Have you ever found yourself looking for tax savings while completing your tax return in April? If so, you probably know that at that point, there’s not much you can do to reduce your balance owing. By the time you prepare your tax return, you’re looking back and simply reporting on the year that has ended. Real tax savings come from looking forward.

But don’t worry. As we approach the end of the year, there’s still time left for forward-looking planning. You can approach year-end planning by asking yourself questions, going through a checklist, considering a framework or using all three methods.
Taking time out of your busy December to think about these questions will help you find better answers that may save you money on your 2016 tax bill and beyond:

Are there any income-splitting techniques available to you?
Can you take advantage of differences in tax brackets and marginal rates in your family with:

- **Income-splitting loans?** The prescribed interest rate applicable to the exemption from income attribution on intra-family loans remains at a low 1% for loans created in 2016.
- **Reasonable salaries to family members?** If you have a business, consider employing your spouse or partner and/or your children to take advantage of income-splitting opportunities. Their salaries must be reasonable for the work they perform.
- **Spousal RRSPs?** In addition to splitting income in retirement years, these may be used to split income before retirement. The higher-income spouse or partner can get the benefit of making contributions to a spousal plan at a high tax rate and, after a three-year non-contribution period, the lower- or no-income spouse can withdraw funds and pay little or no tax.

Have you paid your 2016 tax-deductible or tax-creditable expenses yet?

- **Tax deductible expenses** - A variety of expenses, including interest and child-care costs, can only be claimed as deductions in a tax return if the amounts are paid by the end of the calendar year.
- **Expenditures that give rise to tax credits** - Charitable donations, political contributions, medical expenses, children’s fitness program costs, children’s arts program costs, tuition fees and transit pass costs, must be paid in the year in order to be creditable. And remember the children’s arts and fitness credits are being eliminated in 2017, so make sure you can make your claim in 2016. Also, a new refundable tax credit of up to $150 is available for licensed and certified teachers and educators who purchase up to $1,000 worth of eligible school supplies.

Have you considered the impact of any changes to personal tax rules that are effective for the year?

- **Do you hold any linked notes that are maturing after 2016?** If so, consider disposing of them before year end to trigger any accrued capital gains. Weigh the savings from capital gains treatment against the deferral from recognizing the income on the maturity of the instrument. For more information on linked notes see EY’s Tax Alert 2016 Issue No. 37, *Finance releases draft proposals on taxation of switch funds and linked notes.*
- **Do you own or hold intangible assets subject to the eligible capital property rules?** Discuss the pending changes to the eligible capital property rules with your tax advisor. Take action now if it is advantageous to do so before the rules change on 1 January 2017.

Have you sold a principal residence in 2016?
Some new principal residence exemption rules target both nonresidents who purchase homes in Canada and Canadian homeowners. Specifically, all Canadian homeowners will now be required to report the sale of a principal residence on their tax return for the year of the sale (even if the gain is fully sheltered by the principal residence exemption), or be subject to an extended reassessment period. As a result, it is important for individuals to properly track the cost of multiple residences owned in a year and determine how best to allocate the principal residence exemption on a sale.

These rules were announced on 3 October 2016. For more information, see EY’s Tax Alert 2016 Issue No. 45, *Proposed amendments to principal residence exemption rules for trusts and nonresidents.*
Have you maximized your tax-sheltered investments by contributing to a TFSA or an RRSP?

- **Tax-free savings account (TFSA)** - Make your contribution for 2016 and catch up on prior non-contributory years. You won’t get a deduction for the contribution, but you will benefit from tax-free earnings on invested funds. Also, in order to maximize tax-free earnings, consider making your 2017 contribution in January.

- **Registered retirement savings plan (RRSP)** - The earlier you contribute, the more time your investments have to grow. So consider making your 2017 contribution in January 2017 to maximize the tax-deferred growth. If your income is low in 2016, but you expect to be in a higher bracket in 2017 or beyond, consider contributing to your RRSP as early as possible but holding off on taking the deduction until a future year when you will be in a higher tax bracket.

Have you maximized your education savings by contributing to an RESP for your child or grandchild?

- **Contributions** - Make registered education savings plan (RESP) contributions for your child or grandchild before the end of the year. With a contribution of $2,500 per child under age 18, the federal government will contribute a grant (CESG) of $500 annually (maximum $7,200 per beneficiary).

- **Non-contributory years** - If you have prior non-contributory years, the annual grant can be as much as $1,000 (in respect of a $5,000 contribution).

Is there a way for you to reduce or eliminate your non-deductible interest?

- Interest on funds borrowed for personal purposes is not deductible. Where possible, consider using available cash to repay personal debt before repaying loans for investment or business purposes on which interest may be deductible.

Have you reviewed your investment portfolio?

- **Do you have any accrued losses to use against realized gains?** While taxes should not drive your investment decisions, it may make sense to sell loss securities to reduce capital gains realized earlier in the year. If the losses realized exceed gains realized earlier in the year, they can be carried back and claimed against net gains in the preceding three years and you should receive the related tax refund. Just remember to be careful of the superficial loss rules, which may deny losses on certain related-party transactions. For more on the superficial loss rules, refer to the October 2015 TaxMatters@EY article, “Making the most of investment losses.”

- **Do you have any realized losses carried forward?** If you have capital loss carryforwards from prior years, you might consider cashing in on some of the winners in your portfolio. Or consider transferring qualified securities with accrued gains to your TFSA or RRSP (up to your contribution limit). The resulting capital gain will be sheltered by available capital losses, and you will benefit from tax-free (TFSA) or tax-deferred (RRSP) future earnings on these securities.
Can you improve the cash flow impact of your income taxes?

- **Are you eligible to request reduced source deductions?** If you regularly receive tax refunds because of deductible RRSP contributions, child-care costs or spousal support payments, consider requesting CRA authorization to allow your employer to reduce the tax withheld from your salary (Form T1213). Although it won’t help for your 2016 taxes, in 2017 you’ll receive the tax benefit of those deductions all year instead of waiting until after your 2017 tax return is filed.

- **Are you required to make a 15 December instalment payment?** If you expect your 2016 final tax liability to be significantly lower than your 2015 liability (for example, due to lower income from a particular source, losses realized in 2016 or additional deductions available in 2016) you may have already paid enough in instalments. You are not required to follow the CRA’s suggested schedule, and are entitled to base your instalments on your expected 2016 liability. However, if you underestimate your 2016 balance and your instalments end up being insufficient or the first two payments were low, you will be faced with interest and possibly a penalty.

Have you thought about estate planning?

- **Have you reviewed your will recently?** You should review and update your will periodically to ensure that it reflects changes in your family status and financial situation, as well as changes in the law.

- **Have you considered your life insurance needs?** Life insurance is an important tool to provide for the payment of various debts (including taxes) that may be payable as a result of your death, as well as to provide your dependants with money to replace your earnings. Review your coverage to ensure that it remains appropriate for your financial situation.

- **Have you considered an estate freeze to minimize tax on death and/or probate fees?** An estate freeze is the primary tool used to reduce tax on death and involves the transfer of the future growth of a business, investments or other assets to family members. Consider the impact of changing rules for the taxation of testamentary trusts and charitable planned giving.

- **Have you considered a succession plan for your business?** A succession plan involves devising a strategy to ensure that the benefit of your business assets passes to the right people at the right time.

These questions may seem familiar, but as tax rules become more complex, it becomes more important to think of the bigger tax picture continuously throughout the year, as well as from year to year as your personal circumstances change. Start a conversation with your tax advisor to find better answers.

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**Year-end tax to-do list**

**Before 31 December 2016:**

- Make 2016 TFSA contribution.
- Make 2016 RESP contribution.
- Final RRSP contribution deadline for taxpayers who are 71 years old.
- Pay tax deductible or tax creditable expenses.
- Advise employer in writing if eligible for reduced automobile benefit.
- Request CRA authorization to decrease tax withheld from salary in 2017.
- Investment portfolio review for potential dispositions to realize gains or losses in 2016. (Note the last day for settlement of a trade in 2016 is 23 December on a Canadian stock exchange and 27 December on a US stock exchange.)
- Make capital acquisitions for business.
- Evaluate owner-manager remuneration strategy.
- Consider allowable income-splitting strategies.

**Early 2017:**

- Interest on income splitting loans must be paid by 30 January.
- Make 2016 RRSP contribution (if not already made) by 1 March.
- Make 2017 RRSP contribution.
- Make 2017 TFSA contribution.
- Make 2017 RESP contribution.
Can you improve the cash flow impact of your income taxes?

There are two benefits to doing year-end tax planning while there is enough time left in the year to do it well. First, you are more likely to avoid surprises next April that can be both economically and emotionally stressful. Second, if done from a wide-angle perspective of comprehensive financial and estate planning, year-end tax planning can help you understand whether you are doing the right things in the right way, not just to minimize income taxes, but also to make it that much easier to achieve your longer-term financial goals.

Consider how you can approach current year-end planning with an eye to the future. By assessing any major step taken today for its effect on the tax, financial and estate planning in the next stage(s) of your life, you may preclude choices that will reduce planning flexibility and maybe increase taxable income in the future.

A good place to start is a quick check of some fundamentals that could need some attention while there is still time this year to fix any problems. So do a projection for 2016 taxes to determine whether you had enough tax withheld and/or paid sufficient instalments to avoid an underpayment issue. The projection might suggest that some adjustments are in order (or that you can relax a little).

You should also determine if there will be any significant change in the amount and/or composition of your income next year. Among other things, changes in your personal lifecycle (such as changes in your marital or parental status) need to be considered. This information could prove to be important when selecting and designing particular tax planning steps.

Planning with income

You should understand the composition of your employment, business or professional income (salary, bonus, options, self-employment income, etc.), how each component is taxed in the current or future years and the extent to which you can control the timing and amount of each type of income.

You should also understand the composition of your investment income, meaning interest, dividends and capital gains, and the extent to which you can control the timing, amount and character of each item. An important follow-up inquiry is whether there are capital losses that can be triggered and/or used to offset gains or to avoid year-end distributions. Of course, taxes are only one of the factors to be considered in deciding whether to do some loss planning in your portfolio.

Another tax planning issue associated with investing is “asset location,” meaning selecting the right investments to hold in taxable versus tax-deferred accounts, respectively. Even some minor tweaking here could pay big dividends down the road.

Planning with deductions and credits

On the other side of the ledger from income are deductions. Here again, you should understand what deductions you are entitled to and the extent to which you can control the timing of those deductions. If you can benefit from a deduction or credit this year, make sure you pay the amount before year end (or in the case of RRSP contributions, before 1 March 2017). Or, if you expect to be in a higher tax bracket next year, consider deferring deductions until next year, when they will be worth more.

The larger task may be to review and reassess the tax and financial implications of your major deductions and credits. For example, can you plan to minimize non-deductible interest expense or replace it with deductible interest expense? Or can you plan your usual charitable contributions to maximize their tax benefit?

Estate planning

Your estate plan should start as soon as you begin to accumulate your estate. It should protect your assets and provide tax-efficient income before and after your retirement, as well as a tax-efficient transfer of your wealth to the next generation. Your will is a key part of your estate plan. You and your spouse or partner should each have a will and keep it current to reflect changes in your family status and financial situation as well as changes in the law.

Remember, the taxation of testamentary trusts and estates, as well as the rules for charitable planned giving, changed significantly effective 1 January 2016. It is generally a good idea to review your estate planning goals and wills on a regular basis, but now is an especially good time to do that review in light of the new rules.

These suggestions for year-end tax planning should help you set the agenda for a comprehensive discussion with your tax advisor this year and in years to come.
Year-end remuneration planning

Gabriel Baron and Irina Rakhimova, Toronto

Corporate business owners have great flexibility in making decisions about their remuneration from a private company. This flexibility also extends to other types of businesses, such as incorporated professionals and business consultants. It’s important that decisions about remuneration be made before year end, as well as considered during the business’s financial statement and tax return finalization processes.

Remuneration planning will also need to consider the impact of increased personal tax rates for higher income earners, effective 1 January 2016. Some options and ideas to consider are highlighted below.

Basic considerations

- In general, if a corporate owner-manager does not need personal funds for spending, monies and earnings should be left in the corporation to grow and be subject to tax at corporate tax rates, which are less than personal tax rates. The beneficial difference between corporate tax rates and personal tax rates for 2016 can range from as little as 19.8% in Newfoundland and Labrador when applying the general corporate tax rate, to as high as 40.5% when applying the small-business corporate tax in Nova Scotia. Deferring tax allows you to reinvest the corporate earnings and earn a rate of return on the personal tax you would have otherwise paid when extracting the funds from the business.

- Even if funds are not required for personal consumption, business owners may want enough salary to create sufficient earned income to maximize their RRSP contribution and use tax savings associated with graduated income tax rates. Whether or not this is an appropriate strategy depends on an overall review of the owner-manager’s financial plan for the near future, as well as the long term. In order to contribute the maximum RRSP amount of $26,010 for 2017, business owners will need 2016 earned income of at least $144,500. One method to generate earned income is to receive a salary in the year. Note, salary must be earned and received in the calendar year. The salary would also maximize CPP pensionable earnings for the year (based on maximum pensionable earnings of $54,900 for 2016).

- If funds are needed for personal consumption, the Canada Revenue Agency has a longstanding policy of not challenging the reasonableness of remuneration where the recipient is active in the business and a direct or indirect shareholder. This criterion of reasonability is relevant when considering if the remuneration is deductible to the paying corporation. It is generally more advantageous to distribute corporate profits as a salary or bonus to an active owner-manager based on current provincial corporate and personal tax rates. However, this may not be applicable for all provinces, and certain provinces levy additional payroll taxes, such as Ontario’s employer health tax, which may impact an analysis of the optimal compensation strategy.
• Many provinces have an overall “tax cost” to distributing business profits in the form of a dividend, meaning the total corporate and personal tax paid on fully distributed business earnings exceeds that province’s personal tax rate. This situation may be irrelevant to business owners, as future cash needs may be satisfied by salaries or bonuses from future profits. Earnings subject to a large deferral of tax can remain reinvested in the business or corporate environment for many years, and sometimes indefinitely.

Advanced considerations
• Shareholder loans made to the corporation can be repaid tax free and represent an important component of remuneration planning. Advance tax planning may permit creation of tax-free shareholder loans.
• Recent changes in the tax rules associated with otherwise tax-free intercorporate dividends could result in the dividends being recharacterized as capital gains. Advanced tax planning may be available to mitigate this issue, or to benefit from corporation distributions taxed at reduced tax rates associated with capital gains.
• A business owner who holds personal investments such as marketable securities can sell these to a private corporation in exchange for a tax-paid note or shareholder loan. While capital gains may arise on the transfer, the personal tax rate on capital gains is generally lower than the personal tax rate on eligible or non-eligible dividends. Advance tax planning may also allow recognition of the capital gain to be deferred; however, tax losses may not be realized on a transfer to an affiliated corporation.
• Corporate-level M&A transactions such as the divestiture of a business or real estate may also generate favourable tax attributes such as tax-free capital dividend account (CDA) balances, or refundable taxes. These attributes form an important component of remuneration planning.
• A business can claim a capital cost allowance (CCA) deduction for the purchase of depreciable assets that are available for business use on or before the business’s fiscal year end. A business that is contemplating a future asset purchase and has discretion in the timing of acquisition may choose to make the purchase sooner rather than later and then bring the asset into use to allow CCA to be claimed.
• Retaining earnings in a corporation may affect a CCPC’s entitlement to refundable scientific research and experimental development (SR&ED) investment tax credits. A business should compare the investment return from deferring tax on corporate earnings against the forgone benefit of high-rate refundable SR&ED investment tax credits.
• Leaving earnings in the corporation may also impact its status as a qualified small-business corporation (QSBC) for the purpose of the shareholder’s lifetime capital gains exemption (currently $824,176). Advance tax planning may be available to mitigate this issue and permit continued accumulation of corporate profits at low rates, without impacting QSBC status.
• Paying dividends may occasionally be a tax-efficient way of getting funds out of a company. Capital dividends are completely tax free, eligible dividends are subject to a preferential tax rate, and all types of taxable dividends generate a dividend refund in a corporation with a refundable dividend tax account (RDTOH). A review of the company’s tax attributes will identify whether these advantageous dividends can be paid.
• Dividends and other forms of investment income from private corporations do not represent earned income and so do not create RRSP contribution room for the recipient. An individual also requires earned income to be able to claim other personal tax deductions, such as child care and moving expenses. Business owners should consider how much earned income they need in light of the RRSP contributions they wish to make or personal tax deductions they wish to claim.

Income splitting considerations
• Consider paying a reasonable salary to a spouse or adult child who provides services (e.g., bookkeeping, administrative, marketing) to the business in order to split income.
• If a spouse or adult child is not active in the business and has no other sources of income, consider an income-splitting corporate reorganization whereby the family members become direct or indirect shareholders (such as a beneficiary of a personal trust) in the business. Depending on the province of residence, an individual who has no other source of income can receive anywhere between approximately $9,000 and $51,000 of dividends tax free. These amounts increase where the recipient has access to tax credits such as the tuition tax credit in the case of adult-child students. Commercial and family law considerations, in conjunction with the tax benefits, will determine whether it is worthwhile pursuing such a strategy.
• In select cases, a low-interest family loan can be advantageous for permissible income splitting. Given the low 1% "prescribed rate," it may be worthwhile exploring this planning option, especially if the return on investment exceeds the prescribed rate.
Managing tax cash flow

- If there is a plan to pay salary, remember that bonuses can be accrued and deducted by the business in 2016, but not included in the business owner’s personal income until paid in 2017. To be deductible to a corporation, the accrued bonus must be paid within 179 days after the company’s year end, permitting a deferral of tax on salaries of up to six months.

- If earnings left in the corporation exceeded the available small business deduction limit for the preceding tax year, corporate taxes for the current year will be due two months, rather than three months, after the year end. The current rate for late payment arrears interest is 5% and is not deductible for income tax purposes.

- Monthly and quarterly tax instalments (for corporate and personal income, respectively) must be managed to avoid arrears interest and penalty interest. A single midyear payment strategy can be used to simplify the obligation of making recurring payments, and generally reduce or eliminate interest and penalties.

- Use of a shareholder “debit” loan account (where the corporation has a receivable from the individual shareholder) may simplify the need to project exact owner-manager remuneration requirements. Shareholder “debit” loans must be repaid within one year after the end of the year in which the loan was made, or else the loan will be included in the business owner’s income in the year funds were withdrawn. The repayment of a shareholder loan cannot constitute a series of loans or other transactions and repayments if the one-year repayment is to be considered valid.

- Borrowing from the company within the permissible time limits will cause a nominal income inclusion at the prescribed rate, currently only 1%. The cost of financing from the corporation using shareholder loans can therefore currently be achieved at tax-effected rates of 0.44% to 0.54% at the highest marginal rates of tax, depending on your province of residence.

For more information on remuneration planning and other tax-planning and tax-saving ideas, contact your EY professional advisor.
As concerns about wealth preservation and succession planning in family businesses continue to rise, wealthy families are increasingly evaluating the benefits of setting up a family office.

What is a family office?

Family offices have their roots in the sixth century, when a king’s steward was responsible for managing royal wealth. Later on, the aristocracy also called on this service from the steward, creating the concept of stewardship that still exists today. But the modern concept of the family office developed in the 19th century. In 1838, the family of financier and art collector J.P. Morgan founded the House of Morgan to manage the family assets.

Although each family office is unique to some extent and varies with the individual needs and objectives of the family it is devoted to, it can be characterized as a family-owned organization that manages private wealth and other family affairs.

The reasons why

There are many reasons why setting up a family office makes sense, but at the root of these is the desire to ensure smooth intergenerational transfer of wealth and reduce intrafamily disputes. This desire inevitably increases from one generation to the next, as the complexity of managing the family’s wealth grows.

Without being exhaustive, the following points set out reasons why a family office makes sense:

- **Privacy and confidentiality** - For many families, the most important aspect of handling of their private wealth is privacy and the highest possible level of confidentiality. The family office often is, and should be, the only entity that keeps all the information for all family members, covering the entire portfolio of assets and general personal information on a holistic basis.

- **Governance and management structure** - A family office can provide governance and management structures that can deal with the complexities of the family’s wealth transparently, helping the family to avoid future conflicts. At the same time, confidentiality is ensured under the family office structure, as wealth management and other advisory services for the family members are under a single entity owned by the family.

- **Alignment of interest** - A family office structure also ensures that there is a better alignment of interest between financial advisors and the family. Such an alignment is questionable in a non-family office structure where multiple advisors work with multiple family members.

- **Potential higher returns** - Through the centralization and professionalization of asset management activities, family offices may be more likely to achieve higher returns, or lower risk, from their investment decisions. Family offices can also help formalize the investment process, and maximize investment returns for all family members.
• **Separation** – Family offices allow for separation, or at least a distinction, between the family business and the family’s wealth or surplus holdings.

• **Risk management** – Family offices allow for operational consolidation of risk, performance management and reporting. This helps the advisor and principals to make more effective decisions to meet the family’s investment objectives.

• **Centralization of other services** – Family offices can also coordinate other professional services, including philanthropy, tax and estate planning, family governance, communications and education, to meet the family’s mission and goals.

• **Focal point for the family** – In cases where the main family business has been sold, a family office can offer a new focal point of identification for the family members, for example when the family office manages the family’s philanthropic activities.

**Why might there be doubts about setting up a family office?**

The establishment of a family office is a big undertaking, and there have been cases when family offices have not met the family's expectations. Some of the potential doubts and concerns about setting up a family office include:

• **Cost** – The cost of regulatory and compliance reporting remains high, which means that the level of assets under management that a family office needs to underpin must be sufficient to offset its fixed costs.

• **Market, legal and tax infrastructures** – Family offices function better when operating from centers where there are sophisticated markets and legal and tax structures. The absence of these in emerging markets has undermined the development of family offices there.

This has often meant that there has been little connection between the huge level of wealth in some emerging markets and the number of family offices. Much of the wealth in emerging markets is still controlled by the first generation. This has also inhibited the growth of family offices, because many are launched during a wealth transition from one generation to the next.

• **The MFO offering** – To address the problem of the high operating costs of a family office, families often set up multifamily offices (MFOs), in which several families pool their wealth together. Often these MFOs will be directed by the “lead” family that initiated the office. In MFOs, all assets are managed under one umbrella. But MFOs typically cater to a range of family size, wealth and maturity levels. This means that families can run the risk of not receiving the personalized advice that they would have in a dedicated family office setup.

When considering establishing a family office, some can see potential positives as negatives. This tends to be particularly prevalent in the following cases:

• **The preference for privacy** – Some families may be hesitant about consolidating their wealth information through a centralized family office structure.

• **Trust of external managers** – Setting up a family office is typically contingent on the level of trust and comfort families have with external asset managers. However, trust typically stems from longstanding relationships with external managers.

• **Expectations** – Ultimately, family offices rely on their longevity through ensuring wealth preservation. This difficulty of securing market returns in recent years has led to some tension in this respect. Furthermore, during generational transitions, family office structures are tested, often to the point of destruction, as the next generation presses for different goals and objectives to manage the family’s wealth.
Main types of family offices

Embedded family office
An embedded family office (EFO) is usually an informal structure that exists in a business owned by an individual or a family. The family considers private assets as part of their family business and therefore allocates private wealth management to trusted and loyal employees of the family business.
Usually the chief finance officer of the family business and the finance department's employees are entrusted with the family office duties. As this is not necessarily the most efficient of structures, more and more entrepreneurial families are separating their private from their business wealth and are considering taking the family office functions outside the family business, not least for reasons of privacy and tax compliance.

Single family office (SFO)
A single family office (SFO) is a separate legal entity serving one family only. There are a number of reasons for setting up an SFO:
- The retirement of the business-owning generation
- A greater desire to diversify and widen the asset structure beyond the local family firm
- A rising exposure to non-investment risks, such as privacy concerns and legal risks
The family owns and controls the office that provides dedicated and tailored services in accordance with the needs of the family members. Typically, a fully functional SFO will engage in all, or part of, the investments, fiduciary trusts and estate management of a family; many will also have a concierge function.

Multifamily office (MFO)
A multifamily office will manage the financial affairs of multiple families, who are not necessarily connected to each other. As with an SFO, an MFO might also manage the fiduciary, trusts and estate business of multiple families as well as their investments. Some will also provide concierge services. Most MFOs are commercial, as they sell their services to other families. A very few are private MFOs, whereby they are exclusive to a few families, but not open to other families.
Over time, SFOs often become MFOs. This transition is often due to the success of the SFO, prompting other families to push for access. Economies of scale are also often easier to achieve through an MFO structure, prompting some families to accept other families into their family office structure.

Learn more
To learn more about establishing a family office, read the EY Family Office Guide: pathway to successful family and wealth management. The guide offers a step-by-step process that aims to demystify what's involved in setting up and running family offices.
And for more information, visit EY Family Office Advisory Services.
Growing your business in foreign markets can offer new growth and expansion opportunities. But you should also be mindful of the impact of potential currency fluctuations on your bottom line. If you’re looking to grow your business beyond borders, you’ll need to have a foreign exchange risk management strategy in place to help mitigate negative exposures to your business.

Here are some important risk management steps you should consider if foreign exchange is a factor for your private business.

**Step 1: Identify and quantify the risk elements**

As you assess your risk, it’s important to have a clear picture of the amount of exposure that your business has in foreign currency on a month-to-month basis. Once you’ve quantified the approximate exposure, determine what your objectives are and who can assist you in meeting your goals.

**Step 2: Determine what works for your business**

When evaluating your foreign exchange risks, there are a number of important questions to address to determine the right course of action for your foreign exchange policy:

- Are you looking to eliminate all foreign exchange risk?
- Do you want to protect against downside risk only?
- Are there ways to minimize your foreign exchange costs?
- When should your foreign exchange exposure be hedged?
- What tools and instruments are you comfortable using and under what circumstances?
- Who should be responsible for managing foreign exchange exposure?
- What are your regular reporting requirements?
- What is the accounting policy for the hedging methodology chosen?

Once you’ve determined how your foreign exchange objectives and processes should be managed, the next step is determining the strategy to achieve those objectives.
What are some of your options?

- **Forward contracts** are agreements to buy or sell a given amount of currency at a set exchange rate on a specific future date. Forwards are obligations and are not generally flexible, should your needs change during the terms of a contract.

- **Futures contracts** allow you to buy or sell a currency at a set exchange rate in a given month. Futures are highly liquid, so they can be closed out before the settlement date, giving you flexibility.

- **Currency options** give you the right, but not the obligation, to buy or sell a currency at a set exchange rate during a specific time period. As a result, they offer a great deal of flexibility.

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**Step 3: Develop the strategy**

When developing the right foreign exchange strategy and tactics to implement it, you’ll want to put in place hedges that are consistent with your company’s policy.

In addition to your internal strategy, it’s also important to evaluate how the market is behaving and the trends that are occurring. The market can be greatly impacted by current economic fundamentals, including various geopolitical situations. Understanding the direction the market is going and whether or not you should be waiting or taking advantage of opportunities can help determine the right direction to pursue, and whether or not a change in plan is required.

**Step 4: Execution and evaluation of your chosen strategy**

Once you’ve determined the course of action for your foreign exchange exposure, it’s critical to evaluate your progress towards managing your risks. Establishing clear objectives and benchmarks will help facilitate this evaluation. It will also help those responsible for implementing the policy to make the measures in place for hedging your risk effective when compared against your goals. Staying up to date on market trends and determining if there are any changes to your objectives or risk elements can help you proactively mitigate your risk.

You should revisit your foreign exchange risk management strategy throughout the year to keep it efficient and effective toward achieving your desired goals. Market variables can quickly change and you’ll want to be prepared to manage those risks.
Software SR&ED credits: what evidence is sufficient evidence?

ACSIS EHR (Electronic Health Record) Inc. v The Queen, 2015 TCC 263
Rachel Robert, Montreal, and Allison Blackler, Vancouver

This case considered whether a taxpayer was entitled to claim scientific research and experimental development (SR&ED) investment tax credits under the Income Tax Act (the Act) in relation to a computer software development project. The Tax Court of Canada (TCC) ruled in favour of the taxpayer and allowed the SR&ED investments tax credits claimed.

Facts
The taxpayer operates a business that develops specialized software, including, in particular, software applications for the centralized management of national, regional and local health care sectors. In 2014, the taxpayer entered into a contract with a foreign governmental authority to implement a national health care system.

Early on in the project, the taxpayer realized that major issues needed to be addressed due to the foreign country’s unstable communications infrastructure. The taxpayer determined that the only way to carry out the contract would be to create a new technology that could mimic a stable system.

The taxpayer claimed the expenditures related to developing that new technology as qualifying SR&ED expenditures. However, the Canada Revenue Agency (CRA) took the position that the work performed did not meet the definition of SR&ED, as the activities did not resolve any scientific or technical uncertainties.

The Tax Court of Canada decision
At issue in this case was whether the software project was “scientific research and experimental development... that was undertaken for the purpose of achieving technological advancement for the purpose of creating new, or improving existing, materials, devices, products or processes, including incremental improvements thereto”\(^1\), and if so, whether any of the particular expenditures could be considered a “qualified expenditure” (subsection 127(9) of the Act).

In order to make that determination, the TCC applied the five criteria, set out in the landmark case Northwest Hydraulic Consultants Ltd. v The Queen, 98 DTC 1839, for determining whether a taxpayer’s activities are SR&ED:

- Is there a technical risk or uncertainty?
- Did the taxpayer formulate hypotheses specifically aimed at reducing or eliminating that technological uncertainty?
- Did the procedures adopted by the taxpayer accord with established and objective principles of scientific method, characterized by trained and systematic observation, measurement and experiment, and the formulation, testing and modification of hypotheses?
- Did the process result in a technological advance, that is to say an advancement in the general understanding?
- Was a detailed record of the hypotheses, tests and results kept as the work progressed?

Applying these criteria, and based on an assessment of the evidence at trial, the TCC determined that the taxpayer’s software system was in fact a technological advancement that addressed a technological uncertainty. The TCC determined that the taxpayer would not have had a reasonable expectation of success with the project as a whole, unless new technological knowledge could be developed to address the infrastructure issues. The TCC concluded that it was reasonable for the taxpayer to determine that the uncertainties could not be resolved using standard procedures.

The TCC also considered the methodology adopted by the taxpayer and whether the scientific method applies differently in the context of software development versus other scientific fields. The TCC observed that software development tests may take many forms and can be executed thousands of times, making it difficult to keep records for every test conducted. However, the TCC ruled that even though the recordkeeping in the context of software development may be different from other scientific fields, it still constituted scientific method. The TCC concluded that in this case, the taxpayer did indeed adopt principles of scientific method since it systematically formulated and tested hypotheses to address the technological uncertainties that it encountered.

\(^1\)Paragraph (c) of the definition of “scientific research and experimental development in subsection 248(1) of the Act.
Perhaps most important, and consistent with a recent line of SR&ED cases (e.g., Les abeilles service de conditionement Inc. v The Queen, 2014 TCC 313, and 6379249 Canada Inc. v The Queen, 2015 TCC 77), the TCC reiterated that there is no legislation requiring contemporaneous documentation to justify the deduction of expenses. The TCC concluded that the documentation and the witnesses’ testimonies in this case were together sufficient to support the SR&ED claim.

As a result, the TCC allowed the taxpayer’s appeal. In addition, the taxpayer applied for enhanced costs and won (2016 DTC 1047).

**Lessons learned**

Quality contemporaneous documentation is always a taxpayer’s best defence to an SR&ED challenge by the CRA. However, this case is an important reminder that it is still possible for a taxpayer to support its claim by a combination of documentation and effective oral testimony.
Tax Alerts – Canada

Finance tables NWMM for 2016 budget measures and various technical changes – 2016 Issue No. 46

On 21 October 2016, federal Finance Minister Bill Morneau tabled a notice of ways and means motion (NWMM) that includes the draft legislative proposals that were released on 29 July 2016 relating to the remaining outstanding measures announced in the 2016 federal budget, as well as certain previously announced measures from the 2015 federal budget.

Publications and articles

Worldwide Personal Tax and Immigration Guide 2016-17

The 2016-17 edition of EY’s Worldwide Personal Tax and Immigration Guide (formerly titled the Worldwide Personal Tax Guide) is now available. The guide is written by the People Advisory Services network and covers the personal income tax, social security and immigration laws in 164 jurisdictions from Afghanistan to Zimbabwe. The content is updated through 1 July 2016, with exceptions noted.

Worldwide digital tax guide

This new guide offers a thought-provoking look at sector-specific digital business models in several diverse industries. In-country EY professionals identify known and emerging tax and law issues, insights and opportunities with those business models, specifically analyzing issues of nexus, indirect taxation and the landscape created by the OECD’s Base Erosion and Profit Shifting initiative.

This guide provides these insights for approximately 120 countries. It also connects readers to the EY subject-matter professionals in those countries who prepared the analysis, as well as to digital tax thought leadership.

2016 Worldwide Capital and Fixed Assets Guide

Newly available, EY’s 2016 Worldwide Capital and Fixed Assets Guide is a powerful tool for navigating the complex global web of fixed assets and depreciation. The guide summarizes the rules relating to tax relief on capital expenditures in 26 jurisdictions and territories.

EY’s Worldwide Estate and Inheritance Tax Guide 2016

EY’s Worldwide Estate and Inheritance Tax Guide summarizes the estate tax planning systems and describes wealth transfer planning considerations in 38 jurisdictions around the world, including Australia, Canada, China, France, Germany, Italy, the Netherlands, the UK and the US.

Online tax calculators and rates

Frequently referred to by financial planning columnists, our mobile-friendly calculators on ey.com let you compare the combined federal and provincial 2015 and 2016 personal tax bills in each province and territory. The site also includes an RRSP savings calculator and personal tax rates and credits for all income levels. Our corporate tax-planning tools include federal and provincial tax rates for small-business rate income, manufacturing and processing rate income, general rate income and investment income.

Tax insights for business leaders

Tax Insights provides deep insights on the most pressing tax and business issues. You can read it online and find additional content, multimedia features, tax publications and other EY Tax news from around the world.

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EY's Complete Guide to GST/HST, 2016 (24th) Edition
Editors: Jean-Hugues Chabot, Dalton Albrecht, Sania Ilahi, David Douglas Robertson

Canada's leading guide on GST/HST, including GST/HST commentary and legislation, as well as a GST-QST comparison. Written in plain language by a team of EY indirect tax professionals, the guide is consolidated to 15 July 2016 and updated to reflect the latest changes to legislation and CRA policy. Includes legislative and regulatory proposals released on 22 July 2016 and 29 July 2016 at the end of Volume 2.