WINTER 2014

THE Quarterly Dividend

Vol. 23 No. 1

Your guide to income tax & financial planning

FAST TRACK

Corruption of Foreign Public Officials

What: as Canada plays a more important role in international trade, individual companies seeking to do business in foreign countries must set themselves apart from the competition in order to win contracts. From time to time, this may involve offering certain benefits to foreign public officials to entice them to "look the other way" in

In this Issue:

Social Benefit Repayments

The Canada Revenue Agency calls them "Social Benefit Repayments" but the rest of us call them "clawback taxes". They are the taking back of certain benefits by the government of payments that had originally been advertised as "universal". This means that even though you may have thought your Old Age Security Pension or Employment Insurance Benefits were certain rights you were entitled to simply by living in Canada and contributing the amounts they said they wanted, perhaps over many years, you would be wrong. They are recovered through the income tax system and here is how they work:

(a) Old Age Security Pensions: Seniors with high incomes must pay back all or some of the pensions they received as their incomes increase above $70954. The amount to be repaid is clawed back at the rate of $15 for every $100 the taxpayer reports that exceeds the threshold. Once net income exceeds $114836 the entire pension he received will have been taken away from him;

(b) Employment Insurance Benefits: When someone files for Employment Insurance he will be assigned benefits as follows: (i) "regular benefits" are paid to individuals who lose their job through no fault of their own, were not dismissed for misconduct, or cases in which the individual left his current employment voluntarily after considering "all reasonable alternatives" which might have allowed him to keep his job; (ii) "maternity benefits" apply to mothers of new-born children; "paternity benefits" allow a parent time from work to bond with their infant child. Both are termed "special benefits"; (iii) "sickness benefits" are paid to individuals who are unable to work due to illness, injury or quarantine; and (iv) "compassionate care" benefits are provided to individuals who take time off from work to take care of a family member who is gravely ill and is at significant risk of dying.

Categories (ii) to (iv) are not subject to repayment. For (i) a maximum of 30% of regular benefits received will have to be repaid when the recipient's net income for the year exceeds $59250. Thus if the taxpayer received $10185 in benefits he will have to commence repaying 30% of his benefits to a maximum of $3055.50 once his income exceeds $49065 ($59250 -10185). The full amount of the clawback will be reached when his net income reaches the threshold.

It therefore becomes important for seniors and employment insurance recipients to try to plan their incomes, as much as possible, to fall below the respective threshold amounts so as not to be hit with the clawback tax. In the case of seniors, pension income splitting between spouses will assist in this endeavour. In the case of employment insurance recipients, contributions to Registered Retirement Savings Plans will lessen the net income figure and possibly reduce or eliminate the clawback.

First-Time Donor's Super Credit

One of the "highlights" of the 2013 Federal Budget involved changes to the way charitable donations will be treated for the next five taxation years. Here are the details:

(a) who: individual taxpayers and their spouses or common-law partners who have not claimed charitable donation non-refundable tax credits within the past five years;

(b) when: the above taxpayers make monetary charitable donations up to $1000;

(c) what: taxpayers are entitled to a federal non-

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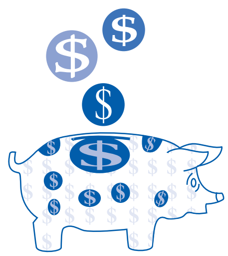


connection with the performance of their duties or inducements to exert their influence on acts or decisions of the foreign state for which they work. These may take the form of direct or indirect loans, rewards or other advantages or benefits depending upon the circumstances.

In response to international recognition of this "situation", the Organisation for Economic Co-operation and Development (OECD) encouraged their members to pass legislation to outlaw such practices and encourage a "level playing field" in all international business.

Canada complied with the "Corruption of Foreign Public Officials Act" in 1999. It provided for monetary fines and possible imprisonment for those found guilty of indictable offenses.

Who: under the Act, perpetrators are not limited to those who pay and receive bribes. It also includes situations where they conspire together to influence a third party who is not part of the scheme. In addition, cash and other benefits do not actually have to have been provided. It is sufficient that the "recipient" only believes that such advantages will be forthcoming.

How: it is important to understand the difference between

refundable tax credit of 15% on the first $200 of the donation and 29% on the rest. This totals $262 for a $1000 donation. The First-Time Donor's Super Credit (FDSC) would allow an additional tax credit of 25% of the donated amount provided it was not a "donation in kind". This would translate into an additional $250;

(d) where: the FDSG can be split between spouses, at their discretion, however this credit can only be claimed once, so it is advisable for couples to pool their charitable receipts between 2013 and 2017 and claim the credit when they have reached the $1000 threshold;

(e) why: to encourage charitable donations at a time when contributions have been "down" and charities are struggling to assist their "clients"

Cash Flow Statement

TONY'S COMPANY

		Dec 31/13 $	Dec 31/12 $	Change	$
	ASSETS				
(c)	Accts Rec	22,370	16,696	increase	5,674 (c)
	Inventory	2,874	2,874	no change	
	Prop, Plant, Equip.	60,000	60,000	no change	
(a)	Acc Amort	(13,840)	(5,536)	increase	8,304 (a)
		71,404	74,034		
	LIABILITIES				
(d)	Bank overdraft	36,068	31,808	increase	4,260 (d)
(c)	Accts Payable	5,290	22,146	decrease	16,856 (c)
(b)	Inc Tax Payable	1,300		increase	1,300 (b)
(c)	Loan Payable		13,550	decrease	13,550 (c)
(b)	Due to Shareholder	14,578	1,955	increase	12,623
		57,236	69,459		
	SHAREHOLDER'S EQUITY				
	Share Capital	100	100	no change	
(a)	Retained Earnings	14,068	4,475	increase	9,593 (a)
		14,168	4,575		
		71,404	74,034		

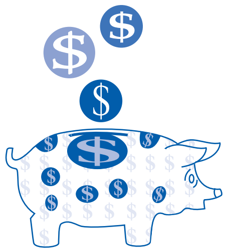
Tony had been eagerly anticipating receiving his 2013 financial statements from his accountant. He believed he must have had a really successful year given all that he was able to accomplish.For the first time in awhile, he was able to pay all his bills and even take home a weekly paycheque.

Like many small business owners, Tony's dealings with the bank are through a "secured line of credit" rather than having a bank loan that is separate from his operating bank account. So every year he determines to himself "how well he did" by seeing whether the company's bank overdraft rose or fell from its balance twelve months earlier.

But when presented with his year-end balance sheet, his mood turned to one of disappointment. After all, his retained earnings, a reflection of corporate net income, increased by $9593 and none of his suppliers were harrassing him for payment like they used to. But the books showed a larger bank overdraft compared with 2012, and this was after he had subsidized the company with $12500 of his own money in June.

Let's see if we can figure out "what happened" by comparing this year's balance sheet figures to those at this time last year. The resulting "cash flow statement" will analyze changes in accounts whose balances have changed, either up or down, from last year. And will furnish Tony with the information he needs to understand why a "successful" year often looks less so until the story behind the numbers has been told.

(a) The starting point of the cash flow statement is the net income of the company for the year adjusted for any expenses that have been deducted in arriving at net income that did not involve the outlay of cash. The most common expense in this category is amortization or depreciation of capital assets. Tony's Company shows a positive net income of $9593 even after amortizing its capital assets



a "bribe" and a "facilitation payment". Let's say you are stranded in a foreign country and somehow misplace your visa. You are entitled to a replacement but the official indicates that it will take four months to have your application processed. In order to speed the process along, you "offer" him $500 to have the matter sorted out quickly. This is not a "bribe". The same is true in situations where ships with perishable goods to offload are advised by the harbour master that the port is short-staffed and cannot accommodate them for three months. You provide the official $500 as an enticement to move your ship ahead of others.

The problem is in determining where you draw the line. How "high up" is the individual who is accepting the "gift" or "payment". To a high ranking official, the $500 may not mean that much but to someone earning much less it may be considered a bribe. It is a judgment call that can only be decided when the situation presents itself. Just remember, bribes are not income tax deductable, facilitation payments are "costs of doing business".

Real-life example:
in 2005 Mr. Karigar was working as a business agent for Cryptometrics Canada (CC) an Ottawa based subsidiary of an American firm. He learned

$8304 for a total of $17897.

(b) Now let's look at those transactions that increased the company's cash position. When a company delays paying its bills, it effectively results in a larger bank balance (or smaller bank overdraft) than what would otherwise have been the case if these bills had been paid prior to the balance sheet date. So when Tony's Company has a higher corporate tax liability at the end of this year than it did at the end of lastlast year, the company is said to have increased its cash flow by that amount. In this case the amount is $1300. In a similar vein, we know that Tony advanced the company $12500 in June. By the end of December, the year-to-year change was actually $12623. The total of these changes is $13923.

(c) Now let's look at those transactions that decreased the company's cash position. When a company pays its bills to suppliers or reduces loan balances from prior-year borrowing it clearly results in a smaller bank balance (or larger bank overdraft) at any point in time. What is not so easily understood, but results in the same outcome, is when year-to-year accounts receivable increase. Because the money has not yet been collected, the company's cash flow has effectively been reduced. This year Tony's Company reduced the amounts owing to suppliers by $16856, paid off another corporate loan of $13550 and accounts receivable rose by $5674.

The total of these changes is $36080.

(d) The final analysis considers the bank overdraft

balance on December 31, 2012	$(31,808)
Add: Results of company's operations (a)	17,897
Add: Items increasing company's cash position (b)	13,923
Less: Items decreasing company's cash position (c)	(36,080)
Bank overdraft on December 31, 2013	$(36,068)

This is $4260 higher than it had been twelve months earlier. However, overall Tony should be commended for achieving a "good year" and using the funds generated in a positive manner for his company. He has paid off his corporate loan and the balances owing regarding his suppliers and taxes are under control. Once he collects his accounts receivable he can reduce his bank overdraft and/or pay himself back for the loan he advanced to the company last June.

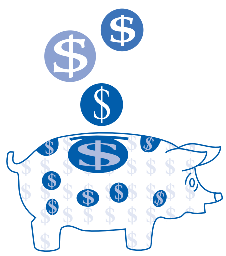
Take the CRA Sudoku Challenge

Sudoku grids appear in almost every newspaper throughout the country and have caught the immagination of people who attempt them each day. The Canada Revenue Agency (CRA) affects everyones' lives each day in ways they can never imagine. So take the CRA Sudoku Challenge below. If done correctly, you will find a hidden word in the bottom right corner of the puzzle. It will give you bragging rights amongst your friends, family and co-workers. The complete answer is available from the person whose name appears on page one.

Clues:

1. UCCB Universal Child Care Benefit
2. EI Employment Insurance
3. RRSP Registered Retirement Savings Plan
4. RPP Registered Pension Plan
5. OAS Old Age Security Pension
6. TFSA Tax-Free Savings Account
7. ABIL Allowable Business Investment Loss
8. CPP Canada Pension Plan
9. RESP Resgistered Education Savings Plan

			RESP					
	CPP	OAS		RRSP		RPP		
RPP			UCCB				TFSA	RRSP
EI	RPP				OAS			RESP
RESP		RRSP	TFSA	EI	UCCB	OAS		CPP
OAS			RPP				UCCB	EI
UCCB	OAS				TFSA			ABIL
		TFSA		UCCB		CPP	EI	
					RRSP			



that Air India was planning to acquire certain technology related to their passenger security system. Mr. Karigar and CC signed an agreement whereby Mr. Karigar and an associate would assist CC in bidding on the Air India contract in return for 30% of the expected revenue stream.

Mr. Karigar introduced CC executives to Air India officials. He provided the company with certain insider information on the bidding process as well as a list of Air India personnel who were to receive cash and CC shares.

The American parent company transferred $200000 to Mr. Karigar's bank account with a promise of an additional $250000 once the contract was secured. The bid was ultimately unsuccessful and there is no evidence of "what happened" to the original $200000.

Mr. Karigar was prosecuted under the Act and awaits sentencing.

Tax Free Savings Accounts Withdrawals

The financial community has been almost unanimous in their praise of the Tax-Free Savings Account since it was introduced in 2009. The rules about contribution limits and qualifying investments were straight-forward. The only complexity concerned the "penalty tax".

If you exceed the amount of contributions you are entitled to make to a Tax Free Savings Account, you will be subject to a "penalty tax" calculated at the rate of 1% per month on the highest amount of the excess during that particular month.

Here is an example of how this tax is determined:

Ernie Jones had never contributed to a TFSA before and became intrigued with the idea of investing a sum of money and having the interest earned on the amount received tax free.

Since he had never contribtuted to a TFSA before, he could catch-up on his contributions going back to Day One. The annual contribution limit was $5000 for the years 2009 to 2012 and $5500 for 2013 (and 2014). He determined his limit was $25500. He read the literature provided by the financial institution and contributed and withdrew money in his account on the fifteen of each month.

2013	(a) Contributions	(b) Withdrawals	(c) Cumulative Contribution	(d) Amount subject to penalty tax	(e) Max contib room Dec 31 prior year	(f) Over-contrib	(g) Penalty tax
April	150	50	150	150	25,500	NIL	
May	250	40	400	400	25,500	NIL	
June	600	10	1,000	1,000	25,500	NIL	
July	50,000		51,000	51,000	25,500	25,500	255
August		25,000		51,000	25,500	25,500	255
Sept		6,000		26,000	25,500	500	5
October				20,000	25,500	NIL	

Rules: (1) contributions are tracked separately from the running balance in the account and cannot exceed the cumulative allowable amount (column e);

Ernie had never contributed to a TFSA before so his cumulative allowable limit was $25500. Had he made contributions in previous years, his cumulative allowable limit would have been that much less.

(2) cumulative contributions during the year (column c) are compared to the maximum contribution room allowed that year (column e) and any over-contribution is recorded in (column f);

There was no "over-contribution" until Ernie made a $50000 contribution on July 15, 2013

(3) positive balances in column (f) are taxed at the rate of 1% per month (column g).

Withdrawals will reduce the monthly balance in the account, but since the penalty tax is levied on the highest balance of the month, they will not eliminate the penalty until the following month. Ernie's September withdrawal brought him below the $25500 limit but did not prevent him from having to pay the tax for that month.

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