



Saklas & Co.

Chartered Accountants

Accounting and Tax Made Simple!

#200 - 2121-152nd Street, Surrey BC V4A 4P1
www.saklasaccountina.com

b: 604.531.2292 f: 604.531.7400
email: kim@saklasaccountina.com

Tax Tips & Traps

2012 First Quarter

PERSONAL TAX

MEDICAL EXPENSES - COSMETIC PROCEDURES

In an August 31, 2011 Technical Interpretation, Canada Revenue Agency (CRA) noted that medical expenses paid after March 4, 2010 for purely cosmetic procedures are ineligible for the Medical Expense Tax Credit (METC).

This generally includes surgical and non-surgical procedures purely aimed at enhancing an individual's appearance, such as liposuction, hair replacement procedures, botulinum toxin injections, and teeth whitening. The CRA has posted on its website some examples of procedures that will generally be ineligible as medical expenses at www.cra.gc.ca/gncy/bdgt/2010/mdcl-eng.html.

MOVING EXPENSES

In a December 1, 2011 Tax Court of Canada case, the taxpayer worked for Boehringer Ingelheim Ltd. (B). In 2007 the taxpayer accepted a promotion and he determined that he would need to move closer to

his place of work in Burlington, Ontario. The Appellant moved from

Toronto to Oakville and there is no dispute that the new residence is 40 kilometers closer to his work than his former residence.

Taxpayer Wins!

The Court allowed the moving expenses.

CHILDREN'S ART TAX CREDIT (CATC)

Commencing in 2011 a non-refundable CATC will be available to parents of children who are under age 16 at the beginning of the year, or age 18 if the child is disabled. The CATC is based on 15% of eligible expenses paid for the cost of registration or membership in a prescribed program of artistic, cultural, recreational, or development activity. The maximum 15% CATC is based on \$500. This is similar to the Fitness Credit introduced in



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2010. Therefore, a parent is eligible for a maximum \$150, 15% tax credit (arts, \$500 and fitness, \$500).

Eligible CATC programs include:

a weekly program of a minimum of eight consecutive weeks duration in which a minimum of 90% of all activities are eligible activities or, offered by an organization where a 50% eligible activity test is met; and

a program of a minimum of five consecutive days in which more than 50% of the activities are eligible.

a program that is part of a school curriculum will not be eligible.

Eligible CATC activities will include development of creative skills or expertise in artistic or cultural activities; providing of substantial focus on wilderness and a natural environment; helping children develop and use particular intellectual skills; structured interaction among children where supervisors teach or help children develop interpersonal skills; and providing enrichment or tutoring in academic subjects.

For more information see the Children's Arts Tax Credit (CATC) Questions and Answers on the CRA website.

NATURAL PERSON SOVEREIGN PERSON

In an October 20, 2011 Tax Court of Canada case, the taxpayer was assessed gross negligence penalties, late filing penalties, interest and taxes for the years 1999 to 2001 for unreported income.

In this case, the Appellant argued that he is a "sovereign person" and cannot be taxed unless there is contract between him and the government. The Court found that this argument is without merit.

EMPLOYMENT INCOME

HIRING CREDIT FOR SMALL BUSINESS (HCSB)



The 2011 Federal Budget created a one-time hiring credit for small business. The HCSB gives small

businesses relief from the employer's share of Employment Insurance (EI) premiums paid in 2011 by

paying up to \$1,000, based on the increase in an employer's EI premiums paid in 2011 over those paid in 2010.

Eligibility

You are eligible for this credit if you meet all of the following conditions:

- you deducted EI premiums from the remuneration you paid to your employees, or paid the worker's share of EI premiums for barbers, hairdressers, fishers or drivers of taxis and other passenger-carrying vehicles, and you remitted these premiums (along with your share of EI premiums) to your payroll (RP) account;
- you reported the income and deductions on a T4 Slip and filed this information on your RP account for 2010 and 2011;
- the total of employer EI premiums you paid for 2010 was \$10,000 or less; and
- your total employer EI premiums increased in 2011.

If you are eligible, the CRA will automatically calculate the amount of your HCSB using the EI information from the T4 Slips you filed with your 2010 and 2011 T4 Information Returns. The amount to be credited to your payroll account will be no more than \$1,000.

INDEPENDENT CONTRACTOR VS. EMPLOYEE - TRUCK DRIVERS

In a September 22, 2011 Federal Court of Appeal case, the Tax Court had previously concluded that 43 of the truck drivers were independent contractors because they signed

Agreements that indicated this intent. However, the other 53 truck drivers were considered to be employees.

Taxpayer Loses

The Federal Court found that 39 of the 43 independent contractors were in fact employees. Therefore, of the 96 truck drivers, the Federal Court concluded that 92 of them were in fact employees. A significant loss for the Corporation.

EMPLOYMENT INSURANCE FOR NON-ARM'S LENGTH EMPLOYEES

In an October 20, 2011 Tax Court of Canada case, the major shareholder's daughter worked for the corporation and the corporation successfully argued that the salary was not subject to Employment Insurance because the Employment Insurance Act excludes non-arm's length situations where the terms and conditions of the employment are not substantially similar to contracts of employment with arm's length people.

In an October 3, 2011 Tax Court of Canada case, the individual was the spouse of the owner of the corporation and claimed that her employment was subject to EI and, therefore, made an application for Employment Insurance.

The Court again concluded that her employment was not insurable on the basis that her terms and conditions of employment were not the same as an arm's length person.

Questions? Call Kim:

604 531 2292 x 23 or

kim@saklasaccounting.com

BUSINESS/PROPERTY INCOME

SCIENTIFIC RESEARCH AND EXPERIMENTAL DEVELOPMENT (SR&ED)

In December, 2011, CRA issued Guide RC4467 which notes that:

- In 2010 the SR&ED Program provided approximately \$3.5 billion of tax assistance for over 21,000 claimants. Of these, 75% were small businesses.

- The SR&ED Program provides financial assistance through the form of refundable investment tax credits, and a reduction of taxes payable, or both.

- The SR&ED Program is available to any business operating and doing SR&ED in Canada. Any business that is involved in basic or applied

research, or in developing new or improved materials, devices, products, or processes may be eligible under the SR&ED Program.

- To determine if your work meets the SR&ED requirements, see the CRA Eligibility Self-Assessment Tool at www.cra.gc.ca/sred-assessment.

- Also, CRA has a First Time Claimant Service; a Pre-Claim Project Review Service (provides a preliminary opinion on the eligibility of projects for SR&ED tax incentives); and the Account Executive Service (provides a designated contact person who will be available to answer your questions on SR&ED).

For more information see www.cra.gc.ca/sred.



OWNER-MANAGER REMUNERATION

DIRECTOR LIABILITY

In an April 21, 2011 Federal Court of Appeal case, the Federal Court reviewed the “due diligence defence” and found the taxpayer/director personally liable with respect to unpaid GST/HST and source deductions and noted that:

- The director’s efforts should be to prevent failures.

- There is a need for stronger corporate internal controls and director’s meetings to ensure that the statutory obligations under the Income Tax Act and the Excise Tax Act are met.

- This is a warning to directors that they must meet statutory obligations with respect to source deductions and GST/HST remittances.

INDIVIDUAL PENSION PLANS

An Individual Pension Plan (IPP) could be used as a replacement retirement savings vehicle for, say, a Registered Retirement Savings Plan (RRSP). Some points to consider include:



- 1.An RRSP may work well for younger employees however, older employees that have corporations may prefer a defined benefit type of Pension Plan such as an IPP to provide current contributions that are in excess of the RRSP deduction limit.

- 2.An IPP may also allow the employer to make past service

contributions.

- 3.An employee must receive T4-type (T4 or T4PS) employment income from an employer as compensation for IPP pension contribution purposes. For example, self-employment, dividend and interest incomes are not pension eligible.

- 4.An ideal IPP candidate is between age 50 and 71, is a shareholder of an owner-managed corporation or a senior executive, is of high net worth and highly compensated, desires significantly higher contributions than an RRSP, has significant profits and cash flows to meet corporate-funded IPP obligations, has no need to access the IPP fund except in the form of a pension, and has no need to borrow against IPP assets.

ESTATE PLANNING

CPP CHANGES FOR 2012

In July 14 and October 7, 2011 Releases, CRA discussed the 2012 CPP changes and notes that if you are under age 65 and you work in Canada, you and your employer will have to make CPP

contributions.

Also, working

individuals who are at least 65 years of age but under 70 will

be subject to the CPP, even if you are receiving a CPP or QPP pension, unless you elect to stop contributing by filing Form CPT30.

Some other CPP changes include:



1. A person who delays receiving their CPP until after age 65 will receive a larger increase than was available prior to 2012. Under the old rules, the CPP would be increased by .5% per month after age 65.

From 2011 to 2013 this percentage will increase from .5% per month to .7% per month.

2. Individuals that elect to receive their CPP before age 65 will have a larger reduction. Previously it was .5% for each month before age 65.

The change is a phased-in reduction that will increase the early CPP reduction to .6% per month.

3. Under the old rules, an individual had to stop working for two months before they could apply to receive CPP between the ages of 60 and 65. Commencing in 2012, this test will no longer apply.

RRSPs/RRIFs - ANTI-AVOIDANCE RULES

The 2011 Federal Budget enhances the existing RRSP/RRIF Anti-Avoidance Rules. For example, the new rules would require the income received by an RRSP/RRIF (including capital gains) from a "prohibited investment" (for example, shares in which the annuitant or a related person owns 10% or more) to be 100% taxed.

Also, the Budget proposes a special tax on the fair market value of a "prohibited investment".

CAUTION

This is complicated legislation

and needs a special review before application to a fact situation. A special election could be made before July, 2012 for pre-March 22, 2011 prohibited investments.

RRSP SCAM

In a November 23, 2011 Tax Court of Canada case, the issue was whether CRA was correct in reassessing the Appellants to include in income the amounts that they paid for corporate shares acquired using funds in their self-directed RRSP accounts for 2001 and 2002.

The Appellants were defrauded by being persuaded to transfer their existing registered funds into new, self-directed registered accounts, and then purchase corporate shares that were not qualified investments and that had no value at the time of purchase.

Taxpayer Loses

The amounts were required to be included in income. However, the Court deleted the gross negligence penalties on the basis that the Appellants were innocent victims.

NON-PROFIT ORGANIZATIONS (NPO)

In an October 24, 2011 Technical Interpretation, CRA took the position that the Organization would not likely qualify for tax-free status as a NPO because it is operating for a profitable purpose. In this case, the Organization was receiving revenues in excess of expenses for advertising undertaken by it for other persons.

CRA noted that the large amount of retained earnings suggest that the Organization

has not operated exclusively for any purpose except profit.

TAX-FREE SAVINGS ACCOUNT (TFSA)

In the Fall of 2011, many taxpayers received a TFSA over-contribution package concerning their 2010 TFSA contributions. For example, if a person made a contribution in 2010, withdrew it, and then re-contributed it in the same year or, withdrew funds and contributed them into another TFSA, there could have been a 1% per month penalty.

If a taxpayer has received a TFSA over-contribution package, they may ask the CRA to review the file and consider waiving the penalty.

WEB TIPS

ONLINE TRANSLATOR - GOOGLE

If you are looking for a quick and easy translator to use, consider going to:
<http://translate.google.com>.

This translator converts typed-in words and phrases in addition to entire uploaded documents.

CANADIAN FINANCIAL CALCULATORS

Over 40 excellent Canada specific financial calculators can be found at:

<http://www.cchwebsites.com/content/calculators/indexcanadian.html>



Examples of the calculators available are listed on the next page.

LIST OF CALCULATORS:

- Adjustable Rate Mortgage Calculator
- Interest Only Mortgage Calculator
- Refinance Breakeven
- Rent vs. Buy
- Amortizing Loan Calculator
- Student Loan Consolidation and Debt Payoff
- Home Equity Loan vs. Auto loan
- Future Value Calculator
- Taxable vs. Tax Advantaged Investments
- Retirement Nestegg Calculator
- Tax Free Savings Account (TFSA) Comparison (Canadian)
- Taxable vs. Tax Advantaged Investments (Canadian)

INTERNATIONAL

U.S. CITIZENS IN CANADA - AN UPDATE

On December 7, 2011 the IRS released a fact sheet entitled "Information for U.S. Citizens or Dual Citizens Residing Outside the U.S.". This seven point release provides a commentary and examples on the filing obligations, processes, and related penalties for U.S. Citizens residing abroad that are delinquent in their filings (example, in Canada).

The release can be found at: <http://www.irs.gov/newsroom/article/0,,id=250788,00.html>

Editor's Comment

These filing requirements could apply to persons born in the U.S., or, in some cases, children of people born in the U.S. and, Green Card hold

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.

Although every reasonable effort has been made to ensure the accuracy of the information contained in this newsletter, no individual or organization involved in either the preparation or distribution of this letter accepts any contractual, tortious, or any other form of liability for its contents.

For any questions... give us a call.

**SCROLL DOWN FOR
YOUR 2011 TAX
PREP CHECKLIST**



INFORMATION REQUIRED TO COMPLETE 2011 PERSONAL INCOME TAX RETURN

1. All **information slips** such as T3, T4, T4A, T4A(OAS), T4A(P), T4E, T4PS, T4RIF, T4RSP, T5, T10, T2200, T2202, T101, T1163, T1164, TL11A, B, C and D; T5003, T5007, T5008, T5013, T5018 (Subcontractors), RC62 and corresponding provincial slips.

2. Details of **other income** for which no T slips have been received such as:

- other employment income (including stock option plans and Election Form T1212),
- business income,
- partnership income,
- rental income,
- alimony, separation allowances, child maintenance,
- pensions (certain pension income may now be **split** between spouses - see #35), U.S. and German Social Security Pensions have special rules.
- interest income earned but not yet received - example Canada Savings Bonds, Deferred Annuities, Term Deposits, Treasury Bills, Mutual Funds, Strip Bonds, Compound Interest Bonds
- professional fees,
- director fees,
- scholarships, fellowships, bursaries,
- replacement properties acquired.

3. Details of **other expenses** such as:

- employment related expenses - Provide Form T2200 - Declaration of Conditions of Employment,
 - tools acquired by apprentice vehicle mechanics,
 - business and employment purchases like vehicles, supplies, etc.,
 - interest on money borrowed to purchase investments,
 - investment counsel fees,
 - moving expenses - including costs of maintaining a vacant former residence,
 - child care expenses,
 - alimony, separation allowances, child maintenance,
 - safety deposit box fees,
 - accounting fees,
 - pension plan contributions,
 - film and video production eligible for tax credit,
 - mining tax credit expenses,
 - business research and development,
 - adoption related expenses,
 - clergy residence deduction information, including Form T1223,
 - amounts paid for **programs of physical activity** for children **under age 16** at any time during the year (**under 18** for children with **disabilities**).
- Up to **\$500** may be claimed for both a **fitness** and an **arts** tax credit. The types of programs that qualify are **very broad**.

4. Details of **other investments** such as:
 - real estate or oil and gas investments - including financial statements,
 - labour-sponsored funds.
5. Details and **receipts** for:
 - Registered Retirement Savings Plan (RRSP) contributions,
 - professional dues,
 - tuition fees for both **full-time** and **part-time** courses for you or a dependant - including mandatory ancillary fees, and Forms T2202, TL11A, B, C and D where applicable,
 - charitable donations (including publicly traded securities),
 - medical expenses for you or a dependent person (including certain medical related modifications to new or existing home and travel expenses). Note that purely cosmetic procedures do not qualify after March 4, 2010.
 - political contributions.
6. Details of **capital gains and losses** realized in 2011.
7. Details of previous **capital gain exemptions** claimed, **business investment losses** and **cumulative net investment loss accounts**.
8. Name, address, date of birth, S.I.N., and province of **residence** on December 31, 2011.
9. **Marital/common-law status** and spouse/partner's income, S.I.N. and birth date.
10. List of **dependants/children** - including their incomes and birth dates.
11. If you or one of your dependants was in attendance at a **college or university**, details concerning name of institution, number of months in attendance, tuition fees, income of dependant, Form T2202.
12. Are you **disabled or are any of your dependants** disabled? Provide Form T2201 - disability tax credit certificate. This also includes extensive therapy such as kidney dialysis and certain cystic fibrosis therapy. Also, the **transfer rules** include relatives such as parents, grandparents, child, grandchild, brothers, sisters, aunts, uncles, nephews or nieces.

Persons with **disabilities** also may receive tax relief for the cost of **disability supports** (eg. sign language services, talking textbooks, etc.) incurred for the purpose of **employment or education**.

Also, see #33 for **Registered Disability Savings Plan** information.
13. Details regarding residence in a prescribed area which qualifies for the **Isolated Area Deduction**.
14. Information regarding **child tax benefit** receipts.
15. Details regarding contributions and withdrawals from **Registered Education Savings Plans**.
16. Details regarding **RRSP - Home Buyers' Plan** withdrawals and repayments; **RRSP - Lifelong Learning Plan** repayment.
17. Receipts for 2011 income tax **installments** or, payments of tax.

18. Copy of 2010 personal tax **returns**, 2010 Assessment **Notices** and any correspondence from Canada Revenue Agency (CRA).
19. 2011 **Personalized Tax information** which CRA may have sent you.
20. Do you want your **tax refund or credit** deposited directly to your account in a financial institution? Yes/No.
To start direct deposit, or to change banking information, attach a void personalized cheque or your branch, institution and account number.
21. Details of **carry forwards** from previous years including losses, donations, forward averaging amounts, registered retirement savings plans.
22. Details of **foreign property** owned at **any time** in 2011 including cash, stocks, trusts, partnerships, real estate, tangible and intangible property, contingent interests, convertible property, etc..
23. Details of **income** from, or **distributions to**, **foreign entities** such as foreign affiliates and trusts.
24. Details of your **Pension Adjustment Reversal** if you ceased employment and were in a Registered Pension Plan or a Deferred Profit Sharing Plan. (T10 Slip)
25. If you provided **in-home care** for a **parent or grandparent** (including in-laws) 65 years of age or over, or an infirm **dependent relative**, a federal tax credit may be available.
Also, the caregiver may claim related **training costs** as a medical expense credit.
26. Interest paid on qualifying **student loans** is eligible for a tax credit.
- 27. Retroactive lump-sum payments**
Individuals receiving qualifying retroactive **lump-sum payments** over \$3,000 may be allowed to use a special mechanism to compute the tax.
28. Changes in **family circumstance** that could affect the **Goods and Services Tax Credit**, such as births, deaths, marriages, reaching the age of 19 years, and becoming or ceasing to be a resident in Canada.
29. **Children** of low or middle income parents may be entitled to a **Canada Learning Bond** of **\$500** in the initial year and **\$100** per year until age 15. Please ask us for details.
30. Do you have any **personal interest expense** - such as on a house mortgage or vehicle?
If so, it may be possible to take steps to convert this into deductible interest. Please ask us for details.
31. An **investment tax credit** is available in respect of each **eligible apprentice** employed in one of the 45 Red Seal Trades. Also, a **\$1,000 grant** is available for first and second year apprentices effective **January 1, 2007**.
32. Have you received the **Universal Child Care Benefit** of **\$100 per month** for each child under **6 years** of age?

33. Any person eligible for the **disability tax credit**, or their parent or legal representative, may establish a **Registered Disability Savings Plan** which receives **government grants**. Please ask us for details.

See #12 for information on **disabilities**.

34. The age limit for **maturing** Registered Pension Plans, Registered Retirement Savings Plans, and Deferred Profit Sharing Plans is **71 years** of age.

35. Spouses may **jointly elect** to have up to 50% of **certain pension income** reported by the **other spouse**. Please ask us for details.

36. Individuals 18 years of age and older may deposit **up to \$5000** per year into a **Tax-Free Savings Account** commencing in 2009. Please ask us for details.

37. Are you a first-time **home buyer** in 2011?

A tax credit based on \$5,000 (@15% = \$750) is available for qualifying homes acquired after January 27, 2009.

38. If required income or Forms have **not been reported** in the past to the CRA, a **Voluntary Disclosure** to the CRA may be available to avoid penalties. Contact us for details.

39. Commencing July 2010, the law is changed to allow two eligible individuals who **share custody** after a **relationship breakdown** to share the Canada Child Tax Benefit, Universal Child Care Benefit, and the GST/HST Credit in respect of the child.

40. Are you a **U.S. citizen, Green Card Holder**, or were you, or your parents **born in the United States**? You likely have U.S. filing obligations.

41. Do you have, or share, **custody** of a **child** after a relationship breakdown? You may be entitled to the CCTB, UCCB and GST/HST Credit.

CONFUSED?

Call Kim:

604 531 2292 x 23

or

EMAIL

kim@saklasaccounting.com