

# Minding YOUR BUSINESS



S P R I N G 2 0 0 9

## Celebrating 30 Years!

Yes, it has been that long since Dan established his own public practice firm in British Columbia, 28 of those years partnering with Barrie. Looking back, we remember bookkeeping, spreadsheets and tax returns all done by hand; multiple copies of financial statements produced using the typewriter and carbon paper. We are proud and grateful that many of our clients have grown alongside us over this span of time, some in excess of 20-25 years.

Dan recalls The Income Tax Act compiled in a one inch thick book 30 years ago. Today the Act is 4 inches thick. This requires today's professionals to constantly be reading and updating themselves regarding changes in the Income Tax Law.

Accounting Standards likewise have increased exponentially. Today's professionals are required a minimum average of 40 hours of professional development courses annually to maintain their professional designation. Dan notes that Chartered Accountants also have peer reviews which entail having their files reviewed and critiqued. Standards are set high and this is all for the benefit of the client.

Dan and Barrie have many fond memories; some scary ones too! Like the year Barrie got the flu in the midst of tax season. That year saw Dan and Barrie assembling tax returns working round the clock to meet the deadline.

Sandy joined the team 13 years ago and continues to make valuable contributions including managing quality control, staff and keeping the ship on course. As a team of 3, each recognizes

continued on page 4

From The Desk Of

## Watch Your Pennies—See Your Tax Savings

Taxpayers often lament they pay far too much in taxes. In truth, many would pay less if they took advantage of tax-saving opportunities. A little care and attention can cut your annual tax bill. The key to maxing out your tax deductions can be as easy as counting to 10.

### 1. Contribute to an RRSP

All contributions are fully deductible and are not taxed until withdrawal. The contribution limit for 2008 was \$20,000 minus adjustments related to membership in a registered pension plan or deferred profit sharing plan. For the 2009 calendar year the contribution limit will increase to \$21,000.

### 2. Keep receipts

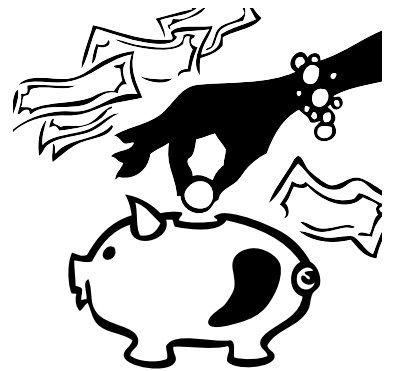
Probably the number one reason individuals pay more taxes than they should is because they fail to keep receipts for expenditures made to earn income. Sales or commissioned staff and the self-employed often provide tax advisors with insufficient source documents for purchases, or submit spreadsheet summaries suggesting that purchases are lower than normal. Failure to submit \$2,000 worth of receipts when the taxpayer's tax rate is a low 23%, for example, adds \$460 to the tax bill.

### 3. Cash in RRSPs

RRSP withdrawals are taxed when the funds are removed from the RRSP. If, as a single taxpayer, your taxable income from self-employment or employment is \$50,000, the tax before non-refundable credits approximates \$8,400 of federal tax plus provincial tax. Withdraw \$10,000 from your RRSP in the same taxation year and the tax before non-refundable credits rises to federal tax of \$10,600 plus provincial tax. The \$10,000 withdrawal has actually cost \$2,200 of federal tax plus provincial tax.

### 4. Keep track of kilometres driven

Each year taxpayers are asked by the CRA to provide proof of the kilometres driven to earn income. In many instances the taxpayer is unable to provide documentation to establish the number of kilometres driven on business. If you are self-employed, keep a log of the



continued on page 2

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: "Opportunity favors a prepared mind" – Anonymous :  
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## OUR COMMITMENT *To You.*

*We recognize that while "accounting" is an integral part of your business, it is only a part of your business. Our approach to accounting doesn't miss the forest for the trees or the people for the numbers. Our dedicated professionals will provide you with the creative, proactive and timely solutions to assist you in responding to the daily challenges confronting your business.*



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## Watch Your Pennies

continued from page 1

kilometers travelled and the business purposes of your trips in order to create a supporting document for the expense. If you receive a set monthly car allowance, maintain a similar log to establish that the funds received are reasonable for the work done.

### 5. Interest deductibility

Owner/managers borrow funds for a plethora of reasons. Whether the loan is for investments, capital assets, or everyday purchases made with charge cards, interest is usually deductible if the purpose of the loan is to earn income. To avoid controversy, ensure the loan is easily traceable to a specific purchase. For instance, if the taxpayer borrows \$20,000 personally and purchases \$20,000 worth of shares of XYZ Co. Ltd., the taxpayer should be able to produce documentation attesting to that fact. The deductibility of interest becomes problematic, however, in the case of a charge card used to purchase goods or obtain cash advances, if the same card is used for both personal and business purposes. Since it is difficult to differentiate personal and business expenses on the monthly statements, it is best to make business purchases with a card dedicated specifically for business expenses.

Taxpayers who borrow on house equity or finance their business with funds drawn from a personal mortgage should ensure the audit trail indicates the principal amount placed into the business. This record combined with the terms of the mortgage and the interest rate will allow the computation of interest expense deductible to the business.

### 6. Pay your children and your spouse

A spouse or other family members often work for self-employed individuals. Payment to family members working in the business is a legitimate form of expense, if the individual actually works and is paid a reasonable amount for the task performed. To avoid future problems with the CRA, it is prudent to have an employee/employer contract establishing the duties and responsibilities and the pay to be expected.

Employers should pay with a cheque to establish payment was made or, if

cash is paid, the employee should sign a receipt for funds received.

Income splitting within a business certainly saves personal income tax. Given that a couple needs \$60,000 a year to live, an individual with a dependent spouse would pay combined federal and provincial (B.C.) taxes approximating \$10,348. If each spouse earned \$30,000 the combined income tax would approximate \$7,920. This difference (based upon 2008 tax rates) establishes a tax savings of approximately \$2,428. Provincial and territorial tax rates as applied to differing personal situations will dictate the actual savings. Nevertheless, it may be worthwhile for you to discuss the possibility of income splitting with Majewski Shaler & Co.

### 7. Purchase a capital asset before the end of the year

If an asset is purchased before the end of the year, half of the capital cost allowance normally permitted in the year of purchase may be deducted. That is, a \$5,000 asset with a tax write off rate of 30% would normally reduce taxable income by \$1,500. In the year of purchase this would amount to only 15% or \$750. Thus, if the asset is purchased near the end of the year, the business receives a write-off of \$750 for the end of the first year and an additional \$1275 in the year following.

The taxpayer not only gains a \$1,275 accelerated tax deduction advantage by purchasing in December, but also is able to claim the GST-ITC of \$250 at the time of the December purchase (calculation assumes no PST on \$5,000).

### 8. Investment related expenses

Taxpayers who invest through brokers may be charged fees for safekeeping, investment counsel, accounting and a myriad other services. Ensure all monthly and other statements are retained for presentation to Majewski Shaler & Co. at the end of the year. Statements provided by investment brokers can be confusing. If there is uncertainty as to whether service charges have been added call your broker for an explanation before the end of the year.

continued on page 4

# Tax Tips & Traps

## PERSONAL TAX

### Disability Tax Credit Transfer

If a disabled person does not need to claim the Disability Tax Credit (DTC) to reduce his/her tax payable to nil, the unutilized portion may be transferred to a spouse or common-law partner or to another supporting person. Another supporting person may claim the DTC for a parent, grandparent, child, grandchild, brother, sister, aunt, uncle, nephew or niece of the individual.

We understand that "support" could include assistance with the basic necessities of living such as food, clothing or shelter. Also, the credit may be transferred to a supporting relative even if the dependent person is not living with the supporting relative.

### Employee vs. Independent Contractor

In three Federal Court of Appeal cases, the Federal Court confirmed the Tax Court decision that in all three cases the workers were employees of the payor, not independent contractors, and the payor was required to remit Employment Insurance and Canada Pension Plan. Also, the workers were not allowed to deduct business expenses.

The first case consisted of 130 health care workers who were placed by the Appellant in a number of health care facilities for short-term work. The second case was a worker for a family corporation. The third case was simply a worker being treated as an employee of the payor.

## BUSINESS/PROPERTY INCOME

### Travel Expenses

In a September 30, 2008 Tax Court of Canada case, the taxpayers owned a rental property in Florida in which they made several trips to meet with the condo association to review the interview process for renting the property, to repair and paint the property, to inspect the property



and to purchase minor items for the property. The taxpayer deducted the motor vehicle expenses to travel to Florida. CRA disallowed these expenses on the basis that the property was managed by an independent company and the travel and motor vehicle expenses were of a personal nature.

### Taxpayer Wins!

The Court accepted the taxpayers' evidence that the trips did not have a personal component. Therefore, the travel expenses were allowed. The travel expenses were supported by a log which recorded 14,596 kilometres for the trips in 2001 and 10,927 kilometres for the trips in 2002.

## RRSP DIVISION OF MATRIMONIAL PROPERTY

In an October 16, 2008 External Technical Interpretation, CRA notes that the Income Tax Act permits a direct transfer of an amount from an individual's RRSP to an RRSP of which his/her former spouse is the annuitant, where the payor and recipient are living separate and apart. The payment or transfer must be made under a Decree, Order or Judgment of a competent tribunal or under a Written Separation Agreement, and the transfer or payment relates to the division of property in settlement of rights arising on the breakdown of a marriage.

## ESTATE PLANNING

### Structured Settlement

In a 2008 Advance Income Tax Ruling, an individual (Plaintiff) was injured and commenced an action for damages against various Defendants. In an out of Court settlement, the casualty insurer of the Defendants will assign their rights to an assignment company who will purchase a single premium annuity contract with a life insurance company to provide the proposed periodic payments to be received under a structured settlement arrangement by the Plaintiff.

The assignment company will direct the life insurance company to pay the periodic payments under an annuity contract to the Plaintiff or the Plaintiff's Estate. Such payments will not be taxable in the hands of the Plaintiff.

### DID YOU KNOW... CREDITOR PROTECTION

Amendments to the Bankruptcy and Insolvency Act that extend creditor protection to all RRSPs, RRIFs and DPSPs came into force on July 7, 2008. The provision is subject to a clawback of contributions made in the twelve months prior to bankruptcy subject to overriding protection under certain provincial legislation.

Also, new regulations with respect to unpaid wages came into force at that time.

### Editor's Comment

This is a specialized area which may need assistance from a Bankruptcy Trustee.

## OWNER-MANAGER REMUNERATION

### Shareholder vs. Employee Status

In a December 16, 2008 External Technical Interpretation, CRA notes that where a shareholder receives a loan from his/her corporation, the amount of the loan is included in

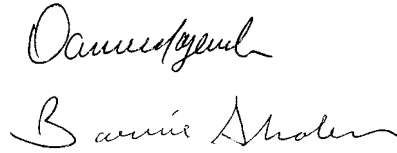
## Celebrating 30 Years

continued from page 1

and appreciates the strengths and contributions of the others. It's a complimentary combination of talent and personalities.

We want to acknowledge our clients, staff and business associates for continued confidence, loyalty and support. It is our hope and desire to continue serving you and living up to the high standards we have set for

ourselves, satisfying and exceeding your expectations. Our history speaks for itself. Our future will be built on a strong foundation.



## Tax Tips & Traps

continued from page 3

computing the shareholder's income unless one of the exceptions in the Income Tax Act applies.

With respect to a "home purchase loan", to qualify the home purchase loan must be made because of the person's employment, and not shareholding status.

Generally a benefit will be considered to be conferred qua employee if it is reasonable to conclude that a benefit is part of a reasonable employee remuneration package. Even where the shareholder is the only employee, CRA will generally consider a loan to be received by virtue of employment where a shareholder-employee can show that employees with similar duties and responsibilities to another employer of similar size, but who are not shareholders of that other employer-corporation, receive loans of similar amounts under similar conditions.

If the facts support that a "home purchase loan" is conferred qua employee, the loan will not be required to be included in the shareholder's income. However, the individual will be deemed to have received an interest benefit at the prescribed rate if interest is not charged.

If the loan is qua shareholder, the loan must be included in the shareholder's income for the year.

### TAX-LOSS SELLING

Taxpayers that sell non-registered securities with accrued capital losses before the end of the year may deduct the capital losses from capital

gains realized earlier in the current year, or in the three preceding tax years, or may be carried forward.

Some things to consider before selling to trigger a loss include:

1. Does it make sense from an investment perspective to sell the property.
2. The superficial loss rules should be reviewed to ensure that the capital loss is not deemed nil because of an acquisition by an "affiliated person" of a same or identical property within thirty days before or after the disposition, and the security is owned at the end of that period. The denied loss will be added to the adjusted cost base of the identical security acquired.

An "affiliated person" includes the person, a spouse or common-law partner, a corporation which either of you control, or an affiliated partnership or Trust such as an RRSP or a Tax-Free Savings Account.

Therefore, the superficial loss rules do not apply on a disposition to a child or a parent or grandparent.

3. Also, if Mrs. A has unrealized capital losses and Mr. A has the capital gains, it may make sense to transfer the loss security to Mr. A for fair market value and have the loss deemed nil to Mrs. A but have an increased cost base to Mr. A (must elect not to have a rollover). Mr. A must wait thirty-one days before selling to ensure that the superficial loss rules apply to Mrs. A and bump-up his cost base.

## Watch Your Pennies cont. from page 2

### 9. Claim loss Carryovers

Many taxpayers have self-employed income in addition to a day job earning T4 income. Unfortunately, losses in the early stages of a new sole proprietorship are often a reality. Losses from self-employed businesses and property can, however, first be deducted from other income sources for the year. Many individuals are unaware that, to the extent they exceed other income in the year, their part-time business losses can be carried back three years and carried forward 20. It is not mandatory to apply non-capital losses carried forward simply because the year following the loss has taxable income. Thus, if you knew your T4 income was going to be higher two years from now, you could decide to defer application of the loss rather than apply it in year one.

A word of caution regarding non-capital losses. Changes to the carry forward dates mean that non-capital losses incurred in taxation years that ended after March 22, 2004, and before 2006 can be carried forward for only 10 years; losses incurred during taxation years that ended before March 23, 2004 can be carried forward only seven years. So, for example, losses incurred in 2003 expire in 2010 and should therefore be used as soon as possible.

### 10. File T1-adjustments

Many taxpayers discover additional deductions or expenses after filing their income tax but decide not to request an adjustment from the CRA. You may feel it is not worthwhile to request an adjustment for a \$10 expense; keep in mind, however, that if the CRA unearths \$100 that you have not reported they will reassess and add interest on the unpaid balance. Thus, if you discover expenses, union dues or other tax deductible items that were not submitted, do not hesitate to inform the CRA of the changes.

By providing full and correct information to Majewski Shaler & Co. you ensure the deductions you are entitled to are maximized and your taxes payable are minimized.