**Canadian Income Taxation: Planning and Decision Making- 2019-2020 Edition**

**Exam Case Questions**

Cases 1 – 4 address material from the first ten chapters. Cases 5 – 10 cover both personal and corporate tax issues. Cases 11 to 13 covers material from specific chapters (detailed below). The cases have been designed to allow instructors to delete paragraphs that may be more advanced in nature, thus tailoring each case to the material that has been covered in class.

‘Required’ questions have been provided with the cases, though instructors may choose to omit these and simply request that reports be written for the individuals and or the businesses.

Case One addresses concepts found in Chapters 3, 4, 6, and 9.

Case Two addresses concepts found in Chapters 3, 4, 5, 8, and 10.

Case Three addresses concepts found in Chapters 3, 8, 9, and 10.

Case Four addresses concepts found in Chapters 7, 8, 9, and 10.

Case Five addresses concepts found in Chapters 3, 4, 5, 6, 9, 10, 11, and 13.

Case Six addresses concepts from Chapters 5, 6, 8, 10, 12, and 13.

Case Seven addresses concepts from Chapters 3, 4, 5, 6, 7, 8, 9, 10, and 11.

Case Eight addresses concepts from Chapters 3, 4, 5, 6, 7, 8, 9, 10, 11, 12, 14, and 15.

Case Nine addresses concepts from Chapters 3, 4, 5, 7, 8, 10, 13, 14, and 19.

Case Ten addresses concepts from Chapters 5, 7, 10, and 12.

Case Eleven addresses concepts from Chapter 18.

Case Twelve addresses concepts from Chapter 12.

Case Thirteen addresses concepts from Chapter 13.

**Exam Case One**

It is March of 20x5 and George White has asked you to help him with his 20x4 taxes. During your meeting with George you learn the following:

George is thirty years old, divorced, and has an eight-year-old son from his former marriage. He pays $500 a month in child support.

George lives in City A, where he is a salesman for a large manufacturing plant. He receives a base salary of $4,000 per month plus a commission of 1% on the sales he makes in the month. His sales were $50,000 every month in 20x4.

George moved to City A from City B on December 1st of 20x3 when he was promoted and transferred with his company to the office in City A. George’s tax deductible moving expenses totaled $9,500. He did not receive a reimbursement from his employer. He was able to claim $4,500 of this expense on his 20x3 tax return. George took out a $120,000 mortgage to purchase his new home. His interest payments were $8,400 in 20x4.

In order to perform his work duties, George is required to drive his own vehicle and pay for his expenses, for which he is not reimbursed. However, he does receive an allowance of $400 each month which is treated as unreasonable for tax purposes. George purchased a new car in 20x3 which he uses seventy-five percent of the time for business purposes. The undepreciated capital cost of the vehicle at the beginning of 20x4 was $28,000. Total costs to operate the vehicle are $800 per month. Interest expense on his car loan is $200 per month.

George spends $300 per month on suits for work. He also updates his cell phone regularly and typically spends $500 per year on a new phone. George’s cell phone bill is $80 per month, of which twenty-five percent is for personal use.

George takes his files home with him at the end of the day and reviews his sales calls in his home office. He then returns the files to his office at his place of employment in the morning prior to leaving for the day to make sales calls. George’s monthly total expense for his home insurance, property taxes, maintenance, and utilities is $1,000. His home office occupies ten percent of the square footage in his home.

George maximizes his RRSP contribution each year. His earned income in 20x3 was $42,000 which consisted of $6,000 in commissions.

**Required:**

(Use tax rules applicable for 2019.)

1. Calculate George’s minimum net income for tax purposes for 20x4. Use the aggregating formula from Section 3 of the Income Tax Act to show your answer.
2. Indicate why any items have been omitted from your calculations.

**Solution:**



**ITA 3(a):**

Employment income:

Salary (12 x $4,000) $48,000

Travel allowance (12 x $400) (unreasonable) 4,800

Commissions (12 x $50,000 x .01) 6,000

$58,800

Salesperson expenses:

Phone expense ($80 x 12) $ 960

Automobile operating costs

12 x $800 $9,600

$10,560

Employment portion 75% x $10,560 $7,920

Limited to commission income ( 6,000)

Other automobile costs:

Capital cost allowance

30% x $28,000 $8,400

Interest on car loan

$200 x 12 2,400

$10,800

Employment portion 75% x $10,800 ( 8,100)

Employment income $44,700

**ITA 3(c):**

Other deductions:

Moving expenses (carry-forward portion from 20x3: $9,500-4,500) ( 5,000)

RRSP contribution

Lesser of: 18% x $42,000 (20x3 earned income)

Limit: $26,500 (2019) ( 7,560)

Net income for tax purposes (20x4) $32,140

1. The following items have been omitted from the calculations:
   1. Child support is not a deductible expense.
   2. Clothing is not a deductible expense.
   3. The cell phone purchase is a capital outlay, so denied as an expense, and CCA is not allowed on this type of capital asset for an employee.
   4. Home office expense: George would have to perform more than 50% of his duties from this office, or he would have to use the office exclusively to earn income on a regular and continuous basis to meet with clients. He has not met either of these tests.
   5. Personal mortgage interest is not a deductible expense.

**Exam Case Two**

It is February 1st, 20x8 and Chloe and Bart have come to ask you some questions regarding their 20x7 tax returns. The couple lives in a common-law relationship. Bart is a chef at a luxury hotel and Chloe is an electrician in a nearby city.

Bart’s remuneration (salary) in 20x7 was $84,000. The following information is available from Bart’s 20x7 T4 slip:

Deductions from pay:

CPP and EI 3,609

Registered Pension Plan Contribution 2,000

Income tax deducted 25, 000

Bart’s employer contributes an equal portion to Bart’s RPP. Bart is also provided with a company car for use during the entire year. The car is leased by the hotel. Lease payments are $550 per month. The hotel pays $400 per month for the operating costs of the vehicle. Bart drove the car a total of 22,000 kilometres last year. 9,000 of these were for personal travel. Bart also earned $3,000 in 20x7 from the restaurant’s tip pool. His employer did not report the tips on Bart’s T4.

Bart withdrew $10,000 from his RRSP in 20x7 for use other than education or home ownership. Both Bart and Chloe contribute to their TFSAs each year. They each have a balance of $8,000 in their TFSAs, bearing 3% annual interest.

Chloe earns $65,000. She is waiting for her T4 from the electrical company to arrive in the mail, so will address some other issues at this point in time which she believes might affect her 20x7 taxes.

1. She sold a small piece of land in 20x7 (which is capital in nature) for $68,000. The land originally cost $50,000. Selling costs were $800. She received $35,000 of the proceeds in 20x7 and will receive the remainder of the funds this year (20x8).
2. Chloe began a small farming operation on the couple’s acreage in 20x7. Her farm revenue totaled $5,000 in 20x7 and her expenses were $17,000. She has never farmed before, but her business looks promising and she expects a significant increase in sales in 20x8.

**Required:**

(Use tax rules applicable for 2019.)

1. Calculate Bart’s minimum net income for tax purposes, and taxable income, for 20x7. Show your work using the statutory formula from Section 3 of the Income Tax Act.
2. Calculate Bart’s federal tax liability for 20x7.
3. Calculate the 20x7 tax consequences from Chloe’s two issues.

**Solution:**

ITA 3(a)

Employment income:

Remuneration $84,000

Gratuities 3,000

Standby charge 1,980

[($550 x 2/3 x 12) x 9,000/(1,667 x 12)]

Operating benefit

Lessor of $2,520 ($9,000 x .28)

and $990 ($1,980 x .5) 990

RPP contribution (2,000)

Employment income $87,970

ITA 3(c)

Other income:

RRSP withdrawal $10,000

Net income for tax purposes $97,970

Taxable income $97,970

(Amounts are rounded)

1. Federal tax liability



1. 1. Capital gain on sale of land

Proceeds $68,000 – Adjusted cost base $50,000 – Selling costs $800 = Capital gain of $17,200



Chloe will have a taxable capital gain this year of $4,426 (rounded) due to the deferral of a portion of the proceeds.

2. Farming income loss

Revenue $ 5,000

Expenses ($17,000)

Net loss for tax purposes ($12,000)

Since farming is not Chloe’s chief source of income, the amount of her loss will be restricted. She will be allowed to deduct $7,250\*:

$2,500 + 50% ($12,000 - $2,500) = $7,250

\*(Restricted farm loss cannot exceed $17,500)

The $4,750 difference between this year’s $12,000 loss and the allowable deduction of $7,250 can be carried back three years or forwards twenty years and applied against Chloe’s farming income. (Since she did not farm prior to 20x7, the loss will be carried forward.)