TAX NEWSLETTER

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Special points of interest:

- *Personal tax instalments:*
  - *► December 15, 2015*
  - *► March 15, 2016*
  - *► June 15, 2016*
  - *► September 15, 2016*
- *New CRA service allows businesses to receive correspondence online.*
- *Starting October 19, 2015, CRA to provide GST/HST registrants new access code for electronic services.*
- *Use CRA Payroll Deduction Online Calculator to calculate payroll deductions.*

Disposition by Non-Resident—Purchaser Beware

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To facilitate the Canadian Government collecting its income tax on dispositions of "taxable Canadian property" (TCP) by non-residents, Canadian tax law makes purchasers of TCP liable for remitting Canadian withholding tax. As a result, any purchaser acquiring TCP from a non-resident vendor should always consider whether a portion of the purchase price should be remitted to CRA. Failure to do so could result in significant costs.

TCP generally includes, but is not limited to:

- Real property in Canada including Canadian resource property
- Shares of private corporations *
- Certain public company shares*
- Certain interests in Trusts and Estates*

* If, at any time in the past 60 months, more than 50% of their value is derived from Canadian real property, Canadian resource property, and certain other properties.

Generally, the purchaser must remit 25% of the purchase price for TCP directly to CRA, unless the property is Treaty protected, or the non-resident vendor has previously submitted Form T2062 and obtained a Certificate of Compliance (CC) reducing the required withholding [Subsection 116(4)]. The vendor is required to file a T2062 no later than 10 days after the transaction. Late filing of Form T2062 can result in a maximum penalty of $2,500 [Subsection 162(7)].

Unless a CC waiving any withholding is received, the purchaser must remit the withholding to CRA no later than 30 days after the end of the month in which the transaction occurred. Failure to comply could result in a 10% penalty (Subsection 227(8)), plus interest charges.

Given the potential costs, purchasers should never assume the vendor has been issued a CC without verification, as the provisions in Section 116 of the ITA effectively require the non-compliant purchaser to pay the vendor's taxes if a CC has not been issued.

In a December 19, 2014, Tax Court of Canada case (0lympia Trust Company vs. H.M.Q. TCC 2013-189(IT)G, the Trustee of various self-administered RRSPs, and not the RRSP holders themselves, was held liable for unremitted withholding taxes on a purchase from non-residents. In a simpler example, the issue of beneficial ownership could arise where a parent purchases a home for their adult child. If the vendor is a non-resident and proper measures are not taken to ensure that withholding taxes are remitted, then the generous parent could be liable for the applicable withholding tax on their child's home - 25% of the purchase price, plus penalties and interest.

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Employee Versus Self-employed: What to Expect Tax-wise

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Think you could make more money as an owner than working for someone else? Before you take the plunge, there are some important changes to consider. From a financial perspective, some of the biggest changes you will face when starting out as a self-employed individual include how the Canada Revenue Agency (CRA) treats you.

Claiming Expenses

Employees typically do not claim expenses, since employers generally pay for everything. Some exceptions include the use of your vehicle or an office space in your home. In these cases, your employer signs a T2200—declaration of conditions of employment—that allows you to claim expenses that are required as part of your job.

When you are self-employed, you can claim all business related expenses. While some expenses are clearly business related, others fall into a grey area. Perhaps you use a room in your house to meet with clients occasionally. Maybe you use your vehicle for business and personal use. What if you take a business trip but extend your stay to visit family? The CRA has guidelines to help business owners determine what they can deduct as an expense. You can find for more information at http://www.cra-arc.gc.ca/tx/bsnss/tpcs/slprtnr/bsnssxpnss/menu-eng.html

Record Keeping

As an employee, you are typically not expected to track income or expenses; that's your employer's job.

As your own boss, you are required to do this yourself or to hire someone to do it for you. You will need to track income and expenses, both for yourself and any employees, so that everything is accurate at tax time. If you have staff working for you, you must track hours worked, remit payroll deductions, and prepare annual T4 slips.

The better your record-keeping, the smoother your business will run. By keeping a handle on all business records, you will be able to determine your profitability in a timely manner, instead of scrambling to find the right information when something goes wrong. And, if the CRA decides to audit your business, you will thank yourself immensely for being well organized.

Payroll

Once your business starts to grow, it may be time to hire an employee or two. Employers incur additional payroll costs beyond wages and vacation pay, such as Workers' Compensation Plan premiums, and the employer's share of Canada Pension Plan (CPP) and Employment Insurance (EI) premiums. These premiums are based on how much your employees earn during the year.

Other possible payroll costs include health and dental benefits and pensions plans. These costs should be considered in preparing your budget.

Harmonized Sales Tax (HST)

You can voluntarily register for HST to recover the HST on purchases while starting your business. You must register for HST if your gross sales exceed $30,000 in any month or in any 4 calendar quarters. CRA has examples of how this works at http://www.cra-arc.gc.ca/tx/bsnss/sm/gsthst-tpstvh/rgstr-eng.html

Once you register, or are required to register, you must charge HST on all taxable sales. Depending on what you do, some sales may be exempt or "zero-rated" (taxable at 0%). HST paid on expenses related to taxable or "zero-rated" sales will be deductible from the HST that you must remit to CRA.

Be Ready for the Income Tax Bill

As an employee, income tax and CPP are deducted before you get your pay cheque. At tax time, you should generally owe very little. You may even receive a refund!

When you are self-employed, you pay taxes out of your business profits. As a P.E.I. resident, if your profit is $53,600, then your income tax would be $10,823. You must also pay both parts of the CPP premium. That is an additional $4,960. You would owe $15,783 to CRA that is not automatically withheld and remitted from your self-employed earnings.

It is important to plan for your new obligations as a self-employed individual. Failure to do so may result in a painful tax bill. If you would like to discuss these topics further please contact one of the members of the MRSB tax team.

Thinking of Moving to the US?

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As the world becomes more interconnected, careers often require individuals to move outside of Canada. Given our proximity to the United States, a permanent move to the US may be contemplated. Unfortunately, inadequate planning for departure results in tax inefficiencies, including taxation as a resident in multiple jurisdictions, taxation in a high-tax jurisdiction longer than necessary, and the missing of crucial tax filings due to inadequately severed residential ties.

The following provides a general commentary on determining residence and when the changeover of tax residence occurs for individuals moving to the US.

Determining Residency

Residency for Canadian Income Tax Purposes

For Canadian tax purposes, the primary residential ties that will be examined by the Canada Revenue Agency ("CRA") are whether the individual has a home, spouse or dependants in Canada.

If these ties are inconclusive, a non-exhaustive list of other factors that may be examined by the CRA includes the presence of Canadian property, memberships, passports, licenses, bank accounts, and credit cards.

If there is any uncertainty as to whether the ties constitute residency, Form NR73—Determination of Residency Status—can be submitted to allow the CRA to provide a written determination of residency status.

Residency for US Income Tax Purposes

For US income tax purposes, an individual is resident if they meet one of the following tests:

1) **The individual has been issued a green card**

2) **The Substantial Presence Test**

   The individual is present for more than 31 days in the current year and 183 days in the past 3 years, determined by the following formula:

   Days in the current year + 1/3 of the days last year + 1/6 of the days two years ago.

   This became a concern, especially for people who, on average, spend approximately 120 days or more per year in the US.

3) **The First-Year Choice**

   If an individual did not satisfy the substantial presence test until a subsequent year, but wishes to be considered resident in the current year, they may choose to be considered resident effective the 1st day of the 31-day period in the current year if the individual was present in the US for at least 31 consecutive days in the year and 75% of the days from the 1st day of the 31-day period to the end of the year.

Applying the Treaty in Determining Residency

In cases where the domestic law results in residency in both countries, the "tie breaker rules" under Article IV of the Canada–US Tax Convention will determine in which country the individual is resident. Generally, the Treaty looks to where the individual has the closest ties.

Determining Date of Residency Change

Departure from Canada

The CRA has taken the position that the date of departure for Canadian tax purposes will be the later of three dates:

1) The date the individual physically leaves Canada;
2) The date the individual's spouse or dependants leave Canada; or
3) The date the individual becomes a resident of the US.

Commencement of Residency in the US

For US purposes, residency commences on either the date the green card was received, or, if qualifying under the Substantial Presence Test, the first day the individual was present in the US in the calendar year.

Changes to the Taxation of Testamentary Trusts

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Changes to the taxation of testamentary trusts become effective January 1, 2016. One of the significant changes relates to the taxation of life interest trusts.

Where this life interest trust is a spousal trust, a deemed disposition would occur upon the death of the spouse. Under the original changes to the trust rules, the gain resulting from the deemed disposition of trust assets would be taxed on the spouse's final tax return rather than on the trust tax return.

This would result in the beneficiaries of the spouse's estate paying the tax on assets that would flow to beneficiaries of the trust. Where those beneficiaries are different, it would create issues. Also, if the beneficiaries of the trust were charities, the donation credits would not be able to be applied against the gain resulting from the deemed disposition of the assets, thereby suspending the donation credits.

After representations from the Canadian Bar Association, the Chartered Professional Accountants of Canada, the Conference for Advanced Life Underwriting, and STEP Canada, the Department of Finance issued a letter on November 16, 2015, outlining possible changes to the trust rules.

These changes will allow donations made by the trust after the beneficiary's death, but during the calendar year in which the death occurs, to be claimed by the trust. Also, the letter proposed to allow the taxation of the gain on the assets of the spousal trust at the time of the spouse's death to be taxed on the trust tax return. This will match the trust assets with the tax associated with the deemed disposition of these assets.

For more details on these changes, contact your local DFK representative.