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# CHAPTER 4



## Taxable Income And Tax Payable For Individuals

### Introduction

4-1. As discussed in Chapter 1, Taxable Income is Net Income For Tax Purposes, less a group of deductions that are specified in Division C of Part I of the *Income Tax Act*. Also noted in the Chapter 1 material was the fact that Net Income For Tax Purposes is made up of several different income components. These components are employment income, business and property income, taxable capital gains, other sources, and other deductions.

4-2. Some tax texts defer any coverage of Taxable Income and Tax Payable until all of the income components that make up Net Income For Tax Purposes have been given detailed consideration. Despite the fact that the only component of Taxable Income that we have covered to this point is employment income, we have decided to introduce material on Taxable Income and Tax Payable for individuals at this point in the text.

**Major Reason** The major reason for this approach is that it allows us to introduce the many tax credits that go into the calculation of Tax Payable at an earlier stage in the text. We believe that this will enhance the presentation of the material in subsequent Chapters on business income, property income, and taxable capital gains. For example, in our discussion of property income, we can deal with after tax rates of return, as well as provide a meaningful discussion of the economics of the dividend gross up/tax credit procedures.

**Other Reasons** Other reasons for this organization of the material are more pedagogical in nature.

- Leaving the coverage of tax credits until after the completion of the material on all of the components of Taxable Income places this complex subject in the last weeks of most one semester tax courses. This can create significant difficulties for students.
- By introducing Taxable Income and Tax Payable at this earlier stage in the text, instructors who wish to do so can make more extensive use of the tax software programs provided with the text.

4-3. Since a significant portion of the material on Taxable Income and Tax Payable can be best understood after covering the other types of income that make up Net Income For Tax

Purposes, we require a second Chapter dealing with the subject of Taxable Income and Tax Payable. In addition, a few of the credits that are available in the calculation of Tax Payable require an understanding of additional aspects of business income, property income, and taxable capital gains. Given this, Chapter 11 is devoted to completing the necessary coverage of Taxable Income and Tax Payable for individuals. The determination of Taxable Income and Tax Payable for corporations is covered in Chapters 12 and 13. The determination of Taxable Income and Tax Payable for trusts is covered in Chapter 19.

## Taxable Income Of Individuals

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### Available Deductions

4-4. The deductions that are available in calculating the Taxable Income of an individual can be found in Division C of Part I of the *Income Tax Act*. As indicated in the introduction to this Chapter, some of these deductions will be dealt with in this Chapter. However, coverage of the more complex items is deferred until Chapter 11. The available deductions, along with a description of their coverage in this text, are as follows:

**ITA 110(1)(d), (d.01), and (d.1) - Employee Stock Options** Our basic coverage of stock options and stock option deductions is included in Chapter 3. This coverage will not be repeated here. We would note, however, that Supplementary Reading No. 2 - *Stock Option Shares Deemed Not Identical Property*, provides coverage of a more advanced issue in this area. The Supplementary Readings can be found on the Student CD-ROM which accompanies this text.

**ITA 110(1)(f) - Deductions For Payments** This deduction, which is available for social assistance and workers' compensation received, is covered beginning in Paragraph 4-6.

**ITA 110(1)(j) - Home Relocation Loan** We refer to this deduction in Chapter 3 as it is related to a taxable benefit that is included in employment income. However, more detailed coverage is found in this Chapter beginning in Paragraph 4-9.

**ITA 110.2 - Lump Sum Payments** ITA 110.2 provides a deduction for certain lump-sum payments (e.g., an amount received as a court-ordered termination benefit and included in employment income). It provides the basis for taxing this amount as though it were received over several taxation years (i.e., income averaging). Because of its limited applicability, no additional coverage is given to this provision.

**ITA 110.6 - Lifetime Capital Gains Deduction** The provisions related to this deduction are very complex and require a fairly complete understanding of capital gains. As a consequence, this deduction is covered in Chapter 11.

**ITA 110.7 - Residing In Prescribed Zone (Northern Residents Deductions)** These deductions, which are limited to individuals living in prescribed regions of northern Canada, are covered in Paragraph 4-13.

**ITA 111 - Losses Deductible** This is a group of deductions that is available for carrying forward or carrying back various types of losses. The application of these provisions can be complex and requires a fairly complete understanding of business income, property income, and capital gains. Coverage of this material is deferred until Chapter 11.

### Ordering Of Deductions

4-5. ITA 111.1 specifies, to some degree, the order in which individuals must subtract the various deductions that may be available in the calculation of Taxable Income. As our coverage of these deductions is not complete in this Chapter, we will defer coverage of this ordering provision until Chapter 11.

## Deductions For Payments - ITA 110(1)(f)

4-6. ITA 110(1)(f) provides for the deduction of certain amounts that have been included in the calculation of Net Income For Tax Purposes. The items listed here are:

- amounts that are exempt from tax in Canada by virtue of a provision in a tax treaty or agreement with another country;
- workers' compensation payments received as a result of injury or death;
- income from employment with a prescribed international organization; and
- social assistance payments made on the basis of a means, needs, or income test and included in the taxpayer's income.

4-7. At first glance, this seems to be a fairly inefficient way of not taxing these items. For example, if the government does not intend to tax social assistance payments, why go to the trouble of including them in Net Income For Tax Purposes, then deducting an equivalent amount in the calculation of Taxable Income?

4-8. There is, however, a reason for this. There are a number of items that influence an individual's tax obligation that are altered on the basis of the individual's Net Income For Tax Purposes. For example, we will find later in this Chapter that the amount of the age tax credit is reduced by the individual's Net Income For Tax Purposes in excess of a specified amount (a.k.a. the threshold amount or the income threshold). In order to ensure that income tests of this type are applied on an equitable basis, amounts are included in Net Income For Tax Purposes, even in situations where the ultimate intent is not to assess tax on these amounts.

## Home Relocation Loan - ITA 110(1)(j)

4-9. As discussed in Chapter 3, if an employer provides an employee with a loan on which interest is payable at a rate that is less than the prescribed rate, a taxable benefit must be included in the employee's income. Under ITA 80.4(1), the benefit will be measured as the difference between the interest that would have been paid on the loan at the prescribed rate and the amount of interest that was actually paid. This taxable benefit must be included in income, even in situations where the loan qualifies as a "home relocation loan".

4-10. A home relocation loan is defined in ITA 248(1) as a loan made by an employer to an employee in order to assist him in acquiring a dwelling. This dwelling acquisition must be related to employment at a new work location, and the new dwelling must be at least 40 kilometers closer to the new work location. As is discussed more completely in Chapter 9, the distance is the same 40 kilometer test that is used in determining whether or not an individual can deduct moving expenses.

4-11. Provided the loan qualifies as a home relocation loan, ITA 110(1)(j) provides a deduction in the calculation of the individual's Taxable Income equal to the lesser of:

- **The Benefit Included In Income Under ITA 80.4(1)** As presented in detail in Chapter 3, the benefit on employee provided loans is determined by applying the prescribed rate to the principal amount of the loan on a quarterly basis. The amount of the benefit is then reduced by any interest payments made by the employee for that year which are paid in the year, or within 30 days of the year end. When the loan is a home purchase loan or a home relocation loan, ITA 80.4(4) limits the benefit to the amount that would be determined by applying the prescribed rate that was applicable when the loan was made to the principal amount on an annual basis. This limit is in place for the first five years the loan is outstanding.
- **The Amount That Would Have Been Calculated Under ITA 80.4(1)(a) On A \$25,000 Loan** This deduction is calculated using the same rules that are applicable to housing loans in general, except for the fact that it is:

- (1) based on \$25,000 rather than the actual amount of the loan, and
- (2) the amount is not reduced by interest payments made by the employee.

*Calculation Of Tax Payable*

By not deducting interest payments made by the employee, this effectively bases the calculation of the amount on an interest free loan of \$25,000. If this amount exceeds the benefit included under ITA 80.4(1), the deduction will equal the taxable benefit and the net effect will be nil.

4-12. This deduction is available for a period of up to five years. However, as the deduction is designed to offset a benefit that is included in employment income, the deduction will not be available after the loan has been paid off and there is no longer an employment income inclusion. While the calculation of the benefit and the deduction can be based on the number of days in each quarter, an example in IT-421R2 makes it clear that treating each calendar quarter as one-quarter of a year is an acceptable procedure.

**Example** On July 1, 2013, Janice Brock receives an interest free loan from her employer that is provided to assist her with acquiring a home in a new work location. The amount of the loan is \$150,000 and it must be repaid on June 30, 2015. The prescribed rate throughout 2013 is 1 percent.

**Analysis** Janice will have a taxable benefit of \$750  $[(2/4)(1\%)(\$150,000)]$ , an amount that will be included in her Net Income For Tax Purposes. She will have an offsetting deduction of \$125  $[(2/4)(1\%)(\$25,000)]$  in the determination of Taxable Income. This amount is the lesser of \$125 and \$750.

### Exercise Four - 1

**Subject:** Home Relocation Loan

On January 1 of the current year, in order to facilitate an employee's relocation, Lee Ltd. provides her with a five year, \$82,000 loan. The employee pays 2 percent annual interest on the loan on December 31 of each year. Assume that at the time the loan is granted the prescribed rate is 4 percent. However, the rate is increased to 5 percent for the third and fourth quarters of the current year. What is the effect of this loan on the employee's Taxable Income for the current year?

**End of Exercise. Solution available in Study Guide.**

### Northern Residents Deductions - ITA 110.7

4-13. Residents of Labrador, the Territories, as well as parts of some of the provinces, are eligible for deductions under ITA 110.7. To qualify for these deductions, the taxpayer must be resident in these prescribed regions for a continuous period of six months beginning or ending in the taxation year. The amount of the deductions involves fairly complex calculations that go beyond the scope of this text. The purpose of these deductions is to compensate individuals for the high costs that are associated with living in such prescribed northern zones.

## Calculation Of Tax Payable

### Federal Tax Payable Before Credits

4-14. The calculation of federal Tax Payable for individuals requires the application of a group of progressive rates to marginal increments in Taxable Income. The rates are progressive, starting at a low rate of 15 percent and increasing to rates of 22 percent, 26 percent, and 29 percent as the individual's Taxable Income increases. In order to maintain fairness, the brackets (i.e., income segments) to which these rates apply are indexed to reflect changes in the Consumer Price Index. Without such indexation, taxpayers could find themselves effectively subject to higher rates without having an increased level of real, inflation adjusted income.

*Calculation Of Tax Payable*

4-15. For 2013, the brackets to which these four rates apply are as follows:

| <b>Taxable Income<br/>In Excess Of</b> | <b>Federal Tax</b> | <b>Marginal Rate<br/>On Excess</b> |
|--|--------------------|------------------------------------|
| \$ -0-                                 | \$ -0-             | 15%                                |
| 43,561                                 | 6,534              | 22%                                |
| 87,123                                 | 16,118             | 26%                                |
| 135,054                                | 28,580             | 29%                                |

4-16. Note that the average rate for an individual just entering the 22 percent bracket is 15 percent ( $\$6,534 \div \$43,561$ ). For an individual just entering the highest 29 percent bracket, the average rate is 21.2 percent ( $\$28,580 \div \$135,054$ ).

4-17. There is a common misconception that once Taxable Income reaches the next tax bracket, all income is taxed at a higher rate. This is not the case as each rate is a marginal rate. For example, if Taxable Income is  $\$135,055$  ( $\$135,054 + \$1$ ), only  $\$1$  is taxed at 29 percent.

4-18. The preceding table suggests that individuals are taxed on their first dollar of income. While the 15 percent rate is, in fact, applied to all of the first  $\$43,561$  of Taxable Income, a portion of this amount is not really subject to taxes. As will be discussed later in this Chapter, every individual resident in Canada is entitled to a personal tax credit. For 2013, this tax credit is  $\$1,656$  [ $(15\%)(\$11,038)$ ]. In effect, this means that no taxes will be paid on at least the first  $\$11,038$  of an individual's Taxable Income. The amount that could be earned tax free would be even higher for individuals with additional tax credits (e.g., the age credit).

4-19. As an example of the calculation of federal Tax Payable before credits, consider an individual with Taxable Income of  $\$92,300$ . The calculation would be as follows:

|  |                               |
|--|-------------------------------|
| Tax On First $\$87,123$                                | $\$16,118$                    |
| Tax On Next $\$5,177$ ( $\$92,300 - \$87,123$ ) At 26% | 1,346                         |
| <b>Federal Tax Payable Before Credits</b>              | <b><math>\\$17,464</math></b> |

4-20. A surtax is an additional tax calculated on the basis of the regular Tax Payable calculation. While such additional taxes are not assessed at the federal level, they are used in two provinces, most notably in Ontario. For 2013, Ontario has a surtax of 56 percent on amounts of Ontario Tax Payable in excess of  $\$5,489$ . This significantly increases the highest rate in Ontario from the stated 13.16 percent to 20.53 percent.

## Provincial Tax Payable Before Credits

### *Provincial Rates*

4-21. As is the case at the federal level, provincial Tax Payable is calculated by multiplying Taxable Income by either a single tax rate or a group of progressive rates. In general, the provinces other than Quebec use the same Taxable Income figure that is used at the federal level.

4-22. With respect to rates, Alberta uses a single flat rate of 10 percent applied to all levels of income. All of the other provinces use either 3, 4, or 5 different rates which are applied in tax brackets that are similar to those established at the federal level. In addition, two provinces (Ontario and P.E.I.) apply surtaxes when the provincial Tax Payable figure reaches a certain level.

4-23. To give you some idea of the range of provincial rates, the 2013 minimum and maximum rates for provinces other than Quebec are as found in the following table. The maximum rates include surtaxes where applicable. These rates are correct as of April 1, 2013. You may see other rates after this point in time as provincial budgets are introduced.

*Calculation Of Tax Payable*

| Province                                    | Minimum Tax Rate | Maximum Tax Rate |
|---|------------------|------------------|
| Alberta                                     | 10.00%           | 10.00%           |
| British Columbia                            | 5.06%            | 14.70%           |
| Manitoba                                    | 10.80%           | 17.40%           |
| New Brunswick                               | 9.10%            | 14.30%           |
| Newfoundland and Labrador                   | 7.70%            | 13.30%           |
| Nova Scotia                                 | 8.79%            | 21.00%           |
| Ontario (including 56% surtax)              | 5.05%            | 20.53%           |
| Prince Edward Island (including 10% surtax) | 9.80%            | 18.37%           |
| Saskatchewan                                | 11.00%           | 15.00%           |

4-24. You should note the significant differences in rates between the provinces. The maximum 21 percent rate in Nova Scotia is more than double the flat 10 percent rate in Alberta. This amounts to extra taxes of \$11,000 per year on each additional \$100,000 of income. This can make provincial tax differences a major consideration when an individual decides where he should establish provincial residency.

4-25. When these provincial rates are combined with the federal rate schedule, the minimum combined rate varies from a low of 20.05 percent in Ontario (15 percent federal, plus 5.05 percent provincial), to a high of 26 percent in Saskatchewan (15 percent federal, plus 11 percent provincial).

4-26. Maximum combined rates are lowest in Alberta where the rate is 39 percent (29 percent federal, plus 10 percent provincial). They are highest in Nova Scotia where the combined rate is 50 percent (29 percent federal, plus 21 percent provincial). Because the calculations are completely different, we have not included Quebec in this list of rates. We would note however, the overall rate in Quebec ranges from a low of 28.53 percent to a high of 49.97 percent.

### Exercise Four - 2

**Subject:** Calculation Of Tax Payable Before Credits

During 2013, Joan Matel is a resident of Ontario and has calculated her Taxable Income to be \$46,700. Assume that Ontario's rates are 5.05 percent on Taxable Income up to \$43,561 and 9.15 percent on the next \$43,561. Calculate her 2013 federal and provincial Tax Payable before consideration of credits, and her average rate of tax.

**End of Exercise. Solution available in Study Guide.**

### **Provincial Residence**

4-27. Given the significant differences in provincial tax rates on individuals, it is somewhat surprising that the rules related to where an individual will pay provincial taxes are fairly simple. With respect to an individual's income other than business income, it is subject to tax in the province in which he resides on the last day of the taxation year. This means that, if an individual moves to Ontario from Nova Scotia on December 30 of the current year, any income for the year, other than business income, will be taxed in Ontario.

### **Types Of Income**

4-28. In terms of the effective tax rates, the income accruing to Canadian individuals can be divided into three categories:

**Ordinary Income** This would include employment income, business income, property income other than dividends, and other sources of income. In general, the

effective tax rates on this category are those presented in the preceding tables. For example, the marginal rate for an individual living in Alberta and earning more than \$135,054, would be 39 percent (29 percent federal, plus 10 percent provincial).

**Capital Gains** As will be discussed in detail in Chapter 8, capital gains arise on the disposition of capital property. Only one-half of such gains are included in Net Income For Tax Purposes and Taxable Income. This means that the effective tax rate on this category of income is only one-half of the rates presented in the preceding tables. Returning to our Alberta resident who is earning more than \$135,054, his effective marginal rate on capital gains would be 19.5 percent  $[(1/2)(29\% + 10\%)]$ .

**Dividends** As will be explained in Chapter 7, dividends from taxable Canadian companies are subject to a gross up and tax credit procedure which reduces the effective tax rate on this type of income. Also in that Chapter, we explain the difference between eligible dividends and non-eligible dividends. Continuing with our Alberta example, maximum federal/provincial tax rates on dividends are as follows:

|                        |       |
|------------------------|-------|
| Eligible Dividends     | 19.3% |
| Non-Eligible Dividends | 27.7% |

4-29. A more complete discussion of the different effective tax rates mentioned here is provided in Chapter 7 (dividends) and Chapter 8 (capital gains).

## Taxes On Income Not Earned In A Province

4-30. As will be discussed in Chapter 20, International Issues In Taxation, it is possible for an individual to be considered a resident of Canada for tax purposes, without being a resident of a particular province or territory. This would be the case, for example, for members of the Canadian Armed Forces who are stationed outside of Canada. It is also possible for non-residents to earn income in Canada that is not taxed in a particular province (e.g. Canadian employment income).

4-31. Income that is not subject to provincial or territorial tax is subject to additional taxation at the federal level. This additional tax is a surtax of 48 percent on federal tax payable. This gives a maximum rate of 42.9 percent  $[(29\%)(148\%)]$ . This additional tax is paid to the federal government.

## Calculating Tax Credits

### Federal Amounts

4-32. The most direct way of applying a tax credit system is to simply specify the amount of each tax credit available. In 2013, for example, the basic personal tax credit could have been specified to be \$1,656. However, the Canadian tax system is based on a less direct approach. Rather than specifying the amount of each credit, a base amount is provided, to which the minimum federal tax rate (15 percent) is applied. This means that, for 2013, the basic personal tax credit is calculated by taking 15 percent of \$11,038 (we will refer to this number as the tax credit base), resulting in a credit against Tax Payable in the amount of \$1,656.

4-33. Note that the legislation is such that, if the minimum federal tax rate of 15 percent is changed, the new rate will be used in determining individual tax credits. In our tax credit calculations, we will usually calculate the sum of the tax credit bases and apply the 15 percent rate to the total. This approach (rather than applying 15 percent to each credit base) makes relationships between the various credit bases easier to see and reduces calculation errors.

4-34. As was the case with the tax rate brackets, in order to avoid having these credits decline in value in terms of real dollars, the base for the tax credits needs to be adjusted for changing prices. While it is not a common occurrence, there may be adjustments to tax credit bases for amounts that do not simply reflect the rate of inflation. For example, in 2009, the base for the basic personal credit was increased to \$10,320, \$220 more than would have been required by a simple inflation adjustment.



*Personal Tax Credits - ITA 118(1)*

4-35. A technical problem in calculating credits will arise in the year a person becomes a Canadian resident, or ceases to be a Canadian resident. As discussed in Chapter 20, such individuals will only be subject to Canadian taxation for a part of the year. Given this, it would not be appropriate for them to receive the same credits as an individual who is subject to Canadian taxation for the full year. This view is reflected in ITA 118.91, which requires a pro rata calculation for personal tax credits, the disability tax credit and tax credits transferred from a spouse or a person supported by the taxpayer. Other tax credits, for example the tax credits for charitable donations and adoption expenses, are not reduced because of part year residence. This is because these credits reflect actual amounts paid or costs incurred during the period of Canadian residency.

### Provincial Amounts

4-36. In determining provincial tax credits, the provinces use the same approach as that used at the federal level. That is, the minimum provincial rate is applied to a base that is indexed each year. In most cases, the base used is different from the base used at the federal level. For 2013, the basic personal tax credit at the federal level is \$1,656 [(15%)(\$11,038)]. Comparative 2013 figures for selected provinces are as follows:

| Province                  | Base     | Rate   | Credit     |
|---------------------------|----------|--------|------------|
| Alberta                   | \$17,593 | 10.00% | \$1,759    |
| British Columbia          | 10,276   | 5.06%  | 520        |
| Newfoundland And Labrador | 8,451    | 7.70%  | <b>651</b> |
| Ontario                   | 9,574    | 5.05%  | 483        |

## Personal Tax Credits - ITA 118(1)

### A Note On The Family Caregiver Amount

4-37. The 2011 budget introduced what is referred to as the Family Caregiver Amount (FCA). When introduced for 2012, the FCA was \$2,000. However, as it is indexed, the figure for 2013 is \$2,040.

4-38. The FCA becomes available when an individual is claiming one or more of five different credits. These credits are the:

- spousal or common-law partner credit
- eligible dependant credit
- credit for children under the age of 18
- credit for infirm dependants age 18 or older
- caregiver credit (not to be confused with the family caregiver amount)

4-39. In general, the FCA will be added to the each credit base provided the following conditions are met:

- If the credit is claimed for an individual age 18 or older, the individual must be dependent on the taxpayer by reason of physical or mental infirmity.
- If the credit is claimed for a child under the age of 18, the child must have a medical or physical infirmity and as a result of that infirmity is, and is likely to be for a long continued period of indefinite duration, dependent on others for significantly more assistance in attending to the child's personal needs and care when compared to children of the same age.

It would appear that this does not require a disability so severe that the child would qualify for the disability tax credit. However, it is a stronger requirement than that applicable to dependants who are 18 years of age or older.

- In the case of the amount for an infirm dependant age 18 or older, the FCA amount is automatically added to the credit base, reflecting the fact, if a dependant is eligible for the infirm dependant credit, they will also be eligible for the family caregiver credit.

4-40. We would also note the following with respect to the FCA:

- While not a standard requirement, the CRA can require a signed statement from a medical doctor certifying that the dependant is eligible for the FCA.
- The FCA can be claimed for each dependant that qualifies, i.e., it can be claimed for multiple dependants.
- In those cases where both the eligible dependant credit and the child under 18 credit is claimed for the same individual, only the amount for a child under 18 will be increased by the FCA.

## Individuals With A Spouse Or Common-Law Partner - ITA 118(1)(a)

### Basic Personal Plus Spousal Tax Credits

4-41. For individuals with a spouse or common-law partner filing tax returns in 2013, ITA 118(1)(a) provides for two tax credits — one for the individual (sometimes referred to as the basic personal credit) and one for his or her spouse or common-law partner (sometimes referred to as the spousal credit). For 2013, the **basic personal credit is \$1,656** [(15%)(\$11,038)].

### Calculation Of Spousal Tax Credit

4-42. If the individual's spouse is not dependent because of a mental or physical infirmity, the spousal credit is calculated using the same base as the basic personal credit. However, it must be reduced by the spouse or common-law partner's Net Income For Tax Purposes.

4-43. As discussed beginning in Paragraph 4-37, the FCA may be added to this credit in situations where a spouse or common-law partner is dependent because of a physical or mental infirmity. Note, if the spouse or common-law partner is dependent simply because they have little or no income, the FCA is not available. The dependency must be the result of an infirmity.

4-44. For 2013, the calculation of the spousal credit, with and without the FCA, is as follows:

#### Spousal Credit - No FCA

$$= [(15\%)(\$11,038 - \text{Spouse Or Common-Law Partner's Net Income})]$$

#### Spousal Credit - With FCA

$$= [(15\%)(\$11,038 + \$2,040 - \text{Spouse Or Common-Law Partner's Net Income})]$$

4-45. As an example, consider an individual with a spouse who had Net Income For Tax Purposes of \$5,200. The total personal credits under ITA 118(1)(a) if the spouse (1) was not eligible for the FCA and (2) was eligible for the FCA, would be calculated as follows:

|   | No FCA    | With FCA  |
|---|-----------|-----------|
| Basic Personal Amount                         | \$ 11,038 | \$ 11,038 |
| Spousal Amount (\$11,038 - \$5,200)           | 5,838     |           |
| Spousal Amount (\$11,038 + \$2,040 - \$5,200) |           | 7,878     |
| Credit Base                                   | \$16,876  | \$18,916  |
| Rate  | 15%       | 15%       |
| Personal Tax Credits                          | \$ 2,531  | \$ 2,837  |

4-46. There are several other points to be made with respect to the credits for an individual with a spouse or common-law partner:

**Spouse Or Common-Law Partner's Income** The income figure that is used for limiting the spousal amount is Net Income For Tax Purposes, with no adjustments of any sort.

**Applicability To Either Spouse Or Common-Law Partner** The ITA 118(1)(a) provision is applicable to both spouses and, while each is eligible to claim the basic amount of \$11,038, IT-513R specifies that only one spouse or common-law partner may claim the spousal amount. IT-513R indicates that the spouse making the claim should be the one that supports the other (support is defined in Appendix A of IT-513R).

**Eligibility** The additional credit can be claimed for either a spouse or a common-law partner. There is no definition of spouse in the *Income Tax Act*, so it would appear that the usual dictionary definition would apply. That is, a spouse is one of a pair of persons who are legally married. With respect to common-law partner, ITA 248(1) defines such an individual as a person who cohabits with the taxpayer in a conjugal relationship and:

- has so cohabited for a continuous period of at least one year; or
- is the parent of a child of whom the taxpayer is also a parent.

There is no requirement in the income tax legislation that either a spouse or a common-law partner be a person of the opposite sex. One can, however, assume that they must be of the same species (e.g., you can't claim your dog).

**Multiple Relationships** Based on these definitions, it would be possible for an individual to have both a spouse and a common-law partner. ITA 118(4)(a) makes it clear that, if this is the case, a credit can only be claimed for one of these individuals. In such cases, determining your tax credits may be the least of your problems.

**Year Of Separation Or Divorce** In general, ITA 118(5) does not allow a tax credit based on the spousal amount in situations where the individual is making a deduction for the support of a spouse or common-law partner (spousal support is covered in Chapter 9). However, IT-513R indicates that, in the year of separation or divorce, an individual can choose to deduct amounts paid for spousal support, or claim the additional tax credit for a spouse.

### Exercise Four - 3

**Subject:** Spousal Tax Credit

Mr. Johan Sprinkle is married and has 2013 Net Income For Tax Purposes of \$35,450. His spouse has 2013 Net Income For Tax Purposes of \$2,600. Assuming that Johan's spouse does not have a mental or physical infirmity, determine Mr. Sprinkle's federal tax credits for 2013. How would your answer differ if Johan's spouse was dependent because of a mental or physical infirmity?

**End of Exercise. Solution available in Study Guide.**

## Individuals Supporting A Wholly Dependent Person - ITA 118(1)(b)

### *Eligibility And Eligible Dependant Defined*

4-47. The ITA 118(1)(b) credit is available to an individual who is not claiming the spousal credit and who supports a wholly dependent person who lives with them in a self-contained domestic establishment (we will refer to this person as an eligible dependant). To qualify for this credit, the individual must be:

- unmarried;
- not living in a common-law partnership; or
- a person who is married or has a common-law partner but neither supports nor lives with that spouse or common-law partner.

4-48. To claim this credit, the eligible dependant must be "related" to the individual making

the claim and “wholly dependent”. ITA 251(2) defines related individuals as those who are related by blood, marriage, common-law partnership, or adoption. IT-419R2 indicates that this would exclude aunts, uncles, nieces, nephews, and cousins. To be “wholly dependent” would mean that the individual provides all means of support (food, clothing, shelter), as well as all financial support. For example, a young child would normally be wholly dependent on a parent. The death of a spouse or common-law partner severs all marriage and common-law relationships. For example, a taxpayer is no longer related to his deceased wife’s mother.

4-49. In view of today’s less stable family arrangements, the question of exactly who is considered a child for tax purposes requires some elaboration. As explained in IT-513R, the credit may be taken for natural children, children who have been formally adopted, as well as for natural and adopted children of a spouse or common-law partner.

### Calculation Of Eligible Dependant Tax Credit

4-50. We have noted that the FCA may be added to the eligible dependant credit amount. For the FCA to be added to the base for this credit, two conditions must present:

- The eligible dependant must be mentally or physically infirm.
- The eligible dependant is not a child under the age of 18. The reason for this condition is that a taxpayer is allowed to take both the eligible dependant tax credit and the child tax credit for the same child. As the FCA is generally available on both of these credits, there could be a double application of this amount. To prevent this, ITA 118(1)(b) does not allow the FCA to be added when the eligible dependant is a child under 18. This ensures that only one FCA can be claimed for a specific child.

4-51. If these conditions are met, the eligible dependant credit includes the FCA.

4-52. Like the spousal credit, it is calculated using the same base as the basic personal credit and must be reduced by the eligible dependant's Net Income For Tax Purposes. For 2013, the calculation of the eligible dependant credit, with and without the FCA, is as follows:

#### Eligible Dependant Credit - No FCA

$$= [(15\%)(\$11,038 - \text{Eligible Dependant's Net Income})]$$

#### Eligible Dependant Credit - With FCA

$$= [(15\%)(\$11,038 + \$2,040 - \text{Eligible Dependant's Net Income})]$$

4-53. As an example, consider an unmarried person supporting an adult eligible dependant who has Net Income For Tax Purposes of \$5,200. The total personal credits under ITA 118(1)(b) if the dependant (1) was not eligible for the FCA and (2) was eligible for the FCA, would be calculated as follows:

|   | No FCA    | With FCA  |
|---|-----------|-----------|
| Basic Personal Amount                             | \$ 11,038 | \$ 11,038 |
| Eligible Dependant Amount<br>(\$11,038 - \$5,200) | 5,838     |           |
|   |           | 7,878     |
| Credit Base                                       | \$16,876  | \$18,916  |
| Rate  | 15%       | 15%       |
| Personal Tax Credits                              | \$ 2,531  | \$ 2,837  |

4-52. Note that this credit provides for the same total credits that would be available to an individual with a spouse who had Net Income For Tax Purposes of \$5,200 (see Paragraph 4-45). For this reason, it is sometimes referred to as the equivalent to married tax credit.

### Application

4-55. This credit is most commonly claimed by single parents who are supporting a minor child. More generally, this credit is available to individuals who are single, widowed, divorced, or separated, and supporting a dependant who is:

*Personal Tax Credits - ITA 118(1)*

- related to the individual by blood, marriage, adoption or common-law relationship;
- wholly dependent on the individual for support;
- under 18 at any time during the year, or mentally or physically infirm, or the individual's parent or grandparent;
- living with the individual in a home that the individual maintains (this would not disqualify a child who moves away during the school year to attend an educational institution as long as the home remains the child's home); and
- residing in Canada (this requirement is not applicable to an individual's child as long as they are living with the individual).

4-56. The eligible dependant credit cannot be claimed by an individual:

- if the individual is claiming the spousal credit;
- if the individual is living with, supporting, or being supported by a spouse (the claim is only available for individuals who are either single, or living separately from their spouse);
- for more than one person;
- if the dependant's Net Income exceeds \$11,038 or \$13,078 if the FCA is applicable;
- if someone other than the individual is making this claim for the same individual; or
- for the individual's child, if the individual is making child support payments to another individual, for that child. As is noted in Chapter 9, when child support is being paid, only the recipient of such payments can claim this tax credit. This is the case without regard to whether or not the individual making the child support payments is able to deduct the payments in determining Net Income For Tax Purposes.

**Child Tax Credit - ITA 118(1)(b.1)**

4-57. An individual is eligible for a tax credit for each child who is under 18 years of age at the end of the taxation year. For 2013, the **child tax credit is \$335** per child [(15%)(\$2,234)]. In addition, if the child is mentally or physically infirm, the parent can claim the FCA, which brings the total value of the credit to \$641 [(15%)(\$2,234 + \$2,040)]. Somewhat surprisingly, it is not reduced by the child's income or family income.

4-58. Also surprising is the fact that this credit can be claimed for a particular child, even when the ITA 118(1)(b) eligible dependant credit is being claimed for that same child. For example, if a single mother was supporting a child under 18 in a self-contained domestic establishment, she could claim both the eligible dependant tax credit and the child tax credit for that one child. We would remind you, however, that if that child was eligible for the FCA, she would receive the extra \$2,040 only on the child tax credit. It would not be available on both credits.

4-59. Other relevant points are as follows:

- Provided the child resides with both parents throughout the year, it can be claimed by either parent. The phrase "throughout the year" is defined to include the fraction of the year subsequent to the birth or adoption of the child and the fraction of the year prior to the death of a child.
- If the parents are living separately, this credit can only be claimed by the parent who claims the eligible dependant credit for the child, or who would have been able to claim the eligible dependant credit for the child if not for the one person restriction. However, unlike the eligible dependant credit, the child tax credit can be claimed for more than one child.

**Single Persons (Basic Personal Tax Credit) - ITA 118(1)(c)**

4-60. Individuals living with a spouse, common-law partner or eligible dependant receive a credit for themselves and their spouse or common-law partner under ITA 118(1)(a), or themselves and their eligible dependant under ITA 118(1)(b). For individuals who do not have a spouse, common-law partner or eligible dependant, a basic personal tax credit is received under ITA 118(1)(c). For 2013, the credit is equal to \$1,656 [(15%)(\$11,038)].

### Caregiver Tax Credit - ITA 118(1)(c.1)

4-61. ITA 118(1)(c.1) allows for a caregiver tax credit to an individual who provides in home care for certain related adults (18 years or older) who is not a spouse or a common-law partner. To qualify, the related adult must be:

- the parent or grandparent of the individual, or the parent or grandparent of the individual's spouse or common-law partner, who is a resident of Canada and is 65 years of age or older, regardless of whether there is dependency due to a mental or physical infirmity, or
- the adult child or grandchild of the individual who is dependent because of a mental or physical infirmity, regardless of whether the (grand)child is a resident of Canada; or
- the adult brother, sister, aunt, uncle, nephew or niece of the individual, or the adult brother, sister, aunt, uncle, nephew or niece of the individual's spouse or common-law partner, who is a resident of Canada and is dependent because of a mental or physical infirmity.

4-62. A credit may be claimed for each individual who qualifies.

4-63. The caregiver tax credit is one of the credits where the FCA is added when dependency is based on mental or physical infirmity. For 2013, the caregiver tax credit without the FCA has a maximum value of \$674 [(15%)(\$4,490)]. With the FCA, the maximum value is \$980 [(15%)(\$4,490 + \$2,040)].

4-64. The base for the credit is reduced by the amount of the dependant's Net Income in excess of \$15,334. This means that this tax credit is not available once the dependant's Net Income is more than \$19,824 (\$15,334 + \$4,490), or \$21,864 if the FCA is available.

4-65. As dependency based on mental or physical infirmity is one of the general criteria for this credit, the FCA would usually be added to the caregiver credit. The one exception would be when the related adult is a parent or grandparent who is 65 or over. Such individuals qualify for the caregiver credit, without having to be mentally or physically infirm.

### Exercise Four - 4

**Subject:** Caregiver Tax Credit

Joan Barton lives with her husband. Two years ago her father, who is 69 years old and very active, moved in with her. His Net Income For Tax Purposes for 2013 is \$15,600. Determine the amount of Joan's caregiver tax credit, if any, for 2013. How would your answer differ if her father was mentally or physically infirm?

**End of Exercise. Solution available in Study Guide.**

### Infirm Dependant Over 17 Tax Credit - ITA 118(1)(d)

4-66. ITA 118(1)(d) specifies a credit for dependants who are age 18 or older prior to the end of the year, provided they are dependent by reason of mental or physical infirmity. For purposes of this credit, the *Income Tax Act* defines dependant as follows:

**ITA 118(6)** Definition of "dependant" — ..."dependant" of an individual for a taxation year means a person who at any time in the year is dependent on the individual for support and is

- (a) the child or grandchild of the individual or of the individual's spouse or common-law partner; or
- (b) the parent, grandparent, brother, sister, uncle, aunt, niece or nephew, if resident in Canada at any time in the year, of the individual or of the individual's spouse or common-law partner.

*Personal Tax Credits - ITA 118(1)*

4-67. Note that this definition is not the same as that applicable to the ITA 118(1)(b) credit for a wholly dependent person, a.k.a. eligible dependant (see Paragraph 4-47). The definition here includes aunts, uncles, nieces, and nephews. These relatives could not be considered eligible dependants for purposes of the ITA 118(1)(b) credit.

4-68. The FCA is already included in this credit base. Unlike the situation with the other credits where the FCA can be available, the FCA will always be included with this credit as criteria for this credit and the FCA are the same. Both credits are available for dependants who are mentally or physically infirm.

4-69. For 2013, this credit has a value of \$980 [(15%)( $\$6,530$ )]. The base for the credit is reduced by the amount of the dependant's Net Income in excess of \$6,548. This means that this tax credit is not available once the dependant's Net Income is more than \$13,078 ( $\$6,530 + \$6,548$ ).

4-70. The ITA 118(1)(d) infirm dependant over 17 credit should not be confused with the mental and physical impairment credit (a.k.a., disability tax credit) that is available to disabled individuals under ITA 118.3. The ITA 118.3 disability credit requires a doctor to certify that there is a prolonged impairment that severely restricts basic living activities. The disability credit is claimed by the disabled person, but can be transferred to a supporting person if it cannot be fully utilized (see Paragraph 4-148).

4-71. In contrast, the ITA 118(1)(d) credit can only be claimed by the supporting person and a doctor's certification of the mental or physical infirmity is not required. For example, a daughter would be eligible to claim this credit if her mother is living in a nursing home because she is too frail to live alone, and her mother has income of less than \$13,078 during the year.

4-72. Note that because the disability credit can be transferred to a supporting person, the supporting person may be able to claim both the credit for an infirm dependant over 17, and the disability tax credit for the same person.

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**Exercise Four - 5**

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**Subject:** Infirm Dependiant Over 17 Tax Credit

Harold Reed is married. His 70 year old mother has severe arthritis and lives in a nursing home. Her Net Income For Tax Purposes for 2013 is \$7,600 and she relies on Harold for support. Determine the amount of Harold's caregiver and infirm dependant over 17 tax credit for 2013.

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**End of Exercise. Solution available in Study Guide.**

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**Interaction: Eligible Dependiant Credit Vs. Caregiver Or Infirm Dependiant Over 17 Credits**

4-73. In reading through the material related to these three tax credits, it may have occurred to you that a taxpayer could have a dependant who was eligible for both the ITA 118(1)(b) eligible dependant credit and either the caregiver credit or infirm dependant over 17 credit. This did not happen in either Exercise Four-4 or Four-5 because both Joan Barton and Harold Reed were living with their spouses, making them ineligible to claim the eligible dependant credit.

4-74. In contrast, assume a single individual has a disabled child over 17 years of age. In the absence of some restriction, this individual could claim both the eligible dependant credit and the infirm dependant over 17 credit. ITA 118(4)(c) provides such a restriction. This paragraph indicates that, if a taxpayer is eligible for the ITA 118(1)(b) eligible dependant credit for a particular individual, he cannot claim either the caregiver credit or the infirm dependant over 17 credit for that individual. Note that ITA 118(4)(c) refers to "entitled to", without regard to whether the credit is actually taken.

4-75. ITA 118(4)(c) requires careful interpretation. If a taxpayer has only one dependant and that dependant is eligible for both the eligible dependant credit and either the caregiver or infirm dependant credits, the taxpayer must take the eligible dependant credit. However, if you add a second dependant who also qualifies for the eligible dependant credit, the situation changes. If the eligible dependant credit is claimed for the second dependant, the first dependant is no longer entitled to the eligible dependant credit because only one claim can be made for this credit. This means the caregiver or infirm dependant credit could be claimed for the first dependant.

4-76. Because the eligible dependant base has no income threshold, it is reduced if the dependant has any Net Income For Tax Purposes. It is completely eliminated when the dependant's Net Income For Tax Purposes is equal to or greater than \$11,038. In contrast, both the caregiver and infirm dependant over 17 credits are only reduced by the dependant's Net Income For Tax Purposes in excess of a threshold amount. Given this difference, the ITA 118(4)(c) restriction could have the unintended result of reducing the amount of tax credits.

4-77. ITA 118(1)(e) provides a solution to this problem. This provision allows an additional credit to be taken based on the excess of what the caregiver or infirm dependant over 17 credit would have been, over the amount available under the eligible dependant credit.

### Exercise Four - 6

**Subject:** Eligible Dependant Vs. Caregiver Tax Credits

Barry Litvak is a single individual with a 67 year old mother. While his mother is not mentally or physically infirm, she lives with Barry. She has Net Income For Tax Purposes for 2013 of \$7,500. Calculate the tax credits that will be available to Barry as a result of his mother living with him.

**End of Exercise. Solution available in Study Guide.**

### Interaction: Caregiver Vs. Infirm Dependant Over 17 Credits

4-78. It is likely that you have noted that a single individual may qualify for both the caregiver and infirm dependant over 17 tax credits. In terms of qualifying individuals, there are two differences:

- In general, both credits require the qualifying individual to be mentally or physically infirm. However, the caregiver credit makes an exception for parents and grandparents who are over 64. These individuals may qualify for the caregiver credit, but not the infirm dependant over 17 credit.
- The caregiver credit requires that the qualifying individual live with the taxpayer. The infirm dependant over 17 credit does not have this requirement.

4-79. Despite these differences, it is clear that in many cases, an individual who qualifies for the caregiver credit would also qualify for the infirm dependant over 17 credit. This means that, in the absence of some type of restrictive provision, both credits could be claimed for the same individual.

4-80. ITA 118(4)(d) provides such a restriction. This paragraph indicates that, if a taxpayer is entitled to the caregiver credit for a particular individual, that individual is deemed not to be a dependant and, therefore, not eligible for the infirm dependant over 17 credit. This prevents the taxpayer from claiming both credits for the same individual and, in effect, requires the use of the caregiver credit in situations where a single individual is eligible for both credits.



4-81. With the exception of non-infirm parents and grandparents over 64 who are not eligible for the FCA, both credits have a 2013 maximum value of \$980 [(15%)(6,530)]. However, there is a difference in the income thresholds, with the caregiver amount being significantly higher, \$15,334 vs. \$6,548. Because of this, the caregiver credit will be more desirable. This means that, in effect, ITA 118(4)(d) forces the taxpayer to make the more advantageous decision on this issue.

### Exercise Four - 7

**Subject:** Caregiver Vs. Infirm Dependant Over 17 Tax Credits

Suki Leonard is married, lives with her husband, and has a 28 year old son. He lives with her and is dependent because of a physical infirmity. For 2013, the son has investment income of \$8,250. Suki would like to know whether she should take the caregiver tax credit for her son or, alternatively, the infirm dependant over 17 tax credit and how much tax the correct credit will save her.

### Exercise Four - 8

**Subject:** Multiple Credits For Dependants

Ms. Jane Forest is 48 years old and divorced from her husband. She has retained the family home and both of the children of the marriage live with her. Her son is 20 years old and suffers from Down Syndrome. He does not qualify for the disability tax credit. Her daughter is 16 years old and in good health. Her son has no income during 2013, while her daughter has Net Income For Tax Purposes of \$1,800. Determine Ms. Forest's maximum federal tax credits for 2013.

**End of Exercises. Solutions available in Study Guide.**

## Other Tax Credits For Individuals

### Age Tax Credit - ITA 118(2)

4-82. For individuals who attain the age of 65 prior to the end of the year, ITA 118(2) provides an additional tax credit of \$1,028 [(15%)(6,854)]. However, the base for this credit is reduced by 15 percent of the individual's Net Income For Tax Purposes in excess of \$34,562. This means that, at an income level of \$80,255 [(\$6,854 ÷ 15%) + \$34,562], the reduction will be equal to \$6,854 and the individual will not receive an age credit. Note that the reduction is only 15% of the income above the threshold, not a dollar for dollar reduction.

**Example** A 67 year old individual has 2013 Net Income For Tax Purposes of \$35,000.

**Analysis** An age credit of \$1,018 {[15%][6,854 - (15%)(35,000 - 34,562)]} will be available to this individual.

4-83. As we shall see when we consider the transfer of credits to a spouse, if an individual does not have sufficient Tax Payable to use this credit, it can be transferred to a spouse.

### Exercise Four - 9

**Subject:** Age Tax Credit

Joshua Smythe is 72 years old and has 2013 Net Income For Tax Purposes of \$51,500. Determine Mr. Smythe's age credit for 2013.

**End Of Exercise. Solution available in Study Guide.**

## Pension Income Tax Credit - ITA 118(3)

### General Rules

4-84. The pension income credit is equal to 15 percent of the first \$2,000 of eligible pension income. This results in a maximum value of \$300 [(15%)(2,000)]. The base for this credit is not indexed for inflation.

4-85. The credit is only available with respect to "eligible pension income". Specifically excluded from this definition are:

- payments under the Old Age Security Act or Canada Pension Plan;
- payments under certain provincial pension plans;
- payments under salary deferral arrangements;
- payments under retirement compensation arrangements;
- payments under an employee benefit plan; and
- death benefits.

4-86. Like the age credit, if an individual does not have sufficient Tax Payable to use this credit, it can be transferred to a spouse.

### Individuals 65 Or Over

4-87. For an individual who has reached age 65 before the end of the year, this credit is available on "pension income" as defined in ITA 118(7). This includes payments that are:

- periodic (not lump sum) payments from a registered pension plan (RPP);
- an annuity payment out of a Registered Retirement Savings Plan (RRSP);
- a payment out of a Registered Retirement Income Fund (RRIF);
- an annuity payment from a Deferred Profit Sharing Plan (DPSP); and
- the interest component of other annuities.

### Individuals Under 65

4-88. For an individual who has not reached age 65 during the year, the credit is based on "qualified pension income", also defined in ITA 118(7). In general, this only includes the periodic payments from a registered pension plan. However, if the other types of pension income described in Paragraph 4-87 are received as a consequence of the death of a spouse or common-law partner, these amounts are also qualified, regardless of the age of the recipient.

## Canada Employment Tax Credit - ITA 118(10)

4-89. This credit is available to all individuals who have Canadian employment income. From a conceptual point of view, it is designed to provide limited recognition of the fact that there are costs associated with earning employment income. As only limited deductions are available against employment income, this would appear to be an appropriate form of relief.

4-90. For 2013, the amount of the credit is equal to 15 percent of the lesser of:

- \$1,117; and
- the individual's Net Employment Income, calculated without the deduction of any employment related expenses.

4-91. For most employed individuals, this will produce a credit of \$168 [(15%)(1,117)].

## Adoption Expenses Tax Credit - ITA 118.01

4-92. The adoption expenses tax credit is available to a taxpayer who adopts an "eligible child". As defined in ITA 118.01(1), an eligible child means a child who has not attained the age of 18 years at the time that an adoption order is issued or recognized by a government in Canada in respect of the adoption of that child.

4-93. The 2013 credit is based on up to \$11,669 in eligible adoption expenses, resulting in a maximum of \$1,750 [(15%)(11,669)]. The expenses can only be claimed in the year in which the adoption is finalized. The total amount of eligible expenses is reduced by any

assistance that is received and not included in that taxpayer's income. Note, however, if an employer makes a provision for an employee's adoption expenses, this amount will normally be treated as a taxable benefit. Given this, such amounts will not be deducted from the adoption expenses that form the basis for this credit.

4-94. An "adoption period" is defined in ITA 118.01(1).

It begins at the earlier of:

- the time that the eligible child's adoption file is opened with a provincial ministry responsible for adoption (or with an adoption agency licensed by a provincial government), and
- the time that an application related to the adoption is made to a Canadian court.

**2013 Budget** In recognition of the fact that there may be substantial costs incurred prior to the actual opening of an adoption file, it is proposed that the "adoption period" begins when an adoptive parent makes an application to register with a provincial ministry, with a licensed adoption agency, or with a Canadian court. This measure will be effective for adoptions finalized after 2012.

It ends at the later of:

- the time an adoption order is issued by, or recognized by, a government in Canada in respect of that child, and
- the time that the child first begins to reside permanently with the individual.

4-95. Eligible adoption expenses must be incurred during the adoption period and include:

- (a) fees paid to an adoption agency licensed by a provincial government;
- (b) court costs and legal and administrative expenses related to an adoption order in respect of that child;
- (c) reasonable and necessary travel and living expenses of the child and the adoptive parents;
- (d) document translation fees;
- (e) mandatory fees paid to a foreign institution;
- (f) mandatory expenses paid in respect of the immigration of the child; and
- (g) any other reasonable expenses related to the adoption required by a provincial government or an adoption agency licensed by a provincial government.

4-96. In the usual situation, a child will be adopted by a couple, either legally married or co-habiting on a common-law basis. The legislation points out that, while both parties are eligible for this credit, the \$11,669 limit must be shared by the couple. The claim can be made by either party or split at their discretion.

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### Exercise Four - 10

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**Subject:** Adoption Expenses Tax Credit

Ary Kapit and his spouse have adopted an infant Chinese orphan. The adoption process began in June, 2012 when they applied to a licensed adoption agency. Later that year they traveled to China to discuss the adoption and view available children. The cost of this trip was \$4,250. Their provincial government opens the adoption file on February 13, 2013, and the adoption order is issued on August 27, 2013. In September, the couple returns to China to pick up their new daughter. The happy family returns to Canada on September 18, 2013. The cost of this trip is \$6,420.

Additional expenses paid during the first week of September, 2013 were \$1,600 paid to the Chinese orphanage and \$3,200 paid to a Canadian adoption agency. Legal fees incurred during the adoption period were \$2,700. After arrival in Canada, an additional \$2,500 in medical expenses were incurred for the child prior to the end of 2013. Mr. Kapit's employer has a policy of providing reimbursement for up to \$5,000

in adoption expenses eligible for the adoption expenses tax credit. This amount is received in September, 2013 and will be considered a taxable benefit to Mr. Kapit. What is the maximum adoption expenses tax credit that can be claimed by the couple?

**End of Exercise. Solution available in Study Guide.**

### Public Transit Passes Tax Credit - ITA 118.02

4-97. This credit is equal to 15 percent of the cost of eligible public transit passes attributable to the use of an individual, his spouse or common-law partner, and his children who have not attained the age of 19 during the year.

4-98. Eligible public transit passes are defined as follows:

- Passes that provide for unlimited travel for an uninterrupted period of at least 28 days (monthly passes).
- Passes that provide for unlimited travel for an uninterrupted period of at least 5 days, provided a sufficient number of such passes are acquired that at least 20 days will be covered in a period of 28 days (a group of weekly passes).

4-99. The credit is also available with respect to the costs of "eligible electronic payment cards". These must provide for at least 32 one-way trips during an uninterrupted period that does not exceed 31 days.

4-100. The passes must be for use on "public commuter transit services" which means services offered to the general public, ordinarily for a period of at least five days per week, of transporting individuals, from a place in Canada to another place in Canada, by means of bus, ferry, subway, train or tram, and in respect of which it can reasonably be expected that those individuals would return daily to the place of their departure.

4-101. As was the case with adoption expenses, the costs that are eligible for the credit must be reduced by any amounts that are reimbursed and not included in the taxpayer's income. Note, however, that employer reimbursements are generally included in an employee's income and, as a consequence, would not reduce the base for this credit.

### Child Fitness Tax Credit - ITA 118.03 And Children's Arts Tax Credit - ITA 118.031

#### General Rules

4-102. The child fitness and children's arts credits are two tax credits available to parents who enroll their children in eligible programs. They are very similar except for the definition of the relevant eligible activities. Although the ITA refers to the child fitness credit, it appears that the CRA is moving towards using the term children's fitness credit (similar to children's arts credit) as that term is used on the T1 tax return and the CRA website.

4-103. Both credits are equal to 15 percent of the lesser of \$500 and the eligible fees paid. This provides a maximum credit of \$75 [(15%)(500)]. The base for these credits is not subject to indexation. The credit is available in the years the fees are paid, not the year in which the program is scheduled. Both credits can be claimed by either parent or may be shared between them.

4-104. For both credits, there is an additional credit of \$75 [(15%)(500)] available for children who qualify for the Disability Tax Credit (see discussion beginning in Paragraph 4-148) and who are under 18 at the beginning of the year. While these credit supplements are not based on actual costs, their availability requires a minimum of \$100 in eligible fees to be paid. The base for these supplements is not subject to indexation.

4-105. To qualify for these credits, the costs must be related to a child who is under 16 years of age at the beginning of the year (under 18 if the child qualifies for the disability tax credit).

**Eligible Programs And Fees**

4-106. As described on the CRA web site, a qualifying fitness program must require significant physical activity that contributes to cardiorespiratory endurance, plus one or more of:

- muscular strength,
- muscular endurance,
- flexibility, and/or
- balance.

4-107. Again referencing the CRA web site, a qualifying arts program has to meet at least one of the following criteria:

- it contributes to the development of creative skills or expertise in an artistic or cultural activity;
- it provides a substantial focus on wilderness and the natural environment;
- it helps children develop and use particular intellectual skills;
- it includes structured interaction among children where supervisors teach or help children develop interpersonal skills; or
- it provides enrichment or tutoring in academic subjects.

4-108. With respect to both credits, a qualifying program must be supervised and suitable for children. In addition, the program must be "ongoing". Ongoing is defined as follows:

- for general programs – eight consecutive weeks with at least one session per week; or
- for camps – five consecutive days.

4-109. The eligible costs do not include the cost of accommodation, travel or food. The eligible costs must be reduced by any reimbursements received unless the reimbursed amount is included in the taxpayer's income.

**Problems With Children's Fitness Credit Vs. Children's Arts Credit**

4-110. By creating two separate concepts, the government has created a somewhat confusing situation for organizations offering programs for children. For example, do ballet lessons involve physical activity or artistic endeavor? Even more challenging are situations where a program involves both types of activity. For example, when a child attends a summer camp, it may involve both physical activity (e.g., swimming) and artistic endeavor (e.g., singing lessons). Going further, the costs of sending a child to camp could also be viewed as deductible child care costs (see Chapter 9).

4-111. Normally the organization issuing the receipt will specify the amounts paid that qualify for either of the credits, or for child care costs. It would be possible to have a receipt from an organization that shows an amount paid for a program qualifying for the fitness credit, a separate amount paid for a program qualifying for the arts credit and another separate amount paid for child care costs. The legislation is clear that double counting is not allowed.

4-112. The relationship between these credits and deductible child care costs will be given further consideration in Chapter 9 when we discuss other deductions from income.

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**Exercise Four - 11**

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**Subject:** Child Fitness Tax Credit

Jerod Smithers has enrolled his 12 year old son Buff in a body building program at a cost of \$1,200. The program commences in July, 2013, with a two hour class once per week for a period of 15 consecutive weeks. The cost of the program must be paid in full when the program commences. Buff is in good health and does not have a disability. What is the maximum child fitness tax credit that would be available to John?

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**End of Exercise. Solution available in Study Guide**

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### **First Time Home Buyer's Tax Credit - ITA 118.05**

4-113. A tax credit is available for first-time home buyers who acquire a qualifying home. The credit is equal to 15 percent of the first \$5,000 of the cost of a qualifying home, resulting in a maximum credit of \$750. This amount is not indexed. To be eligible for the credit, the buyer must intend to occupy the home no later than one year after its acquisition.

4-114. An individual will be considered a first-time home buyer if neither the individual nor the individual's spouse or common-law partner, owned and lived in another home in the calendar year of the home purchase or in any of the four preceding calendar years.

4-115. The credit may be claimed by the individual who acquires the home or by that individual's spouse or common-law partner. For the purpose of this credit, a home is considered to be acquired by an individual only if the individual's interest in the home is registered in accordance with the applicable land registration system.

### **Volunteer Firefighters Tax Credit - ITA 118.06**

4-116. There is a tax credit for volunteer firefighters who perform at least 200 hours of volunteer firefighting services during a taxation year. The base for the non-refundable credit is \$3,000. This amount is not indexed.

4-117. If the individual provides paid services to a particular fire department, volunteer hours at that department will not count towards the required 200. There is an exemption under ITA 81(4)(b) for up to \$1,000 in compensation received for volunteer firefighting duties. This exemption is not available to individuals who claim the tax credit for volunteer firefighters.

### **Charitable Donations Tax Credit - ITA 118.1**

#### ***Extent Of Coverage In This Chapter***

4-118. For tax purposes, donations, even in the form of cash, are segregated into categories, each with a different set of rules. Additional complications arise when non-cash donations are made. To be able to deal with gifts of depreciable capital property, a full understanding of capital gains and CCA procedures is required. Given these complications, a comprehensive treatment of charitable gifts is deferred until we revisit Taxable Income and Tax Payable in Chapter 11. However, there is limited coverage of charitable donations in this Chapter including the First-Time Donor's Super Credit (FDSC) that was proposed in the 2013 budget.

#### ***Eligible Gifts***

4-119. In our coverage of donations in this Chapter, we will deal only with gifts of cash or monetary assets. Donations of other types of property are covered in Chapter 11.

4-120. In this Chapter, our coverage will be limited to what is referred to in ITA 118.1 as total charitable gifts. These include amounts donated to entities such as:

- a registered charity;
- a registered Canadian amateur athletic association;
- a Canadian municipality;
- the Canadian government;
- a university outside of Canada which normally enrolls Canadian students; and
- a charitable organization outside of Canada to which the Canadian government made a gift in the current or preceding taxation year.

#### ***Limits On Amount Claimed***

4-121. It is the policy of the government to limit the amount of charitable donations that are eligible for the tax credit to a portion of a taxpayer's Net Income For Tax Purposes. Note that, while corporations deduct their donations from Taxable Income as opposed to receiving a credit against Tax Payable, the limits on the amount of eligible donations are the same for corporations as they are for individuals.

4-122. The general limit on eligible amounts of charitable gifts is 75 percent of Net Income For Tax Purposes. For individuals, this limit is increased to 100 percent of Net Income For Tax Purposes in the year of death and the preceding year.

### **Calculating The Credit (Without The First-Time Donor's Super Credit)**

4-123. Once the contribution base is established, the credit is equal to 15 percent of the first \$200, and 29 percent of any additional donations. The charitable donations credit is the only credit that features two rates for determining the allowable credit. The reason for this approach was concern that, because charitable donations are voluntary, an overall credit at the lowest bracket rate of 15 percent would have resulted in a decline in donations from individual with high incomes. The 29 percent credit on donations over \$200 was added in order to encourage larger donations.

4-124. While the same level of total giving could probably have been achieved with a compromise rate somewhere between 15 and 29 percent, this would have changed the composition of sources for donations. Such a compromise rate would have been an incentive for low income donors and would have increased donations to organizations such as churches that rely on this sector of the population. In contrast, high income donors would have less incentive to contribute, and this would have reduced donations to such beneficiaries as educational institutions. The government did not view this as a desirable result and, as a consequence, we have a two rate system for charitable donations.

4-125. The following example illustrates the calculation of the charitable donations tax credit, including the determination of eligible amounts:

**Example** Nancy Hart has 2013 Net Income For Tax Purposes of \$100,000 and Taxable Income of \$40,000. On the receipt of a large inheritance, she makes a charitable donation of \$15,000. She chooses to claim only \$2,000 in donations in 2013.

**Analysis** The total for all eligible gifts is limited to 75 percent of her Net Income For Tax Purposes, or \$75,000. As her gift is less than \$75,000, she could have claimed all of it. However, since she has chosen to claim \$2,000, \$13,000 (\$15,000 - \$2,000) in donations are carried forward. Her 2013 tax credit would be calculated as follows:

|   |              |
|---|--------------|
| 15 Percent Of \$200                     | \$ 30        |
| 29 Percent Of \$1,800 (\$2,000 - \$200) | 522          |
| <b>Total Credit</b>                     | <b>\$552</b> |

4-126. For couples, the CRA's administrative practices permit either spouse or common-law partner to claim all of the donations made by both spouses or common-law partners. Given the dual rates on the credit, there is a small advantage in combining the donations. In addition, this may be an important consideration when one spouse has a sufficiently low income that it is limiting the use of his or her donations.

### **First-Time Donor's Super Credit (FDSC)**

4-127. In a move designed to encourage charitable giving by new donors, especially young new donors, the 2013 budget proposes a temporary First-Time Donor's Super Credit (FDSC). This credit, which is added to the regular donations tax credit, provides an additional 25 percent credit on up to \$1,000 in eligible donations. In effect, this means that the first \$200 of donations will receive a credit of 40 percent (15% + 25%), while an additional amount of \$800 will receive a credit of 54 percent (29% + 25%).

4-128. An individual will be considered a first-time donor if neither the individual nor the individual's spouse or common-law partner has claimed a charitable donations tax credit since 2007 (the 5 years preceding 2013). The FDSC may be shared by first-time donor couples. In additions, couples must share the \$1,000 limit.

4-129. The FDSC is a one time benefit to taxpayers and it has a total value at the federal level of \$250 [(25%)(1,000)]. The FDSC is available for use in any taxation year prior to 2018. For

contributions made in 2013, this creates the same 5 year carried forward that is generally available with respect to charitable donation tax credits.

### Carry Forward Of Charitable Donations

4-130. With the limit set at 75 percent of Net Income, individuals will normally be able to claim all of the donations that they make in a year. However, if their donations exceed the 75 percent limit, or they choose not to claim all of the donations that year, any unused amounts can be carried forward and used in the subsequent five year period.

4-131. A further point here is that this limit is based on Net Income For Tax Purposes. This means that an individual could have eligible donations in excess of Taxable Income. This could occur, for example, if the individual deducted a large loss carry forward from a previous year. In situations such as this, it is important to recognize that the charitable donations tax credit is non-refundable. Given this, only the amount of donations required to reduce Tax Payable to nil should be claimed. Any additional amounts should be carried forward to future periods. Any claim that does not serve to reduce Tax Payable will simply be lost.

**Example** Barry Mann has Net Income For Tax Purposes of \$80,000. This is reduced to a Taxable Income of \$20,000 because of a large business loss carry forward from a previous year. Because of a fortuitous lottery win, he chooses to make a charitable donation of \$100,000.

**Analysis** The potential base for Barry's charitable donations tax credit is \$60,000 [(75%)(80,000)]. However, if he were to claim this amount, the credit of \$17,372 [(15%)(200) + (29%)(59,800)] would be far in excess of the Tax Payable on only \$20,000 of Taxable Income. Claiming the maximum amount would result in simply losing the greater part of the available credit. The preferable alternative would be to claim only enough to reduce his Tax Payable to nil and carry the remainder forward.

4-132. Determining the specific amounts to be used and carried forward will be discussed in Chapter 11.

## Exercise Four - 12

**Subject:** Charitable Donations Tax Credit

Marion Scalpal has Net Income For Tax Purposes of \$65,000 in 2013. In addition during 2013, after years of losses at her local casino, her luck changes and she wins over \$200,000. As she had promised in her prayers, she immediately donates \$100,000 to her church. She chooses to claim \$10,000 of her donation in 2013. Determine her charitable donations tax credit for 2013, assuming (1) that Marion is not eligible for the FDSC, and (2) that Marion is eligible for the FDSC. Until what year can she claim any unused portions of her 2013 donation?

**End of Exercise. Solution available in Study Guide.**

## Medical Expense Tax Credit - ITA 118.2

### Qualifying Medical Expenses

4-133. There are many types of medical expenses which qualify for the credit under ITA 118.2. (For more detailed information see S1-F1-C1, *Medical Expense Tax Credit*.) The list of qualifying medical expenses has been repeatedly extended in various budgets and includes amounts paid for:

- the services of authorized medical practitioners, dentists and registered nurses,
- artificial limbs, aids and other devices and equipment,
- products required because of incontinence,
- prescription eyeglasses or contact lenses,



- oxygen tents,
- guide and hearing-ear dogs and other specially trained animals,
- the costs of arranging a bone marrow or organ transplant,
- the costs of home modifications for those with severe mobility restrictions, and to allow individuals confined to a wheelchair to be mobile within their home,
- the cost of rehabilitative therapy to adjust for speech or hearing loss,
- devices and equipment listed in ITR 5700 and prescribed by a medical practitioner,
- preventive, diagnostic and other laboratory work,
- prescribed drugs, medicaments and other preparations or substances,
- dentures, and
- premiums to private health services plan

4-134. Although payments for attendants, nursing home care and care in an institution are qualifying medical expenses, there are many complications with claiming these expenses. They will be briefly covered after we have dealt with the disability tax credit.

4-135. Not all budget changes have expanded the list of qualifying expenditures. Costs incurred for purely cosmetic reasons no longer qualify for the medical expense tax credit. Examples of non-qualifying procedures include liposuction, hair replacement procedures, Botox injections and teeth whitening. Cosmetic procedures continue to qualify if they are required for medical or reconstructive purposes (e.g., facial surgery required due to a car accident). Somewhat amusingly, the CRA refused to deal with the question of whether male infant circumcision was, or was not, cosmetic.

4-136. An important qualifying factor here is the fact that the provinces control the identification of authorized medical practitioners for purposes of this credit. For example, only Alberta, British Columbia, and Quebec consider acupuncturists to be authorized. Similarly, massage therapists are considered authorized in British Columbia, Newfoundland, and Ontario, but not in other provinces. This means that there is considerable variation between the provinces in the types of costs that qualify for the medical expense tax credit.

### ***Determining The Credit***

4-137. Qualifying medical expenses of an individual do not include any expense for which the individual has been, or is entitled to be, reimbursed unless the amount is required to be included in income. An amount reimbursed under a public or private medical, dental or hospitalization plan would not qualify for purposes of the medical expense tax credit.

4-138. The medical expense tax credit is determined by the following formula:

**A [(B - C) + D],** where:

**A** is the appropriate percentage for the taxation year (15 percent).

**B** is the total of an individual's medical expenses for himself, his spouse or common-law partner, and any of his children who have not reached 18 years of age at the end of the year.

**C** is the lesser of 3 percent of the individual's Net Income For Tax Purposes and \$2,152 (2013 figure). Note that the B - C total cannot be negative.

**D** is the total of all amounts each of which is, in respect of a dependant of the individual (other than a child of the individual who has not attained the age of 18 years before the end of the taxation year), the amount determined by the formula

**E - F,** where:

**E** is the total of the dependant's medical expenses

**F** is the lesser of 3 percent of the dependant's Net Income For Tax Purposes and \$2,152 (2013 figure).

*Other Tax Credits For Individuals*

4-139. If the taxpayer has no dependants who are 18 years of age or older, components D, E and F in the formula are not relevant (see Paragraph 4-66 for the definition of dependant found in ITA 118(6)). In this case, the credit base is equal to the total of the qualifying medical expenses of the individual taxpayer, his spouse or common-law partner, and his minor children. This balance is reduced by the lesser of 3 percent of the taxpayer's income and an indexed figure which for 2013 is equal to \$2,152. This latter figure will be the limiting factor once an individual's 2013 Net Income For Tax Purposes reaches \$71,733 ( $\$2,152 \div 3\%$ ).

4-140. If the taxpayer has dependants who are 18 years of age or older, a separate credit base calculation is required for each of these dependants. This credit base is equal to the dependant's qualifying medical expenses, reduced by the lesser of 3 percent of the dependant's Net Income For Tax Purposes and \$2,152 (E and F in the formula). The taxpayer adds the total of these amounts to the credit base calculated for the taxpayer, his spouse or common-law partner and his minor children.

4-141. A further point here relates to who actually pays for medical expenses. The credit is only available to the individual who pays the eligible amounts. For an individual to claim the medical expenses of a child or other dependant, he must have paid them. Correspondingly, if the individual makes the payment, the child or dependant cannot claim the payment for the credit.

**Twelve Month Period**

4-142. Medical expenses can be claimed for any period of 12 months that ends in the taxation year. This provision is extended to 24 months in the year of death. The ability to claim expenses for a 12 month period ending in the year is advantageous for individuals with large expenses in a 12 month period other than a calendar year.

**Example** Alex Lau has Net Income For Tax Purposes of \$60,000 in both 2012 and 2013. In July, 2012, he began a year long (and very painful) corrective dental surgery program. During July to December, 2012 he paid \$10,000 in dental fees. During January to June, 2013 he paid \$12,000 in dental fees.

**Analysis** The 2012 claim could be deferred and the \$22,000 total could be claimed in full in the 2013 taxation year. The advantage of doing this is that the threshold amount reduction would be applied only once in 2013. If medical expenses had to be claimed in the year in which they were incurred, Mr. Lau would have to apply the threshold reduction of \$1,800 [ $(3\%)(\$60,000)$ ] in both years. If the full amount is claimed in 2013, federal tax savings would total \$270 [ $(15\%)(\$1,800)$ ].

**Example Of Medical Expense Tax Credit Calculation**

4-143. The following example will serve to illustrate the application of the medical expense tax credit formula:

**Example** Sam Jonas and his dependent family members had the following Net Income For Tax Purposes and medical expenses for 2013. Sam paid for all of the medical expenses.

| <b>Individual</b>                       | <b>Net<br/>Income</b> | <b>Medical<br/>Expenses</b> |
|---|-----------------------|-----------------------------|
| Sam Jonas                               | \$100,000             | \$ 5,000                    |
| Kelly (Sam's Wife)                      | 12,000                | 4,400                       |
| Sue (Sam's 16 Year Old Daughter)        | 8,500                 | 4,100                       |
| Sharon (Sam's 69 Year Old Mother)       | 6,000                 | 16,500                      |
| Martin (Sam's 70 Year Old Blind Father) | 12,000                | 4,000                       |
| <b>Total Medical Expenses</b>           |                       | <b>\$34,000</b>             |

**Analysis** Sam's 2013 medical expense tax credit, using the formula in Paragraph 4-138, would be calculated as follows:

|   |          |          |
|---|----------|----------|
| <b>Amount B</b> Qualifying Expenses (\$5,000 + \$4,400 + \$4,100) |          | \$13,500 |
| <b>Amount C</b>   |          |          |
| Lesser Of:  |          |          |
| • [(3%)(\$100,000)] = \$3,000                                     |          |          |
| • 2013 Threshold Amount = \$2,152                                 |          | ( 2,152) |
| Subtotal  |          | \$11,348 |
| <b>Amount D</b>   |          |          |
| Sharon's Medical Expenses   | \$16,500 |          |
| Reduced By The Lesser Of:   |          |          |
| • \$2,152   |          |          |
| • [(3%)(\$6,000)] = \$180   | ( 180)   | 16,320   |
| Martin's Medical Expenses   | \$ 4,000 |          |
| Reduced By The Lesser Of:   |          |          |
| • \$2,152   |          |          |
| • [(3%)(\$12,000)] = \$360  | ( 360)   | 3,640    |
| Allowable Amount Of Medical Expenses                              |          | \$31,308 |
| <b>Amount A</b> The Appropriate Rate (Minimum Rate)               |          | 15%      |
| Medical Expense Tax Credit  |          | \$ 4,696 |

### Exercise Four - 13

**Subject:** Medical Expense Tax Credit

Ms. Maxine Davies and her spouse, Lance Davies, have 2013 medical expenses which total \$4,330. While Ms. Davies has 2013 Net Income For Tax Purposes of \$150,000, Lance has no income during the year. They have two children. Their 12 year old daughter, Mandy, has 2013 medical expenses of \$4,600 and no Net Income For Tax Purposes. Their 21 year old son, Max, has 2013 medical expenses of \$8,425 and Net Income For Tax Purposes of \$8,250. Ms. Davies pays all of the medical expenses. Determine Ms. Davies' medical expense tax credit for 2013.

**End of Exercise. Solution available in Study Guide.**

### Refundable Medical Expense Supplement - ITA 122.51

4-144. The tax credits that we have discussed to this point are referred to as non-refundable. This means that, if the individual does not have sufficient Tax Payable to use the credit, it is of no benefit to the taxpayer. In contrast, there are a limited number of refundable credits. In the case of these credits, if the individual does not have sufficient Tax Payable to use the credit, the government will issue a cheque for the unused amount. The ITA 122.51 refundable medical expense supplement is this type of credit.

4-145. To be eligible for the 2013 medical expense supplement, the individual must be 18 or over at the end of the year, and must have earned income (employment or business) of at least \$3,333. The credit is the lesser of \$1,142 and 25/15 of the medical expense tax credit that can be claimed for the year. This can also be described as 25 percent of the expenses eligible for the medical expense tax credit plus 25 percent of the disability supports deduction (see Paragraph 4-158).

4-146. The lesser amount is reduced by 5 percent of "family net income" in excess of an indexed threshold amount. Family net income is the sum of the income of the taxpayer and his spouse or common-law partner, but not that of an eligible dependant. For 2013, the income threshold is \$25,278 and the credit is completely eliminated when family net income reaches \$48,118. A simple example will serve to illustrate this provision:

**Example** For 2013, Mr. Larry Futon and his spouse have medical expenses that total \$4,650. His Net Income For Tax Purposes is \$26,900, all of which qualifies as earned income. His spouse has Net Income For Tax Purposes of \$500. Mr. Futon claims the caregiver tax credit for his mother who has Net Income of \$8,000. She is not mentally or physically infirm.

**Analysis** Mr. Futon's allowable medical expenses for tax credit purposes would be \$3,843 [ $\$4,650 - (3\%)(\$26,900)$ ], resulting in a tax credit of \$576 [(15%)(\\$3,843)]. Given this, 25/15 of the credit, or alternatively, 25 percent of the allowable medical expenses, would equal \$961. Since this is less than the maximum of \$1,142, his refundable credit would be \$961 less a reduction of \$106 [(5%)(\\$26,900 + \$500 - \$25,278)], leaving a balance of \$855 (\$961 - \$106).

4-147. The receipt of this refundable credit does not affect an individual's ability to claim a tax credit for the same medical expenses that are used to calculate the refundable credit. Assuming he has no tax credits other than the basic personal, spousal, caregiver, and medical expense, his federal Tax Payable would be reduced to nil {[15%][\\$26,900 - \$11,038 - (\$11,038 - \$500) - \$4,490 - \$3,843]}. This means that he will be able to claim the entire \$855 as a refund.

### Exercise Four - 14

**Subject:** Refundable Medical Expense Supplement

During 2013, Ms. Lara Brunt and her common-law partner, Sara, have medical expenses that total \$6,250. Her Net Income For Tax Purposes is \$26,400, all of which qualifies as earned income. Sara has no income of her own. Determine Lara's minimum Tax Payable for 2013.

**End of Exercise. Solution available in Study Guide.**

## Disability Tax Credit - ITA 118.3

### Calculation

4-148. The disability credit is available under ITA 118.3 and, for 2013, it is equal to \$1,155 [(15%)( \$7,697)]. In addition, there is a supplement to this amount for a disabled child who is under the age of 18 at the end of the year. For 2013, the base for the supplement is \$4,490, providing a total credit for a disabled minor of \$1,828 [(15%)(\\$7,697 + \$4,490)]. Note, however, that the supplement amount of \$4,490 is reduced by the total of amounts paid for attendant care or supervision in excess of \$2,630 that are deducted as child care costs, deducted as a disability support amount, or claimed as a medical expense in calculating the medical expense tax credit. This means that once such costs reach \$7,120 for the year, the supplement is completely eliminated.

4-149. To qualify for this credit, the requirement is that the impairment must be such that there is a "marked" restriction of the activities of daily living or a "significant" restriction in more than one activity (while both terms are undefined, it appears that significant is less severe than marked). In addition, it must have lasted, or be expected to last, for at least 12 months.

4-150. In general, a medical doctor, or optometrist, must certify on Form T2201 that a severe physical or mental impairment exists. In the case of restrictions on the ability to walk, a physiotherapist can make the required certification.

4-151. ITA 118.4(1) tries to make the conditions for qualifying for this credit as clear as possible. This Subsection points out that an individual clearly qualifies if they are blind. They also qualify if 90 percent of the time they cannot perform, or take an inordinate amount of time to perform, a basic activity of daily living. The following are listed as basic activities:

- mental functions necessary for everyday life;

- feeding oneself or dressing oneself;
- speaking such that the individual can be understood in a quiet setting by someone familiar with the individual;
- hearing such that the individual can, in a quiet setting, understand someone familiar with the individual;
- bowel or bladder functions; or
- walking.

### **Disability Credit Transfer To A Supporting Person**

4-152. In many cases, an individual who is sufficiently infirm to qualify for the disability credit will not have sufficient Tax Payable to use it. In this situation, all or part of the credit may be transferred to a spouse, or a supporting person who claimed the disabled individual as:

- a dependant under the eligible dependant provision [ITA 118(1)(b)];
- a dependant for purposes of the caregiver tax credit [ITA 118(1)(c.1)]; or
- a disabled dependant over 17 [ITA 118(1)(d)].

4-153. In order to make the disability credit transfer available in situations where there is a disabled dependant who does not qualify for one of these credits, the transfer is extended by a somewhat awkward measure to situations in which the supporting person:

- could have claimed the eligible dependant credit, if neither the supporting person nor the disabled dependant were married; or
- could have claimed the disabled dependant over 17, or the caregiver credit, if the dependant had been 18 years of age or older and had no income.

4-154. The amount that can be transferred is the same \$1,155 (or \$1,828 if the full under 18 supplement is available) that could be claimed by the disabled individual. However, if the disabled individual has Tax Payable in excess of credits under ITA 118 (personal credits), 118.01 to 118.06 (various credits including adoption expenses and child fitness credits) and 118.7 (CPP and EI credits), the credit must first be applied to reduce the disabled individual's Tax Payable to nil. If a balance remains after all Tax Payable has been eliminated, it can then be transferred to the supporting person.

4-155. Work on the new Income Tax Folios has resulted in three Chapters in Folio 1, "Health and Medical" (as of April 30, 2013). S1-F1-C2, "Disability Tax Credit" provides detailed guidance on the disability tax credit, including its transfer to a supporting person.

## **Exercise Four - 15**

**Subject:** Disability Tax Credit

John Leslie lives with his wife and 21 year old blind son, Keith, who qualifies for the disability tax credit. Keith has no income of his own. During 2013, John paid medical expenses of \$16,240 for Keith. None of these expenses involve attendant care. His Taxable Income for 2013 was \$100,000. Determine the total amount of tax credits related to Keith that will be available to John.

**End of Exercise. Solution available in Study Guide.**

### **Other Credits And Deductions Related To Disabilities**

4-156. For disabled individuals who earn employment or business income, the "working income tax benefit supplement" provides an additional amount for individuals who qualify for the disability tax credit. This benefit is covered beginning at Paragraph 4-208

4-157. Disabled individuals, or a supporting person, may have paid significant medical expenses involving attendant care and/or nursing home care. The availability of the medical expense tax credit for these costs is limited by the following considerations:

- Neither the individual, nor a supporting person, can claim the disability credit if a medical expense credit is claimed for a full time attendant, or for full time care in a nursing home. However, the individual or supporting person can claim either of the two amounts.
- The disability credit can be claimed if a medical expense credit is claimed for a part-time attendant. Part-time is defined as expenses claimed of less than \$10,000 for the year (\$20,000 in the year of death). Note that part-time attendant care can only be claimed as a medical expense credit if no part of that care is claimed as child care costs or for attendant care required to produce income.

4-158. For disabled individuals who work, or who attend a designated educational institution or secondary school, the disability supports deduction provides tax relief for a number of medical expenses, including attendant care, which would assist a disabled person to work or go to school. (See Chapter 9, Other Income, Other Deductions And Other Issues for coverage of this deduction.)

4-159. There are complications and restrictions related to claiming these and many other types of medical expenses. Complete coverage of all the relevant rules goes beyond the scope of this text. For those interested in this subject, we refer you to the new Income Tax Folio 1, "Health and Medical". The three Chapters (as of April 30, 2013) provide detailed guidance on the medical expense tax credit (S1-F1-C1), disability tax credit (S1-F1-C2) and disability supports deduction (S1-F1-C3).

## Education Related Tax Credits

### **Tuition Fees Tax Credit - ITA 118.5(1) To ITA 118.5(4)**

4-160. Under ITA 118.5, individuals receive a credit against Tax Payable equal to 15 percent of qualifying tuition fees paid with respect to the calendar year, regardless of the year in which they are actually paid. The fees must total at least \$100, but there is no upper limit on this credit. The following tuition fees qualify:

- Tuition fees paid to a university, college, or other institution for post-secondary courses located in Canada.
- Tuition fees paid to an institution certified by the Minister of Human Resources and Skills Development for a course that developed or improved skills in an occupation (the individual must be 16 or older).
- Tuition fees paid to a university outside Canada. To qualify the course must have a minimum duration of 3 weeks.
- For individuals who live near the U.S. border and commute, tuition fees paid to a U.S. college or university for part-time studies.

### **Examination Fees Included In Tuition Fees Tax Credit**

4-161. To qualify for this credit, the fees must exceed \$100. The credit base includes ancillary fees such as the cost of examination materials or required identification cards. It does not include the costs for travel, parking, or required equipment (e.g., computers).

4-162. In addition to fees for university examinations, the credit base includes fees for professional examinations such as bar examinations and examinations required by the CPAs, CGAs, CAs, or CMAs. It does not, however, include fees for examinations required for entrance to professional programs (e.g., the CMA entrance examination).

### **Ancillary Fees Included In Tuition Fees Tax Credit**

4-163. It has been noted that universities are relying more heavily on ancillary fees for such items as health services, athletics, and various other services. As a reflection of this situation, ITA 118.5(3) extends the tuition fees tax credit to cover all mandatory ancillary fees that are imposed by universities on all of their full time, or all of their part-time students. In addition, ITA 118.5(3)(d) allows up to \$250 in such ancillary fees to be added to the total, even if they do not meet the condition of being required for all full or part-time students.

**Education Tax Credit - ITA 118.6(2)**

4-164. Under ITA 118.6(2), there is a credit for 2013 equal to \$60 [(15%)(400)] per month of full time attendance at a designated educational institution or enrollment in a “qualifying educational program”. For this purpose, designated educational institutions include universities, colleges, and institutions certified by the Minister of Human Resource And Skills Development for a course that develops or improves skills in an occupation.

4-165. Enrollment in a qualifying educational program is described in S1-F2-C1, "Education And Textbook Tax Credits" as a program that runs for at least 3 consecutive weeks and must require instruction or work in the program of at least 10 hours a week throughout its duration. Both of these descriptions can be thought of as full time pursuit of educational activities.

4-166. An alternative education credit of \$18 [(15%)(120)] per month is available for attendance in a “specified educational program”. This credit is normally claimed by part-time students. In general terms, this is defined as a program that, were it not for the 10 hours per week requirement, would be a qualifying educational program. This means that, while a specified educational program must run for at least 3 consecutive weeks, there is no minimum hours of work required to comply with the definition.

4-167. For individuals who either qualify for the disability tax credit or, because of a mental or physical disability, cannot pursue educational activities on a full time basis, the full education credit of \$60 per month is available, without regard to whether their attendance is full or part-time.

**Textbook Tax Credit - ITA 118.6(2.1)**

4-168. While this credit is described as a “textbook” tax credit, it is not based on an actual purchase of such books. Rather, it is simply an addition to the education credit. This “textbook” credit is equal to \$10 [(15%)(65)] for each month in which the student is entitled to claim the education credit as a full-time student, or \$3 [(15%)(20)] for each month in which the student is entitled to claim the education credit as a part-time student.

4-169. This credit is added to the tuition and education credits as part of the amount that is eligible for a carry forward by the student (see Paragraph 4-167). It is also added to these credits in determining the amount that can be transferred to a spouse, parent or grandparent (see Paragraph 4-177). As was the case with the education credit, students who qualify for the disability tax credit or, because of mental or physical disability, cannot pursue full time education activities, will receive the full \$10 per month textbook credit.

**Interest On Student Loans Tax Credit - ITA 118.62**

4-170. There is a credit available under ITA 118.62 if a student or a related person has paid interest on student loans. The credit for the student is equal to 15 percent of interest paid in the year, or in any of the five preceding years. The interest paid must be on a loan under the *Canada Student Loans Act*, the *Canada Student Financial Assistance Act*, or a provincial statute governing the granting of financial assistance to students at the post-secondary school level.

**Education Related Issues With Employee Benefits**

4-171. It is not uncommon for employers to provide education assistance, the most common form being reimbursement for tuition fees. In situations where the employer pays for an employee's tuition, the employee can only claim the tuition tax credit if the payment was included in the employee's income as a taxable benefit.

4-172. With respect to the education and textbook credits, they are only available for a "qualifying" educational program. The ITA 118.6(1) definition of a qualifying educational program excludes the program if the student receives, from a person with whom the student is dealing at arm's length, any allowance, benefit, grant or reimbursement for expenses in respect of the program. It would appear that this means that, if any payments for the program are received from an employer, without regard to whether they create a taxable benefit, the education and textbook credits are not be available to the recipient of the payment.

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**Exercise Four - 16**

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**Subject:** Education Related Tax Credits

During 2013, Sarah Bright attends university for four months of full time study and two months of part-time study. Her total tuition for the year, including all ancillary fees, is \$3,200 of which she prepaid \$1,000 in 2012. The amount paid in 2013 includes \$400 in fees that are only charged to students in her geology program. Interest paid for the year on her student loan was \$325. Determine the total amount of education related tax credits that would be available for Ms. Bright for 2013.

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**End of Exercise. Solution available in Study Guide.**

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**Carry Forward Of Tuition, Education, And Textbook Credits - ITA 118.61**

4-173. There are situations in which a student does not have sufficient Tax Payable to use their tuition, education, and textbook credits and, in addition, has not transferred them to a spouse, parent, or grandparent (see Paragraph 4-177). To deal with this type of situation, ITA 118.61 allows a carry forward of unused tuition, education, and textbook credits. There is no time limit on this carry forward. In addition, ITA 118.62 provides for a 5 year carry forward of unused interest on student loans.

4-174. Unfortunately, the calculation of the amount that is carried forward can be complex. Although the *Income Tax Act* uses Tax Payable and credit amounts to calculate carry forwards and transfers, Schedule 11 in the personal tax return uses Taxable Income and credit base amounts in its calculations. We will explain the *Income Tax Act* approach in the text, but illustrate both approaches in the example in Paragraph 4-181.

4-175. To carry amounts forward, the total available credits must be reduced by the student's Tax Payable, calculated using the following credits (note the medical expense tax credit is not included in the list):

- ITA 118 (Personal)
- ITA 118.01 Through ITA 118.06 (Various credits)
- ITA 118.3 (Disability)
- ITA 118.7 (CPP And EI)

4-176. The available amount is also reduced by transfers to other individuals. The resulting balance can be carried forward and is available for the student's personal use in any subsequent year. However, once it is carried forward, it cannot be transferred to another individual.

**Transfer Of Tuition, Education, And Textbook Credits - ITA 118.9**

4-177. ITA 118.9 provides for a transfer of these tax credits to a parent or grandparent. ITA 118.8 provides for a transfer of these credits (plus several others), to a spouse or common-law partner. ITA 118.81 limits the total amount of tuition, education, and textbook credits that can be transferred under either of these provisions. The transfer is at the discretion of the student and the legislation states that he must indicate in writing the amount that he is willing to transfer.

4-178. The maximum transfer for an individual student is the lesser of the available credits and \$5,000, multiplied by the tax rate for the minimum tax bracket (referred to as the "appropriate percentage"). This amount is \$750 [(15%)(5,000)].

4-179. This \$750 maximum amount must be reduced by the student's Tax Payable calculated after the same credits used to calculate the carry forward of education related credits. As described in Paragraph 4-175, these are the credits available under ITA 118 through ITA 118.06, 118.3 and 118.7. Added to the list for this purpose are any education related credits carried forward from a previous year under ITA 118.61. If these credits reduce the student's Tax Payable to nil, the full \$750 is available for transfer.



4-180. The \$750 limit is on a per student basis. A parent or grandparent could have \$750 transfers from any number of children or grandchildren. For obvious reasons, transfers from more than one spouse would not be acceptable for tax purposes (tax considerations might be the least of such an individual's problems). If the student is married, the supporting parent or grandparent can make the claim only if the student's spouse did not claim the spousal credit, or any unused credits transferred by the student (see Paragraph 4-189).

4-181. An example will serve to illustrate both the ITA 118.9 transfer, as well as the ITA 118.81 limits on this transfer.

**Example** Megan Doxy has 2013 Taxable Income of \$12,000, all of which is rental income. She attends university full time for 8 months of the year, paying a total amount for tuition of \$8,000. This gives her a tuition amount of \$8,000, an education amount of \$3,200 [(8)(\$400)], and a textbook amount of \$520 [(8)(\$65)], a total of \$11,720. Her only other tax credit is her personal amount of \$1,656 [(15%)(11,038)]. She would like to transfer the maximum credits to her father.

**Analysis - Income Tax Act Approach** Megan's education related credits total \$1,758 [(15%)(8,000 + 3,200 + 520)], well in excess of the maximum transfer of \$750. However, this maximum of \$750 would have to be reduced by Megan's Tax Payable after the deduction of her personal amount. This amount would be \$144 [(15%)(12,000 - 11,038)], leaving a maximum transfer of \$606 (\$750 - \$144). This would leave Megan with remaining unused credits of \$1,008 (\$1,758 - \$144 - \$606) which can be carried forward to future years, for her own use. These calculations are the result of using the approach presented in the *Income Tax Act*.

**Analysis - Tax Return Approach** The alternative calculation approach that is used in the tax return would begin with the total education related amount of \$11,720. The maximum transfer amount in this approach is \$5,000. This would be reduced by \$962 (\$12,000 - 11,038), the excess of Megan's Taxable Income over her basic personal amount. This results in a maximum transfer of \$4,038 (\$5,000 - \$962). Megan's carry forward amount is \$6,720 (\$11,720 - \$962 - \$4,038). Multiplying these amounts by the 15 percent minimum rate will give you the same \$1,008 of unused credits as the calculations using the preceding *Income Tax Act* approach.

### Exercise Four - 17

**Subject:** Carry Forward Of Education Related Credits

At the beginning of 2013, Kerri Holmes has a carry forward of education credits from 2012 of \$300 [(15%)(2,000)]. During 2013, she is in full time attendance at a Canadian university for 8 months of the year. Her tuition fees total \$4,800 for the year. Her Taxable Income for 2013 is \$24,000. Other than education related tax credits, her only tax credit is her basic personal credit. Determine Kerri's total education related tax credits and any available carry forward.

### Exercise Four - 18

**Subject:** Transfer And Carry Forward Of Education Related Credits

Jerry Fall has 2013 Taxable Income of \$11,250. He attends an American university on a full time basis for 11 months of the year, paying a total amount for tuition of \$23,500 (Canadian dollars). His only tax credits, other than education related credits, are his basic personal credit and a medical expense credit of \$233 [(15%)(1,555)]. Determine Jerry's total education related tax credits and indicate how much of this total could be transferred to a parent and how much would be carried forward.

**End of Exercises. Solutions available in Study Guide.**

## Employment Insurance (EI) And Canada Pension Plan (CPP) Tax Credits - ITA 118.7

4-182. ITA 118.7 provides a tax credit equal to 15 percent of the Employment Insurance (EI) premiums paid by an individual, all of the Canada Pension Plan (CPP) contributions paid on employment income, and half of the CPP contributions paid on self-employed income.

4-183. For 2013, an employee's CPP contributions are based on maximum pensionable earnings of \$51,100, less a basic exemption of \$3,500. The rate for 2013 is 4.95 percent, resulting in a maximum contribution of \$2,356 [(4.95%)(51,100 - 3,500)]. This provides for a maximum 2013 credit against federal Tax Payable of \$353 [(15%)(2,356)]. The employer matches the contributions made by the employee. However, this matching payment has no tax consequences for the employee.

4-184. A self-employed individual earning business income must make a matching CPP contribution for himself, effectively paying twice the amount he would as an employee. As discussed in Chapter 9, the matching contribution is a deduction from Net Income For Tax Purposes under ITA 60(e) (a Division B, Subdivision e deduction). This treatment for the matching CPP contribution as a deduction is analogous to the treatment used by employers. This means that a self-employed individual will have a tax credit equal to one-half of his CPP contributions for self-employed income, and a deduction for the remaining one-half.

4-185. For 2013, EI premiums are based on maximum insurable earnings of \$47,400. The employee's rate is 1.88 percent, resulting in a maximum annual premium of \$891. This results in a maximum credit against federal Tax Payable of \$134 [(15%)(891)].

4-186. Employers are also required to pay EI premiums, the amount being 1.4 times the premiums paid by the employee. However, these employer paid premiums have no tax consequences for the employee. While self-employed individuals can elect to participate in the EI program, unlike for the CPP, they do not have to remit the employer share. Their premiums will be limited to the same \$891 that is applicable to employees.

## Overpayment Of EI Premiums And CPP Contributions

4-187. It is not uncommon for employers to withhold EI and CPP amounts that are in excess of the amounts required. This can happen through an error on the part of the employer's payroll system. Even in the absence of errors, overpayments can arise when an individual changes employers. We would note that the CRA's form T2204 is designed to assist taxpayers in calculating the amount of any overpayment.

4-188. A refund of these excess amounts is available when an individual files his tax return. While any CPP or EI overpayment is not part of the base for the tax credit, it will increase the refund available or decrease the tax liability that is calculated in the return.

**Example** Jerry Weist changed employers during 2013 and, as a consequence, the total amount of EI premiums withheld during the year was \$991. In a similar fashion, the total amount of CPP contributions withheld by the two employers was \$2,520. His employment income was well in excess of the maximum insurable and pensionable earnings.

**Analysis** In filing his 2013 tax return, Jerry will claim a refund of \$264, calculated as follows:

|                            |          |              |
|----------------------------|----------|--------------|
| EI Premiums Withheld       | \$ 991   |              |
| 2013 Maximum               | ( 891)   | \$100        |
| CPP Contributions Withheld | \$2,520  |              |
| 2013 Maximum               | ( 2,356) | 164          |
| <b>Refund</b>              |          | <b>\$264</b> |

## Transfers To A Spouse Or Common-Law Partner - ITA 118.8

4-189. In the preceding material, we have covered several tax credits that can be claimed by either spouse, such as the children's fitness credit. There are also a number of tax credits that can usually be transferred to a spouse or common-law partner under ITA 118.8. They are:

- the child tax credit (see Paragraph 4-57)
- the age tax credit (see Paragraph 4-82),
- the pension income tax credit (see Paragraph 4-84),
- the disability tax credit (see Paragraph 4-148), and
- the current year tuition, education, and textbook tax credits to a maximum of \$750 (see material beginning in Paragraph 4-177).

4-190. The maximum amount that can be transferred is based on the sum of the preceding credits, reduced by a modified calculation of the spouse or common-law partner's Tax Payable. While the legislation is based on Tax Payable, the T1 tax return uses a simplified approach based on Taxable Income. This approach starts with the sum of the base for all of the preceding credits. From this amount is subtracted the spouse's taxable income, reduced by the bases of:

- the basic personal credit,
- the Canada employment credit, CPP and EI credits,
- the credits under ITA 118.01 through ITA 118.06 (various credits including public transit fees credit and children's fitness credit),
- the tuition, education and textbook credits.

The resulting remainder, if any, is the amount that can be transferred to a spouse or common-law partner.

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### Exercise Four - 19

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**Subject:** Transfer Of Credits From A Spouse

Mr. Martin Levee is 68 years old and has Net Income For Tax Purposes of \$42,000. Of this total, \$24,000 was from a life annuity that he purchased with funds in his RRSP. His spouse is 66 years old, has no income of her own (she is ineligible for OAS), and is attending university on a full time basis. Her tuition fees for the year were \$2,200 and she was in full time attendance for 4 months of the year. Determine Mr. Levee's maximum federal tax credits for 2013. Ignore the possibility of splitting his pension income with his spouse.

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**End of Exercise. Solution available in Study Guide.**

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**We suggest you work Self Study Problem Four-1 at this point.**

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## Political Contributions Tax Credits - ITA 127(3)

### *Federal Accountability Act*

4-191. While no changes have been made in the *Income Tax Act*, the *Federal Accountability Act* limits the ability to make political contributions to individuals only. More specifically, this Act contains the following provisions:

- There is a total ban on contributions by corporations, trade unions and unincorporated associations.
- The amount that can be contributed annually by an individual:
  - to a registered party is limited to \$1,100,
  - to a candidate or a leadership contestant is limited to \$1,100, and
  - to a nomination contestant is limited to \$1,100.

**Income Tax Rules**

4-192. A federal tax credit is available on monetary political contributions made to a registered federal political party, or to candidates at the time of a federal general election or by-election. The maximum value is \$650 and it is available to both individuals and corporations. However, as discussed in the preceding Paragraph, the *Federal Accountability Act* totally bans contributions by corporations. The credit is calculated as follows:

|                | Contributions | Credit Rate | Tax Credit |
|----------------|---------------|-------------|------------|
| First          | \$ 400        | 3/4         | \$300      |
| Next           | 350           | 1/2         | 175        |
| Next           | 525           | 1/3         | 175        |
| Maximum Credit | \$1,275       |             | \$650      |

4-193. The \$650 credit is achieved when contributions total \$1,275. Contributions in excess of this amount do not generate additional credits. Also note that most provinces have a similar credit against provincial Tax Payable. There is a difference, however, in that the eligible contributions must be made to a registered provincial political party.

**Exercise Four - 20**

**Subject:** Political Contributions Tax Credit

Ms. Vivacia Unger contributes \$785 to the Liberal New Conservative Democratic Party, a registered federal political party. Determine the amount of her federal political contributions tax credit.

**End of Exercise. Solution available in Study Guide.**

**Labour Sponsored Funds Tax Credit - ITA 127.4**

4-194. In an effort by the government to encourage investment in small and medium sized enterprises, ITA 127.4 provides a credit for individuals investing in the shares of prescribed labour sponsored venture capital corporations.

4-195. For purposes of this Section, these corporations must be set up under the appropriate legislation and managed by a labour organization. The assets of the corporation must be invested in small and medium sized businesses. Currently, the federal credit is based on 15 percent of the cost of the labour sponsored venture capital corporation shares purchased by the individual. To be eligible for the credit, the investor must be the first registered holder of the shares. In addition, the maximum credit for a year is \$750. This limits the net cost of investments eligible for the credit to \$5,000.

4-196. The government has concluded that this is not an effective program. Based on this, it will be phased out, beginning in 2015. The credit rate will be reduced to 10 percent in that year, to 5 percent in 2016, and to nil in 2017.

**Exercise Four - 21**

**Subject:** Labour Sponsored Funds Credit

On June 30, 2013, Mr. Brad Clintor purchases newly issued shares in a prescribed labour sponsored venture capital corporation at a cost of \$3,000. The province in which Mr. Clintor lives provides a provincial tax credit for this investment. Determine the amount of the federal tax credit that will result from this purchase.

**End of Exercise. Solution available in Study Guide.**

## Dividend Tax Credit

4-197. The dividend tax credit is covered in Chapter 7 as part of our discussion of property income.

## Foreign Tax Credits

4-198. The credits that are available for taxes paid in foreign jurisdictions are covered in Chapters 7 and 11.

## Investment Tax Credits

4-199. When taxpayers make certain types of expenditures, they become eligible for investment tax credits. These credits reduce federal Tax Payable. While these credits can be claimed by individuals as well as corporations, they are much more commonly used by corporations and, as a consequence, we cover investment tax credits in Chapter 14.

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**We suggest you work Self Study Problem Four-2 to Four-4 at this point.**

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## Refundable Credits

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### Introduction

4-200. With the exception of the refundable medical expense supplement, the credits that we have encountered to this point can be described as non-refundable. This means that, unless the taxpayer has Tax Payable for the current taxation year, there is no current benefit from the credit. Further, with the exception of the charitable donations credit and education related credits, there is no carry forward of these non-refundable credits to subsequent taxation years. This means that, if the credits are not used in the current year, they are permanently lost.

4-201. In contrast, refundable credits are paid to the taxpayer, with regard to whether that individual has a Tax Payable balance. In this section we will describe three of these refundable credits:

- the GST/HST tax credit;
- the working income tax benefit (WITB); and
- the Canada child tax benefit.

4-202. With respect to the GST/HST credit and child tax benefit, our coverage will be limited. This reflects the fact that, unlike non-refundable credits, taxpayers do not calculate the eligible amount of these credits in their tax returns. Rather, the CRA calculates the credits from the tax returns that the taxpayer has filed in previous years and pays these amounts to the eligible taxpayers. Given this, there is no need to provide coverage of the detailed calculation of these credits.

### Refundable GST/HST Credit - ITA 122.5

4-203. One of the major problems with the goods and services tax (GST) is the fact that it is a regressive tax. In order to provide some relief from the impact of the GST on low income families, there is a refundable GST credit available under ITA 122.5.

4-204. The GST credit is determined by the CRA on the basis of eligibility information supplied in the individual's tax returns for previous years. Because of this, it is only paid to individuals who file tax returns.

4-205. For 2013, the system provides for a total credit that is calculated as follows:

- \$265 for the "eligible individual". An eligible individual includes a Canadian resident who is 19 years of age or over during the current taxation year, or is married or living common-law, or is a parent who resides with their child. In the case of a married couple, only one spouse can be an eligible individual.

*Refundable Credits*

- \$265 for a “qualified relation”. A qualified relation is defined as a cohabiting spouse or common-law partner. If the eligible individual does not have a qualified relation, he is entitled to an additional credit that is the lesser of \$139 and 2 percent of the individual’s Net Income For Tax Purposes in excess of \$8,608.
- \$265 for a dependant eligible for the eligible dependant tax credit.
- \$139 for each “qualified dependant”. A “qualified dependant” is defined as a person who is the individual's child or is dependent on the individual or the individual's cohabiting spouse or common-law partner for support. In addition, the child or dependent person must be under 19 years of age, reside with the individual, have never had a spouse or common-law partner, and have never been a parent of a child he has resided with.

4-206. The total of these amounts must be reduced by 5 percent of the excess of the individual’s “adjusted income” over an indexed threshold amount. For 2013, this threshold amount is \$34,561. “Adjusted Income” is defined as total income of the individual and his qualified relation, if any.

4-207. The refundable GST credit is available to all eligible individuals, without regard to whether they have Tax Payable. The amount of the credit is calculated by the CRA on the basis of information included in the individual’s tax return for a particular year, and the amounts are automatically paid to the taxpayer in subsequent years.

## Working Income Tax Benefit - ITA 122.7

### *The Welfare Wall*

4-208. Despite the rantings of ostensibly virtuous individuals of a right-wing persuasion, many individuals who are receiving various types of social assistance are not necessarily lazy or lacking in motivation. The simple fact is that, given the types of wages such individuals receive, they are often better off economically if they do not work. The types of wages that such individuals can earn are typically at the legal “minimum” (e.g., the minimum wage ranges from \$9.50 in Saskatchewan to \$10.25 per hour in British Columbia, Manitoba, and Ontario). The amounts earned at this wage are typically offset by reductions in social assistance payments. Additional negative effects flow from loss of subsidized housing, prescription drug assistance, and other benefits that flow to individuals with little or no income.

4-209. It has been demonstrated that, if such individuals find employment, the result can be a reduction in their real income. Instead of rewarding their efforts, our current system can actually punish individuals who make an effort to improve their economic status. This is commonly referred to as the welfare wall.

### *Calculation Of The Basic Working Income Tax Benefit (WITB)*

4-210. To assist eligible working low income individuals, ITA 122.7 provides for a working income tax benefit (WITB). This refundable tax credit is available to “eligible” individuals who are 19 years of age or older and who were not full-time students for more than 13 weeks in the year, or in prison for 90 days or more during the year. Note that, if the individual has an eligible dependant, they qualify for the benefit, even if they are a full time student.

4-211. The benefit is paid on the basis of working income. Working income is defined as gross employment income (i.e., no employment expenses deducted), business income, scholarships, and research grants. The amount of the benefit will depend on whether the individual is single or, alternatively, has a spouse or an eligible dependant. For this purpose, an eligible dependant is a child who lives with the individual and who is under the age of 19 at the end of the year. For 2013 the benefit is calculated as follows:

**Single Individual** In this case, the benefit is equal to the lesser of:

- 25 percent of the individual’s working income in excess of \$3,000; and
- \$989.

This means that the benefit reaches a maximum value of \$989 when working income is

\$6,956 [ $\$3,000 + (\$989 \div 25\%)$ ]. The benefit remains at this level until working income reaches \$11,231. The benefit is reduced by 15 percent of working income in excess of \$11,231. It disappears completely when working income reaches \$17,827.

**Family (Eligible Spouse Or Eligible Dependant)** In this case, the benefit is equal to the lesser of:

- 25 percent of the family working income in excess of \$3,000; and
- \$1,797.

Family working income is the working income of the individual plus that of his spouse or common-law partner, but not that of an eligible dependant. The benefit reaches a maximum value of \$1,797 when family working income is \$10,188 [ $\$3,000 + (\$1,797 \div 25\%)$ ]. The benefit remains at this level until family working income reaches \$15,509. The benefit is reduced by 15 percent of family working income in excess of \$15,509. It disappears completely when family working income reaches \$27,489.

### WITB Disability Supplement

4-212. For individuals qualifying for the disability tax credit, a WITB disability supplement is available. For a single individual, the amount is the lesser of \$495 and 25 percent of working income in excess of \$1,150. For details of the phase out of this benefit, we would refer you to the CRA web site.

## Exercise Four - 22

**Subject:** Working Income Tax Benefit (WITB)

Both Angelina and her common-law partner are employed during 2013. Angelina is an eligible individual and her common-law partner is an eligible spouse for the purposes of the working income tax benefit. Angelina earns \$13,000 (including tips) working at a restaurant while her partner earns \$6,000 in a part-time sales position. Neither Angelina nor her partner is entitled to the disability tax credit for the year. Angelina makes a claim for the WITB for 2013. Determine the amount of her claim.

**End of Exercise. Solution available in Study Guide**

## Canada Child Tax Benefit

### Basic Amount

4-213. The Canada Child Tax Benefit is in the form of a non-taxable monthly payment. Similar to the refundable GST credit, the amount of this benefit is calculated by the CRA. The benefits are subject to indexation and are reduced if family net income for the preceding year is over a threshold amount. For 2013, the benefits are as follows:

- \$1,433 per year (paid monthly) for each qualified dependant, basically a child who is under 18; and
- an additional \$100 per year (paid monthly) for each dependant in excess of two.

4-214. This basic benefit is reduced when 2012 family net income reaches \$43,561. The phase out rate is dependent on the number of children in the family.

### National Child Benefit Supplement

4-215. In addition to the regular Child Tax Benefit, there is also a National Child Benefit Supplement. The amount of the supplement is \$2,221 per year for the first child, \$1,964 per year for the second, and \$1,869 per year for the third and subsequent child. All of these benefits are paid monthly.

4-216. The benefit is reduced when 2012 family Net Income reaches \$25,356. The phase out rate is dependent on the number of children in the family.

### **Universal Child Care Benefit**

4-217. While this is not part of the child tax benefit system, we would note here that there is also a taxable Universal Child Care Benefit. This benefit is paid to the lower income spouse or common-law partner and is included in their Net Income For Tax Purposes (see Chapter 9).

## **Social Benefits Repayment (OAS And EI)**

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### **Basic Concepts**

#### **Clawbacks**

4-218. Many Canadian tax credits and benefits are available on a universal basis, without regard to the income level of the recipient. However, both Old Age Security payments (OAS) and Employment Insurance payments (EI) are reduced for higher income individuals.

4-219. With respect to OAS payments, the government assesses a Part I.2 tax on OAS benefits received by individuals with an adjusted Net Income above a threshold amount. In similar fashion, the *Employment Insurance Act* requires that individuals with an adjusted Net Income above a specified threshold amount repay a portion of any Employment Insurance (EI) benefits received. These required repayments are commonly referred to as "clawbacks".

#### **Treatment In Net And Taxable Income**

4-220. Both OAS payments received and EI payments received must be included in an individual's Net Income For Tax Purposes. However, in situations where all or part of these amounts must be repaid, it would not be appropriate to allow the full amounts received to flow through to Taxable Income and have an influence on Tax Payable.

4-221. This problem is dealt with by providing a deduction for amounts repaid. You may recall from Chapter 1 that one of the components of Net Income For Tax Purposes was Other Deductions (subdivision e of the *Income Tax Act*). While we will not provide detailed coverage of this subdivision until Chapter 9, we need to note here that ITA 60(v.1) provides a deduction for repayments of EI, and ITA 60(w) provides a deduction for repayment of OAS amounts received.

4-222. As both the EI and OAS repayments are calculated on the basis of the individual's income in excess of a threshold amount, the question arises as to whether these tests should be applied using income figures which include the full amount received or, alternatively, income figures from which the repayments have been deducted. The solution to this problem will be discussed in the two sections which follow.

### **Employment Insurance (EI) Benefits Clawback**

4-223. The *Employment Insurance Act* requires the partial repayment of benefits received if the recipient's threshold income is greater than \$59,250 (1.25 times the 2013 maximum insurable earnings of \$47,400). This \$59,250 income figure includes all of the components of Net Income For Tax Purposes except the deductions for repayment of EI benefits [ITA 60(v.1)] and the deduction for the repayment of OAS benefits [ITA 60(w)]. As the EI clawback is deducted from the threshold income used for determining the OAS clawback, the EI clawback must be determined prior to calculating the amount of the OAS clawback.

4-224. Once the amount of threshold income over \$59,250 is determined, it must be compared to the EI benefits included in the current year's Net Income For Tax Purposes. The lesser of these two amounts is multiplied by 30 percent and this becomes the amount that must be repaid for the year as a social benefits repayment. This amount can then be deducted under ITA 60(v.1) in the determination of Net Income For Tax Purposes for the year.

### **Old Age Security (OAS) Benefits Clawback**

4-225. The OAS clawback is the lesser of the OAS payments included in income and 15 percent of the taxpayer's income in excess of the \$70,954 income threshold. For this purpose, income is equal to Net Income For Tax Purposes computed after any EI clawback, but



*Comprehensive Example*

before consideration of the deduction for the OAS clawback.

4-226. For the second quarter of 2013, the OAS benefit is \$546.07 per month. If this rate did not change during the year, the 2013 total would be \$6,552.84. Based on this figure, the benefit would disappear at an income level of \$114,640.

4-227. For higher income seniors, OAS benefits are clawed back on a regular basis, with some individuals receiving no benefits under this program during their lifetime. Given this, the government has an administrative procedure under which they withhold payments that they expect to be clawed back. Expectations are based on tax returns filed in the two previous years.

**Example** In her tax returns for both 2011 and 2012, Sally Leung has reported Taxable Income in excess of \$200,000 per year. Despite the fact that Sally is 70 years of age, she would receive no OAS payments in 2013.

4-228. Interestingly, once an individual has applied for OAS, the government will issue an information slip [T4A(OAS)] indicating that they have received the full benefit, even in cases where no OAS was paid and the full amount has been withheld. The information slip will show any amount that is clawed back. This means the full benefit must be included in income, accompanied by a deduction for the amount “repaid”. For an individual who reaches age 65 with the expectation that they will have very high income for the foreseeable future, this process can be avoided by not applying for OAS. Note that the 2012 Budget introduced voluntary deferral of OAS payments for up to 5 years for an increased amount of OAS pension.

**Exercise Four - 23**

**Subject:** EI and OAS Clawbacks

For 2013, Ms. Marilyn Jacobi has net employment income of \$60,000, receives EI payments of \$10,000, and receives \$6,550 in Old Age Security (OAS) payments. No amount was withheld from the OAS payments because she had very low income in the previous two years due to large rental losses. Determine Ms. Jacobi's Net Income For Tax Purposes for 2013.

**End of Exercise. Solution available in Study Guide.**

**Comprehensive Example**

4-229. While this Chapter has provided a reasonably detailed description of the determination of Tax Payable for individuals, including small examples of some of the issues that arise in this process, a more comprehensive example is appropriate at this point. To simplify calculations, we have ignored provincial income taxes and income tax withholdings on employment income. In the separate paper Study Guide, there is an additional example containing a completed tax return, as well as a Tax Software Self Study Problem, both of which include provincial income taxes.

**Basic Data**

Mr. Thomas Baxter is 66 years of age and his 2013 income is made up of net employment income of \$73,800 and Old Age Security benefits of \$6,550 (because of large business losses during the previous two years, no amount was withheld from these payments). For 2013, Mr. Baxter's employer withheld maximum CPP and EI contributions. Other information pertaining to 2013 is as follows:

1. Mr. Baxter's spouse is 49 years old and qualifies for the disability tax credit. Her only income for the year is \$5,000 in Canadian source interest. The investment funds were inherited from her father at the time of his death.

*Comprehensive Example*

2. Mr. and Mrs. Baxter have two daughters and, at the end of the year, their ages were 14 and 17. Kim, the younger daughter, has income of \$2,700, none of which was employment income. Lori, the older daughter, had net income of \$2,000, none of which was employment income. In September, 2013, Lori began full time attendance at a Canadian university. Mr. Baxter paid her tuition fees of \$5,000, of which \$2,500 was for the fall, 2013 semester.
3. The family medical expenses for the year, all of which were paid by Mr. Baxter, totalled \$2,843. Of this amount, \$300 was paid for Kim and \$900 for Lori.
4. During the year, Mr. Baxter made cash donations to registered Canadian charities in the amount of \$3,000. As he has made donations every year for the last 10 years, he is not eligible for the first time super donor tax credit.
5. During the year, Mr. Baxter made contributions to federal political parties total-ling \$800.
6. During the year, Mr. Baxter paid \$960 for monthly public transit passes.
7. Because of an ongoing problem with her weight, Mr. Baxter enrolled his daughter, Kim, in an eligible fitness program. The annual cost of this program is \$1,800.

**Net And Taxable Income**

|   |                 |
|---|-----------------|
| Net Employment Income                                 | \$73,800        |
| OAS Benefits  | 6,550           |
| <hr/>   |                 |
| Net Income Before Clawback                            | \$80,350        |
| OAS Clawback (Note One)                               | ( 1,409)        |
| <hr/>   |                 |
| <b>Net Income For Tax Purposes And Taxable Income</b> | <b>\$78,941</b> |

**Note One** The required repayment of OAS is the lesser of:

- \$6,550, the OAS payments included in income, and
- \$1,409 [(15%)(80,350 - 70,954)].

**Tax Payable/Federal Balance Owing**

The following notes contain information required in the calculation of the federal balance owing:

**Note Two** Mr. Baxter's age credit would be calculated as follows:

|                                      |               |
|--------------------------------------|---------------|
| Full Base Amount                     | \$6,854       |
| Reduction - Lesser Of:               |               |
| • [(15%)(78,941 - 34,562)] = \$6,657 |               |
| • Full Base Amount = \$6,854         | ( 6,657)      |
| <hr/>                                |               |
| <b>Age Credit</b>                    | <b>\$ 197</b> |

**Note Three** While Mr. Baxter paid \$1,800 for the fitness program, the maximum credit base is \$500.

**Note Four** Since both daughters are under 18 at the end of the year, their expenses can be aggregated with those of Mr. Baxter for the purposes of this calculation.

|   |               |
|---|---------------|
| Medical Expenses                            | \$2,843       |
| Lesser Of:                                  |               |
| • [(3%)(78,941)] = \$2,368                  |               |
| • 2013 Threshold Amount = \$2,152           | ( 2,152)      |
| <hr/>                                       |               |
| <b>Allowable Amount Of Medical Expenses</b> | <b>\$ 692</b> |

## Comprehensive Example

**Note Five** Lori's total education related amount is calculated as follows:

|   |                |
|---|----------------|
| Tuition For 2013 Semester (\$5,000 - \$2,500)               | \$2,500        |
| Education (Four Months At \$400)                            | 1,600          |
| Textbook (Four Months At \$65)                              | 260            |
| <u>Total Amount Available For Transfer Or Carry Forward</u> | <u>\$4,360</u> |

Since Lori has no Tax Payable before consideration of her education related credits, this example assumes that they are all transferred to her supporting parent as they total less than the \$5,000 transfer limit. Alternatively, she could choose to carry forward these credits to apply against her own Tax Payable in a subsequent year.

The federal tax payable and balance owing is calculated as follows:

|  |                   |
|--|-------------------|
| Federal Tax On First \$43,561                                    | \$ 6,534          |
| Federal Tax On Next \$35,380 (\$78,941 - \$43,561) At 22 Percent | <b>7,784</b>      |
| <u>Gross Tax</u>   | <u>\$14,318</u>   |
| Tax Credits:   |                   |
| Basic Personal Amount  | (\$11,038)        |
| Spousal Including FCA  |                   |
| (\$11,038 + \$2,040 - \$5,000)                                   | ( 8,078)          |
| Child - Kim  | ( 2,234)          |
| Child - Lori   | ( 2,234)          |
| Age (Note Two)   | ( 197)            |
| Public Transit Passes  | ( 960)            |
| Child Fitness (Note Three)                                       | ( 500)            |
| Medical Expenses (Note Four)                                     | ( 691)            |
| Mrs. Baxter's Disability Transferred                             | ( 7,697)          |
| Lori's Tuition, Education, And Textbook                          |                   |
| Transferred (Note Five)  | ( 4,360)          |
| EI Premiums (Maximum)  | ( 891)            |
| CPP Contributions (Maximum)                                      | ( 2,356)          |
| Canada Employment  | ( 1,117)          |
| <u>Total</u>   | <u>(\$42,353)</u> |
| Rate   | 15% ( 6,353)      |
| Charitable Donations   |                   |
| {[(15%)(\$200)] + [(29%)(\$3,000 - \$200)]}                      | ( 842)            |
| Political Contributions Tax Credit                               |                   |
| [((\$400)(3/4) + (\$350)(1/2) + (\$50)(1/3)]                     | ( 492)            |
| <u>Federal Tax Payable</u>                                       | <u>\$ 6,631</u>   |
| Social Benefits Repayment (Note One)                             | 1,409             |
| <u>Federal Balance Owing</u>                                     | <u>\$ 8,040</u>   |

**We suggest you work Self Study Problems Four-5 to Four-7 at this point.**

## Key Terms Used In This Chapter

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4-230. The following is a list of the key terms used in this Chapter. These terms, and their meanings, are compiled in the Glossary Of Key Terms located at the back of the separate paper Study Guide.

|                                     |                                       |
|-------------------------------------|---------------------------------------|
| Adoption Expenses Tax Credit        | Infirm Dependant Over 17 Tax Credit   |
| Age Tax Credit                      | Labour Sponsored Funds Tax Credit     |
| Canada Employment Credit            | Medical Expense Tax Credit            |
| Canada Pension Plan (CPP)           | Non-Refundable Tax Credit             |
| Canada Pension Plan Tax Credit      | Northern Residents Deductions         |
| Caregiver Tax Credit                | OAS Clawback                          |
| Charitable Donations Tax Credit     | Old Age Security (OAS) Benefits       |
| Charitable Gifts                    | Pension Income Tax Credit             |
| Child Tax Benefit                   | Personal Tax Credits                  |
| Child Tax Credit                    | Political Contributions Tax Credit    |
| Child Fitness Tax Credit            | Progressive Tax System                |
| Children's Arts Tax Credit          | Public Transit Pass Tax Credit        |
| Clawback                            | Refundable Medical Expense Supplement |
| Common-Law Partner                  | Refundable Tax Credit                 |
| Dependant                           | Regressive Tax System                 |
| Disability Tax Credit               | Social Benefits Repayment             |
| Disability Tax Credit Supplement    | Spousal Tax Credit                    |
| Education Tax Credit                | Spouse                                |
| Eligible Dependant Tax Credit       | Student Loan Interest Tax Credit      |
| Employment Insurance (EI)           | Tax Credit                            |
| Employment Insurance Tax Credit     | Taxable Income                        |
| Family Caregiver Tax Credit         | Textbook Tax Credit                   |
| First Time Home Buyer's Tax Credit  | Tuition Fees Tax Credit               |
| First Time Donor's Super Tax Credit | Volunteer Firefighters Tax Credit     |
| GST Tax Credit                      | Wholly Dependent Person               |
| Home Relocation Loan                | Working Income Tax Benefit            |
| Indexation                          |                                       |

## References

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4-231. For more detailed study of the material in this Chapter, we would refer you to:

|             |                              |
|-------------|------------------------------|
| ITA 110     | Deductions Permitted         |
| ITA 111.1   | Order Of Applying Provisions |
| ITA 117     | Tax Payable Under This Part  |
| ITA 117.1   | Annual Adjustment            |
| ITA 118(1)  | Personal Credits             |
| ITA 118(2)  | Age Credit                   |
| ITA 118(3)  | Pension Credit               |
| ITA 118(10) | Canada Employment Credit     |

|               |   |
|---------------|---|
| ITA 118.01    | Adoption Expense Credit   |
| ITA 118.02    | Public Transit Pass Credit  |
| ITA 118.03    | Child Fitness Credit  |
| ITA 118.031   | Children's Arts Tax Credit  |
| ITA 118.05    | First-Time Home Buyers' Credit  |
| ITA 118.06    | Volunteer Firefighters Tax Credit   |
| ITA 118.1     | Definitions (Charitable Gifts)  |
| ITA 118.2     | Medical Expense Credit  |
| ITA 118.3     | Credit For Mental Or Physical Impairment  |
| ITA 118.5     | Tuition And Other Education Related Credits   |
| ITA 118.6     | Education Credit And Textbook Credit  |
| ITA 118.61    | Unused Tuition And Education Tax Credits  |
| ITA 118.62    | Credit For Interest On Student Loan   |
| ITA 118.7     | Credit for EI and QPIP premiums and CPP contributions   |
| ITA 118.8     | Transfer Of Unused Credits To Spouse Or Common-Law Partner                                      |
| ITA 118.81    | Tuition, Textbook, And Education Tax Credits Transferred  |
| ITA 118.9     | Transfer To Parent Or Grandparent   |
| ITA 122.5     | Definitions (GST Credit)  |
| ITA 122.51    | Definitions (Refundable Medical Expense Supplement  |
| ITA 122.6-.64 | Canada Child Tax Benefit  |
| ITA 122.7     | Working Income Tax Benefit  |
| ITA 127(3)    | Federal Political Contributions Tax Credit  |
| ITA 127.4     | Labour Sponsored Funds Tax Credit   |
| ITA 180.2     | OAS Clawback  |
| ITR 5700      | Prescribed Device Or Equipment  |
| ITR 9400      | Prescribed Program Of Physical Activity   |
| IC 75-2R8     | Contributions To A Registered Political Party Or To A Candidate At A Federal Election           |
| IC 75-23      | Tuition Fees And Charitable Donations Paid To Privately Supported Secular and Religious Schools |
| IC 84-3R6     | Gifts To Certain Organizations Outside Canada   |
| S1-F1-C1      | Medical Expense Tax Credit  |
| S1-F1-C2      | Disability Tax Credit   |
| S1-F1-C3      | Disability Supports Deduction   |
| S1-F2-C1      | Education And Textbook Tax Credits  |
| S1-F2-C2      | Tuition Tax Credit  |
| IT-110R3      | Gifts And Official Donation Receipts  |
| IT-113R4      | Benefits To Employees — Stock Options   |
| IT-226R       | Gift To A Charity Of A Residual Interest In Real Property Or An Equitable Interest In A Trust   |
| IT-244R3      | Gifts By Individuals Of Life Insurance Policies As Charitable Donations                         |
| IT-407R4      | Dispositions Of Cultural Property To Designated Canadian Institutions (Consolidated)            |
| IT-513R       | Personal Tax Credits  |
| IT-523        | Order Of Provisions Applicable In Computing An Individual's Taxable Income And Tax Payable      |

## Sample Tax Return For Chapter 4

The Sample Tax Return for Chapter 4 can be found in the Study Guide beginning on page S-49.

## Problems For Self Study

(The solutions for these problems can be found in the separate Study Guide.)

**NOTE** The **Tax Software Self Study Problem** for Chapter 4 is available in the separate Study Guide.

### Self Study Problem Four - 1 (Individual Tax Payable - 5 Cases)

Ms. Wanda Sykes is 42 years old. The following five independent Cases make varying assumptions for the 2013 taxation year with respect to Ms. Sykes' marital status, number of dependants, and type of income. In all Cases, Ms. Syke had Net Income For Tax Purposes of \$78,000.

**Case A** Ms. Sykes is a single mother. She has a son, John, who is 10 years old and lives with her. John had no income. During 2013, Ms. Sykes attends university for 10 months of the year on a part time basis. Her tuition fees total \$5,640. All of Ms. Sykes' income is from spousal support payments.

**Case B** Ms. Sykes is not married and has no dependants. All of her income is from employment. In December, she wins \$2,000,000 in the provincial lottery. She donates \$150,000 of this amount to the church where she prayed for a winning lottery ticket. She plans to claim \$35,000 of this donation for a tax credit in 2013. As she contributes regularly to this church, she is not eligible for the first-time donor's super credit.

**Case C** Ms. Sykes is married and her husband, Buff has Net Income For Tax Purposes of \$7,600. All of her income is from investments. They have one child, Martin. He is 10 years old, has no income of his own, and qualifies for the disability tax credit. Buff's 73 year old father, Harry, lives with them. His Net Income For Tax Purposes was \$17,600. He is not mentally or physically infirm.

**Case D** Ms. Sykes is married and her husband, Buff has Net Income For Tax Purposes of \$2,540. All of her income is employment income. Wanda and Buff have two children, Janice who is 10 years of age, and Mark who is 20 years of age. Both children are in good health. As Mark has been unable to find full-time employment, he still lives at home. While Mark had Net Income For Tax Purposes of \$2,460 from part-time employment, Janice had no income during the year. During 2013, Ms. Sykes paid for the following medical expenses:

|              |                 |
|--------------|-----------------|
| Wanda        | \$ 2,100        |
| Buff         | 360             |
| Janice       | 3,645           |
| Mark         | 4,520           |
| <b>Total</b> | <b>\$10,625</b> |

**Case E** Ms. Sykes is married and her husband, Buff is 66 years old. All of her income is from employment. Wanda and Buff have two children, a son aged 12 and a daughter aged 14. Both children are in good health and have no income of their own. Buff is disabled and qualifies for the disability tax credit. His only income is \$9,600 in pension income from his former employer as he is not eligible for OAS. He attends university on a full time basis for 8 months of the year and his tuition costs for 2013 are \$8,450.

**Required:** In each Case, calculate Ms. Sykes' minimum federal Tax Payable for 2013. Indicate any carry forwards available to her and her dependants and the carry forward provisions. Ignore any tax amounts that Ms. Sykes might have had withheld or paid in instalments.

### Self Study Problem Four - 2 (Individual Tax Payable - 7 Cases)

The following seven independent Cases make varying assumptions with respect to Stanley Murphy and his 2013 tax status. In all Cases, where Stanley earned employment income, his employer withheld the maximum EI premium and CPP contribution.

**Case A** Stanley Murphy is 48 years of age and has employment income of \$55,000. During the year, Stanley makes contributions to federal political parties in the amount of \$1,000. Stanley is not married and has no dependants.

**Case B** Stanley Murphy is 48 years of age and has income from employment of \$55,000. His wife, Helen, is 43 years of age and has Net Income For Tax Purposes of \$4,650. They have one child, Eileen, who is 11 years of age and has income of \$3,000. During the year, the family had eligible medical expenses of \$1,050 for Stanley, \$1,800 for Helen, and \$300 for Eileen.

**Case C** Stanley Murphy is 48 years old and his wife, Helen, is 43. Stanley has rental income of \$55,000 and Helen has investment income of \$9,400. They have a 19 year disabled son, Albert, who lives with them. His disability qualifies him for the disability tax credit and he has no income of his own. During the year, Stanley and Helen have medical expenses of \$1,250. Medical expenses for Albert during the year total \$8,350.

**Case D** Stanley Murphy is 48 years of age and his wife, Helen, is 43. Stanley has income from employment of \$55,000. Helen has employment income of \$12,000. Helen's 68 year old father, Ahmed, and her 70 year old aunt, Jaleh, live with them. Both are in good health. Ahmed's Net Income For Tax Purposes is \$9,200 and Jaleh's Net Income For Tax Purposes is \$11,000. Stanley paid \$375 in interest related to his student loan during the year.

**Case E** Stanley Murphy is 48 years of age and his common-law partner Bob is 43. Stanley has employment income of \$55,000. Bob has Net Income For Tax Purposes of \$4,500. They have two adopted children, Barry aged 7 and Don aged 9. After living in rented premises for the last 7 years, Stanley and Bob decide to purchase a residence. They acquire a 3 bedroom house in the suburbs at a cost of \$245,000 and move into the house during the year.

**Case F** Stanley Murphy is 48 years of age and his wife, Helen, is 43. Stanley has income from employment of \$55,000. Helen has Net Income For Tax Purposes of \$5,050. They have a son, Albert, who is 19 years old and lives at home. He attends university on a full time basis during 8 months of the year. Stanley pays \$5,400 for Albert's tuition for two semesters during the 2013 calendar year and \$525 for required textbooks. Albert had employment income of \$3,000 that he earned during the summer. He will transfer any unused credits to his father.

**Case G** Stanley Murphy is 67 and his wife Helen is 68. Helen has been completely disabled for a number of years and the extent of her disability qualifies her for the disability tax credit. The components of Stanley and Helen's income are as follows:

|                                     | Stanley         | Helen          |
|-------------------------------------|-----------------|----------------|
| Interest                            | \$ 300          | \$ 50          |
| Canada Pension Plan Benefits        | 4,400           | 200            |
| Old Age Security Benefits           | 6,550           | 6,550          |
| Income From Registered Pension Plan | 31,150          | 450            |
| <b>Total Net Income</b>             | <b>\$42,400</b> | <b>\$7,250</b> |

**Required:** In each Case, calculate Stanley Murphy's minimum federal Tax Payable for 2013. Indicate any carry forwards available to him and his dependants and the carry forward provisions. Ignore any amounts Stanley might have had withheld or paid in instalments and the possibility of pension splitting.

**Self Study Problem Four - 3 (Individual Tax Payable - Simple)**

Mr. Dennis Lane has been a widower for several years. For 2013, both his Net Income For Tax Purposes and Taxable Income were equal to his net employment income of \$70,000. Mr. Lane's employer withheld \$10,100 in federal income taxes, \$891 for Employment Insurance premiums and \$2,391 in Canada Pension Plan contributions. Because of an error by his employer, an overcontribution of \$35 was made for the Canada Pension Plan.

**Other Information:**

1. Mr. Lane made political contributions to federal political parties in the amount of \$450.
2. Mr. Lane has three children, aged 10, 12, and 15. They all live with him in his principal residence and, other than his 15 year old son, have no income of their own. Mr. Lane paid no medical expenses other than \$4,400 for hospital care for his 15 year old son. His son had 2013 Net Income For Tax Purposes of \$8,200.
3. Mr. Lane buys public transit passes for his oldest son and himself. The monthly cost of these passes is \$75 for each individual. Because of a family vacation, no passes were purchased in the month of July.
4. His two younger children are enrolled in an eligible fitness program. The annual cost for each child is \$425.

**Required:** Calculate Mr. Lane's federal tax payable (refund) for 2013.

**Self Study Problem Four - 4 (Tax Payable With Employment Income)**

**Extension of Self Study Problem Three - 8**

Mr. John Barth has been employed for many years as a graphic illustrator in Kamloops, British Columbia. His employer is a large publicly traded Canadian company. During 2013, his gross salary was \$82,500. In addition, he was awarded a \$20,000 bonus to reflect his outstanding performance during the year. As he was in no immediate need of additional income, he arranged with his employer that none of this bonus would be paid until 2018, the year of his expected retirement.

**Other Information:**

For the 2013 taxation year, the following items were relevant.

1. Mr. Barth's employer withheld the following amounts from his income:
 

|  |          |
|--|----------|
| Federal Income Tax                       | \$16,000 |
| Employment Insurance Premiums            | 891      |
| Canada Pension Plan Contributions        | 2,356    |
| United Way Donations                     | 2,000    |
| Registered Pension Plan Contributions    | 3,200    |
| Payments For Personal Use Of Company Car | 3,600    |
2. During the year, Mr. Barth is provided with an automobile owned by his employer. The cost of the automobile was \$47,500. Mr. Barth drove the car a total of 10,000 kilometers during the year, of which only 4,000 kilometers were related to the business of his employer. The automobile was used by Mr. Barth for ten months of the year. During the other two months, he was out of the country he was required to leave the automobile with one of the other employees of the corporation.
3. During the year, the corporation paid Mega Financial Planners a total of \$1,500 for providing counseling services to Mr. Barth with respect to his personal financial situation.



*Problems For Self Study*

4. In order to assist Mr. Barth in purchasing a ski chalet, the corporation provided him with a five year loan of \$150,000. The loan was granted on October 1 at an interest rate of 1 percent. Mr. Barth paid the corporation a total of \$375 in interest for 2013 on January 20, 2014. Assume that, at the time the loan was granted and throughout the remainder of the year, the relevant prescribed rate was 2 percent.
5. Mr. Barth was required to pay professional dues of \$1,800 during the year.
6. On June 6, 2013, when Mr. Barth exercised his stock options to buy 1,000 shares of his employer's common stock at a price of \$15 per share, the shares were trading at \$18 per share. When the options were issued, the shares were trading at \$12 per share. During December, 2013, the shares were sold at \$18 per share.
7. Mr. Barth lives with his wife, Lynda. Lynda is blind and qualifies for the disability tax credit. She has Net Income For Tax Purposes of \$1,250.
8. His 22 year old dependent daughter, Marg, is a full time student at the University of British Columbia for 8 months of the year. She lives in Vancouver and has Net Income For Tax Purposes and Taxable Income of \$13,400. She had withheld from her employment income EI premiums of \$252 [(1.88%)(13,400)] and CPP contributions of \$490 [(4.95%)(13,400 - \$3,500)]. Mr. Barth paid Marg's tuition for 2013 of \$6,300. She has agreed to transfer the maximum credit available to her father.
9. Mr. Barth paid the following medical costs:

|              |         |
|--------------|---------|
| For Himself  | \$ 200  |
| For His Wife | 3,550   |
| For Marg     | 720     |
| Total        | \$4,470 |

10. Because of donations in previous years, he does not qualify for the first-time donor's super tax credit.

**Required:** Calculate, for the 2013 taxation year:

- A. Marg's minimum federal Tax Payable and any carry forward amounts available to her at the end of the year.
- B. Mr. Barth's minimum Taxable Income and federal Tax Payable (Refund).

#### **Self Study Problem Four - 5 (Tax Payable With Multiple Credits)**

Ms. Eleanor Victoria's husband died two years ago. After her husband died, she moved from her house in Prince George, B.C., to a rented house in Victoria, B.C.

Ms. Victoria's widowed mother, Marjorie Toshiro, lives with Ms. Victoria and takes care of the house, Ms. Victoria's younger daughter, Amy, and all of the household cooking. In addition to OAS benefits, Marjorie has a small income from her deceased husband's life insurance policy. She has never filed a tax return and she is not infirm.

Diane Victoria, Eleanor's older daughter, is studying psychology at McGill University in Montreal. Her field is addiction research with a special emphasis on gambling. She does volunteer work at a gambling addiction treatment centre in Montreal in the summers. As Eleanor has paid for her tuition and living costs, Diane has agreed that any credits available should be transferred to her mother.

Diane has decided not to file a tax return this year as she is too busy with her studies and volunteer work. Her income was earned driving for a client of the addiction treatment centre who had lost his licence after being charged with impaired driving.

Other information concerning Ms. Victoria for 2013 is as follows:

1. Eleanor was born on May 15, 1965.

*Problems For Self Study*

2. The birth dates and Net Income For Tax Purposes for the year of her dependants are as follows:

|          | Birth Date (Y/M/D) | Net Income |
|----------|--------------------|------------|
| Diane    | 1993-05-14         | \$2,300    |
| Amy      | 2001-10-11         | Nil        |
| Marjorie | 1932-05-21         | \$8,000    |

3. Eleanor's T4 for 2013 showed the following:

|                              |            |
|------------------------------|------------|
| Salary                       | \$60,202   |
| Employee's EI Premiums       | 891        |
| Employee's CPP Contributions | 2,356      |
| RPP Contributions            | 2,406      |
| Pension Adjustment           | 7,829      |
| Union Dues                   | 749        |
| Charitable Donations         | 175        |
| Income Tax Withheld          | Assume Nil |

4. Eleanor and her family had the following medical expenses for 2013, all of which Eleanor paid for:

| Patient      | Medical Expenses        | Description      | Amount         |
|--------------|-------------------------|------------------|----------------|
| Eleanor      | Grace Hospital          | Ambulance Charge | \$ 392         |
| Eleanor      | Paramed Home Health     | Nursing Care     | 1,350          |
| Marjorie     | Dr. Zhang (Optometrist) | Contact Lenses   | 110            |
| Marjorie     | Pharmacy                | Prescription     | 75             |
| Diane        | Dr. Glassman            | Physiotherapist  | 100            |
| Amy          | Walk Right Foot Clinic  | Orthotics        | 450            |
| Amy          | Dr. Tamo                | Dental           | 1,120          |
| <b>Total</b> |                         |                  | <b>\$3,597</b> |

5. In addition to the \$175 in charitable contributions withheld by Eleanor's employer, Eleanor and Diane had the following charitable donations for 2013:

| Donor   | Charitable Donation Receipts         | Amount |
|---------|--------------------------------------|--------|
| Eleanor | Heart And Stroke                     | \$ 375 |
| Eleanor | Terry Fox Foundation                 | 50     |
| Diane   | Addiction Research Council Of Canada | 100    |

Because of donations in previous years, neither Diane nor Eleanor qualify for the first-time donor's super credit.

6. During 2013, Diane was in university full time for 8 months and part time for an additional 2 months. Her tuition fees for the year were \$7,000.

**Required:** Calculate Eleanor's minimum federal Tax Payable. List any assumptions you have made, and any notes and tax planning issues you feel should be discussed with Eleanor.

**Self Study Problem Four - 6**  
**(Comprehensive Tax Payable With Employment Income)**

Mr. Lance Strong is a skilled carpenter who is employed by a large public company. For 2013, his annual salary is \$72,000. He is required to pay for his own tools, but is reimbursed for out-of-pocket travel costs when he is required to work away from his employer's municipality for more than 12 hours. His disability plan provides periodic benefits that are designed to compensate for lost employment income.

During 2013, Mr. Strong's employer withheld the following amounts from his compensation:

## Problems For Self Study

|  |        |
|--|--------|
| EI Premiums  | \$ 891 |
| CPP Contributions  | 2,356  |
| RPP Contributions  | 4,200  |
| Contributions To Disability Plan (Employer Makes Matching Contribution)* | 430    |

Mr. Strong is married and has two children aged 14 and 16. Neither child has any income during 2013. His spouse has 2013 income of \$5,600. Mr. Strong's 67 year old mother lives with the family. Her Net Income For Tax Purposes of \$7,000 consists of OAS payments and investment income. She is not mentally or physically infirm.

**Other Information:**

- Mr. Strong is provided with an automobile by his employer. During 2013, it is driven 32,000 kilometres, of which only 15,000 are employment related. The automobile is leased by the employer at a monthly rate of \$565, including HST of \$65. The monthly rate also includes a payment for insurance of \$40 per month. The automobile was used by Mr. Strong for 10 months during 2013. During the two that he did not use the automobile, he was required to return it to his employer's garage.
- During 2013, Mr. Strong was required to buy \$2,000 in carpentry tools in order to carry out his employment duties.
- Mr. Strong's employer encourages its employees to take university courses by paying their tuition fees. During 8 months of 2013, Mr. Strong was in part time attendance for two university courses. The first course was devoted to 16th century liturgical chants and the second was a course in spoken French. The tuition for each course was \$600, with the employer paying the full amount. The employer was particularly interested in the French course as it would allow Mr. Strong to deal more effectively with francophone clients.
- Mr. Strong incurred \$4,600 in travel costs during 2013, all of which were reimbursed by his employer.
- During 2013, Mr. Strong sold his house and purchased a heritage home 50 kilometres closer to his employer's main office. To assist with the relocation, on April 1, 2013, his employer provided an interest free loan of \$150,000. It must be repaid in full on April 1, 2017. Assume that during the first two quarters of 2013 the prescribed rate was 2 percent and that during the last two quarters it declined to 1 percent.
- During 2013, Mr. Strong pays for the following eligible medical costs:

|                            |                |
|----------------------------|----------------|
| For Himself                | \$1,250        |
| For His Spouse             | 2,300          |
| For His Two Children       | 850            |
| For His Mother             | 1,960          |
| <b>Total Medical Costs</b> | <b>\$6,360</b> |
- During 2013, Mr. Strong gives cash of \$1,200 to his church. He also donates carpenter services with a market value of \$1,500. Because of donations in previous years, he does not qualify for the first-time donor's super tax credit.
- Mr. Strong buys monthly transit passes for both of his children during the school year. The cost is \$60 per month per child. The passes covered 10 months during 2013.

**Required:**

- Determine Mr. Strong's minimum Net Income For Tax Purposes for the 2013 taxation year.
- Determine Mr. Strong's minimum Taxable Income for the 2013 taxation year.
- Based on your answer in Part B, determine Mr. Strong's federal Tax Payable for the 2013 taxation year. Ignore any amounts that might have been withheld by his employer or paid in instalments.

**Self Study Problem Four - 7**  
**(Comprehensive Tax Payable With Employment Income)**

Mr. Andrew Bosworth is married and has two children. His 19 year old son attends a local university and lives at home. His tuition for the 8 months of attendance during 2013 was \$7,650. His father paid the tuition and, in addition, paid \$560 in ancillary fees and \$425 for textbooks. The ancillary fees were charged to all students attending the university. The son had 2013 Net Income For Tax Purposes of \$12,450 resulting from investments he inherited from his grandfather. The son's only tax credit is the basic personal credit for single persons. He has agreed to transfer any unused education related credits to his father.

Mr. Bosworth's daughter is 12 years old and has been blind since birth. As Mr. Bosworth's spouse is responsible for her care, she has not taken a full-time position of employment. However, she has Net Income For Tax Purposes of \$6,450 resulting from part-time employment.

Mr. Bosworth works for a publicly traded company. During 2013, his base salary was \$180,000. In addition, he received commissions totaling \$11,500 and a bonus of \$38,000. None of the bonus will be paid until January, 2014.

During 2013, his employer withholds the following amounts from his salary:

|  |         |
|--|---------|
| Registered Pension Plan Contributions                                | \$5,200 |
| EI Premiums  | 891     |
| CPP Contributions  | 2,356   |
| Contributions To The Local United Way                                | 2,400   |
| Life Insurance Premiums (The Employer Makes A Matching Contribution) | 460     |

**Other Information**

- Mr. Bosworth's employer provides him with an automobile that is leased for \$925 per month, including a \$75 per month payment for insurance. During 2013, the automobile is driven a total of 62,000 kilometers, of which 41,000 involve employment related activities. Mr. Bosworth paid all of the \$10,300 in 2013 operating costs and is not reimbursed by his employer. The automobile was used by Mr. Bosworth throughout 2013.
- In 2010, Mr. Bosworth received options to acquire 5,000 shares of his employer's common stock at a price of \$9.75 per share. This was the market price of the shares at the time the options were granted. On July 1, 2013, when the shares were trading at \$12.35, Mr. Bosworth exercises all of these options. He is still holding the acquired shares at the end of the current year.
- Mr. Bosworth is not reimbursed for advertising, entertainment or travel costs. In addition to the operating costs for his vehicle, he paid for the following employment related costs:

|                       |                 |
|-----------------------|-----------------|
| Meals While Traveling | \$ 6,420        |
| Hotels                | 10,350          |
| Advertising           | 12,400          |
| Entertainment         | 6,500           |
| <b>Total</b>          | <b>\$35,670</b> |

- Mr. Bosworth's employer provides all employees with a luxury weekend at a local resort. The cost of the gift is \$2,500 for each employee.
- Mr. Bosworth pays for the following medical expenses during 2013:

|  |                 |
|--|-----------------|
| For Andrew   | \$ 1,200        |
| For His Spouse   | 2,250           |
| For His Son  | 2,340           |
| For His Daughter (including \$9,000 in attendant care) | 11,250          |
| <b>Total</b>   | <b>\$17,040</b> |

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6. Mr. Bosworth enrolls both of his children in fitness programs. The cost for his son is \$450 for the year. For his daughter the cost is \$400 for the year.
7. Because of his ongoing interest in Elizabethan drama, Mr. Bosworth enrolls in a course on Shakespeare's tragedies at the local university. His tuition for this part-time attendance was \$1,670 and his required textbooks cost \$165. The duration of the course was 4 months.
8. Because he contributes every year to the United Way, Mr. Bosworth is not eligible for the first-time donor's super credit.

**Required:**

- A. Determine Mr. Bosworth's minimum Net Income For Tax Purposes for the 2013 taxation year.
- B. Determine Mr. Bosworth's minimum Taxable Income for the 2013 taxation year.
- C. Based on your answer in Part B, determine Mr. Bosworth's federal Tax Payable for the 2013 taxation year. Ignore any amounts that might have been withheld by his employer, any amount paid in instalments, as well as any considerations related to HST, GST, or PST.

## Assignment Problems

(The solutions for these problems are only available in the solutions manual that has been provided to your instructor.)

### **Assignment Problem Four - 1 (Personal Tax Credits - 5 Cases)**

In each of the following independent Cases, determine the maximum amount of 2013 personal tax credits, including transfers from a spouse or dependant, that can be applied against federal Tax Payable by the taxpayer.

A calculation of Tax Payable is NOT required, only the applicable credits.

1. Sarah Partridge is 72 years old and has Net Income For Tax Purposes of \$61,300. This total is made up of OAS payments and pension income from her former employer. Her husband is 58 years old and has Net Income For Tax Purposes of \$4,725. Ignore the possibility of splitting Sarah's pension income.
2. Martin Brody was divorced from his wife several years ago. He has custody of their four children, ages 7, 9, 12, and 15. His Net Income For Tax Purposes consists of spousal support payments totaling \$54,000 per year. The children are all in good health. The oldest child has Net Income For Tax Purposes of \$11,200 during the year.
3. Marion Lassiter has Net Income For Tax Purposes of \$132,450, all of which is rental income. Her husband has no income of his own. They have three children, ages 14, 16, and 19. All of these children are in good health and continue to live at home. The 19 year old child has Net Income For Tax Purposes of \$8,460. During the current year, Ms. Lassiter pays the following medical expenses:

|                   |                 |
|-------------------|-----------------|
| Marion            | \$ 4,240        |
| Her Spouse        | 3,450           |
| 14 Year Old Child | 1,860           |
| 16 Year Old Child | 2,450           |
| 19 Year Old Child | 6,720           |
| <b>Total</b>      | <b>\$18,720</b> |

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4. Janice Archer has Net Income For Tax Purposes of \$92,100, none of which is employment income or income from self-employment. Her spouse has Net Income For Tax Purposes of \$7,240. Their daughter is 15 years old, lives with them, and has Net Income For Tax Purposes of \$2,150. Their son is 22 years old and, because of a physical disability, continues to live with them. He has no income of his own. His disability is not severe enough to qualify for the disability tax credit.
5. Joan Baxter has Net Income For Tax Purposes of \$85,000, all of which is employment income. She is married to John Brown whose Net Income For Tax Purposes is \$4,230. They have three children aged 7, 9, and 11. All of the children are in good health and none of them have income of their own.

**Assignment Problem Four - 2 (Individual Tax Payable - 7 Cases)**

There are seven independent cases which follow. Each case involves various assumptions as to the amount and type of income earned by Ms. Barbra Baines during 2013, as well as to other information that is relevant to the determination of her 2013 Tax Payable. In those cases where we have assumed that the income was from employment, the employer withheld the maximum EI premium and CPP contribution.

**Case 1** Barbra and her husband Billy are both 67 years of age. Billy is sufficiently disabled that he qualifies for the disability tax credit. The components of the 2013 income earned by Barbra and Billy are as follows:

|                                     | <b>Barbra</b>   | <b>Billy</b>   |
|-------------------------------------|-----------------|----------------|
| Interest                            | \$ 2,600        | \$ 650         |
| Canada Pension Plan Benefits        | 12,600          | Nil            |
| Old Age Security Benefits           | 6,550           | 6,550          |
| Income From Registered Pension Plan | 22,300          | 1,230          |
| <b>Total Net Income</b>             | <b>\$44,050</b> | <b>\$8,430</b> |

**Case 2** Barbra is 43 years old and has net rental income of \$86,500. Her husband died last year. She has two children. Mark is 15 and is physically infirm, but not sufficiently to qualify for the disability tax credit. He has income from part time work as a graphic artist of \$13,450. The other child, Sandy, is 12 and is in good health. She has no income of her own.

**Case 3** Barbra is 58 years old and has income from investments of \$102,000. She is divorced and has been awarded custody of her 21 year disabled son. The son qualifies for the disability tax credit. He has Net Income For Tax Purposes of \$7,560, and is dependent on his mother for support. Barbra paid \$850 for a 3 month art appreciation course for her son, as well as \$1,500 for a 6 month fitness program.

**Case 4** Barbra is 31 years old, has employment income of \$83,000, and makes contributions of \$5,600 to registered charities. Barbra qualifies for the first-time donor's super credit. She is not married and has no dependants.

**Case 5** Barbra is 58 years old and has employment income of \$93,500. Her common-law partner is 48 years old and has income of \$7,260. They have an adopted child who is 19 years old and lives at home. Barbra and her partner have medical expenses of \$3,200. Medical expenses for the son total \$8,400. The son has Net Income For Tax Purposes of \$5,600.

**Case 6** Barbra is 45 years old and has employment income of \$84,600. Her husband John is 37 years old and has Net Income For Tax Purposes of \$7,200. They have no children. However, they provide in home care for John's father who is 67 years old, dependent because of a physical infirmity and has no income of his own. Also living with them is Barbra's 67 year old father. He is in good physical and mental health and has Net Income For Tax Purposes of \$19,400.

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**Case 7** Barbra is 46 years old and has employment income of \$163,000. Her husband Larry is 41 years old and has Net Income For Tax Purposes of \$7,240. They have a 20 year old son who lives at home. He is dependent because of a physical infirmity, but it is not severe enough to qualify him for the disability tax credit. However, he is able to attend university on a full time basis for 8 months during 2013. Barbra pays his tuition fees of \$8,300, as well as \$640 for the textbooks that he requires in his program. The son has Net Income For Tax Purposes of \$9,600.

**Required:** In each Case, calculate Barbra Baines' minimum federal Tax Payable for 2013. Indicate any carry forwards available to her and her dependants and the carry forward provisions. Ignore any amounts Barbra might have had withheld or paid in instalments, as well as the possibility of pension splitting.

**Assignment Problem Four - 3 (Individual Tax Payable - 5 Cases)**

Mr. William Norris is 45 years old. The following five independent Cases make varying assumptions for the 2013 taxation year with respect to Mr. Norris' marital status and number of dependants. In all Cases, Mr. Norris earned employment income of \$60,000 and his employer withheld the required EI premiums and CPP contributions.

**Case A** Mr. Norris is married and his wife, Susan, has Net Income For Tax Purposes of \$8,800. Susan's 73 year old mother, Bernice, lives with them. Bernice, an avid skier, had Net Income For Tax Purposes of \$16,000 for the year.

**Case B** Mr. Norris is married and his wife, Susan, has Net Income For Tax Purposes of \$4,410. They have one child, Martha, who is 10 years of age. Martha had no income during the year. During the year, the family had medical expenses as follows:

|              |                |
|--------------|----------------|
| William      | \$1,200        |
| Susan        | 1,600          |
| Martha       | 350            |
| <b>Total</b> | <b>\$3,150</b> |

**Case C** Mr. Norris is married and his wife, Susan, has Net Income For Tax Purposes of \$4,500. They have a son, Allen, who is 19 years old and lives at home. He attends university on a full time basis during 8 months of the year. Mr. Norris pays \$4,000 for Allen's tuition and \$900 for required textbooks. Allen had employment income during the summer months of \$2,200. He will transfer any unused credits to his father.

**Case D** Mr. Norris is not married and has no dependants. On receipt of a \$300,000 inheritance in December, he donates \$50,000 to his local hospital, a registered charity. He chooses to claim \$15,000 in 2013. As he has donated to this hospital on a regular basis, he is not eligible for the first-time donor's super credit. He also makes contributions to a federal political party in the amount of \$1,000.

**Case E** Mr. Norris is a single father. He has a daughter, Mary, who is 8 years old and lives with him. Mary had no income for the year. Two years ago, Mr. Norris graduated from a Canadian university. He currently has a Canada Student Loan outstanding. Mr. Norris pays back this loan in monthly instalments of \$300. During the year, he paid \$450 in interest on this loan.

**Required:** In each Case, calculate Mr. Norris' minimum federal Tax Payable for 2013. Indicate any carry forwards available to him and his dependants and the carry forward provisions. Ignore any tax amounts that Mr. Norris might have had withheld or paid in instalments.

**Assignment Problem Four - 4 (Tax Payable With Employment Income)****Extension of Assignment Problem Three - 10**

For the past five years, Mr. Brooks has been employed as a financial analyst by a large Canadian public firm located in Winnipeg. During 2013, his basic gross salary amounts to \$53,000. In addition, he was awarded an \$11,000 bonus based on the performance of his division. Of the total bonus, \$6,500 was paid in 2013 and the remainder is to be paid on January 15, 2014.

During 2013, Mr. Brooks' employer withheld the following amounts from his gross wages:

|  |         |
|--|---------|
| Federal Income Tax                       | \$3,000 |
| Employment Insurance Premiums            | 891     |
| Canada Pension Plan Contributions        | 2,356   |
| Registered Pension Plan Contributions    | 2,800   |
| Donations To The United Way              | 480     |
| Union Dues                               | 240     |
| Payments For Personal Use Of Company Car | 1,000   |

**Other Information:**

- Due to an airplane accident while flying back from Thunder Bay on business, Mr. Brooks was seriously injured and confined to a hospital for two full months during 2013. As his employer provides complete group disability insurance coverage, he received a total of \$4,200 in payments during this period. All of the premiums for this insurance plan are paid by the employer. The plan provides periodic benefits that compensate for lost employment income.
- Mr. Brooks is provided with a car that the company leases at a rate of \$678 per month, including both GST and PST. The company pays for all of the operating costs of the car and these amounted to \$3,500 during 2013. Mr. Brooks drove the car a total of 35,000 kilometers during 2013, 30,000 kilometers of which were carefully documented as employment related travel. While he was in the hospital (see Item 1), his employer required that the car be returned to company premises.
- On January 15, 2013, Mr. Brooks received options to buy 200 shares of his employer's common stock at a price of \$23 per share. At this time, the shares were trading at \$20 per share. Mr. Brooks exercised these options on July 6, 2013, when the shares were trading at \$28 per share. He does not plan to sell the shares for at least a year.
- In order to assist Mr. Brooks in acquiring a new personal residence in Winnipeg, his employer granted him a five year, interest free loan of \$125,000. The loan qualifies as a home relocation loan. The loan was granted on October 1, 2013 and, at this point in time, the interest rate on open five year mortgages was 5 percent. Assume the relevant ITR4301 rate was 2 percent on this date. Mr. Brooks purchases a house for \$235,000 on October 2, 2013. He has not owned a home during any of the preceding four years.
- Other disbursements made by Mr. Brooks include the following:

|   |         |
|---|---------|
| Advanced financial accounting course tuition fees                                       | \$1,200 |
| Music history course tuition fees<br>(University of Manitoba one week intensive course) | 600     |
| Fees paid to financial planner  | 300     |
| Payment of premiums on life insurance   | 642     |

Mr. Brooks' employer reimbursed him for the tuition fees for the accounting course, but not the music course.

- Mr. Brooks is a widower. His wife was killed in a car accident in 2010 that injured his 8 year old son, Harold, so badly that he qualifies for the disability tax credit. Mr. Brooks' mother, Grace, lives with Mr. Brooks and cares for Harold. Harold has no Net Income For Tax Purposes. Grace is 67 years old and her Net Income For Tax Purposes is \$7,500. Grace refused to take any payments for caring for Harold as she received a large



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inheritance in the previous year. As a result, Mr. Brooks did not pay any child care or attendant costs for Harold.

7. Mr. Brooks paid the following eligible medical costs:

|              |                 |
|--------------|-----------------|
| For Himself  | \$ 9,300        |
| For Harold   | 2,450           |
| For Grace    | 1,265           |
| <b>Total</b> | <b>\$13,015</b> |

8. Mr. Brooks buys public transit passes for his son, his mother and himself. The monthly cost of these passes is \$26 (son), \$50 (mother) and \$60 (himself). He purchased these passes for 10 months of the year.
9. As Mr. Brooks contributes every year to the United Way, he is not eligible for the first-time donor's super credit.

**Required:** Calculate, for the 2013 taxation year, Mr. Brooks' minimum Taxable Income and federal Tax Payable (Refund).

**Assignment Problem Four - 5**  
**(Comprehensive Tax Payable With Employment Income)**

Phil Cousteau is an accountant. He works for ModFam Company and was paid a salary of \$70,000 in 2013. He also earned a bonus of \$5,000 in 2013, with one-fifth of the bonus to be paid each year from 2013 to 2017.

During 2013 he received a briefcase worth \$800 as an award for being the "employee of the year" and a Christmas basket from the company worth \$600. All of the Company's employees received a similar basket.

Phil is 47 years old and is married to Claire who is 45 years old and blind. She has no income in 2013 other than \$9,000 in interest on investments she inherited from her mother.

Phil and Claire have two children, a 15 year old daughter, Haley, and a 19 year old son, Manny. Both Haley and Manny live at home.

Haley earned \$800 during 2013 baby-sitting and spent it all on clothes. During 2013, her parents paid for dance classes that cost \$1,000.

Manny has a disability that is not severe enough for his doctor to sign off on the T2201 form. Manny inherited investments from his grandmother and received \$15,000 in interest income from them during 2013.

Phil's brother, Cameron, lives in the basement of Phil's Toronto home. Cameron is 50 years old and his only income for 2013 was EI benefit payments totaling \$3,000. Phil also supports his 85 year old father, Jay, who is physically infirm and lives in a retirement home. Jay had Net Income For Tax Purposes of \$8,500 for 2013. His income consisted of OAS and payments from a registered pension plan.

ModFam transferred Phil from their Toronto office to their Vancouver office in 2013. On April 1, Phil moved his family out of the house they had rented in Toronto for the last 10 years and into a brand new house in Vancouver that cost \$800,000. Although Jay was to stay at the retirement home in Toronto, Cameron moved with the family to Vancouver. Phil was reimbursed by his employer for all of his moving costs. As a consequence, he has no deductible moving costs.

To help finance the new house, ModFam Company lent Phil \$500,000 on April 1 at 1 percent interest. Phil would have paid 5 percent interest on a similar loan from the bank.

ModFam provides Phil with a company car. While he was at the Toronto office, he had a Toyota Highlander that the company leased for \$875 per month (\$50 of which was for insurance). The company paid \$1,600 for the Highlander's other operating costs from January 1 to

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March 31. During that period, Phil drove the car 9,000 kilometers of which 6,000 kilometers were employment related.

On April 1, the Vancouver office gave Phil the keys to a Toyota Camry Hybrid that was purchased for \$31,300. The company paid \$4,500 for the Camry's operating costs from April 1 to December 31. During that period, Phil drove the car 24,000 kilometers of which 10,000 kilometers were employment related.

During 2013, the following amounts were deducted from Phil's pay:

|                               |         |
|-------------------------------|---------|
| Federal Income Tax            | \$8,500 |
| CPP                           | 2,356   |
| EI                            | 891     |
| Group Life Insurance Premiums | 600     |
| Registered Pension Plan       | 1,200   |
| Canada Savings Bonds          | 1,800   |
| United Way Donations          | 1,500   |

The company matched the life insurance and RPP amounts.

During 2013, Phil paid the following amounts of eligible medical expenses:

|         |        |
|---------|--------|
| Himself | \$ 650 |
| Claire  | 1,940  |
| Haley   | 860    |
| Manny   | 1,250  |
| Cameron | 480    |
| Jay     | 990    |

Phil paid \$900 for his 2013 CMA dues. Claire made a \$500 donation to their church during 2013. Because both Phil and Claire contribute to charities on a regular basis, they do not qualify for the first-time donor's super tax credit.

Assume that the prescribed interest rates for 2013 were 2 percent for the first and fourth quarter and 3 percent for the second and third quarter.

**Required:** For the 2013 taxation year, calculate Mr. Cousteau's minimum:

1. Net Income For Tax Purposes,
2. Taxable Income,
3. Federal Tax Owning.

In determining these amounts, ignore GST, PST and HST considerations.

**Assignment Problem Four - 6**  
**(Comprehensive Tax Payable With Employment Income)**

Martin Dorne is 53 years old and employed in construction work by a large public company. His annual salary is \$98,500, none of which involves commissions. As the company was very successful during 2013, Martin has been provided with a \$15,000 bonus. This bonus will be paid in equal amounts (\$3,000) over the period 2013 through 2017.

Martin's employer withheld maximum EI premiums and CPP contributions, along with \$18,000 in federal income taxes. Other amounts withheld by his employer are as follows:

|                   |         |
|-------------------|---------|
| RPP Contributions | \$4,300 |
| Union Dues        | 450     |

Martin's common-law partner is Brian Lassiter. Brian is 48 years old and is legally blind. Brian has 2013 income from investments of \$9,400.

Eight years ago, Martin and Brian adopted three brothers from a third-world country. Information on these children is as follows:

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**David** is 15 years old, in good health, and has income from part time jobs of \$10,500.

**Devon** is 20 years old and has serious breathing problems that prevent him from working on a full time basis. He lives with Martin and Brian and has income from part time jobs of \$5,150.

**Derek** is 22 years old and attends university on a full time basis for 8 months of the year. Martin pays his tuition fees of \$10,300, along with textbook costs of \$1,200. He lives with Martin and Brian and is in good health. He has self-employed income of \$13,500. Assume he pays no CPP contributions on this income.

**Other Information:**

1. During 2013, Martin spent \$12,300 on employment related meals and entertainment with clients of his employer. His employer reimbursed \$7,300 of these costs.
2. During 2013, Martin makes his regular annual contribution of \$2,000 to a registered charity, The Shepherds Of No Hope. (Martin is a very pessimistic individual.)
3. The family's 2013 medical expenses, all of which were paid by Martin, were as follows:
 

|                  |          |
|------------------|----------|
| Martin and Brian | \$ 2,200 |
| David            | 1,700    |
| Devon            | 10,600   |
| Derek            | 4,500    |
4. Martin buys monthly transit passes for David and Derek. The cost is \$85 per month per child. The passes covered 10 months during 2013.
5. During 2012, Martin received options to purchase 500 shares of his employer's stock at a price of \$45 per share. At the time the options were granted, the market price of the shares was \$50 per share. During July, 2013, when the shares are trading at \$70 per share, Martin exercises all of these options. He is still holding these shares on December 31, 2013.
6. As interest rates continue to be very favourable, Martin and Brian purchase a residence near the rented residence that they have lived in for the last 15 years. The cost of the new residence is \$480,000 and, to assist with the purchase, Martin's employer provides a \$280,000 interest free loan. The loan was granted on July 1, 2013 and will have to be repaid on July 1, 2018. Assume the prescribed rate is 1 percent throughout the year 2013.
7. Martin is provided with an automobile by his employer. The automobile was purchased at a cost of \$45,200, including HST at 13 percent. During 2013, the automobile is driven 48,000 kilometers, of which 37,000 were employment related. The automobile was used by Martin for 11 months during 2013. He was required to return the automobile to his employer's garage during the month that he did not use it.
8. During 2013, Martin receives several gifts from his employer:
  - As is the case for all of the company's employees, Martin receives a \$250 gift certificate that can be used for merchandise at a local department store.
  - In recognition of his 10 years of service, Martin receives an engraved wrist watch. The retail value of this watch is \$800.
  - At Christmas, all of the company's employees receive a gift box of vintage wines. The retail value of these wines is \$400.

**Required:**

- A. Determine Martin's minimum Net Income For Tax Purposes for the 2013 taxation year.
- B. Determine Martin's minimum Taxable Income for the 2013 taxation year.
- C. Based on your answer in Part B, determine Martin's federal Tax Payable and amount owing (refund) for the 2013 taxation year.

## Tax Software Assignment Problems

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(The solutions for these problems are only available in the solutions manual that has been provided to your instructor.)

### Tax Software Assignment Problem Four - 1

**DISCLAIMER:** All characters appearing in this problem are fictitious. Any resemblance to real persons, living or dead, is purely coincidental.

**This problem is continued in Chapter 11.**

Mr. Buddy Musician (SIN 527-000-061) was born in Vancouver on August 28, 1945. He has spent most of his working life as a pianist and song writer. He and his family live at 111 WWW Street, Vancouver, B.C. V4H 3W4, phone (604) 111-1111.

Mr. Musician's wife, Natasha (SIN 527-000-129), was born on June 6, 1987. She and Mr. Musician have four children. Each child was born on April 1 of the following years, Linda; 2007, Larry; 2008, Donna; 2009, and Donald; 2010. Natasha's only income during 2012 is \$4,800 [(4)(\$100)(12)] in universal child care benefits.

Buddy and Natasha Musician have two adopted children. Richard (SIN 527-000-285) was born on March 15, 1995 and has income of \$2,800 for the year. Due to his accelerated schooling, he started full time attendance at university in September of 2012 at the age of 17. His first semester tuition fee is \$3,000 and he requires books with a total cost of \$375. These amounts are paid by Mr. Musician.

The other adopted child, Sarah, was born on September 2, 1992, and is in full time attendance at university for all of 2012 (including a four month summer session). Her tuition is \$9,600 and she requires textbooks which cost \$750. These amounts are also paid by Mr. Musician. Sarah has no income during the year.

Neither Richard nor Sarah will have any income in the next three years. Any unused credits of either child are available to be transferred to their father.

Mr. Musician's mother, Eunice, was born on April 10, 1925 and his father, Earl, was born on November 16, 1923. They both live with Mr. Musician and his wife. While his father is still physically active, his mother is blind. Eunice Musician had income of \$9,500 for the year, while Earl Musician had income of \$7,500.

Other information concerning Mr. Musician and his family for 2012 is as follows:

1. Mr. Musician earned \$16,500 for work as the house pianist at the Loose Moose Pub. His T4 showed that his employer withheld \$500 for income taxes and \$301.95 for EI. No CPP was withheld as he has filed an election to stop contributing to the CPP.
2. During the year, Mr. Musician made \$3,000 in donations to Planned Parenthood Of Canada, a registered Canadian charity.
3. Mr. Musician has been married before to Lori Musician (SIN 527-000-319). Lori is 52 years old and lives in Fort Erie, Ontario.
4. Mr. Musician has two additional children who live with their mother, Ms. Dolly Nurse (SIN 527-000-582), in Burnaby, British Columbia. The children are Megan Nurse, aged 12 and Andrew Nurse, aged 14. Neither child has any income during 2012. While Ms. Nurse and Mr. Musician were never married, Mr. Musician acknowledges that he is the father of both children. Although Buddy has provided limited financial aid, the children are not dependent on Buddy for support.
5. Mr. Musician wishes to claim all his medical expenses on a calendar year basis. On December 2, 2012, Mr. Musician paid dental expenses to Canada Wide Dental Clinics for the following individuals:

*Tax Software Assignment Problems*

|   |                |
|---|----------------|
| Himself                                     | \$1,200        |
| Natasha (wife)                              | 700            |
| Richard (adopted son)                       | 800            |
| Sarah (adopted daughter)                    | 300            |
| Linda (daughter)                            | 100            |
| Earl (father)                               | 1,050          |
| Lori (ex-wife)                              | 300            |
| Dolly Nurse (mother of two of his children) | 675            |
| Megan Nurse (daughter of Dolly Nurse)       | 550            |
| <b>Total</b>                                | <b>\$5,675</b> |

- Mr. Musician paid four quarterly instalments of \$1,000 each (total of \$4,000) for 2012, as requested on his Instalment Reminders from the CRA. He paid each instalment on the due date.
- Assume that Mr. Musician has not applied to receive either OAS or CPP benefits.

**Required:** With the objective of minimizing Mr. Musician's Tax Payable, prepare his 2012 income tax return using the ProFile tax software program. List any assumptions you have made, and any notes and tax planning issues you feel should be placed in the file.

***Tax Software Assignment Problem Four - 2***

**DISCLAIMER:** All characters appearing in this problem are fictitious. Any resemblance to real persons, living or dead, is purely coincidental.

**This problem is continued in Chapter 11.**

George Pharmacy is a pharmaceutical salesman who has been very successful at his job in the last few years. Unfortunately, his family life has not been very happy. Three years ago, his only child, Anna, was driving a car that was hit by a drunk driver. She and her husband were killed and their 13 year old son, Kevin, was blinded in the accident. He also suffered extensive injuries to his jaw that have required major and prolonged dental work.

George and his wife, Valerie, adopted Kevin. Valerie quit her part-time job to care for him. She also cares for her mother, Joan Drugstore who lives with them. Joan suffers from dementia, Parkinson's and severe depression. The family doctor has signed a letter stating that she is dependent on George and Valerie because of her impairments. Joan does not meet the residency requirements necessary to qualify for Canadian Old Age Security payments.

Valerie's parents separated two years ago in Scotland after her father, David Drugstore, suffered enormous losses in the stock market. They were forced to sell their home and David moved to Chile. David phones periodically to request that money be deposited in his on-line bank account.

George's brother, Martin, completed an alcohol rehabilitation program after being fired for drinking on the job. He is also living with George and Valerie while he is enrolled as a full time student at Western University. George is paying his tuition and Martin has agreed to transfer any available education related amounts to George. Although Martin plans to file his 2012 tax return, he has not done so yet.

In addition to George's salary, he also earns commissions. His employer requires him to have an office in his home and has signed the form T2200 each year to this effect.

Other information concerning George for 2012 is given on the following pages.

**Required:** Prepare the 2012 income tax return of George Pharmacy using the ProFile tax software program. List any assumptions you have made, and any notes and tax planning issues you feel should be placed in the file. Ignore HST implications in your solutions.

## Tax Software Assignment Problems

| Personal Information                                  | Taxpayer    |
|---|-------------|
| Title   | Mr.         |
| First Name  | George      |
| Last Name   | Pharmacy    |
| SIN   | 527-000-509 |
| Date of birth (Y/M/D)                                 | 1948-07-02  |
| Marital Status  | Married     |
| Canadian citizen?                                     | Yes         |
| Provide information to Elections Canada?              | Yes         |
| Own foreign property of more than \$100,000 Canadian? | No          |

| Taxpayer's Address                      |
|---|
| 123 ZZZ Street, London, Ontario N0Z 0Z0 |
| Phone number (519) 111-1111             |

| Family Members        | Spouse         | Child       | Mother-In-Law |
|-----------------------|----------------|-------------|---------------|
| First Name            | Valerie        | Kevin       | Joan          |
| Last Name             | Pharmacy       | Pharmacy    | Drugstore     |
| SIN                   | 527-000-483    | 527-000-517 | None          |
| Date of birth (Y/M/D) | 1947-12-30     | 1996-10-17  | 1927-02-24    |
| Net income            | \$5,800 in CPP | Nil         | \$500         |

| Family Members        | Father-In-Law | Brother     |
|-----------------------|---------------|-------------|
| First Name            | David         | Martin      |
| Last Name             | Drugstore     | Pharmacy    |
| SIN                   | None          | 527-000-533 |
| Date of birth (Y/M/D) | 1928-01-12    | 1965-06-02  |
| Net income            | Nil           | \$8,300     |

For 2012, George received two children's fitness tax receipts, one from a swim club for \$300 and one from a summer day camp for \$400. He also received a children's arts tax receipt of \$250 for a course at a local theatre school.

During September, David was arrested in Chile. Valerie had to spend three weeks in Chile and \$2,000 in bribes before she could get him released from jail. George had to pay Nannies On Call \$3,500 for in-home help to take care of Kevin while she was gone.

| T2202A - (Martin)                            | Box | Amount |
|--|-----|--------|
| Tuition fees - for Martin Pharmacy (brother) | A   | 6,000  |
| Number of months in school - part-time       | B   | 0      |
| Number of months in school - full-time       | C   | 8      |

## Tax Software Assignment Problems

| T4                           | Box | Amount     |
|------------------------------|-----|------------|
| Issuer - Mega Pharma Inc.    |     |            |
| Employment income            | 14  | 378,000.00 |
| Employee's CPP contributions | 16  | 2,306.70   |
| Employee's EI premiums       | 18  | 839.92     |
| Income tax deducted          | 22  | 114,000.00 |
| Employment commissions       | 42  | 82,000.00  |
| Charitable donations         | 46  | 400.00     |

During 2012, Mega reimbursed George \$3,788 for meals and entertainment with clients, \$2,268 for hotels and \$4,925 for airline tickets.

| Donor   | Charitable Donation Receipts            | Am't  |
|---------|---|-------|
| Valerie | Mothers Against Drunk Drivers (MADD)    | 1,000 |
| George  | Canadian Institute For The Blind (CNIB) | 3,000 |

| (Y/M/D)    | Patient | Medical Expenses        | Description             | Am't      |
|------------|---------|-------------------------|-------------------------|-----------|
| 2012-12-31 | George  | Johnson Inc.            | Out of Canada insurance | 731.30    |
| 2012-08-31 | George  | Dr. Smith               | Dental fees             | 155.40    |
| 2012-09-19 | George  | Optician                | Prescription glasses    | 109.00    |
| 2012-11-07 | Valerie | Pharmacy                | Prescription            | 66.84     |
| 2012-06-07 | Joan    | Dr. Wong                | Psychiatric counseling  | 2,050.00  |
| 2012-03-22 | David   | Tropical Disease Centre | Prescription            | 390.00    |
| 2012-12-20 | Martin  | Dr. Walker              | Group therapy           | 6,000.00  |
| 2012-10-01 | Kevin   | Dr. Takarabe            | Orthodontics and Dental | 30,000.00 |

George paid \$800 for the care and feeding of Kevin's seeing eye dog, Isis, during 2012.

| House Costs   |       |
|---|-------|
| Area of home used for home office (square feet)         | 650   |
| Total area of home (square feet)                        | 5,000 |
| Telephone line including high speed internet connection | 620   |
| Hydro   | 3,200 |
| Insurance - House                                       | 4,000 |
| Maintenance and repairs                                 | 3,800 |
| Mortgage interest                                       | 6,200 |
| Mortgage life insurance premiums                        | 400   |
| Property taxes  | 6,700 |

During 2012, George purchased a new computer and software that will be used solely in his home office for employment related uses. The computer cost \$3,600 and the various software programs cost \$1,250.

**Tax Software Assignment Problem Four - 3**

This Tax Software Assignment Problem is introduced in this Chapter and is continued in Chapters 6 through 11. More information is provided in subsequent chapters that is related to the material covered in that Chapter. Each Tax Software Assignment Problem must be completed in sequence. The information in each problem is applicable to all subsequent problems.

**DISCLAIMER:** All characters appearing in all versions of this problem are fictitious. Any resemblance to real persons, living or dead, is purely coincidental.

Seymour Career and Mary Career are your tax clients. They have been married for two years. In late December, 2012, Mary comes to your office with the tax information for 2012 which she has managed to obtain before the end of the year.

Mary has progressed quickly in MoreCorp, the large, publicly traded firm she is working for due to her strong tax and accounting background. She has been rewarded with a large bonus in 2012. Her firm has an excellent health and dental plan that reimburses 100 percent of all medical expenses.

Although Seymour has been working, his increasing ill health makes it likely that he will not be able to continue to work in 2013. He is contemplating a return to university as a student of music.

In order to estimate her possible financial position in 2013, she would like you to prepare her 2012 tax return assuming that Seymour has no income for 2012. As she is expecting a promotion and the choice of working in any of MoreCorp's offices across Canada, she would also like you to compare her 2012 tax liability in all the different provinces and territories except Quebec assuming Seymour has no income for 2012.

| Personal Information                             | Taxpayer    | Spouse      |
|--|-------------|-------------|
| Title  | Ms.         | Mr.         |
| First Name                                       | Mary        | Seymour     |
| Last Name  | Career      | Career      |
| SIN  | 527-000-129 | 527-000-079 |
| Date of birth (Y/M/D)                            | 1974-12-08  | 1953-01-29  |
| Marital status                                   | Married     | Married     |
| Canadian citizen?                                | Yes         | Yes         |
| Provide information to Elections Canada?         | Yes         | Yes         |
| Own foreign property of more than \$100,000 Cdn? | No          | No          |

| Taxpayer's Address                       |
|--|
| 123 ABC Street, Saint John, N.B. E0E 0E0 |
| Phone number (506) 111-1111              |
| Spouse's address same as taxpayer? Yes   |



| Dependant             | Child       |
|-----------------------|-------------|
| First Name            | William     |
| Last Name             | Career      |
| SIN                   | 527-000-319 |
| Date of Birth (Y/M/D) | 2005-02-24  |
| Net Income            | Nil         |

| T4 - Mary                    | Box | Amount     |
|------------------------------|-----|------------|
| Issuer - MoreCorp            |     |            |
| Employment Income            | 14  | 152,866.08 |
| Employee's CPP Contributions | 16  | 2,306.70   |
| Employee's EI Premiums       | 18  | 839.97     |
| RPP Contributions            | 20  | Nil        |
| Income Tax Deducted          | 22  | 48,665.11  |
| Charitable Donations         | 46  | 1,000.00   |

| Donor   | Charitable Donation Receipts | Amount |
|---------|------------------------------|--------|
| Seymour | Canadian Cancer Foundation   | 500    |
| Seymour | Salvation Army               | 250    |

**Required:**

- With the objective of minimizing Mary's Tax Payable, prepare, but do not print, her 2012 income tax return using the ProFile tax software program. Assume that Seymour has no income in 2012. **Hint:** On her "Info" page, answer "Yes" to the question in the spousal information box "Is spouse's net income zero?". List any other assumptions you have made and provide any explanatory notes and tax planning issues you feel should be placed in the files.
- Access and print Mary's summary (Summary on the Form Explorer, not the T1Summary). This form is a two column summary of the couple's tax information. In this version, the second column is blank.
- Create and print a separate table (not in ProFile) that compares the total federal and provincial Tax Payable (Refund) for Mary for all the territories and provinces other than Quebec. **Hint:** On the "Info" screen, you can change the province of residence. (You must press the "Enter" key for the change to take effect.) The data monitor at the bottom of the screen should show the new balance/refund. The difference can also be seen on the "Summary" form. To see a detailed analysis of the effect of various changes such as province of residence, use the "Snapshot/Variance" feature (information on this feature is available from the Help menu) to create a separate snapshot of the finished return for Mary. Then open the Auditor <F9> and select the Variance tab.