TT TEXTBOOK TESTBANKS

Solutions Manual for Canadian Income Taxation 2023-2024 26th Buckwold

SOLUTIONS MANUAL SAMPLE PREVIEW

PUBLISHER
McGraw-Hill

COPYRIGHT
2023

RESOURCE TYPE
Solutions Manual

ISBN
9781264909551

CHAPTER 1

TAXATION— ITS ROLE IN BUSINESS DECISION MAKING

Review Questions

1. If income tax is imposed after profits have been determined, why is taxation relevant to business decision making?

2. Most business decisions involve the evaluation of alternative courses of action. For example, a marketing manager may be responsible for choosing a strategy for establishing sales in new geographical territories. Briefly explain how the tax factor can be an integral part of this decision.

3. What are the fundamental variables of the income tax system that decision-makers should be familiar with so that they can apply tax issues to their areas of responsibility?

4. What is an "after-tax" approach to decision making?

Solutions to Review Questions

R1-1 Once profit is determined, the *Income Tax Act* determines the amount of income tax that results. However, at all levels of management, alternative courses of action are evaluated. In many cases, the choice of one alternative over the other may affect both the amount and the timing of future taxes on income generated from that activity. Therefore, the person making those decisions has a direct input into future after-tax cash flow. Obviously, decisions that reduce or postpone the payment of tax affect the ultimate return on investment and, in turn, the value of the enterprise. Including the tax variable as a part of the formal decision process will ultimately lead to improved after-tax cash flow.

R1-2 Expansion can be achieved in new geographic areas through direct selling, or by establishing a formal presence in the new territory with a branch office or a separate corporation. The new territories may also cross provincial or international boundaries. Provincial income tax rates vary amongst the provinces. The amount of income that is subject to tax in the new province will be different for each of the three alternatives mentioned above. For example, with direct selling, none of the income is taxed in the new province, but with a separate corporation, all of the income is taxed in the new province. Because the tax cost is different in each case, taxation is a relevant part of the decision and must be included in any cost-benefit analysis that compares the three alternatives [Reg. 400-402.1].

R1-3 A basic understanding of the following variables will significantly strengthen a decision maker's ability to apply tax issues to their area of responsibility.

Types of Income	-	Employment, Business, Property, Capital gains
Taxable Entities	-	Individuals, Corporations, Trusts
Alternative Business Structures	-	Corporation, Proprietorship, Partnership, Limited partnership, Joint arrangement, Income trust
Tax Jurisdictions	-	Federal, Provincial, Foreign

R1-4 All cash flow decisions, whether related to revenues, expenses, asset acquisitions or divestitures, or debt and equity restructuring, will impact the amount and timing of the tax cost. Therefore, cash flow exists only on an after tax basis, and, the tax impacts whether or not the ultimate result of the decision is successful. An after-tax approach to decision-making requires each decision-maker to think "after-tax" for every decision at the time the decision is being made, and, to consider alternative courses of action to minimize the tax cost, in the same way that decisions are made regarding other types of costs.

Failure to apply an after-tax approach at the time that decisions are made may provide inaccurate information for evaluation, and, result in a permanently inefficient tax structure.

COMPREHENSIVE CASE SOLUTIONS

SOLUTION TO COMPREHENSIVE CASE ONE: JOHN SMITH AND BOB JOHNSON

Comparison of two employment offers received by John Smith

1) Offer of employment from ABC Co.

   a. Salary of $45,000 is included in income when received [ITA 5(1)]

   b. Stock option: The option is "in the money" at the date of grant; exercise price = $20; value at grant date = $25.

      If ABC Co is not a Canadian-controlled private corporation (CCPC):

      - there will be an employment income inclusion on the exercise date to the extent the value at the exercise date exceeds $20 [ITA 7(1)]
      - the stock option deduction will not be available [ITA 110(1)(d)]
      - John will have a capital gain or loss on the disposition of the shares based on the difference between the selling price and the value at the date of exercise

      If ABC Co is a CCPC:

      - the employment income inclusion is deferred until the date of disposition of the shares [ITA 7(1.1)]
      - if John does not dispose of the ABC Co shares within two years after acquiring them, John is entitled to the stock option deduction which is equal to ½ of the stock option employment benefit [ITA 110(1)(d.1)]
      - John will have a capital gain or loss on the disposition of the shares based on the difference between the selling price and the value at the date of exercise

   c. Home purchase loan: John will have an imputed interest benefit included in his employment income. The benefit is calculated by multiplying the loan principal by the prescribed rate of interest. The benefit is reduced by the 1% interest paid by John, provided the interest is paid by 30 days after the end of the calendar year.

      If the prescribed rate increases, the loan benefit will continue to be calculated using the 2% prescribed rate in effect at the time the home purchase loan was received (for a period of five years) [ITA 80.4].

   d. Private health services plan: The annual premium for prescription drugs, dental, and vision coverage does not result in a taxable benefit [ITA 6(1)(a)].

   e. Tax deductions: John will be able to claim the following deductions relating to his car in computing his employment income.

CCA	\$25,000 (includes HST) x 30% x 1.5 (CCA rate in the first year; 30% thereafter)	\$11,250	8(1)(j)
Interest	Lesser of :		
	(i) Amount paid \$3,000	3,000	8(1)(j)
	(ii) \$300 x 365/30 = \$3,650		67.2
Gasoline		5,000	8(1)(h.1)
Insurance		2,000	8(1)(h.1)
		\$21,250	
	Employment usage 10,000/30,000	\$7,083	

2) Offer of employment from DEF Co.

a) Salary of \$60,000 is included in income when received [ITA 5(1)].
b) The group term life insurance premiums are included in income [ITA 6(4)].
c) The fitness club membership results in a taxable benefit [ITA 6(1)(a)].
d) The phone is a capital asset and therefore CCA cannot be claimed for the purposes of computing employment income.
e) Taxable benefit with respect to the car is calculated below for 2023 and 2024.

	2023	**2024**
Monthly lease payments	\$700	\$700
	x 2/3	X 2/3
Number of months car available	1	12
Standby Charge	\$467	\$5,600
Personal kilometers	1,200	14,400
Operating expense benefit at \$0.33 per km	396	4,752
TOTAL	\$863	\$10,352

The reduced standby charge is not available because the car is not used primarily for employment purposes.

The employment offer that provides John with the greatest amount of disposable income after tax should be accepted.

Discussion with Bob Johnson, CFO of GHI Inc.

Stock-based compensation is not deductible for CCPC’s and corporations with revenues of \$500 million or less [ITA 7(3)(b)]. For other corporations, a deduction equal to the employee’s taxable benefit is allowed where the employee does not get the stock option deduction solely because of the new \$200,000 annual limit [ITA 110(1)(e)].

The bonuses declared by GHI Inc. in 2022 will not be deductible in 2022 because they were not paid in 2022 or by June 29, 2023 (180 days [ITA 78(4)]. The bonuses will be deductible in 2023 when paid.