Canadian Income Taxation 20172018 (Canadian) 20th edition Buckwold Test Bank

SKU: 9781259266003-TEST-BANK

MULTIPLE CHOICE. Choose the one alternative that best completes the statement or answers the question.

1) The CEO at Big Company Corporation has decided to sell a piece of capital equipment after the company's year-end in order to avoid paying capital gains tax this year. Which tax planning method will the CEO be using?
   A) Transferring income to another entity.
   B) This is a form of tax evasion and is not allowed.
   C) Shifting income from one time period to another.
   D) Converting the nature of income from one type to another.

   Answer: C

2) Which of the following scenarios illustrates a potential tax avoidance scheme?
   A) Dividends received from shares transferred from a wife to her husband are taxed in the hands of the wife.
   B) Property transferred between arm's-length parties is valued at fair market value.
   C) A man transfers property to his child at a value less than fair market value.
   D) A shareholder owns two corporations and undertakes legal steps in order to permit loss utilization between the two companies.

   Answer: C

3) The controller of Little Company Ltd. has decided to sell a piece of capital equipment after the company's year-end in order to avoid paying tax on capital gains this year. The controller is engaging in
   A) tax evasion. B) tax avoidance. C) tax planning. D) GAAR.

   Answer: C

4) Certain skills are necessary for successful tax planning. One of these skills is applying the time value of money. Which of the following is FALSE regarding this skill?
   A) Applying the time value of money is a tool used for wealth accumulation.
   B) If a taxpayer earns an annual return of 12% and is subject to a 40% tax rate, the annual after-tax return is 4.8%.
   C) If a taxpayer invests $1,000 at 8% and subsequently earns $48 in after-tax income on the investment at the end of the first year, the taxpayer's tax rate is 40%.
   D) If a taxpayer invests $1,000 for one year at a rate of return of 14% and is subject to a 45% tax rate, the after-tax value of the investment will be $1,077.

   Answer: B

Canadian Income Taxation 20172018 (Canadian) 20th edition Buckwold Test Bank

5) Which of the following statements regarding GAAR is true?

A) Individuals who organize their affairs in order to pay as little tax as possible will automatically be subject to GAAR.

B) The purpose of GAAR is to catch tax evaders.

C) When an avoidance transaction takes place, the anti-avoidance rule is automatically applied in all circumstances.

D) The Canada Revenue Agency states that "A transaction will not be an avoidance transaction if the taxpayer establishes that it is undertaken primarily for bona fide business, investment or family purposes."

Answer: D

ESSAY. Write your answer in the space provided or on a separate sheet of paper.

6) Steven James earned $150,000 this year in profits from his proprietorship, which placed him in a 45% bracket. The rate of tax for Canadian-controlled private corporations in his province is 15% on the fi $500,000 of income. Personal tax rates (federal plus provincial) in James' province are:

On the first $46,000	24%
On the next $46,000	32%
On the next $50,000	40%
On the next $61,000	45%
On income over $203,000	50%

(*All rates are assumed for this question.*)

Steven withdraws $3,000 per month for his personal living expenses. All remaining profits are used t taxes and to expand the business. Steven expects the same business after-tax profits next year.

Steven is considering incorporating his business next year. If he incorporates, he will pay himself a g salary of $48,000.

Required:

A. Determine the increase in Steven's cash flow if he incorporates his company? Show all calculatior
B. Name the type of tax planning that Steve would be engaging in if he incorporated his company.

Answer: A) Excess cash as a proprietorship:

Pre-tax Profits		$150,000
Tax:		
24% 46,000	$11,040	
32% 46,000	14,720	
40% 50,000	20,000	
45% 8,000	3,600	(49,360)
(Assume federal plus provincial rates)		
After-tax profits		$100,640

Canadian Income Taxation 20172018 (Canadian) 20th edition Buckwold Test Bank

Living expenses withdrawn	(36,000)
Available for expansion	$64,640

Excess cash as a corporation:

Profits before salary	$150,000
Salary	(48,000)
Corporate pre-tax profits	102,000
Tax: 15% x 102,000	(15,300)
After-tax profits (Available for expansion)	$86,700
Excess cash available for expansion ($86,700 - $64,640)	$22,060

C) Transferring income from one entity to another (individual to corporation)

7) Part A: List the three key factors of cash flow.

Part B: List the six skills required for tax planning as suggested in the textbook.

Answer: Part A:

Three key factors of cash flow

1. Amount of money coming in
2. Amount of money going out
3. Timing

Part B:

Six skills required for tax planning

1. Anticipation
2. Flexibility
3. Speculation
4. Applying the 8th Wonder of the World
5. Perspective
6. Global approach

Canadian Income Taxation 20172018 (Canadian) 20th edition Buckwold Test Bank

8) Andrew has $10,000 to invest. He wants to put his money in a one-year investment earning an annua rate of 12%. Andrew is in a 42% tax bracket.

Required:

a) Calculate the total value of Andrew's investment, after-tax, at the end of the year.
b) Calculate the amount of taxes Andrew will have to pay on his investment.

Answer: a) ($10,000 × 1.12) × (1 - .42) = $10,696
b) $10,000 × .12 × .42 = $504

9) Match each of the following terms with the most accurate example. Use each example only once.

TERMS:
Tax evasion
Tax planning
Tax avoidance

EXAMPLES:
A. An individual is seeking a beneficial outcome, and therefore, applies an application that is not spe prohibited by law.
B. A business is seeking a beneficial outcome, and therefore, does not report a portion of revenue ear during the year.
C. Two unrelated companies take steps to become related in order to shift income from the profitable to the company with losses.

Answer: An individual is seeking a beneficial outcome, and therefore, applies an application that is not specifically prohibited by law. **Tax planning**
A business is seeking a beneficial outcome, and therefore, does not report a portion of revenue during the year. **Tax evasion**
Two unrelated companies take steps to become related in order to shift income from the profita business to the company with losses. **Tax avoidance**

Canadian Income Taxation 20172018 (Canadian) 20th edition Buckwold Test Bank

10) For each of the examples listed below, state which of the following three categories of tax planning h
applied:

Shifting income from one time period to another

Shifting income from one entity to another

Shifting income from one type of income to another.

A. Jack has run a successful proprietorship for the past four years, and has now decided to incorporat
company.
B. Karen has decided not to pay herself a dividend from her corporation, (of which she is the sole sha
but has chosen to sell a portion of her shares to an associate instead.
C. XYZ Corporation has chosen to delay the recognition of a discretionary reserve until the followin

Answer: A. Shifting income from one entity to another
B. Shifting income from one type of income to another
C. Shifting income from one time period to another

Canadian Income Taxation 20172018 (Canadian) 20th edition Buckwold Test Bank

1) C
2) C
3) C
4) B
5) D
6) A) Excess cash as a proprietorship:

Pre-tax Profits		$150,000
Tax:		
24% 46,000	$11,040	
32% 46,000	14,720	
40% 50,000	20,000	
45% 8,000	3,600	(49,360)
(Assume federal plus provincial rates)		
After-tax profits		$100,640
Living expenses withdrawn		(36,000)
Available for expansion		$64,640

Excess cash as a corporation:

Profits before salary	$150,000
Salary	(48,000)
Corporate pre-tax profits	102,000
Tax: 15% x 102,000	(15,300)
After-tax profits (Available for expansion)	$86,700
Excess cash available for expansion ($86,700 - $64,640)	$22,060

C) Transferring income from one entity to another (individual to corporation)

Canadian Income Taxation 20172018 (Canadian) 20th edition Buckwold Test Bank

7) Part A:
Three key factors of cash flow

1. Amount of money coming in
2. Amount of money going out
3. Timing

Part B:
Six skills required for tax planning

1. Anticipation
2. Flexibility
3. Speculation
4. Applying the 8th Wonder of the World
5. Perspective
6. Global approach

8) a) ($10,000 × 1.12) × (1 - .42) = $10,696
b) $10,000 × .12 × .42 = $504

9) An individual is seeking a beneficial outcome, and therefore, applies an application that is not specifically prohibited by law. **Tax planning**
A business is seeking a beneficial outcome, and therefore, does not report a portion of revenue earned durir **Tax evasion**
Two unrelated companies take steps to become related in order to shift income from the profitable business company with losses. **Tax avoidance**

10) A. Shifting income from one entity to another
B. Shifting income from one type of income to another
C. Shifting income from one time period to another

Canadian Income Taxation 20172018 (Canadian) 20th edition Buckwold Test Bank

Exam Case Two

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

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

Deductions from pay:	
CPP and EI	3,400
Registered Pension Plan Contribution	2,000
Income tax deducted	25, 000

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

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

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

1) She sold a small piece of land in 20x7 (which is capital in nature) for $68,000. The land originally cost $50,000. Selling costs were $800. She received $35,000 of the proceeds in 20x7 and will receive the remainder of the funds this year (20x8).

2) Chloe began a small farming operation on the couple's acreage in 20x7. Her farm revenue totaled $5,000 in 20x7 and her expenses were $17,000. She has never farmed before, but her business looks promising and she expects a significant increase in sales this year.

Required:

a) Calculate Bart's minimum net income for tax purposes, and taxable income, for 20x7. Show your work using the aggregating formula from Section 3 of the Income Tax Act.

b) Calculate Bart's federal tax liability for 20x7.

c) Calculate the 20x7 tax consequences from Chloe's two issues.

(Use 2017 tax rules.)

Canadian Income Taxation 20172018 (Canadian) 20th edition Buckwold Test Bank

Solution:

a)

ITA 3(a)	
Employment income:	
Remuneration	$84,000
Gratuities	3,000
Standby charge	1,980
[($550 x 2/3 x 12) x 9,000/20,004]	
Operating benefit	
Lessor of $2,250 ($9,000 x .25)	
and $990 ($1,980 x .5)	990
RPP contribution	(2,000)
Employment income	$87,970
ITA 3(c)	
Other income:	
RRSP withdrawal	$10,000
Net income for tax purposes	$97,970
Taxable income	$97,970
(Amounts are rounded)	

b) Federal tax liability

$ 97,970.00			
$ 45,916.00	0.15		$ 6,887
$ 45,915.00	0.205		$ 9,413
$ 6,139.00	0.26		$ 1,596
$ 97,970.00			$ 17,896
NON-REFUNDABLE TAX CREDITS			
BASIC		$ 11,635	
CPP/EI		$ 3,400	
EMPLOYMENT		$ 1,178	
	0.15	$ 16,213	$ 2,432
FEDERAL TAX LIABILITY			$ 15,464

Canadian Income Taxation 20172018 (Canadian) 20th edition Buckwold Test Bank

c) 1. Capital gain on sale of land

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

Capital Gain				$17,200
Less capital gain reserve: lesser of:				
33,000	x	17200	$ 8,347	
68,000				
0.8	x	17200	$ 13,760	
				$ 8,347
Capital gain				$8,853
Taxable capital gain				$4,426

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

2. Farming income loss

Revenue	$ 5,000
Expenses	($17,000)
Net loss for tax purposes	($12,000)

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

$2,500 + 50% ($12,000 - $2,500)
*(Restricted farm loss cannot exceed $17,500)

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

Canadian Income Taxation 20172018 (Canadian) 20th edition Buckwold Test Bank