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In This Issue...

Potential HST Surprise for Medical Practitioners

By Terry Soloman, CPA, CA, TEP
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If you are a physician who has structured your practice as a business (whether as a professional corporation, partnership or proprietorship), you no doubt are aware of the many income tax complexities of running a small business. However, you may not be aware of potential HST obligations that could also apply to your practice.

Many small business owners, including physicians, are aware of the general threshold of $30,000 of HST taxable revenues over your four previous calendar quarters before your business is required to become a HST registrant. Once this threshold is exceeded, failure to register for and collect HST on taxable revenue can result in unexpected HST liabilities, interest and penalties if subsequently discovered by Canada Revenue Agency.

As a medical practitioner, you can take some comfort that the HST legislation exempts medical services of a consultative, diagnostic, or treatment nature when rendered to an individual patient or if the service is covered under a provincial healthcare plan. However, in recent years the types of services delivered by medical practitioners has continued to expand and the Canada Revenue Agency has legislatively and administratively narrowed the types of services that would fall under this general exemption.

The types of services that may attract HST, although not exhaustive, would include:

- Medical/legal reports for Court proceedings or insurance claims
- Expert opinion reports and expert witness fees
- Cosmetic procedures
- On call payments
- Department head fees, if not rendered as an employee
- Preparation of disability certificate forms, CPP disability, drivers license and similar reports
- Consulting services, including medical research and clinical trials
- Block or annual fees

In the late fall of 2014, Canada Revenue Agency released GST/HST Notice 286 containing a draft GST/HST Policy Statement which outlines in some detail their position on the HST application of various services provided by physicians and provides additional guidance and rationale to the above noted list.

If you are required to become a HST registrant, there may also be an opportunity to recover a portion of HST paid on the operating expenses of your practice, depending on the portion of your practice that is engaged in HST taxable activities.

Should you have any questions about this matter or how it may apply to your practice, I would encourage you to contact your DFK sales tax specialist.

More Fallout from the Graduated Rate Estate ("GRE") Tax Rules

By Deanne Muise, CPA, CA, TEP
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Estates and trusts created through Wills ("Testamentary Trusts") are now divided in to GRE's and non-GRE's. GRE's enjoy graduated tax rates for a three year period and then become non-GRE's. Generally, any income taxed in a non-GRE estate or trust is subject to the highest personal tax rates AND a calendar year-end must be adopted.

Prior to 2016, Part XII.2 tax did not apply to Testamentary Trusts and was, in fact, rarely a consideration. With the dawn of GRE and non-GRE estates/trusts, these rules are now very much an issue for many non-GRE trusts. In circumstances where the trust has at least one "designated beneficiary" and earns "designated income" which is paid or payable to any beneficiary, Part XII.2 tax applies at a rate of 40% of the lessor of:

- "Designated Income" of the trust;
- The trust's total income prior to deductions for amounts paid or payable to beneficiaries; and
- 100/60 of the amounts deductible from the trust's income as paid or payable to beneficiaries.

"Designated beneficiaries", include:

- Non-residents of Canada
- Charities, Not for Profit organizations and First Nations (some exceptions apply)
- Certain other entities that act as intermediaries for the above two.

"Designated income", includes income from:

- Canadian real estate, timber or other resource properties (both income and capital gains);
- Income from gains on shares of corporations that derive their value from Canadian real estate, timber or other Canadian resource properties;
- Businesses operated in Canada; and
- Certain other gains that may result from complex emigration planning

This tax is applicable if any amount is paid or payable to ANY beneficiary, even to the Canadian resident ones; however, there is a tax credit available for the Canadian resident beneficiaries.

It is becoming more and more frequent for the children or grandchildren of Canadians to move to the U.S. for employment purposes. If a child or grandchild (or anyone else) is a beneficiary of your estate and they reside in the U.S. (or any other country), then these rules may very well apply to your estate if the estate carries on a business or earns income or capital gains from Canadian real estate or resource properties held directly or indirectly through a corporation.

A common example: you leave your principal residence to your estate that rents the property out and/or sells the property for a gain subsequent to the estate being a GRE (i.e. generally if the estate carries on for more than 3 years). If one of the children or grandchildren that are beneficiaries (or any other beneficiary) are living outside Canada, then the estate is subject to these rules and may have to pay the tax. In circumstances where amounts are not paid or payable to any beneficiaries, these rules will not apply. Note that the terms of your Will govern whether or not options exist to tax the income in the trust. As the costs of this tax can be significant, it is strongly recommended that in circumstances where your beneficiaries are or may become non-residents of Canada, your Will be reviewed to ensure your executors/ trustees have the flexibility to retain income in the estate/trust in cases where it is beneficial to do so.

Bonus Payable In Shares

By Christie Hoem-McNall, CPA, CA
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In a recent technical interpretation, the CRA considered the applicability of a subsections 7(1) or (1.1), dealing with employment income inclusions, to an employment bonus paid via the issuance of shares.

Subsection 7(1) of the Income Tax Act ("ITA") deems an employment income inclusion where an employer agrees to sell or issue securities to an employee. This benefit is equal to the difference between the fair market value of the securities at the time they are acquired by the employee and the actual amount paid by the employee, that is, the difference between their fair market value and their strike or exercise price. Under subsection 7(1), this benefit is included in the employee's income in the year that the employee acquires the securities. However, it is possible to defer the employment benefit until the securities are disposed of by the employee pursuant to subsection 7(1.1) if the securities acquired were those of a Canadian - Controlled Private Corporation ("CCPC"). In addition, subsection 110(1)(d.1) can provide for a deduction of 50% of this employment benefit where the shares acquired by an employee were those of a CCPC and certain other criteria is met.

If a CCPC employer were to provide an employment bonus that is paid via the issuance of its shares, the question posed to the CRA was whether subsection 7(1.1) would apply so that no taxable income will be included in the employee's income until the year of disposition of the securities by the employee.

The response from the CRA outlined that whether either subsection 7(1) or 7(1.1) would apply to such an issuance depended on whether there was a legally binding agreement for the corporation to issue the shares. If an arrangement for such an issuance is expressly discretionary and no legal rights or obligations are created, it will not fall within Section 7. Whether or not an arrangement is legally binding is a question of fact; however, the CRA stated that if the decision to issue the shares is placed in the hands of the employer, the conditions of a legally enforceable commitment have not been met and therefore the issuance would not be subject to the provisions of Section 7. On the other hand, if an employer puts in place an arrangement whereby the employer agrees to award a bonus on the condition that the employee achieves certain measurable performance objectives and the employer agrees to pay the bonus in shares, then such arrangement could be an agreement contemplated by Section 7.

The CRA went on to comment that subsection 7(1.1) changes the time at which an employee is deemed to have received a benefit in respect of shares of a corporation, one of the conditions of which is that the corporation is a CCPC. Where an agreement gives an employee the choice between a stock bonus or a cash bonus and the employee elects payment in shares, the time at which the employee is deemed to have received a benefit is the taxation year in which the employee disposed of the shares or exchanged the shares instead of the taxation year in which the shares were acquired.

It should be noted that if Section 7 does not apply, the full value of the shares will be considered employment income, with no 50% deduction available. As well, the benefit will arise at the time of issuance of the shares, rather than being deferred until their sale. However, the impact on the employer also varies. Where Section 7 applies, the employer receives no deduction in respect of the shares issued to the employee. Where it does not, the employer is able to deduct the value of the shares in its corporate income tax return. For these reasons, employment contracts where the issuance of shares are considered should be carefully reviewed for income tax obligations to both the employee and the corporation prior to execution.

Will the 2017 Federal Budget Increase the Capital Gains Tax?

By John Connolly, BBA, CPA, CMA
MRSB Group

The income tax rate on capital gains is currently half the rate that applies to ordinary income, because you only include 50% of your capital gains in your income. The following chart compares the 2017 combined Federal & P.E.I. personal income tax rates for the top tax bracket (income over $202,800).

	Ordinary Income	Eligible Dividends	Ineligible Dividends
	51.37%	34.22%	43.87%
Capital Gains	25.69%	25.69%	25.69%
Difference	25.68%	8.54%	18.18%

In 2015, the Federal Liberal government was elected on a platform that included modifying or eliminating certain tax benefits and tax credits that primarily benefited the wealthy, and increasing income taxes on the top 1% of income earners. That platform is fueling speculation that they may increase the tax rate on capital gains in the coming 2017 Budget. There was similar speculation in the weeks leading up to the 2016 Budget, but the rate was not increased last March.

In the past, the capital gains inclusion rate has been 75% and 2/3. If the 2017 Budget increases the inclusion rate to 75%, the P.E.I. combined top tax rate on capital gains would be 38.53%, or 34.25% for a 2/3 inclusion rate. Regardless of what tax bracket you are in, raising the inclusion rate to 75% would increase the tax on your capital gains by 50%. Raising the inclusion rate to 2/3 would increase the tax on your capital gains by 1/3.

No one can say for sure if or when the capital gains inclusion rate will increase. Prepaying income tax to avoid a rate increase that does not happen would be expensive. So, what should you do?

Capital gains are taxed when you sell or dispose of a capital asset that has increased in value since you acquired it. Do you expect to realize a significant capital gain in the near future? You may be able to avoid a tax increase by crystalizing that gain before the 2017 budget, because income tax increases generally are not retroactive.

If you are not already planning to sell or dispose of an asset with an accrued gain, you may be able to protect yourself from a rate increase depending on your personal situation.

Tax planning you have set up for your current income, the succession of your business, or passing on of your estate to the next generation could all be affected by an increase in the capital gains inclusion rate.

We recommend that you get professional advice specific to your personal situation from your tax adviser.