<u>Question 1</u> 50 marks, 1A √ = 0.75 marks + 7, 1B √= 1.0 marks

(A) Determination of tax treatment of sale of land and building (**max 35√**)

(a) objective: to determine Rose's intention on the purchase of the Green Street property
primary: did Rose intend to purchase and resell the property for a business profit or to use the property to produce property income (be a capital asset)?
secondary: if the primary intention was to use the property as an asset, did Rose plan to sell the property for a profitable at the time of the purchase

(b) behavioural factors used to infer intention (**illustrative solution**)

1. relationship of the transaction to Rose's business
   - Purchased, leased and sold a number of buildings over the last decade (i = income)
   - Building was continuously rented (c = capital)
   - Rose appears to have been involved in the management of her properties, based on evidence of her dealing with tenants and their complaints (c)
   - She was a real estate professional, trained in real estate development (i)

2. nature of the asset
   - in general, real estate can be either income or capital
   - very small amount of income earned, if any (i)

3. number and frequency of transactions
   - 8 purchases and 5 sales (i.e., 3 properties still owned) in 10 years, is a track record suggesting an intention to turn a quick profit from business (i)
   - the short holding period of this property implies income (i)

4. length of ownership
   - 1.5 years is short for owning a rental property to produce rental income (i)

5. supplemental work (i.e., renovations) done of the property
   - poor quality materials used suggests short-term horizon (i)
   - work done was minimal and most work done immediately prior to sale (i)
   - rent received increased with renovations (c)

6. circumstances causing the disposition
   - Offer was unsolicited (c)
   - Having medical trouble at that time (c)

7. articles of incorporation
   - the articles state that it was own real estate suggesting capital (c)

8. feasibility
   - the income from rental was marginal and not enough to provide a reasonable rate of return on investment (i)

9. location and zoning
   - the property was in a rough neighbourhood, not likely to produce reasonable rents (i)
   - Rose wanted to be part of redevelopment (c)
   - Redevelopment increases her return through appreciation (i)

10. use of borrowed funds
    - By the end, she had equity of less than less than 5%--very high leverage (i)
    - short term debt (i)
    - high interest rates (i)

(c) conclusion and advice

It is reasonable to file the return as a capital gain; however, there is sufficient evidence that Rose may be challenged on this.

OR

She should file using income from business (that of buying, renting, and selling real estate), but this will lead to a higher tax payment now.

(one for conclusion, one for caveat; either conclusion acceptable)

(B) Calculation of taxable income (**max 35 √**)

Net income (accept 497,500 as well)			839,600 √
Add: Amortization			20,000 √
Income tax expense			170,000 √
Bonus declared in 2010			35,000 √
RPP: limited to 18%√ of 300K√ + 45K√, or 22,450√			0
Charity			10,500 √
Entertainment	50% √ x 6,000 √		3,000
Golf fees			4,000 √
Spa costs (personal) √			1,500 √
Legal costs for share restructuring			2,000 √
Less: Gain on sale for accounting		530,000 √	
Bonus declared in 2009, paid 2010		45,000 √	
CCA: f&f	20% √ x 75,000 x .9 √	13,500	
comp	55% √ x 14,500 √	7,975	
CECA:	6,000√ x 75%√ x 0.93 x 0.07√	293	(596,768)
			488,832
Capital gains (or business income without the '0.5'√)			
Land:	0.5√ x (400,000√ – 150,000√)	125,000	
Bldg:	0.5 x (800K √ – 100K √ – 25K √ – 100K √– 300K √)	137,500	262,500
			751,332
Less: Charitable contributions (limited to 75%√ x 751,332√)			(10,500) √
			740,832

<u>Question 2</u> 50 marks, √ = 1.0 marks, max 64 √

(A) Calculation of taxable income (**max 44 √**)

3(a) √
Business income:

Net income			762,000 √
Add: Amortization			80,000 √
Income taxes			281,000 √
Less: Gain on sale			(308,000)√
CCA: Class 1 (old)	4% x 1,600K √	64,000	
Class 1 – NRB 6% √ x ½ √ x (120K √ - 72K√ – 21.4K√)		798	
Class 8 20% √ x (115K + ½ √ (340K √ – 260K √)		31,000	
Class 8 (photocopier 2)	20% x ½ x 24K √	2,400	
Class 8 (photocopier 3)	20% x ½ x 18K √	1,800	
Class 10.1 (old)	30% x ½ x 7,550 √	1,133	
Class 10.1 (new)	30% x ½ x 30K √	4,500	
Class 13 (old)	lesser of (a) 360K / 5 √ (b) 360K / 9 √	40,000	
(new)	½√ of lesser of (a) 224K / 5 √ (b) 224K / 7 √	16,000	
Class 14	184 / (20 x 365) x 160K √√	4,033	(165,664)
Terminal loss: Class 8 (photocopier 1)	11,750 – 3500 √		(8,250)
			641,086
3(b) Net taxable capital gains:			
t.c.g. on land: ½ √ x 50,000 √			25,000
			666,086
Division C			
Dividend received			(5,000)
Net capital losses claimed: lesser of 100,000 √ and 25,000 √			(25,000)
Taxable income			636,086

Subsection 44(1):

	Land	Bldg
Lesser of		
(a) P o D	280 √	120 √
less ACB	(72)√	(48)√
	208	72
(b) P o D	280 √	120 √
less Repl Cost	(230)√	(120)√
	50	0
Lesser	50	0

Paragraph 13(4)(c):

UCC, open			26.6 √
less: lesser:			
(a) P o D	120.0 √		
(b) CC	48.0 √	48.0	
less: lesser			
(a) recap	21.4 √		
(b) Repl C	120.0 √	(21.4)	
			(26.6)

(B) Calculation of tax payable (**max 20 √**)

Basic federal tax	38% √ x 636,086 √		241,713
Abatement	$\frac{1}{2}\sqrt{}\left(\frac{6.3M\sqrt{}}{8.3M\sqrt{}}+\frac{1190K\sqrt{}+170K\sqrt{}}{1700K\sqrt{}+190K\sqrt{}}\right)$ or $\frac{1}{2}\left(76\%+72\%\right)\times 10\%\sqrt{}\times 636,086$		(47,070)
General rate reduction	10% √ x 636,086		(63,609)
Business FTC:			
Least of:	(a) paid	52,000 √	
	(b) $\frac{175,000\sqrt{}}{666,086\sqrt{} - 25,000\sqrt{} - 5,000\sqrt{}}$ x (241,713 √ – 63,609√)	49,000	(49,000)
	(c) (241,713 – 63,609) √√	178,104	
			82,034