CHAPTER 6

Taxable Income And Tax Payable For Individuals

Introduction

6-1. You may recall from Chapter 3 that 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 3 material was the fact that Net Income For Tax Purposes is made up of several different income components. The more important of these components are employment income, business and property income, taxable capital gains, other sources, and other deductions.

6-2. Most tax texts, including earlier editions of *Canadian Tax Principles*, have deferred any coverage of Taxable Income until all of the income components that make up Taxable Income 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.

6-3. The major reason for this approach is that it allows us to introduce the 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 on business income, property income, and taxable capital gains that follows. For example, in our discussion of property income, we can now 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.

6-4. Other reasons for this organization of the material are more pedagogical in nature. One factor here is the fact that 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 week of most one semester tax courses. This appears to create significant difficulties for students. A further consideration is the fact that, 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.

6-5. Since a significant portion of the material on Taxable Income 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 14 is devoted to completing the necessary coverage of Taxable Income and Tax Payable for individuals. For corporations, these subjects are covered in Chapters 15 and 16.

Taxable Income Of Individuals

Available Deductions

6-6. 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 preceding section, some of these deductions will be dealt with in this Chapter. However, coverage of the more complex items is deferred until Chapter 14. 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 5. This coverage will not be repeated here. There are, however, some additional and more complex issues related to stock options. These include revoked elections, application of the identical property rules on dispositions, and stock options held at the time of emigration. These subjects are dealt with in Chapter 14.

ITA 110(1)(f) - Deductions For Payments This deduction, which is available for social assistance and workers' compensation received, is covered beginning in Paragraph 6-8.

ITA 110(1)(j) - Home Relocation Loan We refer to this deduction in Chapter 5 as it is related to a taxable benefit that is included in employment income. However, more detailed coverage is found beginning in Paragraph 6-10.

ITA 110.2 - Lump Sum Payments This Section 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 periods (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 14.

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 6-14.

ITA 111 - Losses Deductible This is a group of deductions that is available for carrying over various types of losses from preceding or subsequent taxation years. 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 14.

Ordering Of Deductions

6-7. In a complete calculation of Taxable Income, the order in which the Division C deductions are made can be of some importance. In addition, ITA 111.1 contains an ordering provision that specifies, at least to some degree, the order in which deductions in this calculation must be made (e.g., the ITA 110 deductions must be made prior to the ITA 111 deductions for losses). Complete coverage of ordering issues is provided in Chapter 14. With respect to the deductions covered in this Chapter, the ITA 110 deductions can be made in any order. However, ITA 111.1 requires that the 110.7 northern residents deductions be made after any deductions that are available under ITA 110.

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

6-8. 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 convention 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.

6-9. 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? 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. We will find later in this Chapter that the amount of the available tax credit for a spouse is reduced or eliminated based on the Net Income For Tax Purposes of that spouse. In order to ensure that income tests of this type are applied on an equitable basis, amounts are left 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)

6-10. As discussed in Chapter 5, 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 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".

6-11. 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 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 in Chapter 11, the distance is the same 40 kilometer criteria that is used in determining whether or not an individual can deduct moving expenses.)

6-12. ITA 110(1)(j) provides a deduction in the calculation of the individual's Taxable Income for home relocation loans equal to the lesser of:

- The taxable benefit that would be assessed under ITA 80.4(1). As covered in Chapter 5, in general, this benefit is calculated by applying the prescribed rate that is applicable to each quarter that the loan is outstanding [ITA 80.4(1)(a)]. However, in the case of a housing loan, this amount cannot exceed the amount that results from applying the prescribed rate that was in effect when the loan was granted, to the loan for the entire period that it was outstanding during the year [ITA 80.4(4)]. The amount of the benefit is reduced by any payments made by the employee during the year or within 30 days of the end of the year [ITA 80.4(1)(c)] for the home relocation loan.

- The amount of interest, calculated at the prescribed rate, that would be applicable to a $25,000 home relocation loan. This amount will be calculated using the prescribed rate in effect for each of the quarters that the loan is outstanding. This amount is not reduced for payments made by the employee.

6-13. 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.

Exercise Six-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. Annual interest at the rate of 2 percent is paid on December 31 of each year. Assume that at the time the loan is granted the prescribed rate is 5 percent. However, the rate is reduced to 4 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

6-14. 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 involve 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

The Basic System

6-15. For individuals, the basic system for calculating Tax Payable is relatively straightforward. At the federal level for 2004, there are four rates, 16 percent, 22 percent, 26 percent, and 29 percent. The specific brackets are described in the following section. In order to maintain fairness, these brackets are indexed to reflect changes in the Consumer Price Index (CPI). In the absence of such indexation, taxpayers could find themselves subject to higher rates without having an increased level of real, inflation adjusted income.

6-16. Until 2000, all of the provinces, with the exception of Quebec, had applied flat rates to graduated amounts of basic federal tax in order to determine the provincial Tax Payable. As of 2001, all of the provinces and territories have switched to a system of calculating their taxes on the basis of a Taxable Income figure. This alternative approach has come to be referred to as the TONI (Tax ON Income) system.

6-17. It is believed that the TONI system eliminates the impact that changes to the federal tax rates and credits have on provincial/territorial revenues. At the same time, the federal government's willingness to continue administering provincial taxes under this system serves to maintain a common federal/provincial Taxable Income base. This has a number of benefits including:

- uniformity across provinces and territories with respect to what income should be taxed by both levels of government;
- a single form for taxpayers;
- a single tax collection agency; and
- substantial cost savings for the provinces and territories as a result of the federal government collecting their taxes, free of charge. It is claimed that, over the past five years, the provinces have saved some $1.5 billion as a result of the federal government administering their taxes.

6-18. In implementing the TONI system, the provinces have generally agreed to use the same Taxable Income figure that is used for the calculation of federal Tax Payable. The exception here is Quebec, which has had a separate system for many years. The Quebec Taxable Income figure can be significantly different than the federal figure, which can considerably complicate the calculation of combined Tax Payable for many taxpayers in that province.

6-19. With respect to rates, it appears that most provinces use graduated rates applied to brackets that are the same, or similar, to those used at the federal level. Ontario, for example, uses three rates, 6.05 percent on Taxable Income up to $33,375, 9.15 percent on additional Taxable Income up to $66,752, and 11.16 percent on Taxable Income over $66,752. There are, however, exceptions to this graduated rate approach. Alberta calculates provincial Tax Payable at a flat 10 percent of Taxable Income, without regard to the individual's level of income. It should also be noted that several provinces use surtaxes which results in effective rates that are higher than the basic rates that are stated.

Federal Tax Payable Before Credits

6-20. The calculation of federal Tax Payable for individuals begins with Taxable Income. As the tax system is progressive in nature, higher rates are applied to higher levels of Taxable Income. The Taxable Income segments to which the various rates apply are referred to as tax brackets and, for 2004, the federal government has four tax brackets. The four brackets, and their rates, are as follows:

Taxable Income In Excess Of	Federal Tax	Marginal Rate On Excess
$ -0-	$ -0-	16%
35,000	5,600	22%
70,000	13,300	26%
113,804	24,689	29%

6-21. Note that the average rate for someone just entering the highest 29 percent bracket is 21.7 percent ($24,689 ÷ $113,804). This illustrates the importance of keeping an annual income level below this bracket. To this point, the average rate is 21.7 percent. For all income that exceeds this level, the federal rate goes to 29 percent. 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 the tax rate is a marginal rate. For example, if Taxable Income is $113,805, only $1 is taxed at 29 percent.

6-22. The preceding table suggests that individuals are taxed on their first dollar of income. While the 16 percent rate is, in fact, applied to all of the first $35,000 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 2004, this tax credit is $1,282 [(16%)($8,012)]. In effect, this means that no taxes will be paid on at least the first $8,012 of an individual's Taxable Income. This tax free amount would be even higher for individuals with additional tax credits (e.g., age credit).

6-23. As an example of the calculation of federal Tax Payable before credits, consider an individual with Taxable Income of $82,300. The calculation would be as follows:

Tax On First $70,000	$13,300
Tax On Next $12,300 At 26%	3,198
Federal Tax Payable Before Credits	$16,498

6-24. Until 2001, there was a federal surtax. A surtax is an additional tax calculated on the basis of the regular Tax Payable calculation. In our opinion, this type of additional taxation is used as a politically expedient way of raising taxes, without raising stated tax rates. Fortunately, this practice has ended at the federal level. However, as we have noted, surtaxes are still used in several provinces, most notably in Ontario. For 2004, Ontario has a surtax of 56 percent on amounts of Ontario Tax Payable in excess of $4,864. This significantly increases the highest rate in Ontario from the stated 11.16 percent to 17.41 percent.

Exercise Six-2

Subject: Calculation Of Tax Payable Before Credits

During 2004, Joan Matel is a resident of Ontario and has calculated her Taxable Income to be $46,700. Calculate her 2004 federal and provincial Tax Payable before consideration of credits.

End of Exercise. Solution available in Study Guide.

Basic Federal Tax Payable

6-25. Basic federal Tax Payable is a figure from which some, but not all tax credits have been deducted. Prior to 2000, this was an important figure in that it was the base that the provinces and territories used in calculating their respective Tax Payable. With the 2001 general adoption of the Tax On Income (TONI) system by the provinces, the basic federal tax figure is not of general importance.

6-26. This concept does, however, have some limited use in specialized situations. The most important of these is that it is used to calculate the additional federal Tax Payable that must be paid by individuals who are deemed Canadian residents but do not reside in a province (e.g., members of the Canadian Armed Forces stationed outside of Canada).

Provincial Tax Payable

TONI

6-27. As of 2001, all of the provinces and territories are using a Tax On Income (TONI) system to calculate provincial Tax Payable. With the exception of Alberta, they are using a graduated range of rates applied to brackets that appear to be similar, but not identical, to those used at the federal level. As noted earlier, Alberta uses a flat rate applied to all levels of income. Adding further complexity to the TONI approach is the fact that several provinces are using surtaxes, sometimes at very formidable levels.

6-28. To give you some idea of the range of provincial rates, the 2004 minimum and maximum rates, along with applicable surtaxes are as found in the following table:

Province	Minimum Tax Rate	Maximum Tax Rate	Applicable Surtax
Alberta	10.00%	10.00%	N/A
British Columbia	6.05%	14.70%	N/A
Manitoba	10.90%	17.40%	N/A
New Brunswick	9.68%	17.84%	N/A
Newfoundland	10.57%	18.02%	9%
Nova Scotia	8.79%	15.17%	10%
Ontario	6.05%	11.16%	20% and 56%
Prince Edward Island	9.80%	16.70%	10%
Quebec	16.00%	24.00%	N/A
Saskatchewan	11.00%	15.00%	N/A

6-29. Given the large differences in brackets and surtaxes, it is not immediately apparent from the preceding table how the real rates of taxation in the various provinces compare. Real comparisons require further calculations in order to give consideration to the manner in which these various components of provincial taxation work together. Further, different effective rates apply depending on the type of income. The following table indicates the maximum effective combined federal/provincial rates that are applicable to ordinary income, dividend income, and capital gains for 2004:

Province	Ordinary Income	Capital Gains	Canadian Dividends
Alberta	39.00%	19.50%	24.08%
British Columbia	43.70%	21.85%	31.58%
Manitoba	46.40%	23.20%	35.08%
New Brunswick	46.84%	23.42%	37.26%
Newfoundland	48.64%	24.32%	37.32%
Nova Scotia	45.69%	22.84%	29.85%
Ontario	46.41%	23.20%	31.33%
Prince Edward Island	47.37%	23.69%	31.96%
Quebec	48.22%	24.11%	32.81%
Saskatchewan	44.00%	22.00%	28.33%

6-30. You should note the significant differences in rates between the provinces. An individual making amounts in excess of the threshold of the maximum bracket is almost ten percentage points better off living in Alberta, as compared to Quebec. This amounts to $10,000 on each additional $100,000 of income. Provincial tax differences could be a major consideration when deciding whether, or where, to move or relocate.

6-31. A further important point is the different rates on alternative sources of income. Both dividends and capital gains have always received favourable tax treatment. Until 2001, these two types of income enjoyed a similar status with respect to effective rates of taxation. However, with the reduction in the capital gains inclusion rate from three-quarters to one-half, the maximum rate on capital gains is now much lower than the maximum rate on dividends. We would note, however, that this is not the case in low tax brackets. For example, in British Columbia, the lowest rate on capital gains is 8.00 percent, while the lowest rate on dividend income is 3.33 percent. This reflects the influence of the dividend tax credit which is discussed in Chapter 9.

6-32. It is clear from the preceding table that there are significant differences in provincial tax rates. Given this, it is somewhat surprising that the rules related to where an individual will be taxed are fairly simple. With respect to an individual's income, other than business income, it is deemed to have been earned 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 deemed to have been earned in Ontario.

Taxes On Income Not Earned In A Province

6-33. As we have noted, 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. Income that is not subject to provincial or territorial tax is subject to additional taxation at the federal level. In addition to the regular federal Tax Payable, there is also a federal surtax equal to 48 percent of basic federal Tax Payable under ITA 120(1). This is paid instead of a provincial or territorial tax.

Credits Against Tax Payable

Calculating The Amount

Federal Tax Credits

6-34. The most direct way of applying a tax credit system is to simply specify the amount of each tax credit available. In 2004, for example, the basic personal tax credit could have been specified to be $1,282. 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 (16 percent) is applied. This means that, for 2004, the basic personal tax credit is calculated by taking 16 percent of $8,012 (we will refer to this number as the tax credit base), resulting in a credit against Tax Payable in the amount of $1,282. Note that the legislation is such that, if the minimum federal tax rate of 16 percent is changed, the new rate will be used in determining individual tax credits. In our tax credit examples and problems, we will generally use the tax credit base in our calculations and apply the 16 percent rate to the subtotals and totals. This approach makes the relationships between the various credits easier to see and reduces calculation errors.

6-35. As was the case with the tax rate brackets, in order to avoid having these credits decline in value in terms of inflation adjusted amounts, the base for the tax credits needs to be adjusted for changing prices. While a few credits are not subject to such adjustments (e.g., the pension income credit has had the same base for many years), most of the credit bases are adjusted using the same CPI rate that is applied to the tax brackets.

6-36. 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 3, 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 charitable donations tax credit, are not reduced because of part year residence.

Provincial Tax Credits

6-37. Prior to the use of the TONI system, provincial Tax Payable was based on basic federal Tax Payable. As provincial tax credits were implicit in the calculation of this figure, they required no further discussion. One of the problems with this approach was that it did not leave the provinces any flexibility with respect to the types or amounts of credits available.

6-38. Under the TONI system, the provinces determine their own provincial tax credits and provincial tax rates. While there is considerable variation from province to province, the basic system is one that follows the federal pattern. That is, the minimum tax rate for the province is applied to an indexed tax credit base.

6-39. While we will not pursue this issue in detail, a simple example is appropriate. In our discussion of the calculation of federal tax credits, we noted that for 2004, individuals are entitled to a credit of $1,282, a base amount of $8,012, multiplied by the lowest federal rate of 16 percent. Ontario calculates this credit on a slightly higher base ($8,044) multiplied by the lowest Ontario rate of 6.05 percent, producing a credit against Ontario Tax Payable of $487. In contrast, Alberta is considerably more generous. The Alberta individual tax credit is based on an amount of $14,337, multiplied by the flat tax rate of 10 percent. The result is a credit of $1,434, larger than the federal credit and almost three times the size of the Ontario credit.

Personal Tax Credits - ITA 118(1)

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

6-40. For individuals with a spouse or common-law partner filing tax returns in 2004, ITA 118(1)(a) provides for two tax credits, with each one being calculated on a different base. The first amount is calculated as 16 percent of the basic personal amount, which for the 2004 taxation year is equal to $8,012. This provides for a credit against Tax Payable of $1,282.

6-41. For 2004, the second amount available to an individual with a spouse or common-law partner is equal to 16 percent of $6,803, an amount of $1,088. However, this amount is reduced by the Net Income For Tax Purposes of the spouse in excess of $681. This limiting amount is generally referred to as the income threshold for the credit. While the expression is not technically correct, this amount is usually referred to as the spousal credit. As the correct expression would be something like "spouse or common-law partner credit", for the sake of convenience, we will continue to use the less accurate term, spousal credit. The complete expression for the credit is as follows:

{[16%][$6,803 - (Spouse or Common-Law Partner's Net Income - $681)]}

6-42. As an example, if an individual had a spouse or common-law partner with Net Income For Tax Purposes of $5,200, the total personal credits under ITA 118(1)(a) would be equal to:

{[16%][$8,012 + [$6,803 - ($5,200 - $681)]} = $1,647

6-43. There are several other points to be made with respect to the credits for individuals 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. Note that when this figure reaches $7,484 ($6,803 + $681), the base for this credit will be nil, and the individual's credit will be calculated using only the basic personal amount.
- **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 $8,012, IT-513R specifies that only one spouse or common-law partner may claim the additional spousal amount (IT-513R has not been revised to reflect common-law partners). IT-513R indicates that the spouse making the claim should be the one that supports the other, a fairly vague concept.
- **Eligibility** As recently as 1992, the only basis for claiming the ITA 118(1)(a) credit was a legally recognized marriage. Starting in 1993, the definition of spouse was extended to cover common-law relationships, but only with an individual of the opposite sex. A further liberalization is applicable for 2001 and subsequent years. Under these latest changes, ITA 248(1) defines a common-law partner as a person who cohabits with the taxpayer in a conjugal relationship 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 longer a requirement that the cohabiting person be of the opposite sex. As there is no longer a definition of spouse in the *Income Tax Act*, 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.
- **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.
- **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. However, IT-513R indicates that, in the year of separation or divorce, an individual can either deduct amounts paid for spousal support, or claim the additional tax credit for a spouse.

Exercise Six-3

Subject: Spousal Tax Credit

Mr. Johan Sprinkle is married and has 2004 Net Income For Tax Purposes of $25,450. His spouse has 2004 Net Income For Tax Purposes of $2,600. Determine Mr. Sprinkle's personal tax credits for 2004.

End of Exercise. Solution available in Study Guide.

Individual Supporting An Eligible Dependant - ITA 118(1)(b)

6-44. For a single individual supporting a dependant in a self-contained domestic establishment, ITA 118(1)(b) allows for a tax credit for a wholly dependent person, a.k.a. eligible dependant. It is calculated using the same two amounts used under ITA 118(1)(a) for individuals with a spouse or common-law partner. In this case, the income threshold amount is based on the Net Income of the eligible dependant. Note that this credit was formerly known as the "equivalent to spouse" credit. The new name reflects the introduction of the common-law partner concept into tax legislation.

6-45. 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 (see definition in Paragraph 6-49) who is:

- related to the individual by blood, marriage, or adoption;
- under 18 at any time during the year, or the individual's parent or grandparent, or mentally or physically infirm;
- living with the individual in a home that the individual maintains; and
- residing in Canada.

6-46. The residence requirement is not applicable to the individual's children. However, the child must still be living with the individual. This would be applicable, for example, to an individual who is a deemed resident (e.g., a member of the Canadian Armed Forces) and living with their child outside of Canada.

6-47. While there is no general tax credit for dependent children under age 18, the amount for the eligible dependant credit can be claimed for dependants in this age group.

6-48. In terms of limitations on this credit, the eligible dependant credit cannot be claimed by an individual:

- for more than one person;
- if the dependant's Net Income exceeds $7,484 ($6,803 + $681);
- 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);
- 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 11, 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 payments is able to deduct them in determining Net Income For Tax Purposes.

Dependants Defined

6-49. A dependant is defined in ITA 118(6) as a person who, at any time in the year, is dependent on the individual for support and includes a child or grandchild of an individual or of his spouse or common-law partner and, if resident in Canada, a parent, grandparent, brother, sister, uncle, aunt, niece, or nephew of the individual or the individual's spouse or common-law partner.

6-50. 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.

Single Persons - ITA 118(1)(c)

6-51. Individuals living with a spouse or common-law partner receive a credit for themselves under ITA 118(1)(a), and individuals living with an eligible dependant receive a corresponding credit under ITA 118(1)(b). For individuals who do not have a spouse, a common-law partner, or an eligible dependant, this same credit is received under ITA 118(1)(c). As noted previously, for 2004, this credit is equal to 16 percent of $8,012, an amount of $1,282.

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

6-52. ITA 118(1)(c.1) allows for a caregiver tax credit to an individual who provides in home care for an adult (18 years or older) relative. To be eligible for this credit, the individual has to maintain a dwelling in which the individual and the relative ordinarily reside, and the relative has to be the individual's, or the individual's spouse's or common-law partner's child, grandchild, parent, grandparent, brother, sister, aunt, uncle, nephew, or niece. Except where the relative is the individual's child or grandchild, the relative must be resident in Canada. Also, except where the relative is the individual's parent or grandparent who is 65 years old or over, the relative must be dependent on the individual because of the relative's mental or physical infirmity. A credit may be claimed for each individual who qualifies.

6-53. For 2004, the credit has a value of $605 [(16%)($3,784)]. The base for the credit is reduced by the amount of the dependant's Net Income in excess of $12,921. This means that it will disappear when the dependant's Net Income reaches $16,705 ($12,921 + $3,784).

6-54. The credit is not available to an individual with respect to a dependant for whom anyone is claiming the eligible dependant credit [ITA 118(1)(b)]. As the eligible dependant credit is worth $1,088, the caregiver credit should not be claimed if the full eligible dependant credit is available. The value of the caregiver credit lies in its higher income threshold ($12,921 vs. $681) and the fact that it can be claimed by an individual who is not single. This makes it clear that this credit is largely targeted at individuals providing support and care for a parent, grandparent, or infirm adult relative whose income level is below $16,705.

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

6-55. 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 2004, the credit is 16 percent of $3,784, or $605. This credit is reduced by 16 percent of the dependant's Net Income in excess of $5,368. This means that this tax credit is not available once the dependant's Net Income is more than $9,152 ($5,368 + $3,784).

6-56. This credit should not be confused with the mental and physical impairment credit (a.k.a., disability tax credit) that is available to individuals under ITA 118.3 (see Paragraph 6-84). The credit here under ITA 118(1)(d) is for an individual with sufficient infirmity that they cannot be self-supporting and, as a result, they are a dependant of the supporting person claiming the credit. For example, a supporting mother would be eligible for this credit if her adult son suffered from a physical handicap severe enough to prevent him from working at a full time job. A doctor's certification of this type of mental or physical infirmity is not required. In contrast, the disability tax credit under ITA 118.3 requires a doctor to certify that there is a prolonged impairment that severely restricts basic living activities. Note, however, because this latter credit can be transferred to a supporting person, one individual may be able to claim both of these credits.

6-57. The credit for an infirm dependant is not available if an eligible dependant credit or caregiver credit is available for the same dependant. In addition, if an individual is making deductible support payments for a child, this credit is not available for that child.

Exercise Six-4

Subject: Caregiver Tax Credit

Melinda Marchand has never married. She maintains a dwelling and, since the death of her mother several years ago, she has taken care of her father who is currently living with her. Her father's Net Income For Tax Purposes during 2004 was $5,600. For 2004, should Jane claim the caregiver tax credit and/or the eligible dependant tax credit with respect to her father? Explain your conclusion.

Exercise Six-5

Subject: Eligible Dependant Credit

Ms. Jane Forest is 48 years old and divorced from her husband. Her Net Income For Tax Purposes for 2004 is $43,000. She has retained the family home and has custody of both of the children of the marriage. 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 2004, while her daughter has Net Income For Tax Purposes of $1,800. Determine Ms. Forest's maximum tax credits for 2004.

End of Exercises. Solutions available in Study Guide.

Age Tax Credit - ITA 118(2)

6-58. For individuals who attain the age of 65 prior to the end of the year, ITA 118(2) provides an additional tax credit of 16 percent of $3,912, or $626. However, the base for this credit is reduced by 15 percent of the individual's Net Income For Tax Purposes in excess of $29,124. This means that, at an income level of $55,204 [($3,912 ÷ .15) + $29,124], the reduction will be equal to $3,912 and the individual will no longer receive an age credit. As an example, a 67 year old individual with 2004 Net Income of $35,000 will have an age credit of $485 {[16%][$3,912 - (15%)($35,000 - $29,124)]}.

6-59. 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 Six-6

Subject: Age Tax Credit

Joshua Smythe is 72 years old and has 2004 Net Income For Tax Purposes of $51,500. Determine Mr. Smythe's age credit for 2004.

End Of Exercise. Solution available in Study Guide.

Pension Income Tax Credit - ITA 118(3)

6-60. ITA 118(3) provides for a credit equal to 16 percent of the first $1,000 of eligible pension income. This results in a maximum credit of $160. There is no provision for indexing this amount and, as a result, the real value of this credit declines each year.

6-61. Not all types of pension income are eligible for this credit. ITA 118(8) specifically excludes payments under the *Old Age Security Act*, the Canada Pension Plan, certain provincial pension plans, a salary deferral arrangement, a retirement compensation arrangement, an employee benefit plan, and death benefits.

6-62. For individuals who have reached age 65 before the end of the year, this credit is available on "pension income" as defined in ITA 118(7). This includes pension payments that are:

- a life annuity out of, or under, a pension plan;
- 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.

6-63. For an individual who has not reached age 65 before the end of the year, the credit is based on "qualified pension income", also defined in ITA 118(7). This includes the life annuities out of, or under, a pension plan and, in situations where such amounts are received as a consequence of the death of a spouse or common-law partner, the other types of pension income described in the preceding Paragraph. However, this means that, in ordinary circumstances, individuals who have not reached age 65 will only be eligible for the pension income tax credit to the extent that their pension income is made up of life annuity payments.

Charitable Donations Credit - ITA 118.1

Extent Of Coverage

6-64. There are several complications associated with cash gifts to registered charities. However, for tax purposes, gifts are segregated into various categories, with different rules applicable to different categories. 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 14. However, limited coverage of this subject will be included in this Chapter.

Eligible Gifts

6-65. In this Chapter, our coverage will be limited to what is referred to in ITA 118.1 as total charitable gifts. These include all amounts donated by an individual to a registered charity, a registered Canadian amateur athletic association, a housing corporation resident in Canada that is exempt from tax under ITA 149(1)(i), a Canadian municipality, the United Nations or an agency thereof, a university outside of Canada which normally enrolls Canadian students, and a charitable organization outside of Canada to which Her Majesty in right of Canada has made a gift.

6-66. 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 14.

Limits On Amount Claimed

6-67. It is the policy of the government to limit 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.

6-68. The 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.

6-69. 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 if they do not have sufficient Tax Payable to absorb the available credits, any unused amounts can be carried over and used in the subsequent five year period. In the carry forward period, the same 75 percent limit will apply in determining eligible amounts.

Calculating The Credit

6-70. Once the contribution base is established, the credit is equal to 16 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 16 percent would have resulted in a decline in donations. The 29 percent credit on larger donations was added in order to mitigate this result.

6-71. While the same level of total giving could probably have been achieved with a compromise rate somewhere between 16 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.

6-72. The following example illustrates the calculation of the charitable donations tax credit, including the determination of eligible amounts:

Example Nancy Hart has 2004 Net Income For Tax Purposes of $100,000. On the receipt of a large inheritance, she makes total charitable donations of $83,000.

Tax Consequences The total for all eligible gifts is limited to 75 percent of her Net Income For Tax Purposes, or $75,000. As her total gifts amount to $83,000, the $75,000 limit applies and $8,000 in donations are carried forward. Given this, her tax credit would be calculated as follows:

16 Percent Of $200	$ 32
29 Percent Of $74,800	21,692
Total Credit	$21,724

6-73. For married couples, the CRA's administrative practices permit either spouse to claim all of the donations made by both spouses. 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.

Exercise Six-7

Subject: Charitable Donations

Marion Scalpal has 2004 Net Income For Tax Purposes of $65,000. While she is not a compulsive gambler, she enjoys the ambiance of casino environments and usually spends at least one evening per week at the blackjack tables. While over the years she has generally experienced small losses, an improvement in her luck resulted in 2004 winnings of over $200,000. As she had promised in her prayers, at the end of 2004 she donates $100,000 of these winnings to her church. In 2005 and 2006, her income remains at $65,000. She makes no further donations in either year. Determine her maximum charitable donations tax credit for each of the years 2004, 2005, and 2006.

End of Exercise. Solution available in Study Guide.

Medical Expense Credit - ITA 118.2 - Current Rules (See Next Section For 2004 Budget Proposals)

General Rules

6-74. Under ITA 118.2, individuals can deduct a credit equal to 16 percent of medical expenses paid and not reimbursed, in excess of the lower of $1,813 and 3 percent of Net Income For Tax Purposes. For individuals with Net Income For Tax Purposes in excess of $60,433, the $1,813 figure is the relevant floor for these expenditures.

Qualifying Expenses

6-75. Medical expenses can be claimed for any 12 month period ending in the year and must be documented by receipts. 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. For example, if an individual with Net Income For Tax Purposes of $60,000 for 2003 and 2004, had $10,000 in medical expenses in the period July to December, 2003, and a further $12,000 in the period January to June, 2004, the 2003 claim could be deferred and the $22,000 total could be claimed in full in the 2004 taxation year. The advantage of doing this is that the threshold amount reduction would be applied only once in 2004. If medical expenses had to be claimed in the year in which they were incurred, this individual would have had to apply the threshold reduction in both 2003 ($1,755) and 2004 ($1,813). Claiming the full amount in 2004 involves a savings in federal Tax Payable of $281 [(16%)($1,755)].

6-76. Qualifying items, as described in ITA 118.2(2), include amounts paid to doctors and dentists, to full time home attendants, for full time nursing home care, to institutions for the disabled, for ambulance transportation, for reasonable travel expenses for medical care, for artificial limbs, for prescription eyeglasses or contact lenses, for oxygen, for seeing eye dogs, for any device prescribed by a medical practitioner, for drugs or medicine, for laboratory work, and for premiums paid for private health services plans.

6-77. This definition has been repeatedly extended in various budgets. Recent additions include 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, costs of up to $10,000 in a year for a part time attendant to help a person with a severe and prolonged mental or physical impairment, the costs for a specially trained animal to help persons with restricted use of arms and legs, products for the incontinent, and the cost of rehabilitative therapy to adjust for speech or hearing loss. The 2003 budget brought further additions to the list including real-time captioning for individuals with a speech or hearing impairment, note-taking services for individuals with a physical or mental impairment, voice recognition software for individuals with a physical impairment, and the incremental cost of acquiring gluten-free foods for individuals with celiac disease.

Spouse And Dependant Expenses

6-78. ITA 118.2(2) defines the medical expenses of an individual to include those of the individual, the individual's spouse or common-law partner, and other individuals who meet the definition of a dependant that is found in ITA 118(6). Note carefully that, in the case of dependants, there is no requirement that the individual claiming the medical expenses be able to claim a tax credit for the dependant. In practical terms, this means that a parent can claim the medical expenses of dependent children of any age, despite the fact that no tax credit is available for the dependants.

6-79. There is, however, a limiting factor on the deduction of a dependant's medical expenses. In situations where a claim is being made for medical expenses of a dependant other than a spouse, the total medical expense credit must be reduced by 68 percent of the dependant's Net Income in excess of the basic personal amount found in ITA 118(1)(c). For 2004, that amount equals $8,012.

Example Mr. Fowles and his spouse have medical expenses that total $12,500. In addition, Mr. Fowles paid qualifying dental expenses of $5,000 for his dependent 20 year old daughter. Mr. Fowles' daughter had Net Income For Tax Purposes of $8,500. Mr. Fowles' Taxable Income exceeds $100,000, while Mrs. Fowles has no Taxable Income.

Tax Consequences The credit that would be available to Mr. Fowles would be calculated as follows:

Total Medical Expenses (For Himself, Spouse, And Daughter)	$17,500
Threshold Amount (Maximum)	(1,813)
Eligible For Credit	$15,687
Rate	16%
Credit Before Reduction	$ 2,510
Reduction [(68%)($8,500 - $8,012)]	(332)
Medical Expense Tax Credit	$ 2,178

While the preceding calculation is consistent with the presentation of this credit in the *Income Tax Act*, the T1 tax return uses an alternative calculation. This alternative calculation is as follows:

Total Medical Expenses (For Himself, Spouse, And Daughter)	$17,500
Threshold Amount (Maximum)	(1,813)
Eligible For Credit	$15,687
Adjustment For Dependant's Income [(4.25*)($8,500 - $8,012)]	(2,074)
Allowable Portion Of Medical Expenses	$13,613
Rate	16%
Medical Expense Tax Credit	$2,178

*4.25 = (68% ÷ 16%)

This alternative calculation will always result in the same credit. It has a practical advantage in that, if the number produced when we multiply 4.25 times the dependant's Net Income in excess of the basic personal credit base is greater than the medical expenses of the dependant, it is an indication that the taxpayer would be better off not claiming the medical expenses of that dependant.

6-80. As his daughter falls within the definition of a dependant, Mr. Fowles is able to use her medical expenses in calculating his credit. This is clearly beneficial to Mr. Fowles in that his additional credit of $800 [(16%)($5,000)] is acquired at a cost of only $332 (in the alternative calculation this conclusion would be based on the fact that the calculated $2,074 is less than the daughter's medical expenses of $5,000). While the medical expenses are no longer available to his daughter, her total federal Tax Payable will only be $78 [(16%)($8,500 - $8,012)]. Even if she cannot claim other credits, she could only use a fraction of the medical expense credit that was available to her.

Exercise Six-8

Subject: Dependant Medical Expenses

Ms. Maxine Davies and her spouse have medical expenses of $4,330. Ms. Davies has Net Income For Tax Purposes in excess of $150,000, her spouse has no income, and her son has Net Income For Tax Purposes of $8,250. Ms. Davies paid $8,425 for medical expenses incurred by her son. Determine Ms. Davies' optimum medical expense tax credit for 2004.

End of Exercise. Solution available in Study Guide.

Refundable Medical Expense Supplement - ITA 122.51

6-81. ITA 122.51 provides for a refundable tax credit for low income working Canadians with above average medical expenses. As this is a refundable supplement, it will be paid even if the taxpayer has no tax liability.

6-82. To be eligible for the medical expense supplement, the individual must be over 17 and must have earned income (employment or business) of at least $2,809. The credit is the lesser of $562 and 25/16 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.) This amount is reduced by 5 percent of family Net Income For Tax Purposes in excess of an indexed threshold amount. For 2004, the amount is $21,301. The credit is completely eliminated when family Net Income For Tax Purposes reaches $32,541. A simple example will serve to illustrate this provision:

Example Mr. Larry Futon and his spouse have medical expenses that total $3,650. His Net Income For Tax Purposes is $21,900, all of which qualifies as earned income. His spouse has Net Income For Tax Purposes of $500. Mr. Futon is also eligible for the full caregiver tax credit for his mother.

Tax Consequences Mr. Futon's allowable medical expenses for tax credit purposes would be $2,993 [$3,650 - (3%)($21,900)], resulting in a tax credit of $479 [(16%)($2,993)]. 25/16 of this amount would be $748. His refundable credit would be based on $562, less a reduction of $55 [(5%)($21,900 + $500 - $21,301)], a balance of $507.

6-83. 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 individual, spousal, caregiver, and medical expense, his federal Tax Payable would be reduced to $49 [(16%)($21,900 - $8,012 - $6,803 - - $3,784 - $2,993)]. When this result is combined with the refundable credit of $507, Mr. Futon winds up with a refund of $458 ($507 - $49) for the year.

Exercise Six-9

Subject: Refundable Medical Expense Supplement

During 2004, Ms. Lara Brunt and her common-law partner Sara have medical expenses that total $6,250. Her Net Income For Tax Purposes is $25,400, all of which qualifies as earned income. Sara has no income of her own. Determine Lara's minimum Tax Payable for 2004.

End of Exercise. Solution available in Study Guide.

Medical Expense Tax Credit - March, 2004 Budget Proposals

Introduction

The March, 2004 budget proposed a fairly major change in the manner in which the medical expense tax credit will be determined beginning with the 2004 taxation year. However, the statements contained in the budget were not entirely clear, they have since been modified in public statements by Mr. Paul Martin, and no draft legislation for implementing the proposals is in sight. Further, the possibility that, at the time of this writing (May, 2004), Mr. Martin and the Liberal Party may not form the next government could result in these proposals never being implemented.

Given these uncertainties, we have chosen not to incorporate these proposals into our basic text or into our problem material. However, we will briefly describe these proposals and provide an example which will make clear how they differ from current legislation. If these proposals, either in their present form or in some modified version, become law, modified text and problem material will be added to our web site as quickly as possible.

The Proposals

The amount that will be eligible for the medical expense tax credit will be divided into two components. They can be described as follows:

Component 1 The basic component will be made up of the medical expenses incurred on behalf of the taxpayer, his spouse or common-law partner, and his children who have not attained the age of 18 by the end of the year. This total will be reduced by the lesser of 3 percent of the individual's Net Income For Tax Purposes and a 2004 amount of $1,813. While this is not stated in the budget papers, we have been assured by individuals at the Department Of Finance that this amount will no longer be reduced by 68 percent of the minor children's income in excess of the basic personal amount ($8,012 for 2004).

Component 2 An additional component will consist of the medical expenses paid by the taxpayer on behalf of any other dependants. Each eligible amount will be reduced by the lesser of 3 percent of the dependant's (not the taxpayer's) Net Income For Tax Purposes and a 2004 amount of $1,813. Here again, the budget papers do not deal with the question of whether this amount will have to be reduced by 68 percent of the dependant's income in excess of the basic personal amount. However, individuals at the Department Of Finance have indicated that the intent is to eliminate this requirement.

The budget papers indicate a limit of $5,000 in medical expenses for this component. Mr. Martin has publicly announced an intention to increase this to $10,000. There may be further changes to this figure as the election campaign progresses. For the purposes of our example, we will use the $5,000 maximum that was included in the budget papers.

Example

This example will serve to illustrate how results under the new system would compare with results under the existing legislation.

Example Sam Jonas and his dependent family members had the following Net Income For Tax Purposes and medical expenses for 2004:

Individual	Net Income	Medical Expenses
Sam Jonas	$100,000	$ 5,000
Kelly Jonas (Sam's Wife)	12,000	4,000
Sue Jonas (Sam's 16 Year Old Daughter)	8,500	4,500
Martin Jonas (Sam's 70 Year Old Father)	18,000	8,000
Sharon Jonas (Sam's 69 Year Old Mother)	12,000	10,000
Total Medical Expenses		$31,500

Tax Consequences - Current Rules Under current legislation, the 2004 medical expense tax credit for Sam would be calculated as follows:

Eligible Expenses ($5,000 + $4,000 +$4,500)	$13,500
Threshold Amount (Maximum)	(1,813)
Eligible For Credit	$11,687
Rate	16%
Credit Before Reduction	$ 1,870
Reduction For Daughter [(68%)($8,500 - $8,012)]	(332)
Medical Expense Tax Credit - Current Rules	$ 1,538

Note that, under the current rules, Sam would not claim the medical expenses of either his father or his mother as in each case, he would have to deduct 68 percent of their income in excess of $8,012, an amount which is greater than 16 percent of their medical expenses.

Tax Consequences - Budget Proposals Under the budget proposals (as we understand them), Sam's 2004 medical expense tax credit would be calculated as follows:

Eligible From Component 1 (As Previously Calculated)		$11,687
Component 2		
Martin [$8,000 - (3%)($18,000)]	$ 7,460	
Sharon [$10,000 - (3%)($12,000)]	9,640	
Available Total	$17,100	
Excess Over $5,000 Limit	(12,100)	5,000
Total Eligible Amount		$16,687
Rate		16%
Medical Expense Tax Credit - Budget Proposals		$ 2,670

This represents a $1,132 ($2,670 - $1,538) improvement over the credit under the current rules. This results from the fact that the credit does not have to be reduced by 68 percent of the daughter's income in excess of the basic personal amount, and from the ability to make use of the medical expenses of Sam's father and mother. If the limit of Component 2 is raised to $10,000, the tax credit would increase by $800 [(16%)($5,000)].

Disability Credit - ITA 118.3

6-84. This credit is available under ITA 118.3 and, for 2004, it is equal to 16 percent of $6,486 or $1,038. 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 2004, the base for the supplement is $3,784, providing a total credit for a disabled minor of $1,643 [(16%)($6,486 + $3,784)]. Note, however, that the supplement amount of $3,784 is reduced by child care and attendant care costs in excess of $2,216. This means that once such costs reach $6,000, the supplement is completely eliminated.

6-85. An individual qualifies for the disability credit when a medical doctor, or optometrist, certifies on form T2201 that a severe physical or mental impairment exists. The impairment must be such that there is a marked restriction of the activities of daily living and has lasted, or can be expected to last, for at least 12 months.

6-86. 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:

- perceiving, thinking, and remembering;
- 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.

6-87. There have been several attempts to provide improved guidance in this area. The latest, a report from the Standing Committee On Human Resources Development And The Status Of Persons With Disabilities, was tabled in the House Of Commons on December 11, 2002. This report was unanimously rejected by the House, leaving a situation in which reassessments appear to be common. Many practitioners feel that the CRA is, perhaps, overly aggressive in its interpretation of the terms "markedly restricted" and an "inordinate amount of time" (e.g., the credit was denied for an individual with cerebral palsy because he was able to walk with braces).

Disability Credit Transfer To A Supporting Person

6-88. 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 these situations, 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, or as a disabled dependant over 17. The list of potential transferees includes parents, grandparents, children, grandchildren, brothers, sisters, aunts, uncles, nieces, and nephews.

6-89. In order to make the disability credit transfer available in most situations where a disabled child, parent, or grandparent is dependent on a taxpayer for support, the transfer is extended by a somewhat awkward measure to situations in which the supporting person:

- could have made the eligible dependant claim, if neither the supporting person nor the disabled dependant were married;
- could have made the disabled dependant over 17 claim or the caregiver credit, if the dependant had been 18 years of age or older; and

- could have made the eligible dependant or disabled dependant over 17 claim or the caregiver credit, if the dependant had no income.

6-90. The amount that can be transferred is the same $1,038 (or $1,643 if the under 18 supplement is available) that could be claimed by the disabled individual. However, if the disabled individual has Tax Payable in excess of his ITA 118 personal credits, pension credit, and 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 be transferred to the supporting person.

Other Credits and Deductions

6-91. Disabled individuals, or a supporting person may have medical expenses that are eligible for tax credits, including attendant care and nursing home care. Further, individuals who qualify for the disability tax credit can deduct from Net Income For Tax Purposes, the full amount of any costs for attendant care that facilitates their ability to earn income (see Chapter 11). Finally, a supporting person may be in a position to deduct child care costs for a disabled individual. There is a fairly complex interplay among these provisions with respect to which of them can be used for a given individual. While a full discussion of this point goes beyond the scope of this material, the following points are relevant:

- 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 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.

Exercise Six-10

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 2004, John paid medical expenses of $6,240 for Keith. None of these expenses involve attendant care. John has medical expenses of his own of more than $2,000. His Taxable Income for 2004 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.

Education Related Credits - ITA 118.5, 118.6, 118.61, 118.62

Tuition Credit

6-92. Under ITA 118.5, individuals receive a credit against Tax Payable equal to 16 percent of qualifying tuition fees paid for the calendar year, regardless of the year in which they are actually paid. There is no upper limit on this credit. To qualify, the fees must be paid to:

- a university, college, or other institution for post-secondary courses;
- an institution certified by the Minister of Human Resource Development for a course that developed or improved skills in an occupation (individual must be 16 or older);
- a university outside Canada, if enrolled full time in a course that was at least 13 consecutive weeks long; or
- for individuals who live near the U.S. border and commute, a U.S. college or university for part time studies.

6-93. It has been noted that universities are relying more heavily on various 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 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 Credit

6-94. Under ITA 118.6(2), there is a credit for 2004 equal to $64 [(16%)($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 Development for a course that develops or improves skills in an occupation. Enrollment in a qualifying educational program is described in IT-515R2 as a program that must run for at least three 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.

6-95. An alternative education credit of $19 [(16%)($120)] per month is available for attendance in a specified educational program. In general terms, this is defined as a program that, were it not for the requirement that at least 10 hours per week be devoted to its requirements, would be a qualifying educational program. In somewhat simplified terms, this credit is available to individuals pursuing part time studies, defined in terms of a minimum of 12 hours per month of course work.

6-96. A further modification of the general rules for the education credit is available to 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 $64 per month is available to such individuals, without regard to whether their attendance is full or part time.

Carry Forward Of Tuition And Education Credits

6-97. There are situations in which a student does not have sufficient Tax Payable to use their tuition and education credits and has not transferred them to a supporting person (see subsequent section on transfers). To deal with this type of situation, ITA 118.61 allows a carry forward of unused tuition and education credits.

6-98. Unfortunately, the calculation of the amount that is carried forward can be complex. Essentially, the carried forward amount is the sum of the current year amounts and unused amounts from the previous year, less the amount claimed for the year. Schedule 11 calculates the tuition and education amounts that must be claimed by using Taxable Income reduced by a figure which is the total of the base for certain credits such as the basic personal amount, spousal amount, CPP and EI amounts, but not others, such as the medical expense credit or dividend tax credit. There appears to be an inequity in that the tuition and education credits must be claimed to reduce Tax Payable to nil, even when there are other credits that are available to the student which will be lost. Any unused credits that have been carried forward will be claimed first. This will reduce the current year amounts that are claimed and is relevant when there is a transfer to a spouse or supporting person. Any transfers reduce the amount available for carry forward.

6-99. Unused amounts that are carried forward will be available for the student's personal use in any subsequent year, but cannot be transferred. While students will have to provide the required information, the CRA tracks the carry forward amounts. Note that, because, starting in 2001, the minimum tax rate was reduced to 16 percent from 17 percent, any carry forward from 2000 will have to be multiplied by the fraction 16/17.

Interest On Student Loans Credit

6-100. A further provision in ITA 118.62 relates to interest on student loans. Under this provision, an individual will be entitled to deduct 16 percent of amounts paid in the year, or in any of the five preceding years, on account of interest 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.

Exercise Six-11

Subject: Education Related Tax Credits

During 2004, 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 paid $1,000 in 2003. The amount paid in 2004 includes $400 in fees that are only charged to students in her geology program. Interest 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 2004.

End of Exercise. Solution available in Study Guide.

Transfer Of Tuition Fee And Education Credits - ITA 118.9

Basic Rules

6-101. ITA 118.9 provides for the transfer of current year unused education credits and tuition fee credits to a supporting parent or grandparent of a student. As will be discussed later in this Chapter, ITA 118.8 provides for a similar transfer to a spouse. The interest on student loans credit cannot be transferred.

6-102. The maximum transfer that can be made by a student is equal to $800 [(16%)($5,000)]. However, this must be reduced by any current year amount claimed by the student. Further, the student must use these credits in calculating his Tax Payable in the order specified under ITA 118.92 (e.g., he cannot deduct a medical expense credit prior to deducting the tuition/education credit).

Example Megan Doxy has 2004 Taxable Income of $11,000. She attends university full time for 8 months of the year, paying a total amount for tuition of $8,000. She has unused tuition and education amounts of $1,000 from the previous year. This gives her a tuition and education amount of $12,200 [(8)($400) + $8,000 + $1,000]. Her only other tax credit is her personal amount of $1,282 [(16%)($8,012)].

Tax Consequences She would be required to use $2,988 ($11,000 - $8,012) of her tuition and education amount to reduce her Tax Payable to nil, leaving an unused amount of $9,212 ($12,200 - $2,988). The $2,988 amount consists of the $1,000 carry forward and $1,988 of the current year amount. The amount of the available transfer would be only $3,012 ($5,000 - $1,988), not the full $5,000, leaving an unused amount to be carried forward of $6,200 ($12,200 - $2,988 - $3,012). Note that Megan would have to claim the carry forward in a subsequent year as it cannot be transferred to a spouse or supporting person.

6-103. It is the transferor who is subject to the $5,000 limit. A parent or grandparent could have $5,000 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 individual 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.

Exercise Six-12

Subject: Transfer Of Education And Tuition Credits

Jerry Fall has 2004 Taxable Income of $9,250. 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 credit, other than the education and tuition credits, is his personal amount of $1,282 [(16%)($8,012)]. Determine Jerry's tuition and education amounts and indicate how much of this total could be transferred to a supporting parent and how much would be carried forward.

End of Exercise. Solution available in Study Guide

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

6-104. ITA 118.7 provides a tax credit equal to 16 percent of the Employment Insurance (EI) premiums paid by an individual, all of the Canada Pension Plan (CPP) contributions paid on employment income, and one-half of the CPP contributions paid on self-employed income.

6-105. For 2004, EI premiums are based on maximum insurable earnings of $39,000. The employee's rate is 1.98 percent, resulting in a maximum annual premium of $772. This results in a maximum credit against federal Tax Payable of $124 [(16%)($772)].

6-106. Employers are also required to pay EI premiums, the amount being 1.4 times the premiums paid by the employee. However, these premiums do not provide the employee with a tax credit. Further, self-employed individuals are not eligible to participate in the EI program and, as a consequence, they will not pay EI premiums, and will not be eligible for any EI tax credit.

6-107. For 2004, an employee's CPP contributions are based on maximum pensionable earnings of $40,500, less a basic exemption of $3,500. The rate for 2004 is 4.95 percent, resulting in a maximum contribution of $1,832. This provides for a maximum 2004 credit against federal Tax Payable of $293 [(16%)($1,832)]. The employer matches the contributions made by the employee. However, this has no tax consequences for the employee.

6-108. 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. Until recently, this total payment was treated as the base for this tax credit. However, as will be discussed in Chapter 11, the matching contribution is now a deduction under ITA 60(e). This means that a self-employed individual, instead of having a tax credit equal to all of his CPP contributions, will have a tax credit equal to one-half of his contributions and a deduction for the remaining one-half. If the individual is in a tax bracket greater than 16 percent, this tax treatment is beneficial.

Overpayment Of Employment Insurance Premiums And Canada Pension Plan Contributions

6-109. 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.

6-110. A refund of these excess amounts is available on an individual's tax return. While any CPP or EI overpayment is not a 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 2004 and, as a consequence, the total amount of EI premiums withheld during the year was $875. In a similar fashion, the total amount of CPP contributions withheld by the two employers was $1,896. His employment income was well in excess of the maximum insurable and pensionable earnings.

Tax Consequences Jerry will claim a refund of $167 calculated as follows:

EI Premiums Withheld	$ 875	
2004 Maximum	(772)	$103
CPP Contributions Withheld	$1,896	
2004 Maximum	(1,832)	64
Refund Due		$167

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

6-111. ITA 118.8 permits the transfer of five specific tax credits to a spouse or common-law partner. The credits that are eligible for transfer are:

- the age credit,
- the disability credit,
- the pension income credit, and
- the current year tuition fee and education credits to a maximum of $800 (see preceding section for rules and limits)

6-112. The transferable amount is the excess of these credits over the spouse's Tax Payable after applying the personal credits under ITA 118(1), as well as the EI and CPP credits. A further point here is that no transfer of these credits is available if the spouses were separated for a period of 90 days or more that included December 31 of the current taxation year.

Exercise Six-13

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 RRSP funds. 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 federal tax credits for 2004.

End of Exercise. Solution available in Study Guide.

Dividend Tax Credit

6-113. The dividend tax credit is covered in Chapter 9 as part of our discussion of property income.

Foreign Tax Credits

6-114. The credits that are available for taxes paid in foreign jurisdictions are covered in Chapters 9 and 14.

Political Contributions Tax Credits - ITA 127(3)

6-115. A tax credit is available on 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. 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

6-116. 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.

6-117. The new Subsections ITA 248(30) and ITA 248(31), originally proposed on December 20, 2002, would require the amount of charitable and political contributions that are eligible for tax credits to be reduced by the amount of any advantage received by the taxpayer. While recent events make it clear that individuals do receive benefits related to their political contributions, it is unlikely that this would occur in the form of a documented transaction that could be used as a basis for assessing the contributing taxpayer. This suggests that these proposed Subsections will have greater applicability in the area of charitable contributions. Given this, we will defer discussion of these proposals until Chapter 14 where we provide our more comprehensive discussion of donations to charitable organizations.

Exercise Six-14

Subject: Political Contributions Tax Credit

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

End of Exercise. Solution available in Study Guide.

Investment Tax Credits

6-118. 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 more commonly used by corporations and, as a consequence, we cover eligibility for investment tax credits in Chapter 15.

Labour Sponsored Funds Tax Credit

6-119. The government wishes to encourage investment in small and medium sized enterprises. To that end, ITA 127.4 provides a credit for individuals investing in the shares of prescribed labour sponsored venture capital corporations. For purposes of this Section, these corporations must be set up under provincial legislation and managed by a labour organization. The assets of the corporation must be invested in small and medium sized businesses. In many cases, there will be a corresponding credit at the provincial level. The credit is based on the cost of the shares purchased by the individual.

6-120. The federal credit is equal to 15 percent of the net cost of the labour sponsored venture capital corporation (LSVCC) shares. To be eligible for the credit, the investor must be the first registered holder of the LSVCC 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.

Exercise Six-15

Subject: Labour Sponsored Funds Credit

On June 30, 2004, Mr. Brad Clintor purchases newly issued shares in a prescribed labour sponsored venture capital corporation at a cost of $3,000. Determine the amount of the federal tax credit that will result from this purchase.

End of Exercise. Solution available in Study Guide.

Refundable GST Credit

6-121. 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. Features that make this credit different from other types of credits is that the CRA calculates it for the individual and it cannot be used as a credit against Tax Payable. Unlike other tax credits, where the relevant calculations are included in the individual's tax return, the GST credit is determined by the CRA on the basis of eligibility information supplied in the individual's tax return. It is only paid if tax returns have been filed.

6-122. For 2004, the system provides for a total credit that is calculated as follows:

- $224 for the "eligible individual". An eligible individual includes a Canadian resident who 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.
- $224 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 $118 and 2 percent of the individual's Net Income For Tax Purposes in excess of $7,253.
- $224 for a dependant eligible for the eligible dependant tax credit.
- $118 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. Further, this credit cannot be claimed for a dependant if the $224 was claimed for that dependant because he or she was eligible for the eligible dependant tax credit.

6-123. 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 2004, this threshold amount is $29,123. "Adjusted Income" is defined as total income of the individual and his qualified relation, if any.

6-124. 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. Taxpayers do calculate this credit in their tax returns, nor do they have the option of applying this credit against the current year's Tax Payable.

Child Tax Benefit System

6-125. The Child Tax Benefit is in the form of a non-taxable monthly payment. As is the case with the refundable GST credit, the amount of this benefit is calculated by the CRA. The benefits under this program have been significantly enhanced in recent years and are subject to indexation. The 2004 level of benefits is as follows:

- $100.66 per month for each qualified dependant, basically a child who is under 18;
- an additional $7.00 per month for each dependant in excess of two;
- an additional $19.91 per month for each dependant under age seven, with this amount being reduced by 25 percent of all child care expenses claimed.

6-126. This basic benefit is subject to being reduced when family Net Income reaches $35,000. For a family with one child, the phase out is at the rate of 2 percent of the excess income. For a family with two or more children, the reduction is based on 4 percent of the excess income.

6-127. In addition to these benefits, there is also a National Child Benefit (NCB) supplement. The amount of the NCB supplement is $125.91 per month for the first child, $107.91 per month for the second, and $101.25 per month for the third and subsequent. The benefit is phased out based on family Net Income in excess of $22,615 (the phase out rate is 12.2 percent for a one child family, 22.7 percent for a two child family, and 32.5 percent for families with more than two children).

6-128. Given that the CRA does the calculations associated with the benefits, the payment is not taxable and will not be included in tax returns, and the fact that its complex data requirements make a realistic calculation extremely difficult, we have not included specific calculations of the Child Tax Benefit in any of the problem material in this text.

Social Benefits Repayment (OAS And EI)

Basic Concepts

6-129. Prior to 1996, one of the cornerstones of Canadian tax and economic policy was that social assistance programs should be provided on a universal basis, without regard to income level or financial need. This was, of course, a very expensive policy. Further, there was some question as to whether providing Old Age Security (OAS) benefits to wealthy individuals was in keeping with such tax policy goals as fairness and equity.

6-130. Whether the decision was based on tax policy goals, or simply reflected a need to reduce expenditures, the concept of universality is no longer being applied. Starting in 1989, the government began to assess a Part I.2 tax on OAS benefits received by individuals with an adjusted Net Income above a threshold amount. While the legislation is in the form of a tax on OAS benefits, this tax is often referred to as a repayment or clawback of OAS benefits.

6-131. 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. While the source of this requirement is a different legislative Act, both the OAS tax and the EI benefits repayment create a deduction in calculating an individual's Net Income For Tax Purposes. In the T1 tax return, the total of these deductions is referred to as the "Social Benefits Repayment".

6-132. These deductions are based on income tests and, because the amounts determined in these tests are deductions in the calculation of Net Income For Tax Purposes, there is a potentially circular calculation process. As will be explained in the material which follows, this problem is avoided by basing the income tests on an income figure which does not include these deductions.

Employment Insurance (EI) Benefits Clawback

6-133. The *Employment Insurance Act* requires the partial repayment of benefits received if the recipient’s threshold income is greater than $48,750 (1.25 times the 2004 maximum insurable earnings of $39,000). For the purposes of this test, the individual’s threshold income is equal to Net Income For Tax Purposes computed without consideration of the deduction for repayment of EI benefits [ITA 60(v.1)] or the deduction for the tax on 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.

6-134. Once the amount of threshold income over $48,750 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

6-135. ITA 180.2 assesses a tax on OAS benefits in an amount equal to 15 percent of the taxpayer's threshold income in excess of $59,790. For this purpose, the threshold income is equal to Net Income For Tax Purposes computed, after any EI clawback, but without consideration of the ITA 60(w) deduction for the tax on OAS benefits.

6-136. For some individuals, all or part of the OAS benefits are taxed away on a recurring basis. Because of this, the government estimates what the taxpayer will have to repay and withholds this amount at the time the payments are made. Estimates are made on the basis of the income for the "base taxation year". For OAS payments made during the first six months of a year, the base taxation year is the second preceding year and for OAS payments made during the last six months of the year, the base taxation year is the immediately preceding year.

6-137. For individuals with consistently high levels of income, this withholding procedure results in the full amount of the OAS benefits being withheld. For the first quarter of 2004, OAS benefits are $462.47 per month (they are adjusted on a quarterly basis). At this rate, the 2004 benefit will be about $5,550. This means that the benefit will be completely withheld or repaid at an income level of about $96,800. Note that, even in cases where no OAS payments are made because the total has been withheld, the individual will receive an information slip [T4A(OAS)] indicating that they were entitled to the amount of the benefit, with the same amount being shown as taxes withheld from the payment.

Exercise Six-16

Subject: EI and OAS Clawbacks

For 2004, Ms. Marilyn Jacobi has net employment income of $50,000, receives EI payments of $10,000, and receives $5,550 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. Determine Ms. Jacobi's Net Income For Tax Purposes for the 2004 taxation year.

End of Exercise. Solution available in Study Guide.

Comprehensive Example

6-138. 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. We have used provincial rates that are based on the federal brackets, and provincial credits that use the same base as the federal credits. At the end of this Chapter, there is an additional example containing a completed tax return.

Example Mr. Thomas Baxter is 66 years of age and his 2004 income is made up of net employment income of $73,800 and Old Age Security benefits of $5,550 (because of large business losses during the previous two years, no amount was withheld from these payments). For 2004, Mr. Baxter's employer withheld maximum CPP and EI contributions and a total of $20,000 in income tax. Other information pertaining to 2004 is as follows:

1. Mr. Baxter's spouse is 49 years old and is physically disabled. Her only 2004 income is $5,000 in Canadian source interest. The investment funds were inherited from her father at the time of his death.
2. Mr. and Mrs. Baxter have two daughters and, on December 31, 2004, their ages were 14 and 17. Kim, the younger daughter, earned $2,700 at her summer job in 2004.

Lori, the older daughter, earned income of $2,000 through part time work in 2004. In September, 2004, 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 semester.

3. The 2004 family medical expenses, all of which are claimed by Mr. Baxter, totalled $2,843.
4. During 2004, Mr. Baxter made donations to registered Canadian charities in the amount of $3,000.
5. Mr. Baxter made contributions to federal political parties totalling $1,500, which enabled him to claim the maximum political donations tax credit of $650.
6. Tax rates used in his province are 8 percent on the first $35,000 of Taxable Income, 10 percent on amounts between $35,000 and $70,000, and 13 percent on any amounts in excess of $70,000. Provincial credits use the same base as the federal credits, with the 8 percent lowest rate generally applied to this base. The exception is charitable donations in excess of $200, where the highest rate of 13 percent is used. The province does not have a political contributions tax credit.

Tax Calculations Mr. Baxter's Net and Taxable Income would be calculated as follows:

Net Employment Income	$73,800
OAS Benefits	5,550
Net Income Before Clawback	$79,350
OAS Clawback	(2,934)
Net Income For Tax Purposes And Taxable Income	$76,416

The required repayment of OAS is the lesser of the actual OAS payments of $5,550 and $2,934 [(15%)($79,350 - $59,790)].

The following notes are relevant to the calculation of Mr. Baxter's Tax Payable:

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

Full Base Amount	$3,912
Reduction - Lesser Of:	
• $7,094 [(15%)($76,416 - $29,124)]	
• $3,912 The Full Base Amount	(3,912)
Age Credit	Nil

Note Two Since Lori had insufficient income to use her tuition fees and education credits, the solution assumes they are transferred to her supporting parent. Alternatively, she could choose to carry forward these credits to apply against her own Tax Payable in a subsequent year. The total credit is calculated as follows:

Education (Four Months At $400)	$1,600
Tuition For 2004 Semester ($5,000 - $2,500)	2,500
Total Credit Available For Transfer Or Carry Forward	$4,100

Note Three Medical expenses eligible for the credit are the actual expenditures of $2,843, less the maximum of $1,813 as this limit is less than 3 percent of Mr. Baxter's Net Income. Since the income of both of Mr. Baxter's daughters is below the basic personal tax credit base of $8,012, there is no reduction in this amount.

Using the preceding Taxable Income and Notes, the total due would be as follows:

Tax On First $35,000 At 24 Percent (16% + 8%)		$ 8,400
Tax On Next $35,000 ($70,000 - $35,000)		
At 32 Percent (22% + 10%)		11,200
Tax On Next $6,416 ($76,416 - $70,000)		
At 39 Percent (26% + 13%)		2,502
Gross Tax		$22,102
Tax Credits:		
Basic Personal Amount	$ 8,012	
Mr. Baxter's Age (Note One)	Nil	
Spouse [$6,803 - ($5,000 - $681)]	2,484	
CPP Contributions (Maximum)	1,832	
EI Premiums (Maximum)	772	
Mrs. Baxter's Disability Transferred	6,486	
Lori's Education And Tuition Transferred		
(Note Two)	4,100	
Medical Expenses (Note Three)		
($2,843 - $1,813)	1,030	
Total	$24,716	
Rate (16% + 8%)	24%	(5,932)
Charitable Donations {[(16% + 8%)($200)]		
+ [(29% + 13%)($3,000 - $200)]}		(1,224)
Federal Political Contributions Tax Credit		(650)
Tax Payable		$14,296
Social Benefits Repayment (OAS)		2,934
Total Payable		$17,230
Income Tax Withheld		(20,000)
Balance Owing (Refund)		($ 2,770)

Key Terms Used In This Chapter

6-139. 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 before the index at the back of the book.

Age Tax Credit
Basic Federal Tax Payable
Canada Pension Plan (CPP)
Canada Pension Plan Tax Credit
Caregiver Tax Credit
Charitable Donations Tax Credit
Child Tax Benefit
Common-Law Partner
Dependant
Disability Tax Credit
Education Tax Credit
Eligible Dependant Tax Credit
Employment Insurance (EI)
Employment Insurance Tax Credit
GST Tax Credit
Home Relocation Loan
Indexation
Labour Sponsored Funds Tax Credit
Medical Expense Tax Credit
Non-Refundable Tax Credit
Northern Residents Deductions
OAS Clawback
Old Age Security Benefits (OAS)
Pension Income Tax Credit
Personal Tax Credits
Progressive Tax System
Refundable Tax Credit
Regressive Tax System
Spouse
Tax Credit
Taxable Income
TONI
Tuition Tax Credit
Wholly Dependant Person

References

6-140. For more detailed study of the material in this Chapter, we would refer you to the following:

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(4)	Limitations [re 118(1)]
ITA 118(5)	Support
ITA 118(6)	Definition Of Dependant
ITA 118(7)	Definition (Pension Income)
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 Credit
ITA 118.6	Education Credit
ITA 118.61	Unused Tuition And Education Tax Credits
ITA 118.7	Credit For UI Premium And CPP Contribution
ITA 118.8	Transfer Of Unused Credits To Spouse Or Common-Law Partner
ITA 118.9	Transfer To Parent Or Grandparent
ITA 122.5	GST Credit
ITA 122.6 To 122.64	Canada Child Tax Benefit
ITA 127(3)	Monetary Contributions - Canada Elections Act (Political Contributions Credit)
ITA 127.4	Labour Sponsored Funds Tax Credit
IC 75-2R6	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 84-3R5	Gifts To Certain Organizations Outside Canada
IC 92-3	Guidelines For Refunds Beyond The Normal Three Year Period
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
IT-513R	Personal Tax Credits
IT-515R2	Education Tax Credit
IT-516R2	Tuition Tax Credit
IT-519R2	Medical Expense And Disability Tax Credits And Attendant Care Expense Deduction
IT-523	Order Of Provisions Applicable In Computing An Individual's Taxable Income And Tax Payable
	Income Tax Technical News #26, December 24, 2002

Sample Personal Tax Return For Chapter 6

The following simplified example contains aT1 individual income tax return completed using the ProFile T1 Personal Income Tax Program for 2003 tax returns from Intuit GreenPoint software. As software for 2004 is not yet available, this example contains 2003 rates and credits. Only employment income and tax credits are contained in this version of the example. This example is expanded in Chapter 14 to contain other components of Taxable Income and Tax Payable.

Sample File On CD-ROM

The complete sample tax return is available on the CD-ROM included with this book in two versions, a T1 ProFile return file and a .PDF file.

GreenPoint ProFile Version

After starting the 2003 ProFile T1 program, open the file "Sample - Chapter 06.03T" in the subdirectory "\Tax Return Files".

To get the maximum benefit from using the program, we strongly advise that you do the tutorials "Getting Started" and "Using the Form Explorer" that are included with the program. The data in the following sample tax return problem can be used in the tutorial.

A Quick Reference Card, as well as complete manuals, are available on the CD-ROM in .PDF format. To view .PDF files, you will need to have Adobe Acrobat installed on your system. This program is also included on the CD-ROM.

When viewing the sample return file, we offer the following suggestions:

- By pressing <F4> you will open the Form Explorer. In the categories of forms appearing in the shaded box on the left, if you choose "A. Used" near the bottom of the column, all the forms that have calculations for the return will be shown. You can then double click on the form itself to view it.
- Right clicking on a number in a field shows a variety of options, including the form or schedule where the amount originated from.
- Clicking on "Show Auditor" under the "Audit" list will display any warnings or potential errors.

For students who would like more assistance in using the software, we have provided "Suggestions For Working With ProFile Software" in the Study Guide. The three pages of suggestions and tips can be found in the Chapter 6 material.

PDF Version

To view the complete return, including schedules, as a .PDF file, start the Adobe Acrobat program and open the file "PDF Sample - Chapter 06.pdf" in the subdirectory "\Tax Return Files".

Sample Problem Data

George Kercher is a divorced, semi-retired air force pilot living in Banff, Alberta. He has been your client for a number of years. George was born on February 24, 1952.

After some discussion with George, you confirm that he has never owned any foreign property. As he has for many years, George authorizes the CRA to provide information to Elections Canada and he authorizes you to e-file his return. He is currently living at 69 Beaver Street in Banff, Alberta T0L 0C0. His home phone number is (111) 111-1111.

He informs you that on February 12, 2003, he received $2 million from his mother's estate. Using some of these funds, George bought a house in Banff. The remainder of the funds were invested with his stockbroker, Bull & Bear Inc. In this Chapter 6 version of the example, assume there is no investment income from these funds.

George supports his two daughters:

- Willa (SIN 527-000-228) was born on January 22, 1987 and is attending university in Edmonton. Willa had Net Income of $3,300 during 2003.
- Janice (SIN 527-000-269), born June 6, 1990, is in high school and she had no earnings during the year.

George loves flying, so for the last two summers he has been flying fire bombers June 1 to September 30 for the provincial forest service fire control squad located in Banff.

He brings you the following receipts and documents:

1. A T4 that is included as Exhibit 1.
2. A T2202A "Tuition And Education Amounts Certificate" for himself from Athabasca University. It showed he was a part time student for 6 months and paid $575 in tuition for 2003.
3. A receipt for $1,000 from the Canadian Wildlife Federation dated December 3, 2003.
4. A statement from the Banff Dental Clinic that he paid a total of $1,200 during 2003. This consisted of $850 for himself on November 24, and $150 for Willa and $200 for Janice on December 15.
5. An instalment statement for 2003 that showed that George had paid the CRA instalments of $1,500 on September 15 and December 15 ($3,000 in total). These were the instalments requested by the CRA for the year due to his self-employed income in the previous year.

Required: With the objective of minimizing George's Tax Payable, complete his 2003 tax return. Ignore any GST implications.

Notes To The Return

1. Janice has been claimed under the equivalent to spouse amount on Schedule 5. Since Willa had Net Income of $3,300 and Janice had no income, if Willa had been claimed for the equivalent to spouse credit, it would have resulted in a reduced claim.
2. Due to his low Net Income For Tax Purposes, George is eligible for the refundable medical expense supplement.
3. Due to his nil Tax Payable, George's $1,000 charitable donation is carried forward.

Printed Return

On the following pages you will find George's T4, his four page tax return (first page truncated) and the two page Schedule 1 (federal tax calculations). The complete return can be found on the Companion CD-ROM.

Employer's name - Nom de l'employeur
Alberta Fire Control

Canada Customs and Revenue Agency — Agence des douanes et du revenu du Canada

T4

STATEMENT OF REMUNERATION PAID
ÉTAT DE LA RÉMUNÉRATION PAYÉE

Year / Année: 2003

VOID / ANNULE		
Employment Income - line 101 / Revenus d'emploi - ligne 101	14	18,000 00
Income tax deducted - line 437 / Impôt sur le revenu retenu - ligne 437	22	3,500 00
Business Number / Numéro d'entreprise	54	RP
Province of employment / Province d'emploi	10	AB
Employee's CPP contributions - line 308 / Cotisations de l'employé au RPC - ligne 308	16	717 75
EI insurable earnings / Gains assurables d'AE	24	
Social insurance number / Numéro d'assurance sociale	12	527 000 145
Exempt-Exemption CPP/QPP RPC/RRQ	28	
Exempt-Exemption EI AE		
Employment code / Code d'emploi	29	
Employee's QPP contributions - line 308 / Cotisations de l'employé au RRQ - ligne 308	17	
CPP/QPP pensionable earnings / Gains donnant droit à pension - RPC/RRQ	26	
Employee's EI premiums - line 312 / Cotisations de l'emplyé à l'AE - ligne 312	18	378 00
Union Dues - line 212 / Cotisations syndicales - ligne 212	44	110 00
RPP contributions - line 207 / Cotisations à un RPA - ligne 207	20	900 00
Charitable donations - Schedule 1 / Dons de bienfaisance - Annexe 1	46	
Pension adjustment - line 206 / Facteur d'équivalence - ligne 206	52	1,800 00
RPP or DPSP registration number / No d'agrément d'un RPA ou d'un RPDB	50	

Employee's name and address - Nom et addresse de l'employé

Last name - Nom de famille	First name - Prénom	Initials - Initiales
Kercher	George	

69 Beaver Street

Banff AB CAN T0L 0C0

1

RC-03-599

Other Information / Autres renseignements

Box/Case	Amount/Montant	Box/Case	Amount/Montant
N/A		N/A	

Box/Case	Amount/Montant	Box/Case	Amount/Montant	Box/Case	Amount/Montant	Box/Case	Amount/Montant
N/A		N/A		N/A		N/A	

T4 (01)

Canada Customs and Revenue Agency — Agence des douanes et du revenu du Canada

T1 GENERAL 2003

Income Tax and Benefit Return

Identification

7

First name and initial: George Chapter 6 Example
Last name: Kercher
Care of:
Mailing address: Apt. No. – Street No. Street name: 69 Beaver Street
P.O. Box, R.R.:
City: Banff — Prov./Terr.: AB — Postal Code: T0L 0C0

Information about your residence

Enter your province or territory of residence on **December 31, 2003**: Alberta

Enter the province or territory where you **currently** reside if it is not the same as that shown above for your mailing address:

If you were self-employed in 2003, enter the province or territory of self-employment: Alberta

If you became or ceased to be a resident of Canada **in 2003**, give:
Month/Day entry — Month/Day or departure

Information about you

Enter your social insurance number: 527 000 145

Enter your date of birth (Year/Month/Day): 1952-02-24

Your language of correspondence: / Votre langue de correspondance : English [X] Francais [ ]

Your marital status on December 31, 2003:
(see the "Marital status" section in the guide for details)

1 [ ] Married 2 [ ] Living common law 3 [ ] Widowed
4 [X] Divorced 5 [ ] Separated 6 [ ] Single

Information about your spouse or common-law partner (if you checked box 1 or 2 above)

Enter his or her social insurance number:

Enter his or her first name:

Enter his or her net income for 2003 to claim certain credits: (see the guide for details)

Check the box if he or she was self-employed in 2003: 1 [ ]

If this return is for a deceased person, enter the date of death: Year/Month/Day

Do not use this area

Complete tax return available on the CD-ROM

Kercher, George Chapter 6 Example SIN: 527 000 145

2

Please answer the following question

Did you own or hold foreign property at any time in 2003 with a total cost of more than CAN$100,000? (read the "Foreign income" section in the guide for details) **266** Yes ☐ 1 No ☒ 2
If *yes*, attach a completed Form T1135.

If you had dealings with a non-resident trust or corporation in 2003, see the "Foreign income" section in the guide.

As a Canadian resident, you have to report your income from all sources both inside and outside Canada.

Total income

Employment income (box 14 on all T4 slips)			**101**	18,000.00
Commissions included on line 101 (box 42 on all T4 slips)	**102**			
Other employment income			**104**	
Old Age Security pension (box 18 on the T4A(OAS) slip)			**113**	
CPP or QPP benefits (box 20 on the T4A(P) slip)			**114**	
Disability benefits included on line 114 (box 16 on the T4A(P) slip)	**152**			
Other pensions or superannuation			**115**	
Employment Insurance and other benefits (box 14 on the T4E slip)			**119**	
Taxable amount of dividends from taxable Canadian corporations (see the guide)			**120**	
Interest and other investment income (attach Schedule 4)			**121**	
Net partnership income: limited or non-active partners only (attach Schedule 4)			**122**	
Rental income	Gross **160**		Net **126**	
Taxable capital gains (attach Schedule 3)			**127**	
Support payments received	Total **156**		Taxable amount **128**	
RRSP income (from all T4RSP slips)			**129**	
Other income	Specify:		**130**	
Self-employment income (see lines 135 to 143 in the guide)				
Business income	Gross **162**		Net **135**	
Professional income	Gross **164**		Net **137**	
Commission income	Gross **166**		Net **139**	
Farming income	Gross **168**		Net **141**	
Fishing income	Gross **170**		Net **143**	
Workers' compensation benefits (box 10 on the T5007 slip)	**144**			
Social assistance payments	**145**			
Net federal supplements (box 21 on the T4A(OAS) slip)	**146**			
Add lines 144, 145, and 146		►	147	
Add lines 101, 104 to 143, and 147 This is your **total income.**			**150**	18,000.00

Kercher, George Chapter 6 Example SIN: 527 000 145

3

Attach your completed Schedule 1 (federal tax), and Form 428 (provincial or territorial tax) here. Also attach here any other schedules, information slips, forms, receipts, and documents that you need to include with your return.

Net income

Enter your **total income** from line 150			150	18,000.00
Pension adjustment (box 52 on all T4 slips and box 34 on all T4A slips)	206	1,800.00		
Registered pension plan deduction (box 20 on all T4 slips and box 32 on all T4A slips)	207	900.00		
RRSP deduction (see Schedule 7; attach receipts)	208			
Saskatchewan Pension Plan deduction (maximum $600)	209			
Annual union, professional, or like dues (box 44 on all T4 slips, or from receipts)	212	110.00		
Child care expenses (attach Form T778)	214			
Attendant care expenses	215			
Business investment loss Gross 228 Allowable deduction	217			
Moving expenses	219			
Support payments made Total 230 Allowable deduction	220			
Carrying charges and interest expenses (attach Schedule 4)	221			
Deduction for CPP or QPP contributions on self-employment and other earnings (attach Schedule 8)	222		•	
Exploration and development expenses (attach Form T1229)	224			
Other employment expenses	229			
Clergy residence deduction	231			
Other deductions Specify:	232			
Add lines 207 to 224, 229, 231 and 232.	233	1,010.00	►	1,010.00
Line 150 minus line 233 (if negative, enter "0"). This is your **net income before adjustments.**			234	16,990.00
Social benefits repayment (if you reported income on line 113, 119, or 146, see line 235 in the guide)			235	•
Line 234 minus line 235 (if negative, enter "0"). If you have a spouse or common-law partner, see line 236 in the guide. This is your **net income.**			236	16,990.00

Taxable income

Employee home relocation loan deduction (box 37 on all T4 slips)	248			
Security options deductions	249			
Other payments deduction (if you reported income on line 147, see line 250 in the guide)	250			
Limited partnership losses of other years	251			
Non-capital losses of other years	252			
Net capital losses of other years	253			
Capital gains deduction	254			
Northern residents deductions (attach Form T2222)	255			
Additional deductions Specify:	256			
Add lines 248 to 256.	257		►	
Line 236 minus line 257 (if negative, enter "0") This is your **taxable income.**			260	16,990.00

Use your taxable income to calculate your federal tax on Schedule 1 and your provincial or territorial tax on Form 428.

Kercher, George Chapter 6 Example SIN: 527 000 145

Refund or Balance owing

4

Net federal tax: Enter the amount from line 19 of Schedule 1 (attach Schedule 1 even if the result is "0")		420	0 00
CPP contributions payable on self-employment and other earnings (from Schedule 8)		421	
Social benefits repayment (enter the amount from line 235)		422	
Provincial or territorial tax (attach Form 428 even if the result is "0")		428	
Add lines 420 to 428 This is your **total payable.**		435	0 00 •
Total income tax deducted (from all information slips)	437	3,500 00 •	
Refundable Québec abatement	440	•	
CPP overpayment (enter your excess contributions)	448	•	
Employment Insurance overpayment (enter your excess contributions)	450	•	
Refundable medical expense supplement	452	172 58 •	
Refund of investment tax credit (attach Form T2038 (IND))	454	•	
Part XII.2 trust tax credit (box 38 on all T3 slips)	456	•	
Employee and partner GST/HST rebate (attach Form GST370)	457	•	
Tax paid by instalments	476	3,000 00 •	
Provincial or territorial credits (attach Form 479 if it applies)	479	•	
Add lines 437 to 479 These are your **total credits.**	482	6,672 58 ▶	6,672 58
Line 435 minus line 482			(6,672 58)

If the result is negative, you have a **refund**.
If it is positive, you have a **balance owing**.
Enter the amount below on whichever line applies.

Generally, we do not charge or refund a difference of $2 or less.

Refund 484 6,672 58 •

Balance owing 485 •

Amount enclosed 486 •

Attach to page 1 a **cheque** or **money order** payable to the Receiver General. Your payment is due no later than April 30, 2004.

Direct Deposit Request - Start or Change (see line 484 in the guide)

You do not have to complete this area every year. Do not complete it this year if your direct deposit information for your refund has not changed.

Refund and GST/HST credit - To start direct deposit or change account information only, attach a "void" cheque or complete lines 460, 461, and 462.

Note: To deposit your **CCTB** payments (including certain related provincial or territorial payments) into the **same** account, also check box 463.

Branch number	Institution number	Account number	CCTB
460	461	462	463

I certify that the information given on this return and in any documents attached is correct, complete, and fully discloses all my income.

Sign here ____________________

It is a serious offence to make a false return.

Telephone (111) 111-1111 Date 2004-06-06

490 X **For professional tax preparers only.**

Name

Address

Telephone ( ) -

Do not use this area 487 488

RC-03-148

Kercher, George Chapter 6 Example SIN: 527 000 145

T1-2003 Federal Tax Schedule 1

Complete this schedule to claim your federal non-refundable tax credits and to calculate your net federal tax.

You must attach a copy of this schedule to your return.

Enter your **taxable income** from line 260 of your return 16,990.00 1

Use the amount on line 1 to determine which **ONE** of the following columns you have to complete.

If the amount on line 1 is:	$32,183 or less	more than $32,183, but not more than $64,368	more than $64,368 but not more than $104,648	more than $104,648
Enter the amount from line 1 above	16,990.00 2	2	2	2
Base amount	3	32,183.00 3	64,368.00 3	104,648.00 3
Line 2 minus line 3 (this amount cannot be negative)	16,990.00 4	4	4	4
Rate	x 16.00 % 5	x 22.00 % 5	x 26.00 % 5	x 29.00 % 5
Multiply the amount on line 4 by the rate on line 5	2,718.40 6	6	6	6
Tax on base amount	0.00 7	5,149.00 7	12,230.00 7	22,703.00 7
Add lines 6 and 7	2,718.40 8	8	8	8

Federal non-refundable tax credits

Basic personal amount		**claim $7,756**	300	7,756.00
Age amount (if you were born in 1938 or earlier)		(maximum $3,787)	301	
Spouse or common-law partner amount:				
Base amount	7,245.00			
Minus: His or her net income (from page 1 of your return)	0.00			
Result: (if negative, enter "0")		(maximum $6,586) ▶	303	
Amount for an eligible dependant		(maximum $6,586)	305	6,586.00
Amount for infirm dependants age 18 or older			306	
CPP or QPP contributions:				
through employment from box 16 and box 17 on all T4 slips		(maximum $1,801.80)	308	717.75 •
on self-employment and other earnings (from Schedule 8)			310	•
Employment Insurance premiums from box 18 on all T4 slips		(maximum $819.00)	312	378.00 •
Pension income amount		(maximum $1,000)	314	
Caregiver amount (attach Schedule 5)			315	
Disability amount			316	
Disability amount transferred from a dependant			318	
Interest paid on your student loans			319	
Tuition and education amounts (attach Schedule 11)			323	1,295.00
Tuition and education amounts transferred from a child			324	
Amounts transferred from your spouse or common-law partner (attach Schedule 2)			326	
Medical expenses (attach receipts)	330	1,200.00		
Minus: $1,755, or 3% of line 236, whichever is **less**		509.70		
Subtotal		690.30		
Minus: Medical expenses adjustment	331			
Allowable portion of medical expenses (if negative, enter "0")		690.30 ▶	332	690.30
Add lines 300 to 326, and 332.			335	17,423.05

	Multiply the amount on line 335 by 16% =	338	2,787.69
Donations and gifts	(attach Schedule 9)	349	
	Total federal non-refundable tax credits: Add lines 338 and 349.	350	2,787.69

Kercher, George Chapter 6 Example SIN: 527 000 145

Net federal tax

Enter the amount from line 8		2,718.40	9		
Federal tax on split income (from line 4 of Form T1206)	424		• 10		
Add lines 9 and 10		2,718.40	▶	2,718.40	11
Enter the amount from line 350	350	2,787.69			
Federal dividend tax credit (13.3333% of the amount on line 120 of your return)	425		•		
Overseas employment tax credit (attach Form T626)	426				
Minimum tax carry-over	427		•		
Add lines 350, 425, 426, and 427		2,787.69	▶	2,787.69	12
Basic federal tax: Line 11 minus line 12 (if negative, enter "0")			429		13
Federal foreign tax credit: Complete the federal foreign tax credit calculation below and enter the amount from line (i) or line (ii), whichever is **less**.					14
Federal logging tax credit					
Federal tax: Line 13 minus line 14 (if negative, enter "0")			406	0.00	15
Total federal political contributions (attach receipts) 409					
Federal political contribution tax credit (see the guide)	410		•		
Investment tax credit (attach Form T2038(IND))	412		•		
Labour-sponsored funds tax credit — Net cost 413 — Allowable credit	414		•		
Add lines 410, 412, and 414.	416		▶		16
Line 15 minus line 16 (if negative, enter "0") (if you have an amount on line 424 above, see Form T1206)			417		17
Additional tax on RESP accumulated income payments (attach Form T1172)			418		18
Net federal tax: Add lines 17 and 18. Enter this amount on line 420 of your return.			420	0.00	19

Federal foreign tax credit: (see lines 431 and 433 in the guide)

Make a separate calculation for each foreign country. Enter the result on line 14 above.

Non-business-income tax paid to a foreign country 431 ________ • (i)

Net foreign non-business income * 433 ________ / Net income ** ________ X Basic federal tax *** ________ = ________ (ii)

* Reduce this amount by any income from that foreign country for which you claimed a capital gains deduction, and by any income from that country that was, under a tax treaty, either exempt from tax in that country or deductible as exempt income in Canada (included on line 256). Also reduce this amount by the lesser of lines E and F on Form T626.

** Line 236 plus the amount on line 3 of Form T1206, minus the total of the amounts on lines 248, 249, 250, 253, 254, and minus any amount included on line 256 for foreign income deductible as exempt income under a tax treaty, income deductible as net employment income from a prescribed international organization, or non-taxable tuition assistance from box 21 of the T4E slip. If the result is less than the amount on line 433, enter your **Basic federal tax***** on line (ii).

*** Line 429 plus the amount on lines 425 and 426, and minus any refundable Québec abatement (line 440) and any federal refundable First Nations abatement (line 441 on the return for residents of Yukon).

Problems For Self Study

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

Self Study Problem Six - 1

The following five independent Cases make varying assumptions with respect to Mr. Stanley Murphy and his 2004 tax status.

Case A Mr. Murphy is 48 years of age and has employment income of $41,000. During the year, Stanley makes contributions to federal political parties in the amount of $1,000. Mr. Murphy is not married and has no dependants.

Case B Mr. Murphy is 48 years of age and has income from employment of $41,000. His wife, Helen Murphy, is 43 years of age and has employment income of $4,650. They have one child, Eileen, who is 11 years of age. During the year, the family had eligible medical expenses of $1,050 for Stanley, $1,800 for Helen, and $300 for Eileen. Eileen has no income in 2004.

Case C Mr. Murphy is 48 years of age and his wife, Helen, is 43. Mr. Murphy has income from employment of $41,000. Helen has employment income 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 2004 calendar year and $525 for required textbooks. Albert had employment income of $3,000 that he earned during the summer.

Case D Mr. Murphy is 67 and his wife Helen is 68. Helen has been completely disabled for a number of years. The components of Stanley and Helen's income are as follows:

	Stanley	Helen
Interest	$ 300	$ 50
Canada Pension Plan	4,400	200
Old Age Security Pension	5,550	5,550
Income From Registered Pension Plan	31,150	450
Total Net Income	$41,400	$6,250

Case E Mr. Murphy is 30 years of age and unmarried. Mr. Murphy provides home care for his 68 year old father. His father's 2004 Net Income For Tax Purposes is $9,200. In June of last year, Stanley graduated from a Canadian university with a degree in mathematics. In January 2004, Stanley began to repay his student loan of $25,000 in monthly installments of $325. Stanley paid $375 in interest related to his student loan in 2004. His only income is $41,000 in net employment income.

Required: In each Case, calculate Mr. Murphy's Taxable Income and minimum federal Tax Payable. To concentrate on the differences generated by the varying assumptions, ignore any amounts Mr. Murphy might have had withheld or paid in instalments, and any EI or CPP contributions.

Self Study Problem Six - 2

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 2004, 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 2009, the year of his expected retirement.

Other Information:
For the 2004 taxation year, the following items were relevant.

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

Federal Income Tax	$16,000
Canada Pension Plan Contributions	1,832
Employment Insurance Premiums	772
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 $27,500. 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 available to Mr. Barth for ten months of the year. During the other two months, he was out of the country and left 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.

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. Assume that, at the time the loan was granted, the relevant prescribed rate was 3 percent. Mr. Barth paid the corporation a total of $375 in interest during the year.

5. Mr. Barth was required to pay professional dues of $1,800 during the year.

6. In 2003, 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. At the time of exercise, he elected to defer the income inclusion on the stock options. Shortly after his purchase, the stock price dropped. Mr. Barth left instructions with his stockbroker to sell his shares as soon as they reached $18 per share. This occurred on August 24, 2004.

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 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 $12,400. She had withheld from her income EI premiums of $246 [(1.98%)($12,400)] and CPP contributions of $441 [(4.95%)($12,400 - $3,500)]. Mr. Barth paid Marg's tuition for 2004 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

Required: Calculate, for the 2004 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 Six - 3

Note To Students This is an extension of Self Study Case Six-1 (tax return preparation case). It has been updated for 2004 rates.

Ms. Eleanor Trubey's husband died two years ago. In addition to her employment income, she receives a pension from his previous employer, and CPP survivor benefits. After her husband died, she moved from her house in Prince George, B.C., to a rented house in Victoria, B.C. She did not sell her house as it is her intention to move back into it within a year. It has been rented on a month-to-month lease since November, 2003.

Ms. Trubey's widowed mother, Marjorie Takarabe, had extremely bad luck the last time she was in Las Vegas. She lost all of her life savings and her house. As a result, she has moved in with Ms. Trubey and takes care of the house, Ms. Trubey's younger daughter, Amy, and all of the household cooking. Marjorie has never filed a tax return and has no Social Insurance Number.

Diane Trubey, 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. Trubey for 2004 is as follows:

1. Eleanor was born on May 15, 1956. She lives in Victoria, B.C.

2. The birth dates and income for the year of her dependants are as follows:

	Birth Date (Y/M/D)	Annual Income
Diane	1984-05-14	$2,300
Amy	1992-10-11	Nil
Marjorie	1923-05-21	5,600

3. Eleanor's T4 for 2004 showed the following:

Employment Income	$60,202
Employee's CPP Contributions	1,832
Employee's EI Premiums	772
RPP Contributions	2,406
Pension Adjustment	7,829
Income Tax Deducted	19,408
Union Dues	749
Charitable Donations	200

4. Eleanor and her family had the following medical expenses for 2004:

Patient	Medical Expenses	Description	Amount
Amy	Walk Right Foot Clinic	Orthodics	$ 450
Amy	Dr. Tamo	Dental	1,120
Marjorie	Dr. Zhang	Acupuncture	50
Marjorie	Pharmacy	Prescription	75
Diane	Dr. Glassman	Physiotherapist	100
Eleanor	Grace Hospital	Ambulance Charge	392
Eleanor	Paramed Home Health	Nursing Care	1,350
Total			$3,537

5. In addition to the $200 in charitable contributions withheld by Eleanor's employer, Eleanor and Diane had the following charitable donations for 2004:

Donor	Charitable Donation Receipts	Amount
Eleanor	Heart And Stroke	$ 350
Eleanor	Terry Fox Foundation	50
Diane	Addiction Research Council Of Canada	100

6. Diane's T2202A showed tuition fees of $4,415, full-time attendance for 8 months, and part-time attendance for 2 months.

Required: Calculate Ms. Trubey's minimum federal Tax Payable for 2004, without consideration of any income tax withheld. List any assumptions you have made, and any notes and tax planning issues you feel should be placed in the file.

Self Study Case Six - 1 (Using ProFile T1 Software For 2003 Tax Returns)

This is extended in Self Study Problem Six-3 to use 2004 rates. This Case is continued in Chapter 14.

Ms. Eleanor Trubey's husband died two years ago. In addition to her employment income, she receives a pension from his previous employer, and CPP survivor benefits. After her husband died, she moved from her house in Prince George, B.C., to a rented house in Victoria, B.C. She did not sell her house as it is her intention to move back into it within a year. It has been rented on a month-to-month lease since November, 2002.

Ms. Trubey's widowed mother, Marjorie Takarabe, had extremely bad luck the last time she was in Las Vegas. She lost all of her life savings and her house. As a result, she has moved in with Ms. Trubey and takes care of the house, Ms. Trubey's younger daughter, Amy, and all of the household cooking. Marjorie has never filed a tax return and has no Social Insurance Number.

Diane Trubey, 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.

Information concerning Ms. Trubey for 2003 is given on the following pages.

Required: With the objective of minimizing Ms. Trubey's Tax Payable, prepare the 2003 income tax return of Eleanor Trubey using the GreenPoint ProFile software. List any assumptions you have made, and any notes and tax planning issues you feel should be placed in the file.

Personal Information	
Title	Ms.
First Name	Eleanor
Last Name	Trubey
SIN	527-000-087
Date of birth (Y/M/D)	1955-05-15
Marital Status	Widowed
Provide information to Elections Canada?	Yes
Own foreign property of more than $100,000 Canadian?	No
Instalments paid on March 15 and June 15 of $1,264	$2,528 total for 2003

Taxpayer's Address
1415 Vancouver Street, Victoria, B.C. V8V 3W4
Phone number (250) 363-0120

Dependants	Child 1	Child 2	Mother
First Name	Diane	Amy	Marjorie
Last Name	Trubey	Trubey	Takarabe
SIN	527-000-293		
Date of birth (Y/M/D)	1983-05-14	1991-10-11	1922-05-21
Net income	$2,300	Nil	$5,600

T2202A - (Diane)	Box	Amount
Tuition fees - for Diane Trubey (daughter)	A	4,414.56
Number of months in school - part-time	B	2
Number of months in school - full-time	C	8

T4	Box	Amount
Issuer - 1750 Canada Inc.		
Employment income	14	60,201.80
Employee's CPP contributions	16	1,801.80
Employee's EI premiums	18	819.00
RPP contributions	20	2,406.16
Pension adjustment	52	7,829.00
Income tax deducted	22	19,408.00
Union dues	44	748.59
Charitable donations	46	200.00

Patient	(Y/M/D)	Medical Expenses	Description	Am't
Amy	2003-05-11	Walk Right Foot Clinic	Orthodics	450
Amy	2003-01-23	Dr. Tamo	Dental	1,120
Marjorie	2003-05-20	Dr. Zhang	Acupuncture	50
Marjorie	2003-07-06	Pharmacy	Prescription	75
Diane	2003-09-01	Dr. Glassman	Physiotherapist	100
Eleanor	2003-08-15	Grace Hospital	Ambulance charge	392
Eleanor	2003-08-18	Paramed Home Health	Nursing care	1,350

Donor	Charitable Donation Receipts	Am't
Eleanor	Heart and Stroke	350
Eleanor	Terry Fox Foundation	50
Diane	Addiction Research Council of Canada	100

Assignment Problems

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

Assignment Problem Six - 1

Mr. William Norris is 45 years old. The following five independent Cases make varying assumptions for the 2004 taxation year with respect to Mr. Norris' marital status, number of dependants, and type of income received. In all Cases, assume his employer has withheld EI premiums of $772 and CPP contributions of $1,832.

Case A Mr. Norris is unmarried and provides in home care for his 73 year old mother, Bernice. Bernice had Net Income For Tax Purposes of $13,500 for the year. Mr. Norris earned employment income of $46,000.

Case B Mr. Norris earned employment income of $46,000. His wife, Susan, has employment income 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
Total	$3,150

Case C Mr. Norris earned employment income of $46,000. His wife, Susan, has employment income 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. His income is made up of $46,000 in employment income. On receipt of a $300,000 inheritance in December, he donates $50,000 to his local hospital. In addition, he makes contributions to federal political parties 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 $12,000 outstanding in Canada Student Loans. Mr. Norris pays back these loans in monthly instalments of $125. During the year, he paid $250 in interest on these loans. Mr. Norris earned employment income of $46,000.

Required: In each Case, calculate Mr. Norris' minimum federal Tax Payable. In making this calculation, ignore any tax amounts that Mr. Norris might have had withheld or paid in instalments. Indicate any carry overs available to him and the carry over provisions.

Assignment Problem Six - 2

Mr. Dennis Lane has been a widower for several years. For 2004, both his Net Income For Tax Purposes and Taxable Income were equal to his net employment income of $65,000. Mr. Lane's employer withheld $12,100 in income taxes, $772 for Employment Insurance premiums and $1,867 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. Due to an extensive business trip, Mr. Lane did not file his 2004 return until June 1, 2005.

3. 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 2004 Net Income For Tax Purposes of $8,200. His son did not use the medical expense credit as he had no Tax Payable.

4. Mr. Lane's provincial Tax Payable, net of all applicable credits, has been correctly calculated to be $4,250.

5. Assume that the prescribed interest rate for all relevant periods, including the extra 4 percent on amounts owing to the Minister, is 7 percent compounded on an annual basis.

Required: Calculate Mr. Lane's amount owing (refund) for 2004. Include in your solution any penalties and interest that will result from the late filing.

Assignment Problem Six - 3

For the past five years, Mr. Brooks has been employed as a financial analyst by a large Canadian public firm located in Winnipeg. During 2004, 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 2004 and the remainder is to be paid on January 15, 2005.

During 2004, Mr. Brooks' employer withheld the following amounts from his gross wages:

Federal Income Tax	$8,000
Canada Pension Plan Contributions	1,832
Employment Insurance Premiums	772
Registered Pension Plan Contributions	2,800
Donations To The United Way	480
Union Dues	240
Contributions To Employee Stock Purchase Plan	800
Payments For Personal Use Of Company Car	1,000

Other Information:

1. Due to an airplane accident while flying to Thunder Bay on business, Mr. Brooks was seriously injured and confined to a Thunder Bay hospital for two full months during 2004. 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.

2. Mr. Brooks is provided with a car that the company leases at a rate of $600 per month, plus provincial sales tax of $48 and $42 in GST. The company also assumes all of the operating costs of the car and these amounted to $3,500 during 2004. Mr. Brooks drove the car a total of 35,000 kilometers during 2004, 30,000 kilometers of which were carefully documented as employment related travel. When he is out of town, the car and its keys are left with his employer.

3. On January 15, 2003, 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, 2004, when the shares were trading at $28 per share. He does not plan to sell the shares for at least a year. As he was not aware that there is a provision which allows him to defer the employment income inclusion on stock options, he did not file the required election.

4. In order to assist Mr. Brooks in acquiring a new personal residence in Winnipeg, his employer granted him a five year loan of $125,000 at an annual interest rate of 2 percent. The loan was granted on October 1, 2004 and, at this point in time, the interest rate on open five year mortgages was 8 percent. Assume the relevant ITR 4301 rate was 3 percent on this date. The loan qualifies as a home relocation loan.

5. Other disbursements made by Mr. Brooks include the following:

Advanced financial accounting course tuition fees	$1,200
Music history course tuition fees (University of Manitoba night 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.

6. Mr. Brooks is a widower. His wife was killed in a car accident 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 only income is OAS payments of $5,550. Grace refused to take any payments for caring for Harold. As a result, Mr. Brooks did not pay any child care or attendant costs for Harold.

7. Mr. Brooks paid the following medical costs:

For Himself	$ 7,300
For Harold	4,450
For Grace	1,220
Total	$12,970

   The medical expenses for himself included $5,700 for acupuncture treatments for pain from a licenced practitioner while he was confined to the Thunder Bay hospital.

Required: Calculate, for the 2004 taxation year, Mr. Brooks' minimum Taxable Income and federal Tax Payable (Refund).

Assignment Problem Six - 4

This is an extension of the Chapter 6 version of the Progressive Running Case (tax return preparation case). It has been updated for 2004 rates.

Seymour Gravel and Mary Walford have been married for more than 10 years. Mary has progressed quickly in the firm she is working for due to her strong tax and accounting background and has been rewarded with a large bonus in 2004.

Other information concerning Seymour and Mary for 2004 is as follows:

1. Seymour was born on January 29, 1945. Mary was born on December 8, 1966. Their son, William, was born on February 24, 1997. He has no income for 2004. They live in Saint John, New Brunswick.

2. Mary's T4 showed employment income of $152,866. Her withholdings consisted of income tax of $52,265, CPP contributions of $1,832, EI premiums of $772, and charitable donations of $1,000.

3. To help deal with his son, who has been refusing to go to school and is displaying hostile tendencies, Seymour enrolled in a three month course on child psychology at Dalhousie University. His T2202A showed tuition fees of $2,200 and full-time attendance for 3 months.

4. In addition to the charitable donations withheld by Mary's employer, Seymour donated $500 to the Canadian Cancer Foundation and $250 to the Salvation Army.

5. Assume in this version of the problem that Seymour has no income for 2004.

Required: Calculate Ms. Walford's minimum federal Tax Payable for 2004, without consideration of any income tax withheld. List any assumptions you have made, and any notes and tax planning issues you feel should be placed in the file.

Assignment Problem Six - 5

This is an extension of Assignment Case Six-2 (tax return preparation case). It has been updated for 2004 rates.

George Hall 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.

George and his wife, Valerie, adopted Kevin. Valerie quit her part-time job to care for him. She also cares for her mother, Joan Parker. Joan suffers from diabetes and severe depression and lives with George and Valerie. Valerie's parents separated two years ago in Scotland after her father, David Parker, suffered enormous losses in the stock market. They were forced to sell their home and David moved to South America. David phones periodically to request that money be deposited in his on-line bank account. Valerie does not meet the residency requirements necessary to qualify for Canadian Old Age Security payments.

George's step-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 the Northern Alberta Institute of Technology. George is paying his tuition and Martin has agreed to transfer the maximum tuition and education amounts to George. Although Martin plans to file his 2004 tax return, he has not done so yet.

George's father died some years ago and left his estate to George's mother, Irene. She has severe Alzheimer's disease and can no longer feed or dress herself. She lives in a nursing home where she requires constant care. Irene invested the entire estate in tax shelters, which have since proved to be worthless.

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 2004 is as follows:

1. George was born on July 2, 1940 and lives in Edmonton, Alberta.
2. The birthdates and income for the year of his dependants are as follows:

	Birth Date (Y/M/D)	Annual Income
Valerie (income from CPP)	1939-12-30	$5,800
Kevin	1988-10-17	Nil
Joan Parker	1919-02-24	500
David Parker	1920-01-12	Nil
Martin	1957-06-02	8,300
Irene Hall	1917-05-21	5,550

3. George's T4 showed employment income of $378,000, which includes employment commissions of $82,000. His withholdings consisted of income tax of $125,000, CPP contributions of $1,832, EI premiums of $772, and charitable donations of $400.
4. Martin's T2202A showed tuition fees of $6,000 and full-time attendance for 8 months.
5. During the year, Valerie donated $1,000 to Mothers Against Drunk Drivers (MADD). George donated $3,000 to the Canadian National Institute For The Blind (CNIB).
6. George and his family had the following medical expenses for 2004:

Patient	Medical Expenses	Description	Amount
Family	Johnson Inc.	Out Of Canada Insurance	$ 731
George	Dr. Smith	Dental Fees	155
George	Optician	Prescription Glasses	109
Valerie	Pharmacy	Prescription	67
Joan	Dr. Wong	Psychiatric Counseling	2,050
David	Tropical Disease Centre	Prescription	390
Martin	Dr. Walker	Group Therapy	4,000
Total			$7,502

7. George paid the annual fees for the Tranquility Nursing Home for his mother, Irene. They totalled $30,000 for 2004. He also paid $800 for the care and feeding of Kevin's seeing eye dog, Isis, during 2004.
8. George's home has a total area of 5,000 square feet. The area of the home used as a home office is 650 square feet. Other costs for the home are as follows:

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
Total	$24,920

9. 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.

Required: Calculate Mr. Hall's minimum federal Tax Payable for 2004, without consideration of any income tax withheld. List any assumptions you have made, and any notes and tax planning issues you feel should be placed in the file. Assume that George does not qualify for the GST rebate for employees.

Assignment Problem Six - 6 (Electronic Library Research Problem)

Provide brief answers to the following questions. Your answers should be supported by references to materials found in your Electronic Library.

A. The education tax credit is available to students enrolled in a "qualifying education program". Would an individual be eligible for this credit if his employer required him to take an appropriate program as part of his employment duties? Would an individual be eligible for this credit if he was taking an appropriate program during a leave of absence that was financed by his employer? Would an individual be eligible for this credit if he was taking an appropriate program, and has received financing from a business that is conditional on his becoming an employee of that business on completion of his studies?

B. For purposes of the medical expense tax credit, ITA 118.2(2) refer to amounts paid to "medical practitioners". Which of the following would qualify for this designation?

    1. A chiropractor
    2. A naturopath
    3. A physiotherapist
    4. An acupuncturist
    5. A faith healer
    6. A dietician
    7. A Christian Science practitioner
    8. A psychologist

Cases - Using ProFile T1 Software For 2003 Tax Returns

Assignment Case Six - 1 (Using ProFile T1 Software For 2003 Tax Returns)

This Case is continued in Chapter 14.

Mr. Buddy Cole (SIN 527-000-061) was born on August 28, 1936. He has spent most of his working life as a pianist and song writer. He and his family live at 1166 West Pender Street, Vancouver, B.C. V6E 3H8, phone (604) 669-7815.

Mr. Cole's wife, Natasha (SIN 527-000-129), was born on June 6, 1978 and was a professional singer prior to her marriage to Mr. Cole. She still enjoys singing, and gave a few weekend performances during 2003 at the Loose Moose Pub. She earned $3,200 for these performances. She and Mr. Cole have four children. Each child was born on April 1 of the following years, Linda; 1998, Larry; 1999, Donna; 2000, and Donald; 2001. She has never filed a tax return before, and does not plan on filing one this year.

Buddy and Natasha Cole have two adopted children. Richard (SIN 527-000-285) was born on March 15, 1986, has income of $2,800, and started full time attendance at university in September of 2003. His first semester tuition fee is $2,000 and he requires books with a total cost of $375. These amounts are paid by Mr. Cole.

The other adopted child, Sarah, was born on September 2, 1983, and is in full time attendance at university for all of 2003 (including a four month summer session). Her tuition is $5,600 and she requires textbooks which cost $750. These amounts are also paid by Mr. Cole. Sarah has no income during the year. Any unused credits of either child are available to be transferred to their father.

Mr. Cole's mother, Eunice, was born on April 10, 1916 and his father, Earl, was born on November 16, 1914. They both live with Mr. Cole and his wife. While his father is still physically active, his mother is blind. Eunice Cole had income of $9,500 for the year, while Earl Cole had income of $7,500.
Other information concerning Mr. Cole and his family for 2003 is as follows:

1. Mr. Cole earned $16,500 for work as the house pianist at the Loose Moose Pub. His T4 showed that his employer withheld $4,200 for income taxes and $386.50 for EI. Due to an error on the part of the payroll accountant, he overpaid his EI by $40. No CPP was withheld.

2. During the year, Mr. Cole made $3,000 in donations to Planned Parenthood Of Canada, a registered Canadian charity.

3. Mr. Cole has been married before to Lori Cole (SIN 527-000-319). Lori is 52 years old and lives in Fort Erie, Ontario.

4. Mr. Cole has two additional children who live with their mother, Ms. Dolly Holt (SIN 527-000-582), in Burnaby, British Columbia. The children are Megan Holt, aged 15 and Andrew Holt, aged 16. While Ms. Holt and Mr. Cole were never married, Mr. Cole 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. On December 2, 2003, Mr. Cole paid dental expenses to Canada Wide Dental Clinics for the following individuals:

Himself	$1,200
Natasha	700
Richard	800
Sarah	300
Linda	100
Earl	1,050
Lori	300
Dolly Holt	675
Megan Holt	550
Total	$5,675

6. Mr. Cole has not applied to receive either OAS or CPP benefits.

Required: With the objective of minimizing Mr. Cole's Tax Payable, prepare his 2003 income tax return using the GreenPoint ProFile software program. List any assumptions you have made, and any notes and tax planning issues you feel should be placed in the file.

Assignment Case Six - 2 (Using ProFile T1 Software For 2003 Tax Returns)

This is extended in Assignment Problem Six-5 to use 2004 rates. This Case is continued in Chapter 14.

George Hall 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.

George and his wife, Valerie, adopted Kevin. Valerie quit her part-time job to care for him. She also cares for her mother, Joan Parker. Joan suffers from diabetes and severe depression and lives with George and Valerie. Valerie's parents separated two years ago in Scotland after her father, David Parker, suffered enormous losses in the stock market. They were forced to sell their home and David moved to South America. David phones periodically to request that money be deposited in his on-line bank account. Valerie does not meet the residency requirements necessary to qualify for Canadian Old Age Security payments.

George's step-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 the Northern Alberta Institute of Technology. George is paying his tuition and Martin has agreed to transfer the maximum tuition and education amounts to George. Although Martin plans to file his 2003 tax return, he has not done so yet.

George's father died some years ago and left his estate to George's mother, Irene. She has severe Alzheimer's disease and can no longer feed or dress herself. She lives in a nursing home where she requires constant care. Irene invested the entire estate in tax shelters, which have since proved to be worthless.

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 2003 is given on the following pages.

Required: Prepare the 2003 income tax return of George Hall using the GreenPoint ProFile software. List any assumptions you have made, and any notes and tax planning issues you feel should be placed in the file. Assume that George does not qualify for the GST rebate.

Personal Information	Taxpayer
Title	Mr.
First Name	George
Last Name	Hall
SIN	527-000-509
Date of birth (Y/M/D)	1939-07-02
Marital Status	Married
Provide information to Elections Canada?	Yes
Own foreign property of more than $100,000 Cdn?	No

Taxpayer's Address
97 Jasper Avenue, Apt 10, Edmonton, Alberta T5J 4C8
Phone number (780) 495-3500

Dependants	Spouse	Child	Mother-In-Law
First Name	Valerie	Kevin	Joan
Last Name	Hall	Hall	Parker
SIN	527-000-483	527-000-517	
Date of birth (Y/M/D)	1938-12-30	1987-10-17	1918-02-24
Net income	$5,800 in CPP	Nil	$500

Dependants	Father-In-Law	Brother	Mother
First Name	David	Martin	Irene
Last Name	Parker	Hall	Hall
SIN		527-000-533	
Date of birth (Y/M/D)	1919-01-12	1956-06-02	1916-05-21
Net income	Nil	$7,800	$5,500

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

T4	Box	Amount
Issuer - Mega Pharma Inc.		
Employment income	14	378,000.00
Employee's CPP contributions	16	1,801.80
Employee's EI premiums	18	819.00
Income tax deducted	22	125,000.00
Employment commissions	42	82,000.00
Charitable donations	46	400.00

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
2003-12-31	Family	Johnson Inc.	Out of Canada insurance	731.30
2003-08-31	George	Dr. Smith	Dental fees	155.40
2003-09-19	George	Optician	Prescription glasses	109.00
2003-11-07	Valerie	Pharmacy	Prescription	66.84
2003-06-07	Joan	Dr. Wong	Psychiatric counseling	2,050.00
2003-03-22	David	Tropical Disease Centre	Prescription	390.00
2003-12-20	Martin	Dr. Walker	Group therapy	4,000.00

George paid the annual fees for the Tranquility Nursing Home for his mother, Irene. They totalled $30,000 for 2003. He also paid $800 for the care and feeding of Kevin's seeing eye dog, Isis during 2003.

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

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.

Progressive Running Case - Chapter 6 Version (Using ProFile T1 Software For 2003 Tax Returns)

This Progressive Running Case requires the use of the ProFile tax software. We have referred to this as a Progressive Running Case because more complex versions will be provided in subsequent Chapters. This version is extended in Assignment Problem Six-4 to use 2004 rates.

It is introduced in this Chapter and is continued in Chapters 8 through 14. Each version must be completed in sequence. The information in each version is applicable to all subsequent versions.

Seymour Gravel and Mary Walford are your tax clients. They have been married for two years. In late December, 2003, Mary comes to your office with the tax information for 2003 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 2003. 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 2004. He is contemplating a return to university as a student of music.

In order to estimate her possible financial position in 2004, she would like you to prepare her 2003 tax return assuming that Seymour has no income for 2003. She would also like you to compare her 2003 tax liability in the different provinces assuming Seymour has no income for 2003.

Personal Information	Taxpayer	Spouse
Title	Ms.	Mr.
First Name	Mary	Seymour
Last Name	Walford	Gravel
SIN	527-000-129	527-000-079
Date of Birth (Y/M/D)	1965-12-08	1944-01-29
Marital Status	Married	Married
Provide Information To Elections Canada?	Yes	Yes
Own Foreign Property of More Than $100,000 Cdn?	No	No

Taxpayer's Address
126 Prince William Street, Saint John, N.B. E2L 4H9
Phone number (506) 636-5997
Spouse's address same as taxpayer? Yes

Dependant	Child
First Name	William
Last Name	Gravel
SIN	527-000-319
Date of Birth (Y/M/D)	1995-02-24
Net Income	Nil

T4 - Mary	Box	Amount
Issuer - MoreCorp		
Employment Income	14	152,866.08
Employee's CPP Contributions	16	1,801.80
Employee's EI Premiums	18	819.00
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:

A. With the objective of minimizing Mary's Tax Payable, prepare, but do not print her 2003 income tax return using the GreenPoint ProFile software program. Assume that Seymour has no income in 2003. List any other assumptions you have made and provide any explanatory notes and tax planning issues you feel should be placed in the files.

B. 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.

C. Create and print a schedule that compares the total federal and provincial Tax Payable for Mary for all the territories and provinces other than Quebec. ***Hint***: To see 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, 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. If you open the Auditor <F9> and select the Variance tab you will see a detailed analysis of the changes.