***Canadian Tax Principles, 2022-2023* (Byrd/Chen)**

**Chapter 18 Partnerships**

18.1 Online Exercises

1) Under the provisions of the ITA, only individuals, corporations, and trusts are considered to be taxable entities and are required to file income tax returns. Given this, explain how the business income, capital gains, and property income of a partnership will be taxed.

Answer: There is a deeming rule applicable to partnerships that requires that it calculate business income, property income, and capital gains as if it was a person resident in Canada. Once these income and gain amounts are determined, they are allocated to the members of the partnership as per the terms of a partnership agreement or to be shared equally in the absence of an agreement. As the partners are taxable entities (e.g., individuals, corporations, or trusts) the allocated amounts will be included in their net income.

Type: ES

Topic: Partnerships - general rules & concepts

2) Briefly describe the three basic elements that are required for a partnership to exist.

Answer: The three elements are:

1. There must be two or more persons.

2. These persons must be carrying on a business in common.

3. The business must be carried on with a view to making a profit.

Type: ES

Topic: Partnerships - meaning of a partnership

3) Mr. Johns, Mr. Klien, and Ms. Langley are all Chartered Professional Accountants (CPAs) who trained in large national firms. However, for the last few years they have each carried on a business as a sole proprietor in their respective small private practices. They are currently discussing the possibility of forming a partnership to combine their practices. List four major points to be considered in the formation of a partnership and in drawing up a partnership agreement.

Answer: The points that could be listed here include:

• the initial and ongoing partner contributions and ownership percentage of each partner,

• the responsibilities of each partner and the division of work between the partners**,**

• how income and drawings will be allocated and the basis for how much compensation is to be paid,

• signing authority on the partnership bank accounts and required approval for purchases,

• procedures for bringing in new partners, and

• procedures to deal with the withdrawal, or the sale of the partnership business.

Type: ES

Topic: Partnerships - general rules & concepts

4) The degree to which partners have responsibility for partnership debts depends on the type of partnership. In terms of this responsibility, briefly describe the three types of partnerships that are discussed in your text.

Answer: The descriptions of the three basic types of partnerships are as follows:

**General Partnership -** In a general partnership, all partners have unlimited liability for partnership debts.

**Limited Partnership -** A limited partnership has at least one general partner who has unlimited liability for the debts of the partnership. Other partners, referred to as limited partners, are only responsible to the extent of their actual and promised contributions to the partnership.

**Limited Liability Partnership -** Members of limited liability partnerships have unlimited liability for most types of partnership debt. There is, however, an important exception. Members of limited liability partnerships are not personally liable for obligations arising from the wrongful or negligent action of:

• their professional partners; or

• the employees, agents or representatives of the partnership who are conducting partnership business.

Type: ES

Topic: Partnerships - three types of partnerships

5) Describe three factors that have been used to distinguish joint venture arrangements from partnership arrangements.

Answer: Factors that could be listed here include:

• co-venturers contractually do not have the power to bind other co-venturers;

• co-venturers retain ownership of property contributed to the undertaking;

• co-venturers are not jointly and severally liable for debt of the undertaking;

• co-venturers share gross revenues, not profits; and

• while partnerships may be formed for the same purpose as a joint venture, they are usually of longer duration and involve more than a single undertaking.

Type: ES

Topic: Partnerships vs joint ventures

6) What is the basic difference between how the ITA applies to partnerships vs joint ventures?

Answer: The basic difference is that, if an arrangement is considered to be a joint venture rather than a partnership, there will be no separate calculation of income at the entity level (e.g. partnership or joint venture). Each participant in the joint venture will determine their own income as it relates to that participation. In contrast, a partnership must determine its income as if it were a separate person. Once this is complete then an allocation of that partnership income can be made amongst the partners.

Type: ES

Topic: Partnerships vs joint ventures

7) What are the rules for determining the fiscal period that a partnership uses to determine its income?

Answer: The general rules are as follows:

• If any member of the partnership is an individual or a professional corporation, the partnership must use December 31 fiscal period.

• Otherwise, any fiscal period can be used as long as it does not end more than 12 months after it begins.

There is an exception to the calendar year requirement that allows the use of a non-calendar fiscal period in situations where all of the partnership members are individuals and an election is filed prior to the end of the partnership's first fiscal period.

Type: ES

Topic: Partnerships - general rules & concepts

8) CCA can only be claimed on depreciable property that is owned by a taxpayer. As a partnership is not a person and therefore not a taxpayer it would appear that it cannot own property however partnership law recognizes that a partnership can own property contributed to it or purchased with partnership property. In contrast members of a partnership are legally considered to own an interest in partnership property. Does this mean that both a partnership and its members can claim CCA?

Answer: There are rules in the Income Tax Regulations and in ITA 96(1) that ensure that members of a partnership cannot claim CCA and that any CCA claims are to be made by the partnership following the basic rule that considers it to be a person but only for the purpose of calculating income to be allocated to its members.

Type: ES

Topic: Partnerships - general rules & concepts

9) The various types of income earned in a partnership retain their character when allocated to the partners. Explain this statement.

Answer: Partnership income may include business income, property income (interest, dividends, rents), and/or capital gains. These amounts will be allocated to the partners as the same types of income. For example:

• When partnership dividend income is allocated to partners who are individuals, the allocated amounts will be subject to the usual gross up and tax credit procedures as if the individual partner received the dividend directly.

• When partnership capital gains are allocated to partners, only one-half of the allocated amount is a taxable capital gain.

Type: ES

Topic: Partnerships - general rules & concepts

10) In determining the business income of a partnership, how are salaries to the partners treated?

Answer: Partnership law does not permit a partnership to pay salaries to partners. As a result the CRA does not permit any claims for salary expenses to partners. Since such amounts are permitted as a deduction for accounting purposes a reconciliation adjustment is required when converting accounting income to income for ITA purposes. Any amounts paid to a partner as a quasi-salary is considered a priority allocation of business profits to that specific partner.

Type: ES

Topic: Partnerships - salary & other payments to partners

11) In reconciling accounting income to income for ITA purposes, is there a need to make an adjustment for drawings by partners?

Answer: Whether a reconciliation adjustment is required depends on how drawings were treated for accounting purposes If drawings were deducted in determining accounting income then the drawings will have to be added back when reconciling to income for ITA purposes. If drawings have not been deducted then no adjustment is required.

Type: ES

Topic: Partnerships - reconciling accounting & income for ITA purposes

12) Partnerships sometimes make donations to registered charities. How are partnership donations treated for income tax purposes?

Answer: Charitable donations are allocated to the partners often in the same manner as the allocation of income or loss. In that sense individual partners will be able to claim a personal tax credit whereas corporate members would be able to claim a taxable income deduction. In terms of accounting based adjustments since accounting rules allow donations to be expensed an adjustment to reverse that effect would be required in the reconciliation process.

Type: ES

Topic: Partnerships - general rules & concepts

13) An individual member of a partnership, because of income tax losses on certain investments, would like to maximize partnership income. To this end, the individual has asked that no CCA be deducted from the individual's share of the partnership income. Can the other partners agree to this request?

Answer: The income tax rules concerning depreciable property restrict the claiming of CCA to the partnership as if the partnership were the owner of the property. This means that the partnership business income is determined applying the regular rules of the ITA that establishes the business income net of all expenses. It is this net amount that is then allocated to partners. As as result the request of the individual partner would not be allowed.

Type: ES

Topic: Partnerships - general rules & concepts

14) Describe the treatment of capital gains in the conversion of accounting income to business income for income tax purposes of a partnership.

Answer: Accounting net income will include gains on the sale of capital property as calculated under ASPE or IFRS (GAAP) as the difference between the sales price and the carrying value for accounting purposes. The accounting gain is unique to accounting and must be reversed in the reconciliation process by deducting the gain. The taxable capital gain would then be added in the reconciliation process.

Type: ES

Topic: Partnerships - reconciling accounting & income for ITA purposes

15) If the partnership agreement does not specify how business profits will be shared, how will the profit allocation be determined?

Answer: In the absence of a provision in the partnership agreement, partnership law will require that business profits or losses be shared equally.

Type: ES

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

16) An individual wishes to become a member of an existing partnership. What are this individual's alternatives for acquiring an interest?

Answer: There are two ways the interest can be acquired:

• The interest can be acquired directly by purchasing part or all of the interest from a current partner or partners.

• The interest can be acquired directly from the partnership by contributing property (including cash) to the partnership. The consideration for the interest in the partnership would be the difference between the FMV of the consideration given to the partnership minus the FMV of any partnership property given to the incoming partner.

Type: ES

Topic: Partnerships - becoming a partner

17) In determining the ACB of a partnership interest, briefly describe the treatment of each of the following:

• capital contributions,

• a partner's share of partnership business income, and

• partner drawings.

Answer: The treatment of each of the items is as follows:

**Capital Contributions -** Capital contributions are added to the ACB of the partnership interest at the time the contribution is made.

**Partner's Share of Partnership Business Income -** Each partner's share of partnership business income is added to the partner's ACB on the first day of the fiscal period following the fiscal period in which the income was earned.

**Partner's Drawings -** Partner's drawings are subtracted from the ACB of the partnership interest at the time the drawings are made.

Type: ES

Topic: Partnerships - the ACB of a partnership interest

18) Describe the treatment of partnership capital gains in the determination of a partner's income and the impact on the ACB of the partnership interest.

Answer: One-half of a partner's share of the partnership's capital gains will be included in the income of the partner based on the fiscal period of the allocation. The partner's share of the partnership's capital gains (i.e. 100%) will be added to the ACB of the partnership interest on the first day of the following fiscal period.

Type: ES

Topic: Partnerships - the ACB of a partnership interest

19) Describe the treatment of partnership taxable dividends in the determination of an individual partner's income and the impact on the ACB of the partnership interest.

Answer: The partner's share of the partnership dividends will be included in income based on the fiscal period of the partnership in which the dividends are received. Partners who are individuals will gross up the allocated taxable dividend and are entitled to a dividend credit against income tax payable in the same manner as if the taxable dividends had been received directly. The partner's share of the partnership dividends will be added to the ACB of the partnership interest on the first day of the following fiscal period of the partnership. This amount will not include the gross up.

Type: ES

Topic: Partnerships - the ACB of a partnership interest

20) Adjustments to the ACB of a partnership interest can sometimes result in a "negative" ACB. What are the income tax consequences of this to the affected partner?

Answer: The negative amount will be treated as a capital gain to the partner the moment it occurs. An ACB adjustment follows immediately to restore the ACB to nil. This treatment does not apply to every partner however but is generally restricted to most limited partners and to inactive general partners.

Type: ES

Topic: Partnerships - negative ACB

21) What is a limited partnership? Your answer should include the meaning of a "limited partner".

Answer: A limited partnership is one that has at least one limited partner and one general partner. As defined in most provincial or territorial partnership legislation, a limited partner is one whose liability for the debts of a partnership is limited to the amount of the persons' contribution (actual and promised) to the partnership. This limited liability limitation however can be lost if the partner participates in the management of the partnership. A partner whose liability is limited under partnership law is considered a limited partner for income tax purposes.

Type: ES

Topic: Partnerships - limited partnerships & limited partners

22) What is the objective of the "at-risk" rules that apply to limited partnerships?

Answer: The at-risk rules are designed to ensure that a limited partner does not receive tax deductions or tax credits that exceed the amount that the limited partner has "at risk". In very simplified terms, the "at risk" amount is the amount of the partner's actual investment, not including amounts owed to the limited partnership or amounts that are designed to reduce the partner's risk (e.g., a guarantee to refund part or all of the amount invested).

Type: ES

Topic: Partnerships - the at-risk rules

23) What is a "Canadian Partnership" and what is its relevance for Canadian income tax purposes?

Answer: A Canadian partnership is defined in ITA 102(1) as follows:

"Canadian partnership" means a partnership all of the members of which were, at any time in respect of which the expression is relevant, resident in Canada.

Many partnership rollover rules only apply if the partnership qualifies as a Canadian partnership.

Type: ES

Topic: Partnerships - "Canadian Partnerships" ITA 102(1)

24) Briefly describe the tax planning steps required to incorporate a partnership on a rollover basis.

Answer: The incorporation of a partnership requires the use of two rollovers. The first (under ITA 85(2)), allows eligible partnership property to be transferred to a taxable Canadian corporation using the rules of ITA 85(1), for either shares or a combination of shares and other consideration. The transfer can take place at elected amounts equal to the tax cost of partnership property as long as the elective ranges are within what is permissible under ITA 85(1).

At this point, the partnership continues to exist with the same partners and the partnership owns shares in the corporation. Technically the business of the partnership would have been incorporated at this stage. The second rollover (under ITA 85(3)) involves the winding up and dissolution of the partnership which distributes the property it owns (e.g. the shares of the corporation) to the partners in return for their partnership interests. At the end of the planning the former partners become shareholders of a corporation which continues the former partnership business and other partnership activity.

Type: ES

Topic: Partnerships - incorporating a partnership (ITA 85(2) & (3))

25) A partnership is not a taxable entity, either for income tax purposes or for GST/HST purposes.

Answer: FALSE

Explanation: While partnerships are not taxable entities for income tax purposes, they are taxable entities for GST/HST purposes.

Type: TF

Topic: Partnerships - general rules & concepts

26) From the point of view of determining an individual's income tax payable, it does not matter whether the individual is a partner or a joint venturer.

Answer: FALSE

Explanation: Participants in joint ventures may have a significantly different income tax payable than would be the case if they were considered to be partners.

Type: TF

Topic: Partnerships vs joint ventures

27) If all of the members of a partnership are individuals, the partnership can use a non-calendar fiscal period.

Answer: TRUE

Type: TF

Topic: Partnerships - general rules & concepts

28) When dividends received by a partnership are allocated to individual partners, these partners will gross up the amount received and be eligible for a dividend tax credit.

Answer: TRUE

Type: TF

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

29) If a partnership pays interest to partners on their capital contributions, the payments can be deducted in determining the business income of the partnership.

Answer: FALSE

Explanation: Interest on capital contributions cannot be deducted. They are generally considered a method to allocate business profits.

Type: TF

Topic: Partnerships - salary & other payments to partners

30) If a partnership sells depreciable property used in a business and there is recapture, this amount will be included in the business income that is allocated to the partners.

Answer: TRUE

Type: TF

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

31) Partnership income that is allocated to partners will retain its income nature (e.g., the partnership's capital gains will be passed to the partners as capital gains).

Answer: TRUE

Type: TF

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

32) In computing a partnership's business income, salaries paid to the partners can only be deducted if they are reasonable.

Answer: FALSE

Explanation: Salaries paid to partners are never deductible. They are generally considered a method of allocating business profits.

Type: TF

Topic: Partnerships - salary & other payments to partners

33) In computing a partnership's business income, the amount that can be claimed as CCA follows the very same rules that apply to taxpayers that are individuals, trusts and corporations.

Answer: TRUE

Type: TF

Topic: Partnerships - general rules & concepts

34) In computing a partnership's business income, charitable donations made by the partnership should be deducted as a business expense.

Answer: FALSE

Explanation: Charitable donations are allocated to the partners on the basis of the partnership agreement. Donations are not a business expense.

Type: TF

Topic: Partnerships - general rules & concepts

35) Only one-half of any partnership capital gains that are allocated to partners will be added to the ACB of a partnership interest.

Answer: FALSE

Explanation: While only one-half of allocated capital gains will be included in a partner's income, 100% of the capital gains are added to the ACB of a partnership interest.

Type: TF

Topic: Partnerships - the ACB of a partnership interest

36) In determining the at-risk amount for a partner, positive amounts of partnership income allocations for the year are added to the opening balance of the partner's ACB.

Answer: TRUE

Type: TF

Topic: Partnerships - the at-risk rules

37) When a capital property is transferred from an existing Canadian partnership to a new Canadian partnership, any capital gain or recapture from the disposition will be considered income of the existing partnership.

Answer: FALSE

Explanation: A rollover treatment is available where all of the property of a Canadian partnership that has ceased to exist is transferred to a new Canadian partnership. A further condition is that all of the members of the new partnership must have been members of the old partnership (ITA 98(6)).

Type: TF

Topic: Partnerships - rollover to a new partnership (ITA 98(6))

38) Which of the following statements is correct with respect to partnerships?

A) At least one of the partners must be an individual.

B) Limited partners cannot participate in the management of the partnership.

C) Partnerships are not required to have a profit motive.

D) The use of a partnership will allow the partners to pay higher salaries to family members.

Answer: B

Explanation: B) Limited partners cannot participate in the management of the company.

Type: MC

Topic: Partnerships - general rules & concepts

39) Which of the following is **NOT** a basic feature required to create a partnership?

A) One of the partners must be an individual.

B) There must be two or more persons involved.

C) The persons must be carrying on a business in common.

D) The business must be carried on with a profit motive.

Answer: A

Explanation: A) One of the partners must be an individual.

Type: MC

Topic: Partnerships - meaning of a partnership

40) Which of the following statements about limited partners is **NOT** correct?

A) They are entitled to share equally in profits and losses, unless there is an agreement to the contrary.

B) They are jointly and severally liable for partnership debt and wrongful acts of other partners.

C) They are not responsible for the wrongful acts of other partners, except to the extent of their actual and promised contributions to the partnership.

D) Property that they contribute to the partnership is considered partnership property.

Answer: B

Explanation: B) Partners are jointly and severally liable for partnership debt and wrongful acts of other partners.

Type: MC

Topic: Partnerships - limited partnerships & limited partners

41) What advantage is offered by a general partnership, as compared to a corporation, as a form of carrying on a business?

A) Partners may be able to reduce their personal income tax if the business has losses.

B) Higher salaries can be paid to family members and claimed as an expense.

C) Creditors cannot seize a partner's personal property to cover partnership debt.

D) Partners will be able to defer income taxes on income that is left within the partnership and not distributed.

Answer: A

Explanation: A) Partners may be able to reduce their personal income taxes if the business has losses.

Type: MC

Topic: Partnerships - general rules & concepts

42) Jesse and Harold decide to form a partnership. They believe that this arrangement will have the following advantages:

1. They may be able to reduce their personal income taxes during the start-up years when there are losses.

2. They may be able to split income with family members who are employed by the business.

3. They may be able to realize a tax deferral on their business income.

4. They will have limited personal liability for the debts of the business.

All of these statements are correct except:

A) 1 and 3.

B) 2 only.

C) 3 and 4.

D) 1 and 2.

Answer: C

Explanation: C) 3 and 4.

Type: MC

Topic: Partnerships - general rules & concepts

43) Which of the following statements regarding partnerships and joint ventures is correct?

A) Joint ventures are taxable entities for both income tax and GST/HST purposes.

B) Both partners and joint venturers have the ability to contractually bind other partners and joint venturers.

C) For both partnerships and joint ventures, all participants must claim the same CCA amount.

D) Partners share the profit of the partnership and joint venturers share the gross revenues of the joint venture.

Answer: D

Explanation: D) While partners share the profit of the partnership, joint venturers share the gross revenues of the joint venture.

Type: MC

Topic: Partnerships vs joint ventures

44) The distinguishing factor that makes an arrangement a co-ownership as opposed to a partnership would be:

A) when profits or losses are accounted for separately for each participant.

B) when profits or losses are split equally.

C) when participants do not have the power to bind other participants.

D) when gross revenue is shared, rather than profits.

Answer: A

Explanation: A) when profits or losses are accounted for separately for each participant.

Type: MC

Topic: Partnerships vs co-ownership arrangements

45) A joint venture might be recognized because it would demonstrate one of the following factors.

A) The joint venture will own all property that co-venturers have contributed to the venture.

B) Co-venturers are jointly and severally liable for activities of the undertaking.

C) Co-venturers share profits not gross revenues.

D) Co-venturers do not have the power to bind other co-venturers contractually.

Answer: D

Explanation: D) Co-venturers do not have the power to bind other co-venturers contractually.

Type: MC

Topic: Partnerships vs joint ventures

46) A group of unrelated insurance companies combine forces to underwrite a very high-risk insurance policy. What is the general nature of the type of arrangement?

A) A partnership.

B) A co-ownership.

C) A joint venture.

D) A syndicate.

Answer: D

Explanation: D) A syndicate.

Type: MC

Topic: Partnerships - general rules & concepts

47) Martin Aggerwal has a 30% interest in a partnership. During the current year, the partnership realized capital gains of $42,000, received non-eligible dividends of $15,000, and made charitable donations of $6,000. Martin has made no charitable donations personally. He has no income that will be subject to the 33% federal income tax rate. Which of the following statements is correct?

A) Martin will have taxable capital gains of $6,300, a federal dividend tax credit of $467, and a charitable donations tax credit of $494.

B) Martin will have taxable capital gains of $12,600, a federal dividend tax credit of $467, and a charitable donations tax credit of $522.

C) Martin will have capital gains of $6,300, a federal dividend tax credit of $933, and a charitable donations tax credit of $494.

D) Martin will have taxable capital gains of $6,300, a federal dividend tax credit of $467, and a charitable donations tax credit of $522.

Answer: A

Explanation: A) Martin will be allocated charitable donations of $1,800 [(30%)($6,000)]. He will have the following amounts as a result of his 30% partnership interest:

• taxable capital gains of [(30%)(1/2)($42,000)] $6,300

• a federal dividend tax credit of [(30%)(9/13)(15%)($15,000)] $ 467

• a charitable donations tax credit of

[(15%)($200) + (29%)($1,800 - $200)] $ 494

Type: MC

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

48) The Bartlo Partnership has accounting income for the fiscal period ending December 31, 2022 of $490,000. As per the partnership agreement, this amount has been determined under ASPE. The agreement also calls for each of the two partners to have an equal share in the income. The following amounts are included in the calculation of this accounting income:

• Non-eligible dividends received of $32,000

• Gains on the sale of shares of $96,000

• Charitable donations of $12,000

• Amortization on equipment of $49,000 (equal to CCA)

The two partners will each have 2022 income allocated from the partnership of:

A) $227,000.

B) $229,400.

C) $223,400.

D) $245,000.

Answer: B

Explanation: A) $227,000 = [50%][($490,000 - (50%)($96,000) + $12,000]

B) $229,400 {[50%][$490,000 + (15%)($32,000) - (1/2)($96,000) + $12,000]}.

C) $223,400 = [50%][($490,000 + (15%)($32,000) - (50%)($96,000)

D) $245,000 [(50%)($490,000)

Type: MC

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

49) The Keisha Partnership has determined that business income for the 2022 fiscal period was $130,000. Ms. Kerry holds a 50% interest in the partnership. Her drawings from the partnership in 2022 totalled $45,000. In addition, Ms. Kerry has made the following business related expenditures personally: meals and entertainment of $5,000; business related automobile costs of $3,500; charitable donations of $3,000. What will her business income be for the 2022 taxation year?

A) $45,000

B) $56,000

C) $59,000

D) $65,000

Answer: C

Explanation: A) $45,000 [drawings]

B) $56,000 [(50%)($130,000) — (50%)($5,000) - $3,500 - $3,000)]

C) $59,000 [(50%)($130,000) — (50%)($5,000) - $3,500)]

D) $65,000 [ (50%)($130,000)]

Type: MC

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

50) Mr. Poulet is a partner in a partnership with a December 31 fiscal period. Mr. Poulet's share of the partnership allocations for 2022 are as follows:

• business income of $120,000

• charitable donations of $1,500

• partnership draws totalling $100,000

Mr. Poulet's partnership interest had an ACB on January 1, 2022 of $222,000. What is the ACB on January 1, 2023?

A) $120,500

B) $240,500

C) $242,000

D) $243,500

Answer: B

Explanation: A) $222,000 - $1,500 - $100,000 = $120,500

B) $222,000 + $120,000 - $1,500 - $100,000 = $240,500

C) $222,000 + $120,000 - $100,000 = $242,000

D) $222,000 + $120,000 + $1,500 - $100,000 = $243,500

Type: MC

Topic: Partnerships - the ACB of a partnership interest

51) Which one of the following statements related to partnerships is **NOT** correct?

A) Dividends received by a partnership are not grossed up by the partnership in the calculation of partnership income.

B) Charitable donations made by a partnership are not deductible by the partnership.

C) Business losses of a partnership cannot be allocated to the partners for them to deduct against other income.

D) Salaries to partners are not deductible by the partnership in the computation of partnership income.

Answer: C

Explanation: C) Business losses of a partnership cannot be allocated to the partners for them to deduct against other income.

Type: MC

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

52) Christine would like to calculate the ACB of her partnership interest. She should include all of the following adjustment in the calculation except for her share of the:

A) capital gains which the partnership realized during the year.

B) charitable donations made during the year by the partnership.

C) business loss of the partnership for the year.

D) dividend gross up on dividends received by the partnership in the year.

Answer: D

Explanation: D) dividend gross up on dividends received by the partnership in the year.

Type: MC

Topic: Partnerships - the ACB of a partnership interest

53) Joe Conners is a member of a partnership with a December 31 fiscal period. Joe's share of the 2022 partnership allocations are as follows:

• Business Loss of $25,000.

• Charitable Donations of $1,000.

Joe withdrew $10,000 from the partnership in 2022. Joe's ACB at January 1, 2022 was $59,000. What is the ACB of Joe's partnership interest on January 1, 2023?

A) $23,000.

B) $24,000.

C) $25,000.

D) $33,000.

Answer: A

Explanation: A) The ACB of Joe's partnership interest is $23,000, calculated as follows:

Opening ACB $59,000

Drawings ( 10,000)

Share of Business Loss ( 25,000)

Share of Charitable Donations ( 1,000)

ACB - January 1, 2023 $23,000

Type: MC

Topic: Partnerships - the ACB of a partnership interest

54) Ms. Sarah McLean has a 50% interest in a partnership that was acquired on January 1, 2022 at a cost of $40,000. The partnership's business income for income tax purposes for the fiscal period ending December 31, 2022 was $50,000, an amount that included a CCA deduction of $36,000. The 2022 business income did not include taxable capital gains of $10,000 realized by the partnership. In 2022, Ms. McLean withdrew $15,000 from the partnership. The ACB of Ms. McLean's partnership interest at January 1, 2023 is:

A) $55,000.

B) $88,000.

C) $50,000.

D) $60,000.

Answer: D

Explanation: D) The ACB of Sarah's partnership interest is $60,000, calculated as follows:

Opening ACB $40,000

Drawings ( 15,000)

Share of Business Income - No CCA Adjustment

[(50%)($50,000)] 25,000

Share of Capital Gains [(50%)(2)($10,000)] 10,000

ACB - January 1, 2023 $60,000

Type: MC

Topic: Partnerships - the ACB of a partnership interest

55) Femi and Fola are sisters who are partners in the Double F Partnership, each with a 50% interest. They wish to bring their brother, Faraji into the partnership on January 1, 2022, with a 20% interest. Faraji will pay $15,000 to each of his sisters in order to purchase 20% of each of their 50% interests. On January 1, 2022, Femi and Fola each have partner capital accounts with a balance of $50,000, which is equal to their ACB. Which of the following statements describes the income tax consequences to Femi and Fola of admitting their brother to the partnership?

A) Each sister will have a taxable capital gain of $2,500.

B) Each sister will have their partner capital account balance and ACB reduced to $35,000.

C) Each sister will have a taxable capital gain of $7,500.

D) There will be no income tax consequences to the two sisters.

Answer: A

Explanation: A) Each sister will have a taxable capital gain of $2,500. [1/2][POD $15,000 — ACB (20%)($50,000)]

Type: MC

Topic: Partnerships - the sale of a partnership interest

56) Jabari becomes a 40% interest partner in an accounting partnership on January 1, 2022. During the fiscal period ended December 31, 2022, the partnership business earns income of $200,000 for accounting purposes. In arriving at this income, the bookkeeper deducted meals and entertainment costs of $20,000, and a charitable donation of $5,000. Jabari withdraws $50,000 from the partnership in 2022. As of January 1, 2023, the ACB of his partnership interest will have increased by:

A) $30,000.

B) $38,000.

C) $34,000.

D) $24,000.

Answer: C

Explanation: A) $30,000. [($200,000)(40%) - $50,000]

B) $36,000. [($215,000 + $5,000)(40%) - $50,000]

C) $34,000. [($215,000 - $5,000)(40%) - $50,000]

Business income of the partnership for income tax purposes is $215,000 {[$200,000 + (1/2)($20,000) + $5,000]}. Jabari's 40% share of the income is reduced by his share of the charitable donation and 100% of his withdrawals. [(40%)($215,000) - $50,000 - (40%)($5,000)] = $34,000

D) $24,000. {[$200,000 - (1/2)($20,000) - $5,000][40%] - $50,000}

Type: MC

Topic: Partnerships - the ACB of a partnership interest

57) Kasinda is a partner in Twins Partnership. At January 1, 2022, the ACB of her 25% partnership interest is $35,000. In 2022, she withdraws $85,000 from the partnership. In 2022, the partnership has business income for income tax purposes of $400,000. What is the ACB of her partnership interest on December 31, 2022, and what income tax consequences will result from the transactions during the year?

A) The ACB of her partnership interest on December 31, 2022 is nil. Because Kasinda has withdrawn more than her ACB from the partnership, she will report a taxable capital gain of $25,000. She will also include $100,000 of business income for 2022.

B) The ACB of her partnership interest on December 31, 2022 is $50,000. Kasinda will include partnership business income of $100,000 for 2022.

C) The ACB of her partnership interest on December 31, 2022 is nil. Kasinda will also include business income of $100,000 for 2022.

D) The ACB of her partnership interest on December 31, 2022 is negative $50,000. Because Kasinda has withdrawn more than her ACB from the partnership, she will have to include partnership business income of $50,000 in 2022.

Answer: C

Explanation: A) She will include a taxable capital gain of $25,000 and business income of $100,000 [ $25,000 = (1/2)($85,000 - $35,000); $100,000 = (25%)($400,000)]

B) The ACB is $50,000. Kasinda will include partnership business income of $100,000. [ $50,000 = ((1/2)($85,000 - $35,000) + $ 100,000) ; $100,000 = (25%)($400,000)]

C) The ACB is nil. Kasinda will include partnership business income of $100,000. [$100,000 = (25%)($400,000)]

D) The ACB is negative $50,000. Because Kasinda has withdrawn more than her ACB from the partnership, she will include partnership business income of $50,000. [($50,000) = ($85,000 - $35,000); $50,000 = (25%)($400,000) - $50,000]

Type: MC

Topic: Partnerships - allocations & the ACB of the partnership interest

58) Red Bush and Green Tree are equal partners in Arbor Partnership. Each partner has contributed capital of $60,000 to the partnership and this is also the current ACB and FMV of their partnership interests. Blue Grass will join the partnership as an equal partner. Which of the following statements is correct?

A) Blue Grass will pay $20,000 directly to each of the original partners and the ACB of the partnership interest of Red Bush and Green Tree will decrease by $20,000 each.

B) Blue Grass will pay $30,000 directly to each of the original partners and the ACB of the partnership interest of Red Bush and Green Tree will decrease by $30,000 each.

C) Blue Grass will pay $40,000 directly to the partnership and the ACB of the partnership interest of Red Bush and Green Tree will increase by $20,000 each.

D) Blue Grass will pay $40,000 directly to the partnership and the ACB of the partnership interest of Red Bush and Green Tree will decrease by $20,000 each.

Answer: A

Explanation: A) If Blue Grass pays $20,000 directly to each of the original partners, the ACB of the partnership interest of both Red Bush and Green Tree would decrease by $20,000 each. Each partner is selling one third of their $60,000 interest. This will reduce their ACB by $20,000 [(1/3)($60,000)]. This is considered a partial disposition or property (ITA 43).

Type: MC

Topic: Partnerships - becoming a partner

59) Which one of the following items does **NOT** affect the calculation of the ACB of a partnership interest?

A) The non-allowable portion of a capital loss on the sale of partnership property.

B) Dividends received by the partnership.

C) Interest on funds borrowed by a partner to make a capital contribution.

D) A charitable donation made by the partnership.

Answer: C

Explanation: C) Interest on funds borrowed by a partner to make a capital contribution.

Type: MC

Topic: Partnerships - the ACB of a partnership interest

60) On January 1, 2022, Barry Score acquires a 25% interest in a limited partnership for $200,000. Barry pays an immediate deposit of $50,000 with the balance owing due in 2024. For the fiscal period ending December 31, 2022, the partnership determines that it has a $40,000 capital gain and a $100,000 business loss. What is Barry's at-risk amount?

A) $30,000.

B) $200,000.

C) $60,000.

D) $55,000.

Answer: C

Explanation: A) $30,000 [$200,000 + (25%)(50%)($40,000) - (25%)($100,000) - ($200,000 - $50,000)]

B) $200,000

C) $60,000 [$200,000 + (25%)($40,000) - ($200,000 - $50,000)]

D) $55,000 [$200,000 + (25%)(50%)($40,000) - ($200,000 - $150,000)]

Type: MC

Topic: Partnerships - the at-risk amount (ARA)

61) Which of the following partners is **NOT** a limited partner?

A) Mayumi, a partner in an engineering firm, entitled to 50% of the profits and responsible for 50% of losses.

B) Guan, a partner in an accounting firm with a guarantee that his partnership interest will be purchased by the other partners for a guaranteed minimum price of $150,000.

C) Ekatarina, a partner in a law firm who is only responsible for the first $50,000 of partnership losses.

D) Danyal, a partner in a construction company, who is reimbursed for any partnership losses by one of the other partners.

Answer: A

Explanation: A) Mayumi, a partner in an engineering firm, entitled to 50% of the profits and responsible for 50% of losses. This is the only choice where the partner does not have some type of special guarantee from the partnership that limits their financial risk.

Type: MC

Topic: Partnerships - limited partnerships & limited partners

62) Which of the following statements best reflects the tax policy objective of the at-risk rules?

A) The objective of the rules is to encourage investment in high-risk ventures.

B) The objective of the rules is to prevent taxpayers from receiving tax deductions or tax credits in excess of the amount that they are in a position to lose on their investment.

C) The objective of the rules is to protect investors from the losses they can incur on their investments in high risk partnerships.

D) The objective of the rules is to discourage investment in high-risk ventures.

Answer: B

Explanation: B) The objective of the rules is to prevent taxpayers from receiving tax deductions or tax credits in excess of the amount that they are in a position to lose on their investment.

Type: MC

Topic: Partnerships - the at-risk amount (ARA)

63) Arnold is a partner in the Polar Partnership. He has some vacant land that is capital property that is situated in a perfect location for a building the partnership wants to construct. He sells the land to the partnership for $155,000 in cash. The land cost him $95,000 and has a FMV of $140,000. What is the effect on the ACB of his partnership interest?

A) An increase of $155,000.

B) A decrease of $15,000.

C) An increase of $15,000.

D) A decrease of $60,000.

Answer: B

Explanation: B) A decrease of $15,000 ($155,000 - $140,000).

Type: MC

Topic: Partnerships - sale of property from a partner to a partnership (ITA 97(1))

64) Aba has just become a partner of the Thursday Partnership. She has a pick up truck which she previously used in her own gardening business and which would be useful to the partnership. She uses the pick-up truck as a capital contribution. The truck cost her $45,000, has a UCC of $28,000 and a FMV of $35,000. The other partner can only contribute cash of $30,000, so the partnership pays Aba $5,000 in cash to keep the initial contributions equal. What are the income tax consequences of this transaction?

A) Aba will have disposed of the truck for $35,000 resulting in recapture.

• The ACB of her partnership interest will be $35,000.

• The partnership will have acquired the truck for $35,000.

B) Aba will have disposed of the truck for $30,000 resulting in recapture.

• The ACB of her partnership interest will be $30,000.

• The partnership will have acquired the truck for $30,000.

C) Aba will have disposed of the truck for $35,000 resulting in recapture.

• The ACB of her partnership interest will be $30,000.

• The partnership will have acquired the truck for $35,000.

D) Aba will have disposed of the truck for $30,000 resulting in recapture.

• The ACB of her partnership interest will be $35,000.

• The partnership will have acquired the truck for $30,000.

Answer: C

Explanation: C) Aba will have disposed of the truck for $35,000 resulting in recapture of $7,000. The ACB of her partnership interest will be $30,000. The partnership will have acquired the truck for $35,000. ITA 97(1) deems this FMV result. The $5,000 paid in cash is effectively treated as drawings which reduces the ACB of her partnership interest to $30,000.

Type: MC

Topic: Partnerships - sale of property from a partner to a partnership (ITA 97(1))

65) Aissa has just become a partner of the Gratitude Partnership. She has some vacant land that is capital property and that is in a perfect location for a building the partnership wants to construct. As her initial capital contribution, she sells the land to the partnership. The land cost her $45,000 and has a FMV of $95,000. No consideration is received other than an interest in the partnership. What are the income tax consequences of this transaction?

A) Aissa will have disposed of the land for its original cost of $45,000.

• The ACB of her partnership interest will be $45,000.

• The partnership will have acquired the land for $45,000.

B) Aissa will have disposed of the land for $95,000 resulting in a taxable capital gain of $25,000.

• The ACB of her partnership interest will be $95,000.

• The partnership will have acquired the land for $95,000.

C) Aissa will have disposed of the land for $95,000 resulting in a taxable capital gain of $25,000.

• The ACB of her partnership interest will be $70,000.

• The partnership will have acquired the land for $70,000.

D) Aissa will have disposed of the land for $45,000.

• The ACB of her partnership interest will be $95,000.

• The partnership will be considered to have acquired the land for $95,000.

Answer: B

Explanation: B) Aissa will have disposed of the land for $95,000 resulting in a taxable capital gain of $25,000. The ACB of her partnership interest will be $95,000. The partnership will have acquired the land for $95,000.

Type: MC

Topic: Partnerships - sale of property from a partner to a partnership (ITA 97(1))

66) The Happy Endings Partnership distributes land that is partnership capital property to Chata, a partner with a 35% interest in the partnership. Chata makes no payment to the partnership. The partners share of income and capital gains is equal to the percentage interest in the partnership. The ACB of the land is $62,000 and the FMV $88,000. What will the net effect of the distribution on the ACB of Chata's partnership interest?

A) A decrease of $62,000.

B) A decrease of $78,900.

C) A decrease of $83,450.

D) A decrease of $88,000.

Answer: B

Explanation: A) A decrease of $62,000. [($88,000-$62,000)-$88,000]

B) A decrease of $78,900. [(35%)($88,000-$62,000)-$88,000]

C) A decrease of $83,450. [(35%)(1/2)($88,000-$62,000)-$88,000]

D) A decrease of $88,000. [the FMV of the land]

Type: MC

Topic: Partnerships - sale of property from a partnership to a partner (ITA 98(2))

67) Which of the following property can be sold by a partner to a Canadian partnership under ITA 85(2), but cannot be sold to a taxable Canadian corporation under ITA 85(1)?

A) Inventory of goods for resale.

B) Vacant land.that is capital property.

C) Real property inventory.

D) Non-depreciable capital property which has declined in value since being purchased.

Answer: C

Explanation: C) Real property inventory.

Type: MC

Topic: Partnerships - incorporating a partnership (ITA 85(2) & (3))

68) During the fiscal period ending December 31, 2022, WIN Partnership has business income of $80,000, capital gains of $23,000, and receives eligible dividends of $8,500. Sally Winters has a 40% interest in partnership income and capital gains. In 2022, Sally withdraws $25,000 from the partnership.

Determine the income tax consequences for Ms. Winters for the 2022 taxation year.

Answer: The following amounts would be added to Ms. Winter's 2022 net income:

Business Income [(40%)($80,000)] $32,000

Taxable Capital Gains [(40%)(1/2)($23,000)] 4,600

Eligible Dividends [(40%)($8,500)] 3,400

Gross Up [(38%)($3,400)] 1,292

Total Partnership Income $41,292

In addition Ms. Winters would be eligible for a federal dividend tax credit of $705 [(6/11)($1,292)]. The fact that she withdrew $25,000 during the year has no consequences with respect to income or capital gains but will result in a reduction in the ACB of her partnership interest.

Type: ES

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

69) James Bonner is one of four brothers who have formed a partnership. They each have a 25% interest in the partnership.

During the fiscal period ending December 31, 2022, the partnership has the following income and capital gains:

Business Income $140,000

Capital Gains 18,000

Eligible Dividends 41,000

In 2022, James withdraws $15,000 in cash from the partnership.

Determine the income tax consequences for James for the 2022 taxation year.

Answer: The following amounts would be added to Mr. Bonner's 2022 net income:

Business Income [(25%)($140,000)] $35,000

Taxable Capital Gains [(25%)(1/2)($18,000)] 2,250

Eligible Dividends [(25%)($41,000)] 10,250

Gross Up [(38%)($10,250)] 3,895

Total Partnership Income $51,395

In addition Mr. Bonner would be eligible for a federal dividend tax credit of $2,125 [(6/11)($3,895)]. The fact that he withdrew $15,000 during the year has no consequences with respect to income or capital gains but will result in a reduction in the ACB of his partnership interest.

Type: ES

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

70) The ID Partnership has two partners. Partner I, who is actively managing the partnership and receives an annual salary of $42,000 as a result. Because Partner D has contributed most of the capital for the business, an interest allocation of $17,000 is made to recognize the capital contributions. The partnership agreement calls for the remaining profits, and all other allocations, to be split 55% to I and 45% to D. The salary and interest amounts are deducted in the determination of accounting income and withdrawn by the partners during the course of the year.

During the fiscal period ending December 31, 2022, the partnership's accounting income is $312,000. Other relevant information is as follows:

• The accountant deducted amortization of $41,000. Maximum CCA is $63,000.

• Accounting income includes a deduction for charitable donations of $4,200.

• Accounting income includes a gain on the sale of land of $31,000.

Determine the amounts of business income for income tax purposes that will be allocated to Partner I and Partner D for the 2022 taxation year.

Answer: The ID Partnership's Business Income would be calculated as follows:

Accounting Income $312,000

Add:

Salary to I $42,000

Interest to D 17,000

Amortization Expense 41,000

Donations 4,200 104,200

$416,200

Deduct:

Maximum CCA ($63,000)

Accounting Gain on sale of Land ( 31,000) ( 94,000)

2022 Business Income $322,200

Priority Allocations for Salaries and

Interest ($42,000 + $17,000) ( 59,000)

Residual to be allocated 55:45 $263,200

The allocation of the 2022 business income for each partner would be as follows:

**Partner I Partner D**

Priority allocation for Salary $ 42,000 N/A

Priority allocation for Interest N/A $17,000

Allocation of Residual

[(55%)($263,200)] 144,760

[(45%)($263,200)] 118,440

2022 Business Income Allocation $186,760 $135,440

While not required, you might note that a taxable capital gain of $15,500 [(1/2)($31,000)], as well as the charitable donations of $4,200, would be allocated to the partners on a 55:45 basis.

Type: ES

Topic: Partnerships - comprehensive problem business income allocation (includes reconciliation from accounting)

71) The Keisha Partnership has income for accounting purposes for the fiscal period ended December 31, 2022 of $625,000. The two partners have an equal share in this income. The following amounts have been included in the calculation of accounting income:

Meals and Entertainment Expenses $32,000

Loss on sale of Investments 48,000

Golf Club Dues for Partners 25,000

Accounting Amortization 62,000

You have correctly calculated CCA of $47,000 and a terminal loss of $31,000.

How much business income should be allocated to each partner for income tax purposes?

Answer: The Keisha Partnership's 2022 Business Income would be calculated as follows:

Accounting Income $625,000

Additions

Non-Deductible Meals and Entertainment

[(50%)($32,000)] $16,000

Loss on sale of Investments 48,000

Golf Club Dues 25,000

Amortization Expense 62,000 151,000

Deductions

CCA ($47,000)

Terminal Loss ( 31,000) ( 78,000)

2022 Business Income $698,000

Each partner would be allocated $349,000 [(50%)($698,000)].

While not required, you might note that the capital loss will be allocated to the partners on a 50:50 basis. However, they can deduct it only to the extent that they have net taxable capital gains for 2022.

Type: ES

Topic: Partnerships - comprehensive problem business income allocation (includes reconciliation from accounting)

72) The MP Partnership has two partners who share all types of income on an equal basis. Partners M and P are both individuals. The Partnership's accounting income for the fiscal period ending December 31, 2022 is $78,000. No salaries or interest payments to partners have been included in this calculation. However, the $78,000 includes $6,500 in eligible dividends, as well as a $16,000 gain on the sale of unused land that is capital property. Amortization Expense deducted is equal to maximum CCA.

Determine the amounts that will be included in the 2022 net income of Partner M and Partner P.

Answer: The MP Partnership's 2022 Business Income would be calculated as follows:

Accounting Income $78,000

Amortization Expense = CCA Nil

Eligible Dividends ( 6,500)

Accounting Gain on sale of Land ( 16,000)

2022 Business Income $55,500

The addition to 2022 net income for each of the two partners would be calculated as follows:

**Partner M Partner P**

Business Income [(50%)($55,500)] $27,750 $27,750

Eligible Dividends [(50%)($6,500)] 3,250 3,250

Gross Up [(38%)($3,250)] 1,235 1,235

Taxable Capital Gain [(50%)(1/2)($16,000)] 4,000 4,000

Total addition to 2022 Net Income $36,235 $36,235

While not required, you might note that each partner would be eligible for a federal dividend tax credit of $674 [(6/11)($1,235)].

Type: ES

Topic: Partnerships - comprehensive problem business income allocation (includes reconciliation from accounting)

73) For the taxation fiscal period ending December 31, 2022, the Barton Partnership has accounting income of $242,000. In determining this amount, no deductions were made for either partner salaries or interest on partner capital contributions. However, the accounting income does include $14,000 in eligible dividends received and a capital gain on the sale of investments of $52,000.

The partnership has two partners, Sam Barton and Sherri Barton. All income is allocated on the basis of 40% to Sam and 60% to Sherri.

Determine the amounts that will be included in the 2022 net income of both partners.

Answer: The Barton Partnership's 2022 Business Income would be calculated as follows:

Accounting Income $242,000

Eligible Dividends ( 14,000)

Accounting Gain on sale of Investments ( 52,000)

2022 Business Income $176,000

The addition to 2022 net income for each of the two partners would be calculated as follows:

**Sam (40%) Sherri (60%)**

Business Income = $176,000 $70,400 $105,600

Eligible Dividends = $14,000 5,600 8,400

Gross Up

[(38%)($5,600)] 2,128

[(38%)($8,400)] 3,192

Taxable Capital Gain = $26,000

[(1/2)($52,000)] 10,400 15,600

2022 Addition to Net Income $88,528 $132,792

While this is not required, you might note that each partner would be eligible for a federal dividend tax credit equal to 6/11 of their respective gross ups.

Type: ES

Topic: Partnerships - comprehensive problem business income allocation (includes reconciliation from accounting)

74) For the fiscal period ending December 31, 2022, the PU Partnership has correctly calculated its business income for income tax purposes to be $213,000. The partnership agreement calls for all allocations to Partner P and Partner U to be on a 40:60 basis. Partner P and U are both individuals and neither has income that is subject to the 33% federal income tax rate.

In reconciling accounting income to business income for income tax purposes, the partnership's accountant added back $4,200 in charitable donations and $900 in contributions to a registered political party. In addition, $2,700 in eligible dividends received were deducted. The partners have made no personal charitable donations or political contributions.

Determine the amount of any income tax credits that will be allocated to Partner P and Partner U for the 2022 taxation year.

Answer: The allocation of the amounts would be as follows:

**Partner P (40%) Partner U (60%)**

Charitable Donations = $4,200 $1,680 $2,520

Political Contributions = $900 360 540

Dividends = $2,700 1,080 1,620

Using these allocations, the tax credits for the two individual partners would be as follows:

**Partner P**

Charitable Donations

[(15%)($200) + (29%)($1,680 - $200)] $459

Political Contributions [(3/4)($360)] 270

Dividends [(6/11)(38%)($1,080)] 224

John's Tax Credits $953

**Partner U**

Charitable Donations

[(15%)($200) + (29%)($2,520 - $200)] $ 703

Political Contributions [(3/4)($400) + (1/2)($140)] 370

Dividends [(6/11)(38%)($1,620)] 336

Partner U's Tax Credits $1,409

These amounts reduce the 2022 federal income tax payable of each of the two partners.

Type: ES

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

75) The Coop Partnership has two members, John and Jill Walther, who share all income on a 60:40 basis. Neither partner has income that is subject to the 33% federal income tax rate.

During the partnership fiscal period ending December 31, 2022, accounting income has been computed as $346,000. This accounting income includes the following amounts:

Charitable Donations $4,500

Contributions to a Registered Political Party 600

Eligible Dividends 14,000

The partners have made no personal charitable donations or political contributions.

Determine the amount of any tax credits that will be allocated to John and Jill Walther for 2022.

Answer: The allocation of the amount would be as follows:

**John (60%) Jill (40%)**

Charitable Donations = $4,500 $2,700 $1,800

Political Contributions = $600 360 240

Dividends = $14,000 8,400 5,600

Using these allocations, the tax credits for the two individual partners would be as follows:

**John**

Charitable Donations

[(15%)($200) + (29%)($2,700 - $200)] $ 755

Political Contributions [(3/4)($360)] 270

Dividends [(6/11)(38%)($8,400)] 1,741

John's Tax Credits $2,766

**Jill**

Charitable Donations

[(15%)($200) + (29%)($1,800 - $200)] $ 494

Political Contributions [(3/4)($240)] 180

Dividends [(6/11)(38%)($5,600)] 1,161

Jill's Tax Credits $1,835

These amounts reduce the 2022 federal income tax payable of each of the two partners.

Type: ES

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

76) Natasha and Felicia are equal partners in the Natty Partnership. On April 30, 2022, Natasha and Felicia's partnership capital account balances are $148,800 each which is the same as the ACB of their partnership interests. Kyra is admitted as an equal partner on April 30, 2022, and pays $124,000 to each of Natasha and Felicia. Calculate the income tax consequences of the partner admission for Natasha and Felicia and determine the partner capital account balances and ACB of the partnership interest for each partner after the admission of Kyra.

Answer: Natasha and Felicia will each have a disposition of one-third of their partnership interests for $124,000. As the ACB of the part of the interest sold is $49,600 [(1/3)($148,800)], Natasha and Felicia will each have a $37,200 [(1/2)($124,000 - $49,600)] taxable capital gain.

The capital account balances and the ACBs after Kyra's admission will be:

**Natasha Felicia Kyra**

Opening Capital Accounts $148,800 $148,800 Nil

Adjustment for Kyra's Admission ( 49,600) ( 49,600) $ 99,200

Ending Capital Accounts

(Accounting Values) $ 99,200 $ 99,200 $ 99,200

ACB of Partnership Interest $ 99,200 $ 99,200 $248,000

Type: ES

Topic: Partnerships - becoming a partner

77) Jerry and Joan are equal partners in the JJ Partnership. On January 1, 2022, the balance in each of their partner capital accounts is $210,000. This is also the ACB of their partnership interests. On this date, John is admitted as an equal partner, paying $130,000 to each of Jerry and Joan. Calculate the income tax consequences of the partner admission for Jerry and Joan. In addition, determine the partner capital account balances and ACB of each partner's partnership interest after the admission of John.

Answer: Jerry and Joan will each have a partial disposition of one-third of their partnership interests for $130,000. As the ACB of the part interest sold is $70,000 [(1/3)($210,000)], they will each have a taxable capital gain of $30,000 [(1/2)($130,000 - $70,000)].

The partners capital account balances and the ACBs after John's admission would be as follows:

**Jerry Joan John**

Opening Capital Accounts $210,000 $210,000 Nil

Adjustment for John's Admission ( 70,000) ( 70,000) $140,000

Ending Capital Accounts

(Accounting Amounts) $140,000 $140,000 $140,000

ACB of Partnership Interest $140,000 $140,000 $260,000

Type: ES

Topic: Partnerships - becoming a partner

78) On January 1, 2022, Rachel and Roberta form the Racherta Partnership. The partnership agreement provides Roberta with a 40% share of profits and losses. Roberta initially contributes $52,500 and makes a further contribution of $30,240 on May 15, 2022. She withdraws $16,800 on August 31, 2022. The Racherta Partnership has the following income and capital gains for the fiscal period ending December 31, 2022:

Capital Gain on sale of Shares $ 48,720

Eligible Dividends from Canadian Corporations 13,020

Business Income 196,140

Determine the ACB of Roberta's partnership interest on December 31, 2022, and on January 1, 2023. In addition, determine the amount that would be included in Roberta's 2022 net income as a consequence of her interest in the Racherta Partnership.

Answer: The ACB of Roberta's partnership interest on December 31, 2022 and January 1, 2023 would be determined as follows:

Original Capital Contribution $ 52,500

Additional Contribution 30,240

Drawings ( 16,800)

ACB - December 31, 2022 $ 65,940

Adjustment for 2022 Income & Capital Gains

[(40%)($48,720 + $13,020 + $196,140)] 103,152

ACB - January 1, 2023 $169,092

Roberta's addition to her 2022 net income would be as follows:

Taxable Capital Gain [(1/2)($48,720)] $ 24,360

Dividends Received 13,020

Gross Up on Eligible Dividends [(38%)($13,020)] 4,948

Business Income 196,140

Subtotal $238,468

Roberta's % Share 40%

Addition to 2022 Net Income $ 95,387

Note that this is not the same $103,152 that was added to the ACB of Roberta's partnership interest to reflect her share of 2022 partnership income.

Type: ES

Topic: Partnerships - the ACB of a partnership interest

79) The XL Partnership is formed on January 1, 2022. Xena is entitled to 60% of the Partnership income, while Larry is entitled to 40%.

Xena's original investment is $125,000. Later in 2022, she makes a further contribution of $75,000. Also in 2022, she withdraws $40,000 in anticipation of partnership business profits.

During the taxation fiscal period ending December 31, 2022, the XL Partnership has the following income & capital gains:

Business Income $435,000

Eligible Dividends 26,000

Capital Gain on the sale of shares 31,000

Determine the ACB of Xena's partnership interest on December 31, 2022, and on January 1, 2023. In addition, determine the amount that would be included in Xena's 2022 net income as a consequence of her interest in the XL Partnership.

Answer: The ACB of Xena's partnership interest on December 31, 2022 and January 1, 2023 would be determined as follows:

Original Capital Contribution $125,000

Additional Contribution 75,000

Drawings ( 40,000)

ACB - December 31, 2022 $160,000

Adjustment for 2022 Income

[(60%)($435,000 + $26,000 + $31,000)] 295,200

ACB - January 1, 2023 $455,200

Xena's 2022 addition to net income would be as follows:

Business Income $435,000

Taxable Capital Gain [(1/2)($31,000)] 15,500

Dividends Received 26,000

Gross Up on Eligible Dividends [(38%)($26,000)] 9,880

Subtotal $486,380

Xena's Share of Partnership Income and Gains 60%

Addition to 2022 Net Income $291,828

Note that this is not the same $295,200 that was added to the ACB of Xena's partnership interest to reflect her share of 2022 partnership income.

Type: ES

Topic: Partnerships - the ACB of a partnership interest

80) In 2022, Blake Robson purchases an interest in a real estate limited partnership for $235,000. The price is paid with $62,000 in cash and a loan provided by the partnership of $173,000. The loan is payable in six years. The general partner has agreed to purchase Blake's interest at any time, returning his $62,000 payment and assuming full responsibility for the loan, without regard to the current value of the interest. For 2022, the limited partnership has allocated losses of $81,400 to Blake. How much of this loss can Blake claim for the 2022 taxation year? What is the amount of his 2022 limited partnership loss if any?

Answer: The required calculations are as follows:

ACB of Partnership Interest $235,000

Share of Partnership Income for 2022 Nil

Subtotal $235,000

Amounts owed to the partnership ($173,000)

Other amounts intended to

reduce investment risk

(General Partner Guarantee) ( 62,000) ( 235,000)

At-Risk Amount - December 31, 2022 Nil

As the at-risk amount is nil, none of the allocated loss can be deducted in 2022. The 2022 limited partnership loss is therefore equal to the allocated loss of $81,400.

Type: ES

Topic: Partnerships - limited partnership losses

81) Early in 2022, Bobby Joe Hyder purchased an interest in a limited partnership for $450,000. Of this amount $250,000 is paid in cash, with the remainder payable to the partnership on January 1, 2025. If Bobby Joe transfers his interest to the general partner prior to January 1, 2025, the general partner will pay him $100,000 and assume full responsibility for the balance owing on January 1, 2025.

For 2022, the limited partnership has allocated business losses of $132,000 to Bobby Joe. How much of this loss is Bobby Joe entitled to claim as a deduction for 2022? What is the amount of his 2022 limited partnership loss, if any?

Answer: The required calculations are as follows:

ACB of Partnership Interest $450,000

Share of Partnership Income for 2022 Nil

Subtotal $450,000

Amounts owed to the Partnership ($200,000)

Other amounts intended to

reduce investment risk

(General Partner Guarantee) ( 100,000) ( 300,000)

At-Risk Amount - December 31, 2022 $150,000

As the at-risk amount is $150,000, all of the $132,000 loss can be deducted in 2022. As a result there is no limited partnership loss for 2022.

Type: ES

Topic: Partnerships - limited partnership losses

82) Martha Stuart is one of four partners in the Homemaker Partnership (HP). During the current year, Martha contributes land that is capital property to the partnership. Martha purchased the land for $59,400 and, at the time of the disposition to the partnership, it is valued at $180,000. Martha does not use a rollover provision to make the transfer. Describe the income tax consequences to Martha and HP in the following three situations:

A. No consideration is received from HP.

B. Martha receives $45,000 in cash from HP on the transfer.

C. Martha receives $201,600 in cash from HP on the transfer.

Answer: **Part A -** Martha is considered to have disposed of the land for $180,000, resulting in a $60,300 [(1/2)($180,000 - $59,400)] taxable capital gain. She is also considered to have made a capital contribution of $180,000 that will be added to the ACB of her partnership interest. HP will be considered to have acquired the land for $180,000.

**Part B -** Martha will have the same $60,300 taxable capital gain as in Part A and HP will be considered to have acquired the land for $180,000. The capital contribution and the addition to the ACB of the partnership interest is $135,000. This is the difference between the FMV of the land HP of $180,000 and the $45,000 in other consideration received by Martha on the disposition of the property.

**Part C -** Martha will have the same $60,300 taxable capital gain as in Part A and HP will be considered to have acquired the land for $180,000. No capital contribution is made. As Martha withdrew $21,600 ($201,600 - $180,000) more from HP than the FMV of the land and the excess will be considered a withdrawal. The ACB of her partnership interest will be reduced by $21,600.

Type: ES

Topic: Partnerships - sale of property from a partner to a partnership (ITA 97(1))

83) Ethan Allen is one of three partners in the Colonial Partnership (CP). In 2022, Ethan transfers land that is capital property to the partnership. The partners agree that the land has a FMV of $220,000. Ethan's ACB for the land is $100,000. Describe the income tax consequences to Ethan and CP in the following three situations:

A. No consideration is received from CP.

B. Ethan receives $60,000 in cash from CP on the transfer.

C. Ethan receives $250,000 in cash from CP on the transfer.

Answer: **Part A -** Ethan is considered to have disposed of the land for its FMV of $220,000, resulting in a taxable capital gain of $60,000 [(1/2)($220,000 - $100,000). This capital contribution will increase the ACB of Ethan's partnership interest by $220,000. The ACB of the land to CP will be $220,000.

**Part B -** Ethan is considered to have disposed of the land for its FMV of $220,000, resulting in a taxable capital gain of $60,000 [(1/2)($220,000 - $100,000)]. However, as he has received $60,000 in cash, the ACB of his partnership interest will only be increased by $160,000 ($220,000 - $60,000). The ACB of the land to CP will be $220,000.

**Part C -** Once again, Ethan will have a taxable capital gain of $60,000 and CP will have acquired the land for $220,000. However, as Ethan has received an amount in excess of the FMV of the land, there will be no increase in the ACB of his partnership interest. The ACB of the partnership interest will be reduced by the $30,000 ($250,000 - $220,000) excess of the cash payment over the FMV of the land. In effect, this $30,000 will be treated as drawings.

Type: ES

Topic: Partnerships - sale of property from a partner to a partnership (ITA 97(1))

84) Lamar is one of 10 equal partners in the Trident Partnership. During its fiscal period ending December 31, 2022, Trident distributes debenture bonds that were held for investment purposes to each of the partners. These bonds have an ACB of $567,750 and, at the time of transfer, they have a FMV of $611,750. Lamar receives 10% of these bonds. At the time of the transfer, the ACB of Lamar's partnership interest is $75,800. What are the income tax consequences to Trident and Lamar with respect to this distribution? Your answer should include the ACB of Lamar's partnership interest on both December 31, 2022 and January 1, 2023.

Answer: ITA 98(2) deems Trident to have disposed of the debenture bonds for their FMV of $611,750, resulting in a $44,000 ($611,750 - $567,750) capital gain. One-tenth of the capital gain, or $4,400, will be allocated to Lamar. One-half of this amount, or $2,200, will be a taxable capital gain that Lamar will have to include in his 2022 income. Lamar will also be considered to have acquired his share of the debenture bonds for $61,175.

The ACB of his partnership interest on December 31, 2022 and on January 1, 2023 is calculated as follows:

Partnership ACB Prior to the Distribution $75,800

Drawings [(10%)($611,750)] ( 61,175)

ACB - December 31, 2022 $14,625

Allocated Capital Gain [(10%)(($611,750 - $567,750)] 4,400

ACB - January 1, 2023 $19,025

Type: ES

Topic: Partnerships - sale of property from a partnership to a partner (ITA 98(2))

85) Patricia Flood holds a 25% interest in the Markham Partnership. The Partnership owns investments with an ACB of $250,000 and a FMV of $475,000. During the fiscal period of the partnership ending December 31, 2022, the Partnership will distribute these investments to the partners in proportion to their interests. Patricia receives 25% of the investments and, at the time that they are received, the ACB of her partnership interest is $180,000. What are the income tax consequences to Patricia and Markham with respect to this distribution? Your answer should include the ACB of Patricia's partnership interest on December 31, 2022 and January 1, 2023.

Answer: The distribution will be treated as a disposition of the investments at their FMV of $475,000. This means that the Partnership will have a capital gain of $225,000 ($475,000 - $250,000). Of this amount, $56,250 [(25%)($225,000)] will be allocated to Patricia. She will have a taxable capital gain of $28,125 [(1/2)($56,250)] which will be included in her 2022 income. The ACB of the investments received will be $118,750 [(25%)($475,000)].

The ACB of her partnership interest on December 31, 2022 and on January 1, 2023 is calculated as follows:

Partnership ACB prior to the Distribution $180,000

Drawings [(25%)($475,000)] ( 118,750)

ACB - December 31, 2022 $ 61,250

Allocated Capital Gain [(25%)(($475,000 - $250,000)] 56,250

ACB - January 1, 2023 $117,500

Type: ES

Topic: Partnerships - sale of property from a partnership to a partner (ITA 98(2))

86) Sol Marinara is one of four equal partners in the MSG Partnership. During the current year, Sol transfers land that is capital property to the partnership as a capital contribution. He had acquired the land several years ago for $146,000. At the time of the contribution to the partnership, the FMV is $472,000. He would like to use any available rollover provision in order to minimize income tax. Assuming the appropriate rollover provision is used, what are the income tax consequences of this contribution?

Answer: ITA 97(2) provides the necessary rollover that allows the rollover provisions of ITA 85(1) to be used where a partner disposes of property to a partnership. Without ITA 97(2), ITA 85(1) would not apply since it requires that dispositions of eligible property be made to a taxable Canadian corporation. Using the partnership modified version of ITA 85(1), the property would be disposed of at the $146,000 ACB of the land. Given this, the transfer would not result in any current income for Sol. The cost of the land to the partnership would be the $146,000 elected amount for the transfer. This same amount would be added to the ACB of Sol's partnership interest.

Type: ES

Topic: Partnerships - rollover of property from a partner to a partnership (ITA 97(2))

87) Sarah Bright owns land that is capital property that was purchased several years earlier at a cost of $250,000. It currently has a FMV of $600,000. She would like to contribute the land to a partnership in which she is one of 6 equal partners. In making the transfer, she would like to use any available rollover provision that would minimize the income tax of the disposition. Assuming the appropriate rollover provision is used, what are the income tax consequences?

Answer: ITA 97(2) provides the necessary rollover that allows the rollover provisions of ITA 85(1) to be used where a partner disposes of property to a partnership. Without ITA 97(2), ITA 85(1) would not apply since it requires that dispositions of eligible property be made to a taxable Canadian corporation. Using the partnership modified version of ITA 85(1), the property would be transferred at the $250,000 ACB of the land. The cost of the land to the partnership would be the $250,000 ITA 85(1) elected amount for the transfer. This same amount would be added to the ACB of Sarah's partnership interest.

Type: ES

Topic: Partnerships - rollover of property from a partner to a partnership (ITA 97(2))

88) Barry and Lance Booker are brothers who live in the same New Brunswick community. Barry is an accountant who specializes in advising small businesses. Lance has held various jobs in restaurants over the last few years. However, he is currently between jobs.

As a result of information he has accumulated while working with his accounting clients, Barry has started a new business involving catering services. To this end, he has acquired a building, furniture, and equipment. He has also registered the business and opened up a bank account under his own name. Barry spends a few hours each day managing the business.

As he is aware of Lance's financial difficulties, he has decided to treat his brother as a partner in this business, sharing profits on a 50:50 basis when filing their annual income tax returns. There is no formal partnership agreement.

**Required:** In the following two **independent** Cases, determine whether a partnership exists.

A. Lance's involvement with the business consists of helping Barry pick out furniture and equipment and occasionally taking messages when Barry is out of town. It appears that the business will be consistently profitable.

B. Lance does all the accounting, payroll and invoicing for the business. He also does most of the ordering and is responsible for paying for the suppliers. While it is unlikely that the business will be profitable in its first year of operation, Barry expects the business to be profitable in subsequent years.

Answer: ***Basis For Conclusion***

The following three partnership questions must all be answered yes for a partnership to exist:

1. Is there a business?

2. Is the business carried on for profit?

3. Is the business carried on in common by two or more persons?

***Case A***

With respect to the first question, it is clear that a business exists in this Case.

With respect to the second question, the business is being carried on for profit.

With respect to the third question, it does not seem that Lance will be making any real contribution to the management of the business. Further, Barry does not hold himself out as a partner or the business as a partnership, as the bank accounts and the business registration are in Barry's name only. Given these factors, we would conclude that the business is not "carried on in common by two or more persons". Therefore, a partnership does not exist in this Case.

***Case B***

With respect to the first question, it is clear that a business exists in this Case.

With respect to the second question, the business is being carried on for profit.

With respect to the third question, Lance appears to be carrying out employment-like functions and does not seem to be involved in the management of the business. This would suggest that the business is not being "carried on in common". Given this, the most likely conclusion would be that partnership does not exist.

Type: ES

Topic: Partnerships - comprehensive problem: the existence of a partnership

89) Mark and George Cooper are brothers with extensive experience in practicing law. Until recently, they have each worked for separate firms in Regina, Saskatchewan. After years of urging from their mother, they have concluded that they could significantly improve their incomes and the quality of their client base if they work together in a partnership arrangement. As a result, as of January 1, 2022, they begin practicing law as the Cooper & Cooper Partnership.

Mark will be entitled to a salary of $60,000 per year, while George's salary will be $40,000. In addition, George will receive interest at 5% on his average capital balance for the year. The salary and interest amounts are withdrawn by the partners during the course of the year.

Subsequent to the priority allocations for salaries and interest, any residual business income will be allocated 65% to Mark and 35% to George in 2022.

**Capital Gains -** As George has contributed the majority of the partnership initial capital, he will be entitled to all capital gains that are realized by the partnership.

**Dividends -** Any dividends received by the partnership will be split equally between the two partners.

For the partnership fiscal period ending December 31, 2022, the accounting income is as follows:

**Cooper & Cooper Partnership Income Statement**

**Fiscal Period Ending December 31, 2022**

Revenues $862,465

Expenses:

Salaries to Staff ($123,656)

Office Rent ( 63,964)

Office Supplies ( 8,434)

Amortization Expense (Note 1) ( 26,360)

Business Meals & Entertainment ( 16,432)

Charitable Donations (Note 2) ( 3,850)

Interest on George's Capital Contribution ( 4,780)

Salary to Mark ( 60,000)

Salary to George ( 40,000) ( 347,476)

Accounting Business Income $514,989

Other Income:

Gains on sales of Investments (Note 3) $ 16,848

Eligible Dividends 9,432 26,280

2022 Accounting Net Income $541,269

**Note 1 -** Accounting amortization is based on ASPE. The brothers intend to claim the maximum allowable CCA of $32,164.

**Note 2 -** The charitable donations will be allocated equally to each brother. Neither brother made any other charitable donations in 2022.

**Note 3 -** The accounting gains on sales of investments are equal to the capital gains.

**Required:**

A. Calculate the amounts of income from the partnership that would be included for 2022 for each brother.

B. Indicate the amount of any federal personal tax credits that each of the two brothers would be entitled to as a result of allocations made by the partnership at December 31, 2022.

Ignore CPP, GST/HST & PST considerations.

Answer:

***Part A - Income Inclusion***

The calculation of the partnership's business income for income tax purposes is as follows:

Business Income for accounting purposes (From Statement) $514,989

Additions:

Amortization Expense 26,360

Business Meals & Entertainment [(1/2)($16,432)] 8,216

Charitable Donations 3,850

Interest on George's Capital Contribution 4,780

Salaries to Partners ($60,000 + $40,000) 100,000 143,206

Subtotal $658,195

Deductions:

Maximum CCA ( 32,164)

Business Income for ITA purposes $626,031

Priority Allocations for Salary & Interest ($4,780 + $100,000) ( 104,780)

Residual t be allocated 65:35 $521,251

Additional partnership income allocations would be as follows:

Taxable Capital Gains [(1/2)($16,848)] $8,424

Eligible Dividends Received 9,432

Gross Up [(38%)($9,432)] 3,584

Grossed Up Eligible Dividends $13,016

The total 2022 addition to the income of each brother is as follows:

**Mark George**

Business Income

Priority Claim - Salaries $ 60,000 $ 40,000

Priority Claim — Interest 4,780

Mark [(65%)($521,251)] 338,813

George [(35%)($521,251)] 182,438

Taxable Capital Gains [(100%)($8,424)] 8,424

Grossed Up Eligible Dividends [(50%)($13,016)] 6,508 6,508

2022 Net Income $405,321 $242,150

***Part B - Tax Credits***

**Charitable Donations**

Each of the brothers would be allocated $1,925 [(50%)($3,850)] of the charitable donations. The donation would provide a federal tax credit of $599 [(15%)($200) + (33%)($1,925 - $200)].

**Dividends**

Each of the brothers will be allocated one-half of the eligible dividends. Given this, they will each have a federal dividend tax credit of $977 [(1/2)(38%)($9,432)(6/11)].

Type: ES

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

90) Sam and Allen Foster are both Chartered Professional Accountants (CPAs). Since acquiring their professional designations, they have both worked for a large CPA firm. However, at the beginning of 2022, they decided to leave the firm and form a two person partnership specializing in tax and accounting for owner-managed private corporations.

The agreement for the new partnership calls for business income to be shared equally. In addition, charitable contributions will also be allocated equally. However, as Allen has contributed most of the capital for the new partnership, he will receive 80% of any capital gains or dividends received by the partnership.

For the partnership fiscal period ending December 31, 2022, the accounting results are as follows:

**Sam And Allen Foster**

**Partnership Income Statement**

**Fiscal Period Ending December 31, 2022**

Revenues $965,000

Expenses:

Employee Salaries ($114,000)

Office Rent ( 82,000)

Office Supplies ( 30,000)

Amortization ( 32,000)

Business Meals & Entertainment ( 14,000)

Charitable Donations ( 13,000)

Salary to Sam ( 150,000)

Salary to Allen ( 150,000) ( 585,000)

2022 Accounting Business Income $380,000

Other Income:

Capital Gains $ 8,000

Eligible Dividends 16,000 24,000

2022 Accounting Net Income $404,000

**Other Information:**

1. The partnership will claim the maximum CCA which is $41,000.

2. Neither of the brothers has any other income outside of the partnership in 2022.

3. The only charitable donations of the brothers in 2022 is from the partnership.

**Required:** Ignore CPP, GST/HST & PST considerations.

A. Calculate the amounts of partnership income and capital gains that would be included in the 2022 net income of each brother.

B. Indicate the amount of any federal personal tax credits that would be available to the two brothers as a result of the partnership.

Answer:

***Part A - Income Inclusion***

The calculation of the partnership's Business Income for income tax purposes is as follows:

Accounting Business Income (From Statement) $380,000

Additions:

Amortization $ 32,000

Business Meals & Entertainment [(1/2)($14,000)] 7,000

Charitable Donations 13,000

Salaries to Partners [(2)($150,000)] 300,000 352,000

$732,000

Deductions:

Maximum CCA ( 41,000)

2022 Business Income $691,000

Additional partnership income would be as follows:

Taxable Capital Gains [(1/2)($8,000)] $ 4,000

Eligible Dividends Received 16,000

Gross Up [(38%)($16,000)] 6,080

Total other Partnership Income $26,080

The 2022 Net Income for each brother is:

**Sam Allen**

Business Income [(50%)($691,000)] $345,500 $345,500

Other Partnership Income

Sam [(20%)($26,080)] 5,216

Allen [(80%)($26,080)] 20,864

2022 Net Income $350,716 $366,364

***Part B - Tax Credits***

**Charitable Donations**

Each of the brothers would be allocated $6,500 [(50%)($13,000)] of the charitable donations. This would provide a federal tax credit of $2,109 [(15%)($200) + (33%)($6,500 - $200)].

**Dividends**

As Sam was allocated only 20% of the dividends, his federal dividend tax credit will be $663 [(20%)(6/11)($6,080)].

Allen's credit will be $2,653 [(80%)(6/11)($6,080)].

Type: ES

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

91) Two lawyers, who had practiced individually for a number of years, decided to form a partnership. The partnership began on January 1, 2022, with each individual contributing $50,000 in cash. There were no further capital contributions in 2022.

In 2022, they each receive a salary of $87,000, as well as interest on their beginning of the year capital balances at an annual rate of 5%. The interest amounts were withdrawn by the partners during the fiscal period ending December 31, 2022. There were no other drawings during 2022.

Any of the partnership's business income that remains after the allocation of salaries and interest to the two partners will be shared on a 50:50 basis.

For the fiscal period ending December 31, 2022, their bookkeeper has prepared the following financial statements. No amortization was deducted in preparing the statements.

**Amigos Unlimited**

**Balance Sheet**

**As At December 31, 2022**

Cash $ 32,278

Accounts Receivable 327,787

Furniture & Fixtures 41,300

Computer Hardware (Cost) 12,400

Computer Applications Software (Cost) 9,600

Total Assets $423,365

Accounts Payable $ 77,850

Initial Partner Capital 100,000

Income for the period 245,515

Total Equities $423,365

**Amigos Unlimited**

**Income Statement**

**For the Fiscal Period Ending December 31**, **2022**

Total Revenues $516,390

Meals & Entertainment ($ 16,432)

Office Supplies ( 8,973)

Partners' Salaries ( 174,000)

Interest on Capital Contributions ( 5,000)

Rent ( 38,000)

Administrative Assistant's Salary ( 28,470)

Total Expenses ($270,875)

2022 Accounting Net Income $245,515

**Required:**

A. The lawyers have come to you to determine the minimum amount that they must include in their 2022 income tax returns as partnership business income.

B. They would also like to know if there are any partner expenses that they may be able to deduct for 2022.

C. Compute the ACB of each partner's partnership interest at December 31, 2022 and January 1, 2023.

Your answers should ignore CPP, GST/HST & PST considerations.

Answer:

***Part A - Business Income from the Partnership***

Business Income from the partnership is as follows:

Accounting Income $245,515

Additions:

Partners' Salaries $174,000

Interest on Capital Contributions 5,000

Meals & Entertainment [(50%)($16,432)] 8,216 187,216

$432,731

Deductions:

CCA:

Class 8 [(150%)(20%)($41,300)] ( 12,390)

Class 50 [(150%)(55%)($12,400)] ( 10,230)

Class 12 [(1/2)(100%)($9,600)] ( 4,800) ( 27,420)

2022 Business Income $405,311

Priority Allocation for Salaries & Interest ($174,000 + $5,000) ( 179,000)

Residual to be allocated 50:50 $226,311

While the partnership agreement refers to salaries and interest, these amounts will be treated as business income in the respective income tax returns of the partners. The amount that would be included in each partner's 2022 individual income tax return would be calculated as follows:

Salary $ 87,000

Interest [(1/2)($5,000)] 2,500

Share of residual Partnership Income [(1/2)($226,311)] 113,156

2022 Business Income for each partner $202,656

***Part B - Deductible Expenses incurred Personally***

The partners may also be able to deduct the following expenses, if they have incurred them personally:

• Any interest expense related to financing their capital contribution of $50,000 each.

• The business portion of any automobile expenses.

• Any promotion expenses, subject to the 50% limitation on meals and entertainment.

• Expenses for an office in the home (to a maximum of business income before the deduction), if the work space is used exclusively for business purposes and it is used on a regular and continuous basis for meeting clients. These expenses are discussed in Chapter 6.

***Part C - ACB of Partnership Interest***

The ACB of each partnership interest is as follows:

Capital Contribution $ 50,000

Drawings ($87,000 + $2,500) ( 89,500)

Negative ACB - December 31, 2022 ($ 39,500)

Allocation of Partnership Income for 2022 202,656

ACB - January 1, 2023 $163,156

The ITA allows general active partners to carry forward a negative ACB, without any income tax consequences. This deferral continues to apply until such time as there is a disposition of the partnership interest at which time the negative component is recognized as an increase in capital gains.

Type: ES

Topic: Partnerships - allocation of income, loss, capital gains & other amounts

92) Jason and Joey Blake are brothers who are both lawyers. While they have worked independently for several years, on January 1, 2022, they decided to form a partnership. On January 1, 2022, they each make a capital contribution of $350,000 in cash. Because Jason's experience is in a more lucrative area of law, he is to receive 60% of all partnership income, with Joey receiving 40%. Capital gains realized by the partnership, dividends received by the partnership and charitable donations will all be shared equally.

In 2022, Jason withdrew $130,000, while Joey withdrew $102,000. The partnership's 2022 Income Statement, prepared in accordance with ASPE, is as follows:

**Income Statement**

**Joey and Jason Blake Partnership**

**Fiscal Period Ending December 31, 2022**

Revenues $823,000

Operating Expenses:

Rent ($95,000)

Amortization Expense (Note 1) ( 22,000)

General Office Expenses ( 42,000)

Meals & Entertainment ( 16,000)

Charitable Donations ( 12,000)

Office Salaries ( 46,000) ( 233,000)

Accounting Business Income $590,000

Other Income:

Gain on sale of Investments (Note 2) $26,000

Eligible Dividends 22,000 48,000

2022 Accounting Net Income $638,000

**Note 1 -** Maximum 2022 CCA to be claimed is $35,000.

**Note 2 -** The gain resulted from the sale of temporary investments. The investments had an ACB of $57,000 and were sold for $83,000.

In 2022, Jason's only income was from the partnership. Other than tax credits related to partnership allocations, Jason's only tax credit was his BPA.

On January 1, 2023, Jason sells his interest in the partnership to an arm's length individual for $643,000.

**Required:** Calculate Jason's federal income tax payable for the 2022 taxation year. In addition, determine the taxable capital gain or allowable capital loss that would result from Jason's sale of his partnership interest. Ignore any CPP implications.

Answer:

***Jason's Federal Income Tax Payable***

The 2022 Business Income (for ITA purposes) would be calculated as follows:

Accounting Business Income $590,000

Additions:

Amortization Expense $22,000

50% of Meals & Entertainment 8,000

Charitable Donations 12,000 42,000

Deductions:

CCA ($35,000)

2022 Business Income $597,000

Jason's 2022 net income, taxable income and share of charitable donations is as follows:

**Partnership Share Taxable Income**

Partnership Business Income $597,000 60% $358,200

Taxable Capital Gain [(1/2)($26,000)] 13,000 50% 6,500

Eligible Dividends 22,000 50% 11,000

38% Gross Up on Dividends Received N/A 4,180

2022 Net Income & Taxable Income $379,880

Charitable Donations $12,000 50% $6,000

Based on the preceding calculation, Jason's 2022 federal income tax payable would be calculated as follows:

Tax on the first $221,708 $51,345

Tax on additional

$158,172 ($379,880 - $221,708) at 33% 52,197

Tax Payable Before Credits $103,542

Basic Personal Credit [(15%)($12,719)] ( 1,908)

Dividend Tax Credit [(6/11)($4,180)] ( 2,280)

Charitable Donations Credit (See Note) ( 1,944)

2022 Federal Income Tax Payable $97,410

**Note -** The charitable donations tax credit would be calculated as follows:

[(15%)(A)] + [(33%)(B)] + [(29%)(C)], where

A = $200

B = The Lesser of:

• $6,000 - $200 = $5,800

• $379,880 - $221,708 = $158,172

C = Nil [$6,000 - ($200 + $5,800)]

The charitable donation credit would be equal to $1,944, calculated as:

[(15%)($200) + (33%)($5,800)].

***Taxable Capital Gain from Sale of Partnership Interest***

The ACB of Jason's partnership interest on January 1, 2023 would be calculated as follows:

**Partnership Share ACB**

Capital Contribution N/A $350,000

2022 Drawings N/A ( 130,000)

December 31, 2022 $220,000

2022 Partnership Business Income $597,000 60% 358,200

2022 Capital Gain 26,000 50% 13,000

2022 Partnership Dividends Received 22,000 50% 11,000

2022 Charitable Donations ( 12,000) 50% ( 6,000)

January 1, 2023 ACB $596,200

Given this calculation, the taxable capital gain on Jason's sale of the partnership interest would be calculated as follows:

POD $643,000

Less: ACB ( 596,200)

Capital Gain $ 46,800

Inclusion Rate 1/2

2023 Taxable Capital Gain $ 23,400

Type: ES

Topic: Partnerships - comprehensive problem: partnership allocations, ACB & the sale of a partnership interest

93) Moe, Larry, and Curly formed a partnership on January 1, 2020. The partnership is formed to provide a variety of entertainment services to a broad range of clients. Each partner makes an initial capital contribution of $180,000. The partners agree to use a December 31 fiscal period for the partnership.

The partnership agreement contains the following provisions with respect to the allocation of income and capital gains to individual partners:

1. Both business income and charitable contributions will be shared equally by the three partners.

2. Any capital gains realized by the partnership will allocated on a 50:50 basis to Curly and Larry.

3. All of the eligible dividends received by the partnership will be allocated to Moe.

During the period January 1, 2020 through December 31, 2022, the partnership was very successful. The following information related to that three year period:

• The partnership has total business income of $209,114.

• Other amounts were as follows:

• The partnership received eligible dividends totaling $4,221.

• The partnership realized a $16,534 capital gain.

• The partnership made charitable donations of $7,260 in 2022. No donations were made in any other fiscal periods.

• Withdrawals from the partnership were as follows:

• Moe - $101,000

• Curly - $208,000

• Larry - $48,000.

• Additional capital was required to expand the operations of the office and, as a consequence, each partner contributed an additional $70,000 in cash.

Near the end of 2022, after a number of heated arguments with Moe and Curly regarding the types of clients the partnership was servicing, Larry decides to withdraw from the partnership effective January 1, 2023. After some negotiations, each of the other partners agreed to pay him $150,000 in cash for one-half of his interest in the partnership, a total of $300,000. The payments are made on February 1, 2023. The partnership has business income of $18,500 for the month of January, 2023.

Larry incurred legal and accounting fees of $1,500 in with respect to the disposition of his partnership interest.

**Required:**

A. Calculate the ACB of Larry's partnership interest as of January 1, 2023.

B. Determine the amount of Larry's capital gain or capital loss on the disposition of his partnership interest.

Explain the income tax consequences of any other amounts related to the partnership in 2023.

C. Indicate how the ACB of each partner's interest will be affected by the withdrawal of Larry from the partnership.

Answer:

***Part A - ACB***

The ACB of Larry's partnership interest would be calculated as follows:

Initial Capital Contribution $180,000

Additional Capital Contribution 70,000

Total Capital Contribution $250,000

Drawings ( 48,000)

Business Income [(1/3)($209,114)] 69,705

Capital Gains to Curly & Larry [(50%)($16,534)] (Note) 8,267

Dividends to Moe N/A

Charitable Donations [(1/3)($7,260)] ( 2,420)

ACB - January 1, 2022 $277,552

**Note -** Only the taxable one-half of the capital gain is included in a partner's income however the full capital gain is added to the ACB of the partnership interest. Given this, the full amount of Larry's share of realized capital gains is added to the ACB of his partnership interest.

***Part B - Taxable Capital Gain on Disposition***

Given the preceding calculation, the capital gain on the disposition of the partnership interest can be calculated as follows:

POD $300,000

ACB:

From Preceding Calculation ($277,552)

Legal & Accounting Fees ( 1,500) ( 279,052)

Capital Gain $ 20,948

Inclusion Rate 1/2

Taxable Capital Gain $ 10,474

This amount would be included in Larry's income for 2023. He would not include any partnership income for January 2023 as he was not allocated any of this income.

***Part C - Effect on other Partners***

The fact that each partner paid $150,000 to Larry in return for one-half of his interest means that both Moe and Curly would have a $150,000 increase in the ACB of their partnership interests.

Type: ES

Topic: Partnerships - comprehensive problem: ACB of partnership interest and withdrawal of a partner

94) On January 1, 2022, Bob Billions acquires a 12% limited partner interest in the Who-Do-You-Trust Partnership. The total cost of the interest is $65,000, with $5,000 being paid in cash. A $60,000 interest-free promissory note is signed for the balance. The note is to be paid in 6 payments of $10,000 each. Payments are due on December 1 of each year, commencing in 2022.

As part of the agreement, the general partner is obligated to purchase Bob's interest on December 31, 2027 for $5,000 more than its FMV at that time.

Bob's share of all of the income, losses, capital gains and capital losses of the Who-Do-You-Trust Partnership is 12%.

For the fiscal period ending December 31, 2022, the Partnership had the following income, loss and capital gains:

Business Loss ($510,000)

Interest Income 63,000

Eligible Dividends 31,000

Capital Gains 53,000

**Required**: Calculate the following amounts for Bob's investment in the Who-Do-You-Trust Partnership for 2022:

• The at-risk amount (ARA) on December 31, 2022.

• The limited partnership income or loss.

• The deductible loss for 2022.

• The 2022 limited partnership loss (LPL) if any.

• The ACB on December 31, 2022 and January 1, 2023.

• The ARA on January 1, 2023.

Answer:

**Note -** We would remind you that in calculating the ACB of the partnership interest, a partner's share of either income, loss or a capital gain or capital loss is not adjusted to the ACB until the first day of the next fiscal period of the partnership.

***At-Risk Amount (ARA) - December 31, 2022***

ACB - December 31, 2022 $65,000

Add: Share of Partnership Income for 2022

[(12%)($63,000 + $31,000 + $53,000)] 17,640

Subtotal $82,640

Amounts owed to the Partnership

($65,000 - $5,000 - $10,000) ($50,000)

Other Amounts that reduce risk ( 5,000) ( 55,000)

ARA - December 31, 2022 $27,640

As the agreement effectively guarantees a value of no less than $5,000, even if the FMV of the partnership interest is nil, this amount is not at risk and reduces the ARA.

***2022 Limited Partnership Loss***

Share of 2022 Partnership Business Loss [(12%)($510,000)] ($61,200)

ARA - December 31, 2022 27,640

2022 LPL ($33,560)

***Deductible Loss for the Year***

Share of 2022 Partnership Business Loss [(12%)($510,000)] ($61,200)

2022 LPL 33,560

Deductible Loss for 2022 ($27,640)

***2022 Limited Partnership Loss***

There is a 2022 LPL of $33,560.

***ACB***

The share of partnership income that is added to the ARA in the year is the amount that will be added to the ACB at the beginning of the partnership's next fiscal period. It does not include the dividend gross up and it is not reduced by the non-taxable half of the capital gain.

**ACB - December 31, 2022 $65,000**

Share of 2022 Partnership Income

[(12%)($63,000 + $31,000 + $53,000)] 17,640

Loss Deducted for 2022 ( 27,640)

ACB - January 1, 2023 $55,000

***ARA - January 1, 2023***

As of January 1, 2023, the ARA would be nil ($27,640 - $27,640).

Type: ES

Topic: Partnerships - limited partnerships comprehensive problem: ACB, ARA & limited partnership loss

95) On January 1, 2022, Jerry Adverse purchases a 25% limited partnership interest in income, losses and capital gains and capital losses of the Precipice Enterprises Partnership for $200,000. Of this total, $120,000 is paid immediately, with the remaining $80,000 due on January 1, 2023. The partnership uses a December 31 fiscal period.

The general partner of the Precipice Enterprises Partnership has agreed to buy back Jerry's interest for $100,000, without regard to its FMV on the buy back date. However, the agreement expires on January 1, 2024.

For the fiscal period ending December 31, 2022, the Precipice Enterprises Partnership has a business loss of $1,200,000 and a capital gain of $80,000.

For the fiscal period ending December 31, 2023, the Precipice Enterprises Partnership has a further business loss of $225,000. There are no other sources of income or capital gains for that fiscal period.

Jerry does not ask the general partner to buy back his interest during the fiscal period ending December 31, 2023. As a consequence, the agreement expires on January 1, 2024.

In 2024, the Precipice Enterprises Partnership has business income of $50,000.

Jerry has sufficient other income to absorb any deductible losses allocated from the partnership.

**Required:** For each of 2022, 2023 and 2024, calculate the following amounts related to Jerry's interest in the Precipice Enterprises Partnership:

• The ACB at the end of each year.

• The at-risk amount (ARA).

• The limited partnership income (loss) for the year.

• The deductible income (loss) for the year.

• The limited partnership loss (LPL) for the year if any.

Answer:

**2022 Results**

The required amounts would be calculated as follows:

ACB of Partnership Interest - January 1, 2022 $200,000

Add: Share of 2022 Partnership Income (Not Loss)

[(25%)(100%)($80,000 Capital Gain)] 20,000

Subtotal $220,000

Amounts owed to the Partnership ( 80,000)

Other Amounts that reduce risk ( 100,000)

ARA - December 31, 2022 $ 40,000

Share of 2022 Loss [(25%)($1,200,000)] ($300,000)

ARA - December 31, 2022 40,000

2022 LPL ($260,000)

Share of 2022 Loss [(25%)($1,200,000) ($300,000)

2022 LPL 260,000

2022 Deductible Loss ($ 40,000)

There is a 2022 LPL of $260,000 ($300,000 - $40,000).

**2023 Results**

ACB of Partnership Interest - December 31, 2022 $200,000

2022 Capital Gain 20,000

Loss Deducted for 2022 ( 40,000)

ACB of Partnership Interest - January 1, 2023 $180,000

Add: Share of 2023 Partnership Income (Not Loss) Nil

Subtotal $180,000

Amounts owed to the Partnership Nil

Other Amounts that reduce risk ( 100,000)

ARA - December 31, 2023 $ 80,000

Share of 2023 Loss [(25%)($225,000)] ($ 56,250)

2022 LPL ( 260,000)

ARA - December 31, 2023 80,000

2022 LPL ($236,250)

Share of 2023 Loss [(25%)($225,000)] ($ 56,250)

2022 LPL deducted ( 23,750)

Deductible Loss for 2023 ($ 80,000)

This will leave a 2022 LPL balance of $236,250.

**2024 Results**

ACB of Partnership Interest - December 31, 2023 $180,000

Loss Deducted for 2023 ( 80,000)

ACB of Partnership Interest - January 1, 2024 $100,000

Add: Share of 2024 Partnership Income

[(25%)($50,000)] 12,500

Subtotal $112,500

Amounts owed Partnership Nil

Other Amounts that reduce risk Nil

ARA - December 31, 2024 $112,500

2022 LPL balance ($236,250)

ARA - December 31, 2024 112,500

2022 LPL Balance ($123,750)

2022 Initial LPL Balance ($236,250)

Deductible 2022 Limited Partnership Loss in 2024 112,500

2022 LPL Balance ($123,750)

**Economic Analysis -** The following calculations will serve to explain the results that have been calculated in the preceding table:

2022 Business Loss [(25%)($1,200,000)] ($300,000)

2023 Business Loss [(25%)($225,000)] ( 56,250)

Total Losses for 2022 to and including 2024 ($356,250)

2022 Investment (Initial) 120,000

2022 Capital Gain [(25%)($80,000)] 20,000

2023 Investment (Balance) 80,000

2024 Business Income [(25%)($50,000)] 12,500

2022 Limited Partnership Loss Balance ($123,750)

Type: ES

Topic: Partnerships - limited partnerships comprehensive problem: ACB, ARA & limited partnership loss

96) **Note To Instructor** - As some of the issues in this problem are not covered directly in the text, this question should not be used on an examination unless Assignment Problem Eighteen-9 has been covered in your classes.

A number of years ago, Jack Howard, Bud Jones, and Dwight Delaney established the Howard, Jones, and Delaney Partnership. At the time the partnership was formed, each of the partners invested $600,000 in cash. The partnership agreement calls for all income and losses to be shared equally. The partnership fiscal period is December 31.

On January 1 of the current year, the ACB of the partnership interests for the three partners are as follows:

Jack Howard $1,173,000

Bud Jones 930,000

Dwight Delaney 756,000

Total $2,859,000

The total net tax cost of all of the property of the partnership is also equal to the $2,859,000 ACB of the partnership interests. On January 2 of the current year, all of the property of the partnership is transferred to a corporation under the rollover of ITA 85(2). The elected amounts are equal to the tax costs of the individual properties.

It has been determined that the FMV of the partnership is $3,900,00. Based on this, the corporation provides the following consideration to the partnership:

Cash $1,200,000

Preferred Shares (FMV) 900,000

Common Shares (FMV) 1,800,000

Total Consideration $3,900,000

The partnership will be liquidated within 60 days of the ITA 85(2) rollover and property received from the corporation by the partnership will be distributed to the three partners in accordance with ITA 85(3). Under the terms of the partnership agreement, the partners receive the following amounts:

**Howard Jones Delaney Total**

Cash $ 620,000 $ 377,000 $ 203,000 $1,200,000

Preferred Shares 300,000 300,000 300,000 900,000

Common Shares 600,000 600,000 600,000 1,800,000

Total $1,520,000 $1,277,000 $1,103,000 $3,900,000

**Required**:

A. Determine the ACB of the consideration received by each of the partners as a result of the incorporation and dissolution of the partnership as a result of ITA 85(2) and ITA 85(3).

B. Calculate the capital gain with respect to the partnership interest for each partner resulting from the distribution of the partnership property to the partners on the dissolution of the partnership.

Answer:

***Part A - ACB of Consideration***

**Cash -** The ACB of the cash would be the dollar amount. These amounts would be $620,000 for Howard, $377,000 for Jones, and $203,000 for Delaney.

**ACB of Preferred Shares -** With respect to the preferred shares ITA 85(3)(e) sets the ACB as lesser of:

• Their FMV, which would be $300,000 for each of the three partners.

• The ACB of their partnership interests, reduced by the amount of NSC received.

This latter amount would be calculated as follows for the three partners:

**Howard Jones Delaney**

ACB $1,173,000 $930,000 $756,000

Cash Received ( 620,000) ( 377,000) ( 203,000)

Balance $ 553,000 $553,000 $553,000

For all three partners, the lower amount is the FMV of $300,000, therefore this would be the ACB of the preferred shares.

**ACB of Common Shares -** Under ITA 85(3)(f), the ACB of the common shares would be the ACB of the partnership interest, less the tax cost of the NSC received and the ACB of the preferred shares. These amounts would be calculated as follows:

**Howard**  **Jones**  **Delaney**

ACB - Partnership Interest $1,173,000 $930,000 $756,000

Cash Received ( 620,000) ( 377,000) ( 203,000)

ACB - Preferred Shares ( 300,000) ( 300,000) ( 300,000)

ACB of Common Shares $ 253,000 $253,000 $253,000

***Part B - Capital Gain or Loss***

The POD of each of the partnership interests is equal to the FMV of NSC plus the ACB of any share consideration. The result is that there are no capital gains to any of the three partners as shown in the following table. If the FMV of the NSC had exceeded the ACB of the partnership interests there would have been a capital gain to the extent of the excess.

**Howard**  **Jones**  **Delaney**

POD:

Cash $ 620,000 $377,000 $203,000

Preferred Shares 300,000 300,000 300,000

Common Shares 253,000 253,000 253,000

Total Proceeds $1,173,000 $930,000 $756,000

ACB ( 1,173,000) ( 930,000) ( 756,000)

Capital Gain (Loss) Nil Nil Nil

From an economic point of view the gain is still present. We have deferred recording it for tax purposes by placing a value on the common shares of $759,000 [(3)($253,000)]. This is $1,041,000 below their current FMV of $1,800,000. Note that $1,041,000 is also the difference between the $3,900,000 FMV of the total consideration given and the $2,859,000 value for the total ACB of the partnership interests.

Type: ES

Topic: Partnerships - comprehensive problem: incorporating a partnership (ITA 85(2) & (3))

97) Sarah and Shelly Duval are sisters and professional accountants. While both sisters had worked in large firms for several years, on January 1, 2021 they decided to leave their former employers and form a partnership. At this time, they each made a capital contribution of $235,000 in cash. Their partnership agreement calls for them to share all profits/losses, capital gains, capital losses and any other amounts that would qualify for tax credits equally.

During the partnership fiscal period ending December 31, 2021, the partnership had income of $225,000, all of which was business income. The partnership made no charitable donations in 2021. In 2021 Sarah withdrew $85,000 and Shelly withdrew $72,000.

The partnership's 2022 Income Statement, prepared in accordance with ASPE, is as follows:

**Income Statement**

**Sarah And Shelly Duval Partnership**

**Fiscal Period Ending December 31, 2022**

Revenues $565,000

Business Expenses:

Rent ($37,000)

Amortization Expense (Note 1) ( 9,000)

Office Salaries ( 47,000)

General Office Expenses ( 14,000)

Meals & Entertainment ( 11,000)

Charitable Donations ( 23,000) ( 141,000)

Business Income $424,000

Other Income:

Gain on Sale of Investments (Note 2) $ 6,000

Non-Eligible Dividends 13,000 19,000

2022 Business Income $443,000

**Note 1 -** Maximum 2022 CCA is $14,000.

**Note 2 -** The gain resulted from the sale of temporary investments. The investments had an ACB of $41,000 and were sold for $47,000.

**Other Information**

1. In 2022, Sarah withdrew $205,000 while Shelly withdrew $187,000.

3. In 2022, Shelly's only income was from the partnership. Assume that other than credits related to partnership allocations, Shelly's only tax credit is her BPA.

4. On January 1, 2023, Shelly sells her interest in the partnership to an arm's length individual for $435,000.

**Required:** Calculate Shelly's 2022 federal income tax payable. In addition, determine the taxable capital gain or allowable capital loss that would result from Shelly's sale of her partnership interest. Ignore all CPP implications.

Answer:

***Shelly's 2022 Federal Income Tax Payable***

The Business Income of the partnership would be calculated as follows:

Business Income for Accounting purposes $424,000

Additions:

Amortization Expense $ 9,000

50% Meals & Entertainment 5,500

Charitable Donations 23,000 37,500

Deductions:

CCA (14,000)

2022 Business Income (for ITA purposes( $447,500

Shelly's income and share of charitable donations would be calculated as follows:

**Partnership Share Taxable Income**

Partnership Business Income $447,500 1/2 $223,750

Taxable Capital Gain [(1/2)($6,000)] 3,000 1/2 1,500

Non-eligible Dividends Income 13,000 1/2 6,500

15% Gross Up on Dividends N/A 975

Total Allocations of Income $232,725

Charitable Donations $23,000 1/2 $11,500

Based on the preceding calculation, Shelly's 2022 federal income tax payable would:

Tax on the first $221,708 $51,345

Tax an additional

$11,017 ($232,725 - $221,708) at 33% 3,636

Income Tax Payable before Credits $54,981

BPA [(15%)($12,719)] ( 1,908)

Dividend Tax Credit [(9/13)($975)] ( 675)

Charitable Donations Credit (See Note 1) ( 3,748)

2022 Federal Income Tax Payable $48,650

**Note 1 -** The charitable donations tax credit would be calculated as follows:

[(15%)(A)] + [(33%)(B)] + [(29%)(C)], where

A = $200

B = The Lesser of:

• $11,500 - $200 = $11,300

• $232,725 - $221,708 =$11,017

C = $283 [$11,500 - ($200 + $11,017)]

The charitable donation credit would be equal to $3,748, calculated as [(15%)($200) + (33%)($11,017) + (29%)($283)].

***Taxable Capital Gain from Sale of Partnership Interest***

The ACB of Shelly's partnership interest on January 1, 2023 would be calculated as follows:

**Partnership Share ACB**

Capital Contribution N/A $235,000

2021 Partnership Business Income $225,000 1/2 112,500

2021 Drawings N/A ( 72,000)

2022 Drawings N/A ( 187,000)

December 31, 2022 $ 88,500

2022 Partnership Business Income $447,500 1/2 223,750

2022 Capital Gain 6,000 1/2 3,000

2022 Dividends Received 13,000 1/2 6,500

2022 Charitable Donations ( 23,000) 1/2 ( 11,500)

ACB - January 1, 2023 $310,250

Given this calculation, the taxable capital gain on Shelly's sale of the partnership interest would be calculated as follows:

POD $435,000

Less: ACB ( 310,250)

Capital Gain $124,750

Inclusion Rate 1/2

2023 Taxable Capital Gain $ 62,375

Type: ES

Topic: Partnerships - comprehensive problem: partnership allocations, ACB & the sale of a partnership interest