**QUESTION 1**

Fuzon Ltd. is a Canadian controlled private corporation. It has been in operation for several years and has a December 31 year end.

For the taxation year ending December 31, 2014, its Net Income For Tax Purposes was made up of the following components:

* Active Business Income $423,400
* Dividends From Canadian Corporations:
  + Wholly-Owned Subsidiary (All Non-Eligible) $223,600
  + Portfolio Investments (All Eligible) $101,400
* Canadian Source Interest $ 48,300
* Taxable Capital Gains [(1/2)($223,500)] $111,750
* Net Income For Tax Purposes $908,450

Dividends paid to Fuzon Ltd. by the wholly-owned subsidiary during 2014 did not result in a dividend refund. The wholly-owned subsidiary has been allocated one-half of the annual business limit for the small business deduction, with the remainder to be used by Fuzon.

On September 4, 2014, Fuzon paid taxable dividends to its shareholders in the amount of $65,600.

As of the end of the 2013 taxation year, Fuzon had a Refundable Dividend Tax On Hand balance of $39,400. During 2013, Fuzon Ltd. paid no dividends.

Required: For Fuzon’s 2014 taxation year, calculate the following items:

A. Federal Part I Tax Payable.

B. Part IV Tax Payable.

C. The balance in the Refundable Dividend Tax On Hand account on December 31, 2014.

D. The dividend refund, if any.

E. Federal Tax Payable (net of any dividend refund).

Show all of the calculations used to provide the required information, including those for which the result is nil.

NI for Tax Purposes: $908,450

To calculate Part 1 taxes, remove dividend to arrive to taxable income. Need to remove all Canadian dividends (portfolio, subsidiary, etc…) Eligible = from public companies, therefore eligible for a lower rate of tax for individual. Not available from small companies. Canadian only, do not remove foreign dividends. Foreign dividends is additional taxes as investment income, also deduct donations and cap losses c/o from prior years (only if company had capital gains this year). T-Bill interest income – if

Short term in nature, interest income (including ARs) is considered ABI. Only long term investments is maturity > 1 year

For SMB, need to remove items that are not eligible for SMB. Ex: long term interest income (considered investment income), rental income, foreign investment income, Canadian dividend, capital gains.

Best approach is to add items and calculate ABI.

Also need to take in consideration of subsidiary; if >10% considered associated company and need to share 500k cap. Take lower of ABI or annual shared limit.

Additional taxes: if Canadian dividend, only pay Part 4 taxes!! 6 2/3% is only one foreign dividend, rental income, etc…

PART IV Tax payable

1/3 $101,400 = $33,800

For dividends of wholly owned subsidiary company, so connected. To collect part 4 tax, % ownership \* dividend refund received when the dividend was paid. Since payer company got 0 refund, payable taxes is 0$.

3 – Balance in RDTOH account

This year balance: 116,000

Dividend refund = lesser of 1/3 dividend paid (1/3 \*$65,600 = $21,867) or ending RDTOH balance.

Final tax balance: 131536+33800-21867 = $143469

QUESTION 2

Mr. Rich is a self-employed businessman currently earning $150,000. He is thinking of incorporating his

company. He has a wife and 2 kids ages 18 and 15. His wife has no income for the year. The family needs

$60,000 of cash after taxes to live comfortably. He is also worried about his family finances if anything

was to happen to him. His company has about $1M market value of assets with a cost base of $100,000.

Assume the following tax rates:

* Corporation 20%
* Individual: Salary 40%, Dividends 20%

Required:

1. Should Mr. Rich incorporate his company? Show him with $$$$$ analysis
2. If he does, should he take a salary or a dividend.
3. What other issues should he consider re:

* Incorporation
* Salary or dividends
* His family’s future

QSBC – Company capital gain will be deductible for QSBC in the future. Could do income splitting if incorporated. If $ in corporation, reduces RRSP contribution potential.

Issues about familiy’s future: planning estate succession planning – trust, rollover, etc…

**QUESTION 3**

Several years ago, Ms. Katrina Bond acquired a business location that included land and a building for a total of $950,000. At the time, it was estimated that the value of the land was $220,000 and the value of the building was $730,000.

Ms. Bond operated the business for several years as a sole proprietorship and, during this period, she took CCA on the building. As there were years in which she experienced losses, she did not always take the maximum amount of CCA.

Ms. Bond has finally agreed to take your advice and incorporate the business. She will use ITA 85(1) to transfer the land and building to the new corporation. At the time of the transfer, the building had a UCC of $625,000. Other relevant values were as follows:

Asset Tax Cost (UCC) Appraised Value Elected Amount

Land $220,000 $510,000 $220,000

Building $625,000 $980,000 $730,000

Total $845,000 $1,490,000 $950,000

There is a $400,000 mortgage on the land and building that will be assumed by the new corporation. In addition, the new corporation will issue $500,000 in new debt to Ms. Bond. The remaining consideration will be in the form of common shares with a fair market value of $590,000.

Total FMV $1,490,000

What is she getting back Consideration:

* Elimination of mortgage: $400,000
* Loan receivable: $500,000
* Common shares: $590,000 \*Common shares must have value to make FMV

Exam question – calculate FMV of shares, or given FMV of shares, how mucg cash must the company give her

Required:

A. What are the tax consequences of making this transfer at the elected value of $950,000? Your answer should include amounts to be included in Ms. Bond’s income as a result of the transfer, as well as the corporation’s tax values for the assets.

Capital gain always selling price – cost

Recapture = amount over depreciated. There will never be a capital loss on a depreciable property (would be a terminal loss which is deductible).

Land: 220-220 = 0

Building: Elected – cost + Recapture on Depreciation = 635-730 = 105,000 100% taxable.

She screwed up; purpose of using section 85 is to not have tax consequence. Set elected amount = UCC.

B. Compute the adjusted cost base of each component of the consideration that Ms. Bond has received from the corporation.

What is the cost base of the shares – which will be used to calculate a capital gain:

Elected Transfer Price – Cash consideration

950,000-$900,000 = $50,000

C. Compute the Paid up capital of the corporation’s newly issued common shares.

NOT IN EXAM – NO PUC

D. What amounts would be included in Ms. Bond’s Net Income For Tax Purposes if, at a later point in time, she sells her common shares for $650,000?

Capital Gain: $650,000-$50,000 = $600,000

Taxable capital gain: $300,000

\*Can be eliminated if company maintains its QSBC status (need to know how to determine a company QSBC – 90% assets ration thing). If eligible, eliminate capital gain

E. What amounts would be included in Ms. Bond’s Net Income For Tax Purposes if, at a later point in time, the corporation redeems her common shares for $650,000?

When a company retracts shares, considered a dividend

QUESTION 4

Kruger Ltd. is a Canadian controlled private corporation that has been in operation for over ten years. Due to increased competition and an inability to adapt to the rapidly changing technological advancements in the industry,

it appears unlikely that Kruger Ltd. will be able to earn a satisfactory return on its invested capital in the future. As a consequence, the shareholders have agreed to a liquidation of the Company.

In contemplation of this liquidation, a Balance Sheet has been prepared based on the tax values of its assets and liabilities as at January 1, 2014, the end of the Company’s taxation year. This Balance Sheet, after all closing entries, is as follows:

Kruger Ltd.

Balance Sheet

As At January 1, 2014

Inventories (Net Realizable Value And Tax Cost) $ 35,000

Refundable Dividend Tax On Hand 27,000

Land - Adjusted Cost Base 623,000

Building - Undepreciated Capital Cost 586,000

Total Assets $1,271,000

Liabilities Nil

Paid Up Capital $ 447,000

Capital Dividend Account 215,000

Other Income Retained 609,000

Total Equities $1,271,000

Other Information:

1. The current fair market value of the Land is $1,243,000.

2. The Building had an capital cost of $775,000. Its fair market value on January 1, 2014 is $1,173,000.

3. The adjusted cost base of the common shares is equal to $447,000, their paid up capital.

4. All of the assets are disposed of on January 1, 2014 at their fair market values. The after tax proceeds are

distributed to shareholders on January 20, 2014.

Required:

USING THE APPROPRIATE FEDERAL CORPORATION INCOME TAX RATES THAT YOU HAVE

LEARNT IN THIS COURSE:

A. Calculate the amount that will be available for distribution to the shareholders after the liquidation.

B. Determine the components of the distribution to the shareholders, and the amount of taxable capital gains that

will accrue to the shareholders as a result of the winding-up of Kruger Ltd. Assume that appropriate elections

or designations will be made to minimize the taxes that will be paid by the shareholders.