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CONTEMPORARY IDEAS FOR BUSINESS MANAGEMENT FALL/WINTER 2022

The 7 Most Common HST Audit Issues

We have a specialized team at DJB that specializes in Commodity Tax. GST/HST can be complex and confusing if not dealt with by a knowledgeable professional. Oversights may trigger an audit and unnecessary penalties and interest assessed by the CRA.

We've compiled a list of the most common audit issues that we've seen to date. If you feel that you may need assistance with any of these HST areas, please contact us – we are happy to assist.

1. Claiming Input Tax Credits (ITCs) without proper documentation (see criteria table for specifics)
   - Ensure that the vendor's GST/HST number is always on the invoice, if not, ask for another to be prepared.
   - Do not used credit cards statements as your support. It is not considered acceptable proof for the CRA.
   - Also note, the CRA does not allow amendments where the sole purpose is to claim additional ITCs – any additions must be claimed on a future return.
2. Invoices made out to the wrong company
   - Holding company invoices cannot be claimed by the operating company
3. Intercompany transactions – Section 156 elections and form RC4616
   - Section 156 elections cannot be filed solely based on a controlling interest
   - Most situations required 90% ownership (parent/sub)
4. Claiming ITCs when a portion of the related revenue is exempt
   - Exempt income does not require GST/HST to be charged however no corresponding ITCs can be claimed on related expenses
5. Self-assessment errors on acquisitions of real estate (two scenarios to be mindful of)

   a. If the real estate acquisition is primarily used for taxable activities (e.g. commercial) – full ITCs can be claimed and the amount of HST owing would be nil. If a self-assessment is not completed, the CRA can reassess and add the HST due on the HST return. Thus, not having the ability to amend a return to add additional ITCs can result in significant cash flow issues and interest assessed by the CRA.

   b. If the real estate acquisition is used for exempt activities (e.g. long-term residential) than no ITCs can be claimed and HST would be owing. In this scenario, if a self-assessment is not completed, CRA can also reassess and include interest (same as scenario a).
6. Claiming 100% ITCs on meals/entertainment and passenger vehicles
   - Meals/entertainment claims are only eligible at 50% of the ITCs.
   - Passenger vehicle ITCs are capped at the GST/HST on $30,000 capital cost (typically $3,900).
7. Failure to charge/collect GST/HST on the sale of assets
   - Commodity tax registrants are required to charge GST/HST when selling an asset used for commercial purposes.

Article written by: **Cory Prince,** CPA, CA

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Residential Property Flipping – Important Taxation Considerations

Canadian residents who dispose of their family home and realize a gain may be eligible to claim an exemption, known as the Principal Residence Exemption (PRE) when computing the tax on that gain. The exemption can eliminate all or part of the taxable capital gain, depending on the circumstances. The PRE has been a part of the Canadian tax system for many years. To qualify for the PRE, an individual must own the property and that individual or their spouse or child must "ordinarily inhabit" it in each year for which the exemption is claimed. This does not require spending all of your time at the residence. Seasonal cottages, for example, can qualify for the PRE.

A married or common-law couple are only allowed to designate each year one property as a PRE. Therefore, if they own a family home and a cottage, one of those properties will be subject to tax when disposed. Fortunately, due to the capital gains rules, only 50% of the gain realized on a sale is subject to tax. The same rule applies to other properties, such as a rental property.

Over the past number of years, more and more individuals have purchased real estate with the intention of reselling the property in a short period of time to realize a profit. Profits from flipping properties are fully taxable as business income, meaning they are not eligible for the 50% capital gains inclusion rate or the PRE.

To avoid paying tax on the entire profit, taxpayers have been reporting their profit as a capital gain. In some cases they have moved into the house even while it is being renovated, claiming the PRE, thus avoiding taxes altogether. Now, it has always been a question of fact as to how the profit on the sale of a house should be taxed. Question of fact is often based on intent. Unfortunately, in many cases, it is difficult for the Canada Revenue Agency to determine intent. Was the intent at the time of purchase to flip the property or was the intent to hold the property for a number of years but circumstances changed, requiring a sale sooner than expected?

To make it more difficult for individual taxpayers to avoid paying taxes on their profits from property flipping, the government proposed in the latest budget the "Residential Property Flipping Rule". This new rule will apply to property sales on or after January 1, 2023. If the sale falls under these rules, then the full profit will be subject to income tax. The intent of the taxpayer will no longer be considered. Specifically, profits arising from dispositions of residential property (including a rental property) that was owned for less than 12 months will be deemed to be business income. The new rule will not apply if the sale took place due to certain life events as follows:

- A disposition due to, or in anticipation of, the death of the taxpayer or a related person.
- A household addition such as the birth of a child or care of an elderly parent.
- A disposition due to the breakdown of a marriage or common-law partnership, where the taxpayer has been living separate and apart from their spouse or common-law partner because of a breakdown in the relationship for a period of at least 90 days.
- A disposition due to a threat to the personal safety of the taxpayer or a related person, such as the threat of domestic violence.
- A disposition due to a taxpayer or a related person suffering from a serious disability or illness.
- A disposition for the taxpayer or their spouse or common-law partner to work at a new location or due to an involuntary termination of employment. In the case of work at a new location, the taxpayer's new home must be at least 40 kilometres closer to the new work location.
- A disposition due to insolvency or to avoid insolvency (i.e., due to an accumulation of debts).
- A disposition against someone's will, for example, due to, expropriation or the destruction or condemnation of the taxpayer's residence due to a natural or man-made disaster.

Profits realized on the sale of properties held for more than 12 months will continue to be taxed based on the facts of each situation. It is also important to point out that these proposals have not yet been enacted into law.

For help determining what your tax obligations might be if you are considering (or in the process of selling real property), please contact one of our tax specialists.

Article written by: **Don Knechtel,** CPA, CA

Saving for Your First Home

Saving for a first home can be a significant challenge for many, especially when the price of the average home in Canada is nearly $630,000. The minimum down payment to qualify for a mortgage is 5% of the purchase price if the purchase price is $500,000 or less and 10% for any amount over $500,000. That means if you purchased an average home in Canada, you would need a down-payment of at least $38,000, however if you were making a down-payment of less than 20% of the purchase price, you would have to pay an insurance payment of $23,680 to the Canadian Housing & Mortgage Corporation. This insurance protects the lending institution in the event that you default on your mortgage in the future.

There are several programs outlined below which are designed to assist first-time homebuyers with saving for their new homes. In addition to the savings programs listed below, there are many tax incentives available for first-time homebuyers. These tax incentives are beyond the scope of this article and should be discussed with your trusted Accountant for more information.

RRSP FIRST-TIME HOME BUYER PLAN (HBP)

- Maximum $35K tax-free withdrawal from RRSP ($70k/couple)
- Repayment over 15 years

1. The repayment period starts the second year after the year when you first withdrew funds from your RRSP(s) for the HBP. For example, if you withdrew funds in 2022, your first year of repayment will be 2024
2. Each year, the Canada Revenue Agency (CRA) will send you a Home Buyers' Plan (HBP) statement of account, with your notice of assessment or notice of reassessment

- The statement will include:
  - The amount you have repaid so far (including any additional payments and amounts you included on your income tax and benefit return because they were not repaid)
  - Your remaining HBP balance
  - The amount you have to contribute to your RRSP(s), PRPP or SPP and designate as a repayment for the following year
  - If you repay less than the required amount owing for the year, any remaining balance owing will be added to your income and taxed as RRSP income
  - Any amounts repaid in excess of the minimum, reduce future annual minimum repayments
  - Contributions to RRSP are tax-deductible and based on your annual maximum contribution room shown on your Notice of Assessment
  - Contributions made in the 89-day period prior to the RRSP home buyers withdrawal are subject to deduction limitations
  - Cannot be used in conjunction with the First Home Savings Account (FHSA)

TAX-FREE SAVINGS ACCOUNT (TFSA)

- Started in 2009 and is available for anyone 18 or older
  - The annual TFSA contribution limits for the years:
  - 2009 to 2012 was $5,000
  - 2013 and 2014 were $5,500
  - 2015 was $10,000
  - 2016 to 2018 was $5,500
  - 2019 to 2022 is $6,000
- The unused contribution room is carried forward and can be used in any future year
- Contributions are not tax-deductible
- No tax on the growth
- Withdrawals are tax-free
- No repayment required
- Any amount withdrawn is added back to your contribution room in the following year

THE FIRST-TIME HOME BUYER INCENTIVE

The First-Time Home Buyer Incentive is a shared-equity mortgage with the Government of Canada, which offers:

1. 5% or 10% for a first-time buyer's purchase of a newly constructed home
2. 5% for a first-time buyer's purchase of a resale (existing) home
3. 5% for a first-time buyer's purchase of a new or resale mobile/manufactured home

Saving For Your First Home - continued

- The shared equity component of the incentive means that the government shares in both the upside and downside of the property value, up to a maximum gain or loss equal to 8% per annum (not compounded) on the Incentive amount from the date of advance to the time of repayment
- The homebuyer will have to repay the Incentive based on the market value of the home at the time of repayment equal to the percentage (for example, 5% or 10%) of the original home value used to determine the Incentive, up to a maximum repayment amount equal to:
  - where the home's value has appreciated, the Incentive plus a maximum gain of 8% per annum (not compounded) on the Incentive amount from the date of advance to the time of repayment; or
  - where the home's value has depreciated, the Incentive minus a maximum loss of 8% per annum (not compounded) on the Incentive amount from the date of advance to the time of repayment
- The homebuyer must repay the Incentive after 25 years, or when the property is sold, whichever comes first. The homebuyer can also repay the Incentive in full any time before, without a pre-payment penalty.

TAX-FREE FIRST HOME SAVINGS ACCOUNT (FHSA) – COMING IN 2023

- Maximum annual tax-deductible contributions $8K
- Maximum lifetime contributions $40K
- Tax-Free withdrawal for qualified first-time home buyer, which is considered to be a person who has not owned a home in which they lived during the current calendar year or the previous four calendar years; an exception to this is made for anyone making a withdrawal within 30 days of moving into their first-time home
- Once the account is open it must be used to purchase a home within 15 years or before the end of the year that the individual turns age 71. If not used to purchase a qualifying first-time home during these periods, it can no longer be used for this purpose and must be either transferred tax-free to a Registered Retirement Savings Plan or Registered Retirement Income Fund or withdrawn and fully taxed as income
- After an FHSA is open any unused contribution limit can be carried forward and used in any subsequent year
- Contributions can be deducted against income in the year they are made or carried forward and deducted in any future year
- Cannot be used in conjunction with the Home-Buyers Plan

Information in this article has been referenced from the Government of Canada website.

Article written by: **Brad Grioux,** CFP®, CLU, CHS

DJB IS PROUD TO HAVE BEEN RECOGNIZED AS A MCGILLIVRAY TRUSTED PROFESSIONAL IN HALTON

From his experience with 100's of real estate investments over the past 20-years, award-winning HGTV celebrity, executive producer, and real estate/renovation expert Scott McGillivray knows first hand about the value that a knowledgeable, connected, and dedicated Real Estate Professional brings to the buying and selling process.

"Partner with the Professionals I trust!"

recommends Scott McGillivray, real estate expert and star of TV shows Income Property, Buyers Bootcamp and Vacation House Rules.

"It's important to partner with professionals that have the market knowledge and expertise guaranteed to make your real estate journey a smooth and successful one."

Pictured above left to right: Ryan Bouskill, Partner at DJB and Scott McGillivray, HGTV" Celebrtiy.

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Payroll Considerations for Foreign Employees Working in Canada

One of the biggest challenges foreign employers are facing is how to ensure payroll compliance in Canada for their foreign employees who are sent to work in Canada. Foreign employers may presume that if they are compliant in their home country, there is no additional payroll compliance requirement in Canada. Employers may also assume that employees who travel to Canada for business meetings, conferences or training, or who work fewer than a certain number of days in Canada, are not subject to tax in Canada, and thus there is no payroll obligation.

However, foreign employers should understand that sending even one employee to work in Canada triggers a payroll obligation. Compliance starts from the first day of the foreign employee's physical presence in Canada. As per the Canada Revenue Agency (CRA), it is the employer's responsibility to set the foreign employee up on a Canadian payroll, deduct Canadian income taxes and Canadian social security taxes (Canadian Pension Plan and Employment Insurance) from the employee's Canadian-source wages, and remit to the CRA on time. The employer must also remit, out of pocket, a matching contribution on the social security taxes, and issue a Canadian wage slip (Form T4) for the foreign employee at year-end. To facilitate these obligations, the foreign employer and employee are required to obtain a Canadian Business Number (BN), and Canadian Social Insurance Number (SIN), respectively.

Currently, CRA is increasing the frequency of payroll audits, which can result in increased payroll noncompliance risks for more and more foreign employers. It is important to note that the CRA can pursue the foreign employer for the payroll taxes not remitted, plus interest and penalties, in the event of noncompliance. This can be a significant cost if the foreign employer has sent multiple employees over a number of years to work in Canada and has historically been unaware of payroll obligations.

With COVID-19, employees can now work virtually from wherever they wish and employers are not restricted to their home country when searching for talent. However, employees on virtual assignments or hired to work from their home in other countries may also create Canadian payroll issues.

There may be an exemption from some of the above-mentioned Canadian payroll obligations, if the foreign employee is exempt from Canadian taxation under a tax treaty between Canada and the foreign employee's country of residence. The foreign employer needs to apply for a payroll waiver from CRA to rely on these exemptions. These waivers must be applied for in advance of the foreign employee arriving in Canada to be effective. There are different waiver applications based on the length of time the employee is physically working in Canada.

There are also exemptions from having to contribute to the CPP and EI, including in respect of the employer's share, depending on agreement between Canada and the foreign home country and certain criteria of employee's home country.

In most cases, employers are already investing significant time and internal resources to send an employee on an international assignment. Employers will want to keep abreast of Canadian payroll tax obligations to minimize unnecessary compliance costs.

Article written by RSM Canada and referenced with permission as a member of RSM Canada Alliance.

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Choosing the Right Software

One of the most important things in any business is making sure you have enough money to pay your bills; this is why it is imperative to choose the correct software for your bookkeeping. Take your time choosing the right software because it can be costly having to repeat this process. You need a system that will track all your day-to-day transactions, such as invoicing, recording payments, tracking expenses, HST, payroll, and reconciling transactions. The more accurate the information is, the better the reports will be and the more insight you will have into your business performance.

Choosing the best accounting software for your individual business is challenging. Each program includes a different set of features. Depending on those features and the number of users, will determine the price point. Some of the questions you have to ask is:

- Would you like your program to be cloud based so you can access it from anywhere on multiple devices?
- What kind of features are you looking for?
- What kind of reporting are you looking for?
- Do you need to track inventory, payroll, HST?
- Do you invoice and pay bills out of the system?
- How many users will be using the system?
- What is the price point you would like to stay within?

Creating a list of needs and wants will help you determine which software is best for you. Reach out to other business owners and ask them what they use and what they like and dislike about the system. Check to see if the system has a free version; see if it can do all the things you want it to do. Talk to your accountant or bookkeeper, they will have suggestions as well. Don't be afraid to ask the questions.

Article written by: **Diane Dos Santos,** CPB

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