Crowe Soberman | Canada

The Checkup

Tax planning, insights and advice for health professionals.

2022 Edition

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Predictions for the upcoming year

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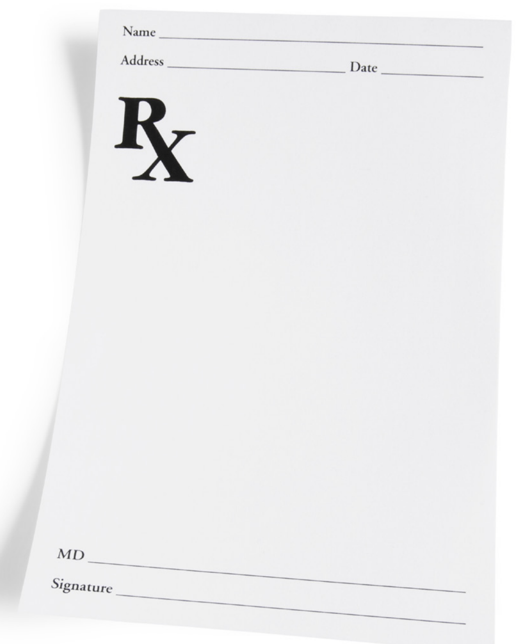

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A Message from the Editor

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I don't know when this pandemic will end. I don't know if there will be a variant after Omicron and whether it will be more contagious or more severe. I don't know if the Leafs will win the 2022 Stanley Cup. I don't know whether the federal government will increase the capital gains rate in the future. I don't know whether the Canada Revenue Agency will object to a taxpayer claiming home office and automobile expenses.

I just don't know.

In fact, even with the answers to almost anything factual at our fingertips, there is still much we all don't know. Perhaps with our increased access to knowledge, we just have more questions. There is certainly more curiosity. But increased access doesn't guarantee increased accuracy. We are seeing more and more BS out there, little desire from non-journalists (and even some journalists) to fact check, no desire to truly understand, and certainly no desire to admit that they just don't know.

I would be remised and a hypocrite if I didn't acknowledge that I have been guilty of this too. However, I am I much more conscious and conscientious, becoming increasingly comfortable with admitting that I don't know. While this admission is presumptively a sign a weakness, I would argue that it is actually a sign of strength. Admitting that you don't know forces you to take stock of your current limits and can be a spark to drive intellectual curiosity. It also, of course, can prevent false information from being disseminated further.

For 2022, let's better ourselves and not be afraid to say those words: I don't know.

There are quite a few things that I do know though, including the fact that this edition of *The Checkup* is jam packed with interesting and informative articles addressing tax and financial issues affecting health professionals. Clara Yang and Guo Chen discuss a way to income split with spouses and minor children by using a prescribed rate loan. If you are a first-time homebuyer looking for tax incentives, then Dennis Reynolds and Hasan Riaz have written an article for you. Michael Amatangelo lays out the tax implications from borrowing money from your corporation and how to repay it tax efficiently. Yvonne Lam examines whether health professionals can deduct automobile expenses from their income. And, of course, we lay out the upcoming 2022 tax deadlines for you.

Enjoy!

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Prescribed Rate Loans – Are They Right for You?

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The use of a prescribed rate loan between spouses, or between a parent and minor child (including a grandparent and minor grandchild), may provide tax savings on investment earnings.

What is a Prescribed Rate Loan?

A prescribed rate loan is a loan which carries interest at the prescribed rate. The prescribed rate is set quarterly by the Canada Revenue Agency (the "CRA") and is based on the three-month average government treasury bill interest rate. With interest rates recently at or near historical lows, the prescribed rate has followed and currently sits at one per cent until at least March 31, 2022.

Interest on a prescribed rate loan must be paid within 30 days after the year-end in which the loan was made. As individuals follow a calendar year-end, this means the interest must be paid by January 30 of the following year. It is important to keep documentation of the interest payments in the event the CRA were ever to request proof of payment.

Benefits of a Prescribed Rate Loan

The investment income earned on funds that originated from a gift or a loan that carries no or a low interest rate (i.e., below the prescribed rate) between spouses and between parents and minor children can result in the application of the attribution rules in the *Income Tax Act* (the "Act"). In these situations, the investment income earned will be attributed back to the spouse or parent who provided the loan and taxed in their hands, rather than in the tax return of the spouse or minor who is presumably in a lower tax bracket. The purpose of the attribution rules is to prevent the transfer of income to related parties subject to a lower tax rate with the objective of minimizing or reducing a family's overall tax burden.

However, charging interest on a loan at a rate no less than the prescribed rate avoids the attribution rules such that investment income earned by the spouse or minor remains taxable to the individual that received the loan. If used correctly, it will permit the investment income earned to be included in the spouse's or minor's income and subject to a lower tax rate.

Consider the following example:

Mr. and Mrs. A are both residents in Ontario. Mr. A's marginal tax rate on investment income is 53.53 per cent (the highest marginal tax rate), while Mrs. A's effective tax rate is 20.05 per cent. Mr. A will make a loan of $800,000 to Mrs. A so she can invest the funds which will generate interest income at an annual rate of return of five per cent. Mr. A is deciding between an interest-free loan or a prescribed rate loan at one per cent

The following tables summarize the couple's tax liability under each scenario.

Table 1: Interest-free Loan

	Mr. A	Mrs. A
Portfolio Interest Income ***Income is attributed back to Mr. A**	$40,000	
Loan Interest Income		
Loan Interest Expense		
Taxable Income	$40,000	$0
Tax	$21,412	$0
Total Tax = ($21,412+ $0) = $21,412		

Table 2: Prescribed Rate Loan (1%)

	Mr. A	Mrs. A
Portfolio Interest Income		$40,000
Loan Interest Income	$8,000	
Loan Interest Expense		$8,000
Taxable Income	$8,000	$32,000
Tax	$4,282	$6,416
Total Tax = ($4,282 + $6,416) = $10,698		

The couple will benefit from tax savings of approximately $10,714 ($21,412 - $10,698) through the use of a prescribed rate loan which will allow the investment income earned to be taxed in the hands of Mrs. A rather than Mr. A.

Final Thoughts

To the extent that an investment portfolio can generate more than a five per cent annual return, or multiple prescribe rate loans can be extended to a spouse, minor children and/or grandchildren, the combined family tax savings can be much higher than illustrated in the example. Transactions between related parties can result in unexpected and undesired tax consequences though, especially if transactions are not properly documented or interest is not paid within 30 days after the end of the calendar year. If you would like to learn more about prescribed rate loans and explore whether they are right for you, we encourage you to contact a member of Crowe Soberman's Tax Group.

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Incentives for First-Time Homebuyers

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The journey towards owning a first home can be a pleasant and joyous one. A goal that many Canadians want to achieve during their lifetime. However, as the current real estate market continues to experience an increase in home prices and demand outpaces supply, the realization of home ownership is becoming ever so more difficult for many Canadians. Luckily, if you're a first-time homebuyer, there are several government programs designed to support individuals entering the housing market.

Home Buyer's Plan

The most frequently inquired about program available to first-time homebuyers is the Home Buyer's Plan ("HBP"), which allows a first-time homebuyer to withdraw up to $35,000 from their Registered Retirement Savings Plan ("RRSP") to use towards a down payment on their first home. This program enables individuals to withdraw from their RRSP on a tax-free basis provided that the individual pays back the amount to the RRSP within 15 years on a straight-line basis.

Under the HBP, the homebuyer must begin to repay the withdrawal back in the second year after the year in which the initial amount was withdrawn. For example, if the homebuyer withdraws the funds in 2022, the first year of repayment would be 2024. It should be noted that the homebuyer is permitted to begin the repayment process prior to this date and is entitled to repay more than the minimum annual repayment amount should they choose. If the homebuyer repays less than the minimum annual amount, the difference is included in their income and is subject to tax.

The Canada Revenue Agency ("CRA") provides participants in the HBP with an annual statement within their notice of assessment or reassessment. This statement indicates the amount repaid through the HBP so far, the remaining HBP balance owing and, the required HBP repayment for the following year. Although repayments to the HBP are considered RRSP contributions by the CRA, repayments to the HBP do not affect the homebuyer's RRSP deduction limit.

Home Buyer's Tax Credit

The Home Buyer's Tax Credit is an incentive program that enables eligible homebuyers to claim a $5,000 non-refundable tax credit in the year the homebuyer purchases a home. To qualify, the homebuyer must:

- Purchase a qualifying home in their own name (or a spouse or common-law partner);
- Not have purchased a property in which they resided in the last four years;

- Not have a spouse or common-law partner who has purchased a property in which neither have resided in the last four years; and
- Use the property as their principal residence.

First-time Home Buyer Incentive

The First-time Home Buyer Incentive allows qualifying buyers to receive an interest-free loan of either five per cent or 10 per cent of the purchase price to be applied towards a down payment. The First-time Home Buyer Incentive is not like a traditional loan; rather, no later than 25 years of ownership or when the property is sold, the buyer will be required to pay back either five per cent or 10 per cent of the fair market value of the property instead of the initial loan amount.

Tax-Free Home Savings Account

During their re-election campaign, the Liberal government proposed a new tax-free home savings account where Canadians under the age of 40 could invest up to $40,000 and withdraw it tax-free if the amount is used towards a down payment on a home. While this initiative offers the opportunity to earn investment income tax-free similar to the Tax-Free Savings Account and provides a larger withdrawal than the HBP, no legislation has been proposed to introduce this program, so it is not an available option for first-time homebuyers at this time.

Given that the Canadian real estate market is showing no signs of slowing down, first-time homebuyers should consider the many incentives available to them as they pursue home ownership. If utilized effectively, these programs can perhaps make the goal of acquiring a first home more attainable.

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Borrowing Money from Your Corporation? Consider the Tax Consequences

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There is a misconception that when a shareholder borrows money from their corporation, the loan can remain outstanding indefinitely without any income tax consequences. This is generally not the case, unfortunately; however, there are various tax-efficient ways to repay or offset the loan.

What happens when I withdraw money from my corporation?

From a tax perspective, if a shareholder withdraws money from a corporation for personal use, the corporation is considered to have loaned those funds to the shareholder. Where there are bona fide terms of repayment, individuals who are employees of the corporation may be able to receive these loans without any adverse tax implications so long as the funds are used to either:

a) Purchase a property to live in;
b) Acquire shares of the corporation from treasury; or
c) Purchase a vehicle for business use.

However, the position held by Canadian jurisprudence and the Canada Revenue Agency ("CRA") is that where the individual is both an employee and a shareholder of the corporation, the assumption is that the loan was received by virtue of the individual's shareholdings and the exceptions above do not apply.

Shareholder loans that are not repaid within one year after the end of the corporation's taxation year must be included in the individual's income and are subject to tax. For example, if a corporation has a December 31, 2021 year-end, any shareholder loan must be repaid by December 31, 2022, regardless of when the funds were withdrawn during 2021. The repayment can also not be withdrawn from the corporation immediately after, as it would likely be considered a series of loans and repayments and not a true repayment of the original loan. It should be noted that if an individual must take the amount of the unpaid loan into their income, any repayments made at a subsequent date will generate a personal tax deduction at that time.

In addition, the shareholder loan must carry a reasonable interest rate. Zero-rate interest loans or loans which carry interest at a rate below the CRA's prescribed interest rate (currently one per cent) will result in a taxable benefit being included in the individual's income for the period the loan is outstanding.

I've borrowed from my corporation and the one-year repayment date is approaching. What can I do?

There are a few ways a shareholder can avoid the full-income inclusion of an outstanding loan. The simplest manner would be to repay the loan before the end of the one-year. Often though, the individual has used these funds and they are no longer available for the repayment.

The shareholder loan can be offset by business expenses paid for personally by the individual. For example, if the individual purchased an asset that is used by the business of the corporation, maintained a home office, or had an automobile that they used for business purposes, any related expenses that have been paid for personally can be used to offset all or a portion of the outstanding shareholder loan.

Another option to avoid the adverse tax consequences of a shareholder loan may be to declare a salary or bonus to the individual sufficient to offset the outstanding loan. While the salary or bonus would be taxable to the individual, the corporation would be entitled to a corporate tax deduction for the amount. For the salary or bonus to have been considered paid by the end of the year for a corporation with a December 31 year-end, the related payroll source deductions must be remitted to the CRA no later than their due date.

Alternatively, the corporation could declare a dividend to the individual to offset the outstanding shareholder loan. The dividend would not be a taxable deduction to the corporation but the personal income tax rate on the dividend would be lower than the tax rate on a salary or bonus.

Finally, more creative tax planning could also be used to avoid the full income inclusion on an outstanding shareholder loan. For example, an asset (i.e., non-registered investment portfolio) could be transferred to the corporation. Assuming the investments have an accrued gain, the original cost of the investments could be used to offset the shareholder loan outstanding. More aggressive types of tax planning- including a "capital gains strip" - may also be available in certain circumstances to mitigate the consequences of a shareholder loan approaching the one-year repayment deadline.

Regardless of a taxpayer's method of repaying a shareholder loan, careful attention must be given to ensuring that repayments are made in a timely manner, or the appropriate action is undertaken to avoid a full income inclusion.

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Claiming Automobile Expenses as a Health Professional

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While the *Income Tax Act* provides tax relief for individual and corporate taxpayers by allowing automobile expenses to be deducted from income, it can be a bit of a grey area, especially for health professionals. Generally speaking, only automobile expenses that are incurred for the purpose of earning business income can be deducted from a taxpayer's income. Since most vehicles are used for both personal and business purposes, it is important that detailed records are maintained if a taxpayer wishes to claim automobile expenses. Keeping track of all expenses incurred - including maintaining receipts, invoices, and records of the number of kilometres travelled for personal and business use - are required to substantiate the deduction claimed on the tax return in the event the Canada Revenue Agency (the "CRA") requests support on a review or audit.

The CRA and the tax courts have identified that travelling from a taxpayer's home to their regular place of work is not considered business use and automobile expenses related to those trips cannot be deducted. However, automobile expenses incurred travelling to a place that is not the taxpayer's regular place of work or principal place of business may be eligible for a tax deduction.

The importance of having a home office for business travel claims

For starters, for a health professional to claim travel from home to the hospital, clinic, or the professional's practising office, the taxpayer must have a home office. Whether the home office is considered the taxpayer's regular place of work or principal place of business is a question of fact. The CRA may take the position that a health professional's principal place of business is where they report to daily and generate their revenues. Most often, this is the place where the professional meets their patients. On the other hand, the courts have suggested that a taxpayer's principal place of business may instead be where they undertake administrative duties (e.g., bookkeeping, billing, reconciling cash receipts, etc.), charting or documenting on patients, or self-study and research. This is especially true if they have no designated physical space to carry out these activities at the hospital, clinic, or practising office. Given this alternative view on the professional's principal place of business, it is quite probable that some, but not necessarily all, health professionals could take the position that a home office is their principal place of business and therefore the travel between home and the hospital, clinic or practising office could be considered business use. Health professionals wishing to take such a position should speak to their tax advisors.

Provided that all the requirements have been met, the types of automobile operating expenses that can be deducted include:

- Gasoline;
- Maintenance;
- Oil change and repairs;
- Car washes;
- Insurance;
- License renewal fees;
- Registration fees;
- Parking charges; and
- Expenses relating to zero-emission vehicles, such as charging fees.

In addition, capital cost allowance (i.e., a tax proxy for depreciation), lease costs (of up to $900 + GST/HST per month for leases entered after January 1, 2022, and $800 + GST/HST per month for leases entered before), and interest (up to $300 per month) can be deducted.

Track all your business travel in a logbook

It is important to note that these expenses must be allocated between personal and business use, with only the business portion being deductible. The method of allocation is calculated based on the distance travelled for each purpose. As such, the best evidence to support the business use of the vehicle is to keep a business travel logbook including the following information:

- Date of travel;
- Destination;
- Business purpose of trip; and
- Number of kilometers driven on that trip.

Two relatively recent court cases not determined in favour of the taxpayers, reinforce the importance of maintaining a logbook. In *Cossette v. QRA*, the self-employed taxpayer used his vehicle for business use when visiting his customers. The taxpayer claimed 93 per cent of his automobile expenses as a deduction in his tax return. The court agreed with the Minister's position that the automobile expenses needed to be substantiated through a reasonable source of documentation to prove the proportionate use of his motor vehicle for business purposes. The taxpayer was unable to provide a logbook and instead, attempted to estimate the amount of usage for business purposes after the fact, based on an estimation of mileage travelled to his customers throughout the year. The court did not accept his unsubstantiated business use percentage and decreased his automobile expense claim significantly. Similarly, in *Quraishi et al vs. HMQ*, the taxpayer failed to keep a logbook to substantiate his automobile business usage and was unable to refute the Minister's reassessed claim.

Final Thoughts

Claiming automobile expenses as a tax deduction is not cut and dry, especially for health professionals. Taxpayers who do wish to make a claim must ensure that they keep proper records of their business travel and maintain copies of the expense receipts. Without this support, it is quite likely that the CRA will deny all or a portion of the tax deduction, resulting in additional tax, interest and possibly even penalties in certain circumstances.

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Important Tax Deadlines

February 24, 2022

- Last day to file a claim for Period 19 of the Canada Emergency Wage Subsidy (CEWS) in respect of wages between August 1 and August 28, 2021.
- Last day to file a claim for Period 12 of the Canada Emergency Rent Subsidy (CERS) in respect of expenses paid between August 1 and August 28, 2021.

February 28, 2022

- Filing due date for T4 Summaries and slips for salaries, bonuses, and retiring allowances paid in 2021.
- Filing due date for T5 Summaries and slips for interest and dividends paid by corporations, partnerships and trusts in 2021.

March 1, 2022

- Last day to make a 2021 RRSP contribution.

March 15, 2022

- Filing due date for Employer Health Tax (EHT) returns for employers with salary and bonuses paid of $1,000,000 or more in 2021.
- First quarterly installment due for 2022 personal income taxes.

March 24, 2022

- Last day to file a claim for Period 20 of the Canada Emergency Wage Subsidy (CEWS) in respect of wages between August 29 and September 25, 2021.
- Last day to file a claim for Period 13 of the Canada Emergency Rent Subsidy (CERS) in respect of expenses paid between August 29 and September 25, 2021.

March 31, 2022

- Filing due date for T5013 Summaries and Slips for professional partnerships where at lease one partner is an individual.
- Final payment of corporate income taxes due for most corporations with a December 31, 2021 fiscal year end.
- Filing and payment due date for annual filers of HST returns for corporations with taxation years ending December 31, 2021.

Important Tax Deadlines

April 21, 2022

- Last day to file a claim for Period 21 of the Canada Emergency Wage Subsidy (CEWS) in respect of wages between September 26 and October 23, 2021.
- Last day to file a claim for Period 14 of the Canada Emergency Rent Subsidy (CERS) in respect of expenses paid between September 26 and October 23, 2021.

May 2, 2022

- Final payment of 2021 Canadian personal income taxes due.
- Personal income tax return filing due date for most Canadian taxpayers for the 2021 year.
- Payment due date for annual filers of HST returns for individuals who reported self-employment income for the taxation year ending December 31, 2021.

June 15, 2022

- Personal income tax return filing due date for Canadian taxpayers who reported self-employment income for the taxation year ending December 31, 2021.
- Filing due date for annual filers of HST returns for individuals who reported self-employment income for the taxation year ending December 31, 2021.
- Second quarterly installment due for 2022 personal income taxes.

June 30, 2022

- Filing due date for corporate income tax returns for professional corporations with a December 31, 2021 fiscal year end.

September 15, 2022

- Third quarterly installment due for 2022 personal income taxes.

December 15, 2022

- Fourth quarterly installment due for 2022 personal income taxes.

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