

# The Tax Break

## SO...INCOME SPRINKLING

### WHERE ARE WE NOW?



On December 13, 2017, the Department of Finance released a number of **updates** relating to the **income sprinkling proposals** (originally announced on July 18, 2017).

Individuals that receive certain types of income derived from a “related business” will be subject to **Tax on Split Income** (TOSI) unless an exclusion applies. TOSI is subject to the **highest personal tax rate** with **no benefit of personal credits**.

Commencing on **January 1, 2018** TOSI will potentially **apply** in respect of **amounts** that are **received by adults**, not just those under 18 years. The application of TOSI to individuals under age 18 (commonly known as the “kiddie tax”) would not generally change.

### Income Streams at Risk

Private corporation dividends, partnership allocations, trust allocations, capital gains, and income from debt may all be subject to TOSI.

This new draft legislation is a **substantial change** from the current rules. The provisions are **lengthy, complex and nuanced**, and it is likely that additional concerns and challenges will be identified. It is **uncertain** whether there will be **further changes**, given the concerns which have already been identified, as well as the recommendations of the Senate Finance Committee released on the same date as these proposals.

**Review whether your earnings may be impacted. Consider whether additional documentation should be kept to prove meaningful contributions and time worked. Also, restructuring of ownership or working relationships may be beneficial in some cases.**



## INPUT TAX CREDITS

### CHECKING UP ON SUPPLIERS

Do I have to check up on a supplier when paying them GST/HST? Yes!

In a January 29, 2016 **Tax Court of Canada** case it was noted that CRA had **denied** over \$500,000 of input tax credits (**ITCs**), and assessed **penalties and interest**, in respect of GST and QST paid to **twelve suppliers**. Unknown to the taxpayer, the **suppliers did not remit the tax**.

The taxpayer, a scrap metal dealer, **obtained evidence** of prospective **suppliers' GST and QST registration** prior to accepting them as suppliers.

### Taxpayer wins – mostly

A taxpayer must use **reasonable procedures** to verify that suppliers are **valid registrants**, their **registration numbers actually exist**, and that they are in the **name of that person or business**.

*continued on next page...*

## IN THIS ISSUE...

- So...Income Sprinkling
- Input Tax Credits
- Loans to a Relative's Business
- Tax Ticklers

Check out our weekly blog at <http://www.accountantsplus.ca/blog>

You can also find us on Twitter: @PELCPA

## TAX SEASON'S GREETINGS!

It's personal tax season again already!? Thank you to those of you who have already brought in your tax information! We look forward to seeing the rest of you soon. Remember our Early Bird Draw deadline – March 31<sup>st</sup>!

If you're still gathering your information together, our T1 checklist can be found on our website at <http://www.accountantsplus.ca/resources/>

*If you are receiving this newsletter by mail and would like to receive it by email instead (or vice versa), or if you no longer wish to receive our newsletter, please contact Julie at [julie@accountantsplus.ca](mailto:julie@accountantsplus.ca) or 604.299.9274.*

Continued... Taxpayer wins – mostly

A taxpayer must use **reasonable procedures** to verify that suppliers are **valid registrants**, their **registration numbers** actually **exist**, and that they are in the **name of that person or business**.

The Court held that the **taxpayer's procedures** (reviewing the suppliers' registrations, stamped by Revenue Quebec) were **generally sufficient**. It was **not relevant** that some suppliers did not have **scrapyards and/or vehicles** to carry on scrap businesses, nor that **payment** was often made in **cash**, making it difficult to verify the suppliers' revenues. The taxpayer could not be expected to query government officials to ensure that GST registrations were properly issued.

However, in respect of **one supplier**, the facts showed that the taxpayer had been **sloppy** to the point of **gross negligence** in accepting evidence of registration where it was **clear** that the **registered supplier** was **not acting on their own account**. Those **ITCs** were **denied**, and the related **gross negligence penalty** upheld.

As well, one purchase was made **on the date the supplier's registration was cancelled**, so the supplier was **not a registrant** on that date, and the **ITC** was **properly denied**. However, the related **gross negligence penalty** was **reversed**, based on the due diligence undertaken in respect of the supplier previously.

**Implement a system for checking GST/HST numbers, especially for major purchases, in CRA's GST/HST registry. You may want to select a purchase dollar level for which extra revision of supplier GST/HST numbers is performed. The registry is located at <https://www.businessregistration-inscriptionentreprise.gc.ca/ebci/br om/registry/>**



## LOANS TO A RELATIVE'S BUSINESS

### WHAT HAPPENS WHEN IT GOES BAD?

You've loaned money to a family member's corporation. Perhaps it was an investment, maybe it was a favor, or both. Or, perhaps, it was made for a completely separate reason. Regardless, sometimes the loan may go bad and you are not able to collect on the debt. What happens from a tax perspective when this occurs?

If the loan was made to earn income and other conditions are met, you may be able to write-off half against your regular income as an allowable business investment loss (ABIL). A recent tax court case shed some light on defining whether the loan was made to earn income.

In a November 3, 2016 **Tax Court of Canada** case, at issue was whether an ABIL could be claimed in respect of the **loan from a taxpayer to his daughter's start-up company**. Within approximately two years, operations had ceased and the daughter had claimed personal bankruptcy.

The loan agreement stipulated that **interest at 6%** was to be charged from the onset, but no payments would be made for approximately the first two years, which, as it would turn out, was after the business eventually ceased. The Minister argued that **no interest**

**was charged**, and therefore, there was no intent to earn income. This was partially **based on accounting records** of the daughter's company which were inconsistent in their reflection of accrued interest.

### Taxpayer wins

Despite the **conflicting records**, the Court opined that the interest rate included in the agreement was **legitimate** and that there was an **intent to earn income**. The **ABIL** was allowed.

The Court **did not opine** on whether the **intention to earn income** requirement would have been met if the agreement only stipulated that interest would begin to be charged or accrued at the time that repayment commenced (i.e. interest-free loan for first two years, but interest generating thereafter).

**Loans to businesses of relatives are more closely scrutinized by CRA due to the inherent possibility that it was made for non-income earning reasons. If considering a loan to a relative's business, ensure that the income earning nature is clearly documented.**



## TAX TICKLERS

- Only the last year of CPP survivor benefits can generally be accessed for late applications. Don't delay submission.
- Of the approximately 28 million personal tax returns filed for the 2016 year, 58% got refunds. 68% received them by direct deposit. The average refund was \$1,735.

*We recommend that you obtain professional advice before acting on information contained in this newsletter.*

**PagnaniniEdwardsLam**

CHARTERED PROFESSIONAL ACCOUNTANTS

306 – 3701 Hastings Street • Burnaby, BC V5C 2H6 • t. 604.299.9274 • f. 604.299.9247 • info@accountantsplus.ca • www.accountantsplus.ca