CHARTERED PROFESSIONAL ACCOUNTANTS

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FORESIGHT

CONTEMPORARY IDEAS FOR BUSINESS MANAGEMENT

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How Does GST/HST Apply When Purchasing a Business?

When you are purchasing a business in a share deal, the GST/HST implications can be fairly straight forward, in that the purchase of shares of a corporation are generally not subject to GST/HST. The complexities arise when you structure your acquisition as an asset purchase.

For GST/HST purposes, under section 167 of the Excise Tax Act, if you buy a business or part of a business, and acquire the use of or possession of all or substantially all of the property that can reasonably be regarded as necessary to carry on the business, you and the vendor may be able to jointly elect to have no GST/HST payable on the sale by completing Form GST44, Election Concerning the Acquisition of a Business or Part of a Business. For the election to apply to the sale, you have to be able to continue to operate the business with the property acquired under the sale agreement.

In GST Memorandum 14-4 Sale of a Business or Part of a Business, it states:

In general, a "part of a business" is an activity that may be a functionally and physically discrete operating unit, or it may be an activity that supports or is related to the broader business, but is organized as a separate activity that is capable of operating on its own.

Where issues have arisen is when the purchaser is acquiring all of the assets but not purchasing the real estate or entering into a lease for the existing premises. It is a question of fact if the CRA will constitute this as obtaining

'all or substantially all' of the property necessary to carry on the business. The CRA's memorandum goes on to state:

The value of any property that is not acquired under the agreement for the supply, but that the recipient requires to carry on the business must generally be not more than 10% of the fair market value of all the property necessary to carry on the business. The recipient must be capable of carrying on the same kind of business that was established or carried on, or acquired, by the supplier, with the property that the recipient has acquired under the agreement.

You cannot use this election if the vendor is a registrant and the buyer is not a registrant for GST and HST purposes. If the transfer is a non-registrant to a non-registrant, the election form need not be filed with the CRA, but must still be completed and kept on file by the vendor and the purchaser. The election form must be filed with the CRA by the purchaser, no later than the due date of the purchaser's GST/HST return for the reporting period in which you would have otherwise had to pay GST/HST on the purchase.

Even when you use the election, GST/HST will still apply to:

- a taxable supply of a service made by the seller;
- a taxable supply of property made by way of lease, licence, or similar arrangement; and
- where the buyer is not a registrant, a taxable sale of real property.

Often in acquisitions, the GST/HST considerations are not front and centre. The CRA is starting to perform audits on the validity of filing for the election, so it is vital that GST/HST is considered along with all other business and income tax considerations. We can help to ensure you structure your deal to help maximize your company's cash flow and minimize your GST/HST burden.

Changes to Compilation Standards

The Auditing and Assurance Standards Board (AASB) has released a new compilation standard that is effective for periods ending on or after December 14, 2021, with early application permitted. These are what have been informally referred to as "Notice to Reader" or "NTR" statements. The new section 4200, Compilation Engagements will replace section 9200, which the AASB recognized as outdated.

The AASB advised that the new standards were designed to respond to stakeholder input and public interest, and listed the following as some of the key features:

- A scope that sets out which services are compilation engagements. Today, practitioners find it difficult to distinguish a bookkeeping service from a compilation engagement. The new standard clarifies that a bookkeeping service may result in system-generated financial information. Such information is excluded from the scope of the standard if no communication is included or attached to it.
- Specific engagement acceptance considerations that apply when the compiled financial information is intended to be used by a third party. Currently, practitioners are unclear about whether it is appropriate to accept or continue a compilation engagement when there is a third-party user.
- Specific required work effort and documentation. The lack of explicit guidance in this area could be a reason for the existing variability in practice.
- A requirement that compiled financial information includes a note describing the basis of accounting that was applied. Today, users generally lack an understanding of how the compiled financial information was prepared.
- A new compilation engagement report that is more informative and insightful than the current Notice to Reader. Users are unclear as to the extent of work performed by the practitioner and have asked for greater transparency about those responsibilities.

How does this affect your business?

As mentioned in our article entitled [Financial Statement Preparation – What-Are-My-Options?] Notice to Reader (NTR) financial statements are generally used when there is no intention for the financial statements to be used by external parties. These new changes will allow for a compilation engagement to be issued with the intention of being used by an external party such as a bank.

In comparison to what is mentioned in our article of minimal work being done by the external accountant, there is no specific work effort and documentation required. This means that there will be additional requests for information, as well as additional discussions on your business and operations, accounting systems, and accounting records. There will also be a discussion about significant judgments that you have been assisted within the preparation of the financial statements.

A basis of accounting must also be chosen and this will be described in your new compilation engagement report. The report page of your financial statements will also look different, however, as noted, this is designed to be more informative and insightful than the current Notice to Reader. There will also be new engagement and representation letters to be signed.

Further information on this can be obtained from CPA Canada.

How does this affect external parties?

As noted above a compilation engagement can now be used with the intention of being provided to an external party. Consistent with the previous standards, however, the reporting practitioner does not provide any assurance on the financial statements and information prepared by management.

The disclosure of a basis of accounting will also improve understandability for external parties. Examples of what this could be are:

- a cash basis of accounting
- a cash basis of accounting with selected accruals and accounting estimates
- a basis of accounting prescribed by a contract or other form of agreement established by a creditor or a regulator, which could be one area of discussion that external parties have with management

It is important for external parties' to understand how financial information is compiled for their review of the financial statements to determine whether it is appropriate for their use.

More information on this can be found here.

Please reach out to your DJB representative to discuss whether a change is right for you. For more information on using a spousal RRSP, contact me.

Article written by: **Matt Miedus,** CPA, CA

Estate Freeze Advantages and Considerations

The Canadian Income Tax law states that taxpayers are deemed to dispose of all of their property at fair market value immediately prior to death. This can result in a significant income tax liability in the year of death. If the estate includes shares of a small business, the lack of funds to pay this liability may make it difficult to continue the business and keep it in the family. This deemed disposition can be deferred when assets are left to a spouse or a spousal trust, but this is only a temporary solution to the problem and does not solve the problem when the shares are transferred to the children.

The purpose of an estate freeze is to transfer the future increase in the value of assets to other individuals. In most cases, this would be other family members but could also include a key employee of the family business. The transferor retains the current value of his/her shares and defers the income taxes on the capital gain to the time of their actual or deemed disposition.

By entering into a freeze transaction, the transferor can determine the taxes that will be due on his/her death. Knowing what the future liability will be makes it easier to plan. For example, a life insurance policy may be considered as an option to fund the liability.

To accomplish the estate freeze an owner of a small business corporation exchanges his/her common shares for fixed value preference shares with dividend rights. New common shares are then issued to the new shareholders. They will enjoy the benefits of the future growth of the business. This will result in a lower capital gain on the deemed disposition when the transferor dies. One of the reasons for a freeze is to transfer the business to the next generation. However, consideration must be given to the share structure to allow the transferor to retain control of the business and, if he/she wants, provide a source of income by paying dividends on his/her freeze shares.

Careful consideration must be given to the value of the shares of the corporation that is being frozen. In many cases, it is recommended that a Chartered Business Valuator be engaged to determine the value of the shares. Unwanted tax consequences could result if the Canada Revenue Agency successfully challenges that the value of the fixed value preference shares does not line up with the value of the corporation at the time of the freeze.

What should be done if you as the business owner want to enter into an estate freeze but you are not sure whom you want the future growth to go to or your children are too young to have share ownership? In this situation, it would be a great idea to create a family trust to hold the new common shares. A family trust allows you to put off this decision for up to twenty-one years. Beneficiaries of the trust normally include all family members. At some date in the future, the trustees of the trust give the shares to the chosen beneficiaries. This is a non-taxable event. To provide for maximum flexibility, the business owner would also be a beneficiary of the trust in the event he/she decides not to transfer future growth and effectively decides to cancel the freeze. In certain circumstances income splitting can be achieved by paying dividends to the trust and then allocating the funds to beneficiaries. It is recommended that you seek professional advice before undertaking such tax planning and to help with the creation of a family trust.

Often the freeze shares that the transferor receives are redeemed over a number of years as part of their retirement income. This spreads out the tax liability and reduces the liability to their estate.

Individuals who have a significant portfolio of investments may want to consider implementing an estate freeze. To do so they would incorporate a holding company in which to transfer the portfolio. At the end of the transactions, the individual will own fixed value preference shares of the holding company and possibly a note receivable from the holding company with a combined value equal to the value of the stock portfolio. Other family members or a family trust will hold the common shares. Careful planning is required, including proper tax filings in order to transfer the portfolio to the holding company on a tax-deferred basis. In addition, the transferor needs to be aware of and to plan around the corporate attribution rules of the Income Tax Act, which could have a negative effect on the planning for years into the future.

In summary, an estate freeze can be a very good tax-planning tool but there are a number of items that must be addressed and considered before undertaking such a plan. A bad plan could result in an unwanted tax bill. The plan should be tailored to fit your needs. I would be happy to discuss your needs and a plan that would be right for you.

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

New Trust Reporting Requirements

The use of a trust can be an effective tool in a variety of estate planning and asset protection arrangements.

Proposed legislation, that once enacted, will significantly expand the reporting requirements for certain trusts for taxation years ending on or after December 31, 2021.

Purpose of Proposed Legislation

The CRA is seeking expanded disclosure requirements to obtain transparency regarding beneficial ownership as well as to ensure that tax liabilities for the trusts and their respective beneficiaries are properly assessed.

Although the legislation was initially released on July 27, 2018, it still remains proposed. The Federal government, however, has confirmed in the 2019 budget that they intend to proceed with the announced measures.

Breakdown of Changes

T3 Filing Requirements

Currently, a personal trust is not required to file an annual return where certain exceptions are met. Under this proposed legislation, a significant number of personal trusts resident in Canada will no longer meet these exemption criteria and will now be required to file an annual return even where there is no income tax liability and the trust made no distributions or allocations during the year.

Exemptions

Certain types of trusts are expected to be exempt from these new reporting requirements, which include:

- A trust has been in existence for less than three months at the end of the year;
- A trust that holds less than $50,000 in assets throughout the taxation year (provided that their holdings are confined to cash, certain debt obligations, and listed securities);
- Regulated trusts such as lawyers' general trust accounts;
- Trusts that qualify as not-for-profit organizations or registered charities;
- Mutual fund trusts, segregated fund trusts and master trusts;
- Qualified disability trusts;
- Employee life and health trusts;
- Certain government funded trusts;
- Graduated rate estates;
- Registered savings plans (i.e. RRSP, RESP, TFSA etc.); and
- Cemetery care trusts or a trust governed by an eligible funeral arrangement.

Important Note: Trusts created to hold personal-use assets for estate planning or asset protection purposes that previously qualified for a filing exemption will now be subject to these new filing requirements.

Additional Information Requirements

Under the proposed regulations, certain types of trusts that are required to file a T3 return must disclose personal information for each trustee, beneficiary, settlor, and any person who has the ability (through the terms of the trust or a related agreement) to exert influence over trustee decisions regarding the appointment of income or capital of the trust. The information that must be disclosed includes the following:

- Name;
- Address;
- Date of birth;
- Jurisdiction of residence; and
- Taxpayer identification number (TIN) (i.e. social insurance number, business number, trust account number, or foreign TIN).

Important Note: A 'settlor' defined in this new disclosure extends beyond the person who established the trust. It will likely include non-arm's length persons who participated in an estate freeze in favour of a trust, sold property or loaned money or property to the trust, or paid expenses on behalf of the trust.

Non-Compliance Penalties

The proposed legislation also introduces an additional penalty that can be imposed. If a false statement, omission or failure to file a return was made by any person knowingly or under circumstances amounting to gross negligence, that person could face a penalty equal to the greater of $2,500 and 5% of the highest fair market value of the assets of the trust during the year.

These proposed penalties are in addition to the existing penalties in respect to T3 Returns. The failure to file penalty for a T3 Return is $25 per day, with a minimum of $100 and a maximum of $2,500.

Be Prepared

Trustees are encouraged to begin accumulating the necessary information well in advance of December 31, 2021, as gathering this information for the first time may be an arduous task in certain circumstances. If you need assistance or require more information on how the new trust reporting rules may affect you, please contact a DJB tax professional.

ACTION ITEM:

The legislation to support this proposed measure is pending. The CRA will administer the new reporting and filing requirements once there is supporting legislation that receives Royal Assent. The CRA will continue to administer the existing rules for trusts, under enacted legislation. The proposed beneficial ownership reporting requirements will not be part of the published 2021 T3 Income Tax Return.

It is not recommended that you delay the filing of your 2021 T3 Tax Return.

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New Ontario Business Registry

On October 19, 2021, the Government of Ontario launched the Ontario Business Registry. This new online platform offers simpler, faster, and more convenient access for organizations that are registered, incorporated, or licensed to carry on business in Ontario. This new online registry is available 24 hours a day, 365 days a year, and makes it easy to interact with the government.

The new Ontario Business Registry allows businesses and not-for-profit corporations to complete over 90 transactions online, including registering, incorporating, dissolving an existing corporation, and updating their information.

Ontario corporations are required to file an Annual Return, which is due within six months after their fiscal year-end. Prior to May 15, 2021, the Annual Return was filed with Canada Revenue Agency (CRA) and was included with the filing of the corporation's T2 Corporation Income Tax Return.

As of May 15, 2021, CRA discontinued accepting these returns on behalf of Ontario.

The Ontario Annual Return must now be filed in the new Ontario Business Registry.

Annual Returns that were due from May 15, 2021, to October 18, 2021, are exempt from filing. For example, an Ontario corporation with a December 31, 2020 year-end would have a 2020 Annual Return deadline of June 30, 2021, which falls within the exempt period, and therefore is exempt from filing for their 2020 year-end. An Ontario corporation with a June 30, 2021 year-end would have an Annual Return deadline of December 31, 2021, and therefore would not be exempt from filing.

To access the Ontario Business Registry, you must obtain a company key. File your Annual Return as soon as possible if it is overdue or nearing the filing deadline. Please note: if you require assistance, your company key can be shared with your accountant or lawyer.

For more details on how to set up a company key for your corporation, please visit the Ontario Government website.

Article written by: **Diana Zampini,** CPA, CMA