provided commentary on its website to discuss recent changes to allow the **electronic distribution of T4 slips**. In the past, an employer could provide a T4 electronically only with the **employee's consent**. For 2017 and subsequent tax years, employers may also satisfy their obligations by providing electronic versions **without specific consent**, provided **other criteria** are met. The employer must provide the following by the last day of February following the calendar year to which the slip relates:

- a secure **electronic portal** through which the employee can access their T4 slip;
- a **secure site** for printing the slip; and
- an **option** to receive paper copies upon request.

Paper copies **must be provided** if:

- one of the above **conditions** are **not met** (unless employee consent has been received);
- the employee **requests** a **paper** copy;
- the employee is on **sick leave** or is **no longer an employee** of that employer; or
- the employee **cannot** be reasonably **expected to have access** to obtain the T4 slip **electronically**.

The above only applies to T4 slips. Employers cannot issue T4 slips by email due to insufficient security features.

Action Item: Consider whether these new rules allow for a more streamlined T4 distribution at your business.

YEAR-END TAX PLANNING

December 31, 2017 is fast approaching… see below for a list of tax planning considerations. Please contact us for further details or to discuss whether these may apply to your tax situation.

SOME 2017 YEAR-END TAX PLANNING TIPS INCLUDE:

1) Certain expenditures made by individuals by December 31, 2017 will be eligible for 2017 tax deductions or credits including: moving expenses, child care expenses, charitable donations, political contributions, medical expenses, alimony, eligible employment expenses, union, professional, or like dues, carrying charges and interest expense. Ensure you keep all receipts that may relate to these expenses.

2) If you own a business or rental property, consider paying a reasonable salary to family members for services rendered. Examples of services include website maintenance, administrative support, and janitorial services. Salary payments require source deductions (such as CPP, EI and payroll taxes) to be remitted to CRA on a timely basis, in addition to T4 filings.

3) A senior whose 2017 net income exceeds $74,788 will lose all, or part, of their Old Age Security. Senior citizens will also begin to lose their age credit if their net income exceeds $36,430. Consider limiting income in excess of these amounts if possible. Another option would be to defer receiving Old Age Security receipts (for up to 60 months) if it would otherwise be eroded due to high income levels.

4) You have until Monday, March 1, 2018 to make tax deductible Registered Retirement Savings Plan (RRSP) contributions for the 2017 year. Consider the higher income earning individual contributing to their spouse's RRSP via a “spousal RRSP” for greater tax savings.

5) Individuals 18 years of age and older may deposit up to $5,500 into a Tax-Free Savings Account in 2017. Consider a catch-up contribution if you have not contributed the maximum amounts for prior years. Contribution room can be found online, on CRA’s My Account.

6) A Canada Education Savings Grant for Registered Education Savings Plan contributions equal to 20% of annual contributions for children (maximum $500 per child per year) is available. In addition, lower income families may be eligible to receive a Canada Learning Bond.

7) A Registered Disability Savings Plan (RDSP) may be established for a person who is under the age of 60 and eligible for the Disability Tax Credit. Non-deductible contributions to a lifetime maximum of $200,000 are permitted. Grants, Bonds and investment income earned in the plan are included in the beneficiary’s income when paid out of the RDSP.

8) Consideration may be given to selling non-registered securities, such as a stock, mutual fund, or exchange traded fund, that has declined in value since it was bought to trigger a capital loss which can be used to offset capital gains in the year. Anti-avoidance rules may apply when selling and buying the same security.

9) Consider restructuring your investment portfolio to convert non-deductible interest into deductible interest. It may also be possible to convert personal interest expense, such as interest on a house mortgage or personal vehicle, into deductible interest.

10) Canada Pension Plan (CPP) receipts may be split between spouses aged 65 or over (application to the CRA is required). Also, it may be advantageous to apply to receive CPP early (age 60-65) or late (age 65-70).

11) Teacher and early childhood educators – A federal non-refundable tax credit of 15% on purchases of up to $1,000 of eligible school supplies by a teacher or early childhood educator used in the performance of their employment duties may be available. Receipts for school supplies will be required.

12) Home accessibility tax credit – A federal non-refundable tax credit of 15% on up to $10,000 of eligible expenditures (renovations to a qualified dwelling to enhance mobility or reduce the risk of harm) may be available each calendar year, if a person 65 years or older, or a person eligible for the disability tax credit, resides in the home.

13) Did you incur costs to access medical intervention required in order to conceive a child which was not previously allowed as a medical expense? Due to a change in law, some of these expenses for the previous 10 years may now be eligible (amounts incurred in 2007 must be claimed by the end of 2017).

14) For individuals who have not yet claimed charitable donations, consider making a donation of up to $1,000 in order to get a “super charged” donation credit.

15) A number of employment insurance (EI) changes have been enacted effective December 3, 2017. These include a new caregiving benefit for up to 15 weeks for those who are temporarily away from work to support or care for a critically ill or injured family member, the option to extend the parental benefit for up to 18 months (from the current 12 months) and the ability to claim EI benefits up to 12 weeks before a mother’s due date (from the current 8 weeks).

16) If EI premiums were paid in error in respect of certain non-arm’s length employees, a refund may be available upon application to CRA.

17) Consider purchasing assets eligible for capital cost allowance (CCA) before the year-end. A half-year of depreciation deduction is allowed for most assets even if it was purchased just before the year-end.

18) Effective July 1, 2017, self-employed commercial ride-sharing drivers (such as Uber drivers), have been required to register for (regardless of their total annual revenues), collect, report and remit GST/HST.

19) Employers of eligible apprentices are entitled to an investment tax credit. Also, a $1,000 Incentive Grant per year is available for the first and second year as apprentices. A $2,000 Apprenticeship Completion Grant may also be available.

20) If income, forms, or elections have been missed in the past, a Voluntary Disclosure to the CRA may be

available to avoid penalties. Effective January 1, 2018, CRA has proposed to tighten the program so greater relief may be available if disclosure is made before the end of the year.

21) Are you a U.S. Resident, Citizen or Green Card Holder? Consider U.S. filing obligations with regards to income and financial asset holdings. Filing obligations may also apply if you were born in the U.S. Information exchange agreements have increased the flow of information between the CRA and the IRS. Collection agreements enable the CRA to collect amounts on behalf of the IRS.

2017 REMUNERATION

Higher levels of personal income are taxed at higher personal rates, while lower levels are taxed at lower rates. Therefore, individuals may want to, where possible, adjust income out of high income years and into low income years. This is particularly useful if the taxpayer is expecting a large fluctuation in income, due to, for example,

- taking maternity/paternity leave;
- receiving a large bonus/dividend; or
- selling a company or investment assets.

In addition to increases in marginal tax rates, individuals should consider other costs of additional income. For example, an individual with a child may lose financial support in the form of reduced Canada Child Benefit (CCB) payments. Likewise, excessive personal income may reduce receipts of OAS, GIS, GST/HST credit and other provincial/ territorial programs.

There are a variety of different ways to legally smooth income over a number of years to ensure an individual is maximizing access to the lowest marginal tax rates. For example,

- In owner/managed companies, owners may take more, or less, earnings out of the company.
- Realizing investments with a capital gain/loss.
- Deciding whether to claim RRSP contributions made in the current year, or carry-forward the contributions.
- Withdrawing funds from an RRSP to increase income. Care should be given, however, to the loss in RRSP room based on the withdrawal.
- Deciding on whether or not to claim CCA on assets used to earn rental income.

While the above is generally true, in certain cases some individuals may wish to pay out additional dividends in 2017. Effective in 2018, there are proposals to increase the tax cost of dividends paid out to shareholders of a corporation that do not "meaningfully contribute" to the business. As such, individuals who may be subject to this higher tax rate in future years may consider increasing dividend payments in 2017. Details on this proposed change are expected to be released by December 21, 2017.

Prior to paying increased dividends, consideration should be given to a number of factors (in addition to the items noted above related to increases in income), such as the impact on the business operations, cash flow, and other agreements (like bank covenants), and whether the dividend can be paid under corporate law.

Three different types of dividends can be paid from a corporation depending on the attributes and earnings of a corporation: eligible, non-eligible and tax-free capital dividends. Due to tax rate changes, the tax cost of non-eligible dividends will likely be increasing in 2018 and 2019. As such, some may consider declaring non-eligible dividends in 2017 to access current tax rates. Changes in provincial/ territorial rates may also impact the above decision.

Year-end planning considerations not specifically related to changes in income levels and marginal tax rates include:

1) Corporate earnings in excess of personal requirements could be left in the company to obtain a tax deferral (the personal tax is paid when cash is withdrawn from the company).

   The effect on the "Qualified Small Business Corporation" status should be reviewed before selling the shares where large amounts of capital have accumulated.

2) Consider paying taxable dividends to obtain a refund from the "Refundable Dividend Tax on Hand" account in the Corporation.

3) Individuals that wish to contribute to the CPP or a RRSP may require a salary to create "earned income". RRSP contribution room increases by 18% of the previous years' "earned income" up to a yearly prescribed maximum ($26,010 for 2017; $26,230 for 2018).

4) Dividend income, as opposed to a salary, will reduce an individual's cumulative net investment loss balance thereby possibly providing greater access to the capital gain exemption.

5) Recent tax changes may make it costlier to earn income in a corporation from sales to other private corporations in which the seller or a non-arm's length person has an

interest. As such, consideration may be given to paying a bonus to the shareholder and specifically tracking it to those higher taxed sales. Such a payment may reduce the total income taxed at higher rates.

6) Proposed changes to the tax regime will likely require more careful tracking of an individual shareholder's labour and capital contribution to the business, as well as risk assumed in respect of the business. Inputs should be tracked in a permanent file.

7) If you are providing services to a small number of clients through a corporation (which would otherwise be considered your employer), CRA could classify the corporation as a Personal Services Business. There are significant negative tax implications of such a classification. In such scenarios, consider discussing risk and exposure minimization strategies (such as paying a salary to the incorporated employee) with your professional advisor.

FIRM NEWS

As we come to the end of another year, we continue to be fortunate to be supported by clients, friends and staff as we enter into our 60th year of practice. We started on 6 December 1958 as a small two partner office and there have been many changes over the years although our focus has remained constant to provide the best quality of service to our clients. Some of the recent changes that we have had include Lindy Do and Hang Nguyen successfully passing their CPA final examinations and celebrating in style on 1 December 2017. Please take time to congratulate these two. In addition, we are very pleased to announce the promotion of Grace Madrazo to Senior Manager. Grace has been with the Firm since January 2009. Reena Bienko has moved to Manager after starting her articles with the firm 6 years ago.

Two years ago, we implemented a David Rolfe Award to the staff member who exhibited certain exemplary characteristics representative of our founding partner, David Rolfe. The award recipient, determined by staff members, for this year is Houston Mo. Houston has been with the firm since March 2013 after joining us from a smaller firm on Vancouver Island. Houston has progressed through the ranks to become a manager in the firm and possesses both strong technical and organizational skills that are certainly recognized around the firm. In addition, Houston volunteers his time in the community while also raising a very young family.

At this time of year we like to ensure that we give back to the community around us and we are very proud of making significant donations to various charities which this year included the Salvation Army, Children's Hospital and Canuck Place. We started this a number of years ago as a replacement to sending Christmas cards to our clients and it seems to have been very well received. In addition, we served dinner at the Salvation Army Harbour Lights Shelter on 4 December which is always well attended by our staff and it helps us recognize how fortunate we are.

We wish all of you the very best of health and happiness in the holiday season and throughout 2018. Merry Christmas.

The preceding information is for educational purposes only. As it is impossible to include all situations, circumstances and exceptions in a newsletter such as this, a further review should be done by a qualified professional.

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