December 2021

Capital Impact on principal residence exemption

You may be surprised to know that capital gain on principal residence is not automatically exempt from Canadian tax. The taxable portion of capital gain from sale of principal residence is calculated by a formula. The formula takes into account the number of years the home was occupied as a principle residence by a Canadian resident and total period of ownership.

Capital gain X (1 +A) /B

A is the number of taxation years ending after the acquisition date for which the property was the individual's principal residence and the individual was a resident of Canada; and

B is the number of taxation years ending after the acquisition date during which the individual owned the property

Taxpayer Rights

CRA audits are not a pleasant experience because we all know CRA's main goal is to find error in taxpayers filing often conclude with taxes owed to CRA. This is a normal part of Canadian tax administration but the enforcement measures imposed by CRA are sometimes painful. Following are some of the tax payers bill of rights:

- Professional and courteous treatment from CRA
- CRA to provide complete, accurate, clear and timely information
- You can lodge a service complaint
- You are expected to be provided with an explanation of CRA's findings
- CRA should warn you about questionable tax schemes in a timely manner, and
- Be represented by a person of your choice.

Tax Treaties

The purpose of tax treaties is generally to ensure that one country allows a foreign tax credit if income is

taxable in both countries. There are tax mechanisms adopted by most countries (under tax treaties) within their domestic tax system that provides foreign tax credit. The treaties contain rules to ensure the tax credit is available and how it would be implemented. For example, which country has the first right to tax and which country will grant a foreign tax credit.

In case of permanent establishment, most tax treaties provide that capital gains from the disposition of real property, resource property, and business property remain taxable in the country in which the property or business is located.

2021 year-end tax planning

2021 year end is fast approaching and it is a good time to review your personal tax situation and take advantage of any tax planning opportunities that may be available to you before December 31st deadline.

• Selling investments for tax loss is a great way to offset capital gains realized elsewhere in your portfolio. If capital loss cannot be used in current tax year, it can be carried back three years or carried forward indefinitely to offset capital gains of other years. If you plan to re-purchase the same investments then beware of the “Superficial loss” rules when you sell investments at a loss and buy back the same within 30 days. Capital loss will be denied in this situation.

• You may be tempted to transfer unregistered investments (at a loss) to RRSP or TFSA without actually disposing the investments. Note that the loss in this situation will be denied. To avoid this issue you can sell investments with accrued loss and contribute cash to TFSA or RRSP (if you have contribution room) to buy back same investments after the 30 days i.e. superficial loss period.

• Make RRSP contribution asap (the deadline is March 1, 2022) to maximize tax-deferred growth

• If you are planning to withdraw from TFSA in early 2022 then consider withdrawing the funds by December 31, 2022 so that you do not have to wait until 2023 to be eligible for re-contribution.

• Pay investment related expenses by year-end to claim a tax deduction

• December 31 is the last day to donate to receive charitable donation tax receipt for 2021

• Donation of stocks by December 31 is a great idea to avoid capital gains tax.

• If you anticipate a substantial difference in 2022 income, it would be worthwhile to explore income and expense shifting wherever possible.

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