

# Your Personal Tax Planning Guide 2009-10

	616	689	3,450	1,338	1,246	193	349	220	109
	8,406	8,830	14,498	5,567	5,545	9,747	1,351	370	759
Canadian \$ in millions)									
Interest Rate Contracts								2008	2007
			Within 1 year	1 to 3 years	3 to 5 years	5 to 10 years	Over 10 years	Total notional amount	Total notional amount
Interest rate swaps			\$ 316,504	\$ 319,302	\$ 243,974	\$ 181,318	\$ 55,604	\$ 1,406,125	\$ 950,125
Interest rate agreements, futures and options			546,259	75,678	32,088	19,000	2,289	589,035	1,094,035
Interest rate contracts			862,763	394,980	276,062	200,318	57,893	1,995,160	2,044,160
Foreign Exchange Contracts									
Foreign currency swaps			1,068	1,025	2,874	43,789	2,482	10,850	10,850
Foreign currency interest rate swaps									
Interest rate swaps			25,873	24,175	18,600	22,814	5,450	92,851	72,851
Forward foreign exchange contracts, futures and options			162,025	7,652	7,524	599	42	173,189	173,189
Foreign exchange contracts, futures and options			188,966	32,827	28,998	1,202	7,974	276,890	276,890
Commodity Contracts									
Commodity swaps			29,200	17,500	3,209	860	335	52,368	66,368
Commodity contracts, futures and options			388,921	159,254	36,547	15	-	584,544	575,544
Commodity contracts			418,121	176,754	39,756	875	335	633,932	641,932
Derivative Contracts									
Derivative contracts			32,102	2,562	2,562	-	875	42,500	33,500
Derivative contracts			37,236	25,689	39,456	16,523	842	122,165	122,165

Prepared by Ontario's  
Certified General  
Accountants



CERTIFIED  
GENERAL  
ACCOUNTANTS

We see more than numbers.

# **Your Personal Tax Planning Guide**

2009-10

# MISSION STATEMENT

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Special thanks to CCH Canadian Limited for providing accounting and taxation reference information that was used in this booklet.

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# Introduction

The objective of personal tax planning is to minimize or defer income taxes payable, as part of a long-recognized right for taxpayers to organize their financial/taxation affairs in the most beneficial way possible within legal confines. This requires a thorough understanding of Canada's *Income Tax Act*, plus bulletins, circulars and rulings put forth by the Canada Revenue Agency (CRA), along with other events such as tax rulings in the courts.

This booklet reflects federal legislation to approximately September 15, 2009, plus other draft legislation introduced but not yet passed into law, which are therefore, subject to change before final passage. Unless otherwise stated, the information in this book generally applies to Canadian citizens or residents.

## GENERAL INCLUSIONS/EXCLUSIONS

The *Income Tax Act* is a wide-ranging document, dealing with broad issues such as income from employment, a business or property, while at the same time outlining specific rules in many areas. There are, for instance, rules dealing with the inclusion in taxable income of items such as:

- employment-insurance (EI) benefits received
- annuity payments
- receipts from deferred-income plans

Some payments, such as workers' compensation (WC), federal supplements and social-assistance payments are not included in taxable income, but are contained in the calculation of threshold income when determining entitlement to the:

- child tax benefit
- age credit
- goods and services tax credit (GST)
- old-age security (OAS)
- some provincial tax credits

Other amounts are specifically excluded from income for tax purposes. Examples, which are not discussed in this booklet, include, but are not limited to, the following:

- Income earned by a member of a First Nations' group on a specified reserve.
- Civilian and veterans' war pensions or allowances, from Canada or any ally of Her Majesty.
- Income earned by Canadian Forces' personnel or police officers while serving in certain high-risk overseas destinations.
- Certain other benefits and awards to members of the Canadian Forces.
- Certain personal damage amounts awarded by the courts.
- Payments received by qualified individuals, their spouses or common-law partners and dependants under the multi-provincial assistance package for individuals infected with HIV through the blood-supply program.

- Payments received by a special trust for distribution to Canadians who were infected with the hepatitis C virus through the blood-distribution system over a specified period.
- Government-related compensation for disaster relief.
- An RCMP pension or compensation received in respect of an injury, disability or death.
- Lottery winnings and other windfalls as defined by the CRA.

Amounts that are exempt from income tax by virtue of a stipulation in a tax convention or agreement with another country with the force of law in Canada are also excluded from income.

Special rules might also apply for certain individuals or groups, such as amateur athletes who are eligible for a tax deferral on certain endorsement or other income earned while they retain their amateur status.

#### KEY TERMINOLOGY

One term that is often used in this booklet is “arm’s-length.” This term refers to two parties who are free to act independently, with neither considered to have undue influence nor control over the other’s decisions. Any deal they make is assumed to be fair for income tax purposes. Conversely, certain related parties, which could include people and/or corporations controlled by them, are not considered to be dealing at arm’s-length. “Non-arm’s-length” transactions are subject to special rules. A special provision of the *Income Tax Act*, for example, automatically reduces an excessive price to fair market value (FMV) in a transaction involving parties who are not dealing at arm’s length from each other.

Another term often used is “rollover,” such as a “spousal rollover,” where property is transferred from one spouse to another upon death on a tax-deferred basis. Various types of rollovers are available under the *Income Tax Act*, and such transactions are often complex, requiring professional assistance.

Readers should also note that social changes over the past few years have contributed toward a broader definition of what constitutes a “spouse.” Most references in the *Income Tax Act* now refer to a “spouse or common-law partner.” The term spouse means a party to a legal marriage to an opposite-sex or same-sex partner. Common-law partner means a person of either the opposite or the same sex who has been cohabiting with the taxpayer in a conjugal relationship for at least one year, or is the natural or adoptive parent of the taxpayer’s child.

Personal tax planning includes a concerted effort to minimize or defer taxes payable, a practice that is generally accepted. However, the *Income Tax Act* includes a general anti-avoidance rule (GAAR), which allows the CRA and tax courts to reassess any transaction that is considered to have defeated the object, spirit and purpose of the Act. Under GAAR, for instance, if it appears that a transaction, or series of transactions, has taken place primarily for the purpose of obtaining a tax benefit, it could be subject to adjustment, particularly if it can be established that its application results in a misuse or abuse of the provisions contained within the Act. There have been several court decisions involving the GAAR recently.

As income tax rules are often complex and ever-developing, however, tax planning should be an ongoing process. Taxpayers should, for instance, revise their tax and financial plans as changes occur in government legislation and as personal circumstances dictate. Readers are advised to review specific tax plans with their certified general accountant.



# Major 2009 Federal and Provincial Changes Affecting Individuals

## Federal

### CPI ADJUSTMENT TO INCOME-TAX BRACKETS AND NON-REFUNDABLE TAX CREDITS

The taxable income thresholds in all four federal tax brackets were increased by 2.5 per cent in 2009 to mirror changes in the consumer-price index (CPI). Furthermore, all indexed non-refundable tax credits also increased by 2.5 per cent in 2009 in order to reflect the CPI adjustment. Please see the chapter on federal and Ontario non-refundable tax credits, as well as Appendices I & III, for further details.

### INCREASE IN BASIC PERSONAL, SPOUSAL & ELIGIBLE DEPENDANT AMOUNTS

The 2009 federal budget increased the basic personal, spousal and eligible dependant amounts beyond the projected CPI increase. The new amounts for all three non-refundable tax credits in 2009 is \$10,320 (up from the CPI-projected \$10,100).

### INCREASE IN THRESHOLD FOR LOWER- AND MIDDLE-INCOME TAX BRACKETS

The 2009 federal budget increased the lower and middle tax bracket threshold beyond the projected CPI increase. The new level for the lowest tax bracket is \$40,726 (up from the CPI-projected \$38,832) and for the middle tax bracket it is \$81,452 (up from \$77,664). These increases will also affect the Canada child tax benefit (CCTB), child disability benefit (CDB), and national child benefit (NCB) supplement.

### INCREASE IN AGE TAX CREDIT

The 2009 federal budget increased the age tax credit for taxpayers 65 and over to \$6,408. This is \$1,000 more than the projected CPI increase for 2009 to \$5,408.

### INCREASE IN RRSP WITHDRAWAL LIMIT FROM HOME BUYERS' PLAN

Commencing January 28, 2009, first-time home buyers can temporarily withdraw, without tax consequences, a maximum of \$25,000 from their registered retirement savings plan (RRSP). This is up from the previous limit of \$20,000.

### TAX-FREE SAVINGS ACCOUNT (TFSA)

The 2008 federal budget introduced a new tax-free savings account (TFSA) which, beginning in 2009, allows Canadians who are 18 and older to save up to \$5,000 per year in the TFSA investment vehicle. Unlike an RRSP, investors cannot deduct contributions to a TFSA for tax purposes; however, investment income, including capital gains earned within the TFSA are not subject to tax, even when the funds are ultimately withdrawn.

### INCREASE IN RRSP ANNUAL CONTRIBUTION LIMIT

The annual RRSP contribution ceiling was raised to \$21,000 in 2009, from \$20,000 in 2008. It is scheduled to rise to at least \$22,000 in 2010, after which the annual maximum contribution rates will be indexed to reflect increases in average wage growth.

## **INCREASE IN RPP ANNUAL CONTRIBUTION LIMIT**

Money-purchase plan registered pension plan (RPP) contribution limits increased in 2009 to \$22,000, from \$21,000 in 2008; in future, they will be indexed annually to account for the average wage growth.

The maximum annual contribution limit for defined-benefit RPPs also increased in 2009 to \$2,444 per year of service, up from \$2,333 in 2008; in future they will be indexed on an annual basis to reflect increases in average wage growth.

## **CANADA CHILD TAX BENEFIT PAYMENTS (CCTB)**

Beginning July 2009, CCTB national child benefit (NCB) supplement payments to Canadians rose to \$2,076 for the first child (from \$2,025), \$1,837 for the second child (from \$1,792) and \$1,747 for each subsequent child (from \$1,704).

As a result, the maximum annual benefit under the combined CCTB and NCB supplement increased to \$3,416 (from \$3,332) for the first child; to \$3,177 (from \$3,099) for the second child; and \$3,180 (from \$3,102) for each subsequent child. The maximum indexed child disability benefit (CDB) supplement for parents in low- and modest-income families with children who have disabilities and a net family income of less than \$40,726 (from \$37,885), increased to \$2,455 (from \$2,395) in 2009.

## **NEW FIRST-TIME HOME BUYERS' TAX CREDIT (HBTC)**

First-time home buyers who purchase a qualifying home on or after January 28, 2009 are eligible for a non-refundable tax credit of up to 15 per cent on \$5,000, or \$750.

## **INTRODUCTION OF TEMPORARY HOME RENOVATION TAX CREDIT (HRTC)**

The 2009 federal budget proposed a temporary home renovation tax credit (HRTC) of 15 per cent on eligible expenditures in excess of \$1,000, and up to \$10,000 for work performed or goods acquired in relation to certain home (including cottage) renovations of an enduring nature incurred between January 28, 2009 and January 31, 2010, inclusive. This credit, worth up to a maximum \$1,350, will only apply to the 2009 taxation year.

## **ACCOUNTING FOR ONLINE INCOME**

The CRA announced in July 2009 that online income earned by individual and corporate taxpayers as a result of selling items via electronic sources such as eBay Canada is taxable.

# **Ontario Provincial**

## **INCREASED THRESHOLD FOR ALL INCOME TAX BRACKETS**

The taxable income thresholds in all three Ontario provincial tax brackets were increased by 2.3 per cent in 2009, reflecting changes to Canada's consumer-price index (CPI) in Ontario. All indexed non-refundable tax credits also increased by 2.3 per cent.

Please see the chapter on federal and Ontario non-refundable tax credits, as well as Appendices I, III and V, for further details.

#### **INCREASE IN ONTARIO CHILD BENEFIT**

The Ontario child benefit (OCB) maximum increased to \$1,100 on July 1, 2009 (up from \$600), reduced by eight per cent of adjusted family net income in excess of \$20,000.

The OCB payment timetable has been accelerated by two years. It was originally supposed to rise to an annual maximum of \$1,100 per child by July 2011. The government has committed to increasing the OCB annual maximum to \$1,310 per child by approximately the end of 2013.

#### **NEW HARMONIZED SALES TAX**

The Ontario government announced in its 2009 budget that it intends to adopt a harmonized sales tax (HST) on July 1, 2010. The HST will be 13 per cent, combining the provincial retail sales tax of 8 per cent, with the federal goods and services tax (GST) of 5 per cent.

#### **REDUCTION IN LOWEST PERSONAL INCOME TAX RATE IN 2010**

The government announced its intention to reduce the rate in the lowest provincial tax bracket by one percentage point, from 6.05 per cent, to 5.05 per cent, effective January 1, 2010.

#### **DECREASE IN PROVINCIAL SURTAX LEVEL IN 2010**

The government announced a decrease to the basic tax level at which provincial 20 per cent and 36 per cent surtaxes are imposed in 2010. The 20 per cent surtax, imposed on basic Ontario tax over \$4,257 in 2009, will be reduced to encompass basic provincial tax over \$3,978 in 2010. The 36 per cent surtax level (for a total of 56 per cent) will be decreased from \$5,370 of basic tax in 2009 to \$5,091 of basic tax in 2010.

#### **VARIOUS PARALLEL MEASURES TO FEDERAL INITIATIVES**

The Ontario provincial government has paralleled certain measures announced by the federal government, including enhancing the limits of the province's Ontario innovation tax credit (OITC) to follow improvements made to the federal scientific-research & experimental-development (SR&ED) tax credit; as well as having announced various capital cost allowance measures (CCA), among others.

# Part One: Income and Expenses

## Employment Income, Expenses and Allowable Deductions

### TAXABLE BENEFITS DERIVED FROM EMPLOYMENT INCOME

The value of most benefits derived from employment is included in personal income. Among the myriad benefits which generally must be included in income are the following:

- Tips and gratuities must be reported as income, even though they may not necessarily be included by employers on the employee's T4 slip.
- Employees who are awarded near-cash merchandise, such as a gift certificate, must take the fair-market value of that award into account as taxable income.
- Subsidized long-term accommodation provided by an employer for the employee's benefit.
- Employees or ex-employees who receive periodic payments under a disability insurance plan, sickness or accident-insurance plan or income-maintenance-insurance plan to compensate for loss of income from an office or employment must include that amount in income if the plan's premiums were paid by the employer; however, they may deduct from income any amount they may have personally contributed toward such a plan.
- Employees who exercise an option to purchase an automobile from their employer at less than its fair-market value (FMV) are considered to have received a taxable benefit for the difference between the price paid and FMV.



Flexible employee benefit programs, which allow employees to custom-design their own package of health and other benefits, are now very popular in the workplace. Take care when structuring such plans, however, because taxable benefits can result. If, for example, an employee accumulates flex credits and those benefits are received in cash, that amount is generally considered taxable income.

### NON-TAXABLE BENEFITS DERIVED FROM EMPLOYMENT INCOME

Although the majority of benefits derived from employment must be included in personal income, there are several exceptions. These include: employers' contributions to private health-service plans; group sickness or accident plans; registered pension plans (RPP); and deferred profit-sharing plans (DPSP).

Other examples of non-taxable benefits include, but are not limited to:

- Ordinary discounts on the employer's merchandise, available to all employees on a non-discriminatory basis.
- Subsidized meals available to all employees, provided a reasonable charge is made to cover direct costs.
- Effective in 2009, an overtime meal allowance of up to \$17 for two or more hours of required overtime adjacent to regular working hours, if the overtime is infrequent or occasional (generally once or twice a week, outside of peak periods).



Non-taxable expenses for a temporary work site might apply for varying lengths of time, such as a week, a month or a year. The key is that they apply for a reasonable and determinate period of time—generally with about a two-year maximum (although this could vary), with a scheduled date of return to the employee's regular place of employment.

- The cost for distinctive uniforms, protective clothing or footwear required to be worn during employment, including related laundry expenses.
- Reimbursement of moving expenses upon relocation.
- Receipt of up to two non-cash gifts (e.g., for Christmas, wedding, birthday) in one year, for certain material items and under certain conditions, with a total cost to the employer not exceeding \$500, including all applicable taxes.
- Receipt of up to two non-cash awards in one year, for certain material items and under certain conditions, with a total cost to the employer not exceeding \$500, including all applicable taxes.
- Use of the employer's recreational facilities, or employer-sponsored membership in a social or athletic club, where such membership is considered all or primarily beneficial to the employer (despite the employer not being able to deduct the cost of such fees).
- An employer-mandated medical examination required as a condition of employment.



The CRA has ruled that there is no taxable benefit to you if your employer arranges for the purchase of a discounted fitness-pass membership from a third party.

- Employer-sponsored personal counselling services in respect of the mental or physical health of an employee or a person related to an employee, or concerning re-employment or retirement.
- Employer-sponsored travel where the trip was undertaken predominantly for business reasons.
- Employer-sponsored training costs that are work-related.
- Tuition and related fees, if the course is required for employment and is primarily for the employer's benefit.
- A reasonable per-kilometre automobile allowance.
- Employer-paid cellular phones and other such hand-held devices as long as they were used primarily for business purposes.
- Board, lodging and transportation to special worksites involving duties of a temporary nature, or to remote worksite venues away from the general community where employees are required to be a reasonable distance from their principal residence for at least 36 hours.
- A reasonable employer-provided allowance for an employee's child to live at and attend the nearest suitable school, if one is not close to where the parents must reside for employment purposes.
- The value of scholarship awards provided by an employer for the benefit of their spouse and/or children.

- Employer-paid expenses for moving employees and their family, along with household effects, out of a remote location upon the termination of employment.
- Exclusive on-site child-care services provided by employers to all employees for minimal or no cost.



If you are an emergency-services volunteer, the first \$1,000 in payment you receive from a government, municipality, or other public authority may be tax free.

#### **SPECIAL CONSIDERATIONS RELATED TO TAXABLE AND NON-TAXABLE EMPLOYMENT INCOME**

Other current issues with respect to the taxability and non-taxability of employee benefits include, but are certainly not limited to, the following points:

- An employer-provided computer and internet service might not represent a taxable benefit under certain circumstances if employees require such a service to carry out their business obligations; however, the costs associated with purchasing an employer-funded computer that is also used for personal reasons would likely result in a taxable benefit.
- Taxpayers who receive an arbitration award from their employer for reasons such as a collective agreement breach to compensate for lost wages, or receive retroactive payments as a result of a decision such as pay equity — a component of which might constitute damages — should consult a certified general accountant to determine the appropriate tax treatment for that payment.
- In some cases, the courts may be more lenient toward an employee than a shareholder in terms of any benefit amount deemed to be non-taxable. For instance, employees might be able to exclude 100 per cent of membership fees in a golf club if their membership is primarily for the benefit of their employer. On the other hand, corporate shareholders might have to apportion the tax-exempt and taxable portion of their fees between business and personal use, respectively. Taxpayers — especially those with dual employee/shareholder roles — should clarify the proper tax treatment with their certified general accountant.
- Although child-care expenses that have been paid for by an employer are generally considered a taxable benefit, if an employee is required to travel out of town on employment-related business and, as a result, incurs additional child-care expenses that are reimbursed by the employer, that amount will not be a taxable benefit.
- If spouses accompany employees on a business trip, and the employers reimburse their travel expenses, that payment is a taxable benefit to the employees unless the spouses were engaged primarily in business activities on behalf of the employers during that trip.
- Certain accumulated personal credit arising from loyalty incentives (i.e., frequent-flyer programs during business trips) are taxable to employees and included in their income, especially if they use a company credit card. However, in other instances and under certain circumstances involving a personal credit card, it may be non-taxable. In 2009, for instance, the CRA introduced more lenient rules with respect to points accumulated through loyalty programs.

- Certain members of the clergy or religious organizations are entitled to exclude from income reasonable allowances with respect to transportation expenses incurred while discharging their duties.

Check with your certified general accountant for details.

#### **EMPLOYEE STOCK OPTIONS**

Employees who acquire certain publicly listed shares under employee stock-option plans are entitled to defer the associated stock-option benefit, subject to an annual \$100,000 vesting limit, until such shares have been disposed. This deferral is available for shares acquired after February 27, 2000, but is also subject to certain conditions.

If all conditions have been met and the employees elect to defer that tax, they must file a letter by January 15 of the year after the share is acquired (e.g., January 15, 2010, for shares acquired in 2009), complete with the following information:

- A request to have the deferral provisions apply.
- The stock option benefit amount related to the deferred shares.
- Confirmation that the employees were resident in Canada when the shares were acquired.
- Confirmation that the \$100,000 annual vesting limit has not been exceeded.

The tax consequences with respect to stock-option plan shares exercised after February 27, 2000, can be quite complicated. For example, special rules might apply that create a deemed dividend and a capital loss.

Holders of employee stock options exercised prior to February 28, 2000, were subject to the long-standing rule that during the year they exercised such an option, the excess of the stock's fair-market value (FMV) at the date acquired, over the option's exercise price, was taxable as employment income and must be added to the cost-base of shares. Any subsequent gain or loss on disposal — measured from the cost base — was a capital gain or loss.

There were, however, also a series of complex exceptions to that rule and holders of stock-option shares exercised on or after February 28, 2000, which do not qualify for the deduction, are still subject to those rules and exceptions.

Consult your certified general accountant for more details about the correct treatment for stock options or other arrangements, such as exercising warrants to buy or sell shares from an employer.

#### **DEFERRED COMPENSATION**

A deferred compensation agreement is an agreement to pay wages at a later date for services rendered now. However, the *Income Tax Act* does not allow employees to defer income recognition until it is received. Remuneration that would have been paid had the employee not opted to defer it must be included in the employee's income and also deducted by the employer.

This eliminates the potential income tax advantages that could arise from funded and unfunded deferral plans that are based on unlikely contingencies. When receipt of funds is subject to contingencies, those conditions will be

ignored and the employee taxed unless there is a substantial risk the contingency will not occur, with the amount, therefore, forfeited.

Deferred signing bonuses may also be considered part of a salary-deferral arrangement unless the employment contract stipulates that the employee must render additional services in exchange for earning that extra amount.

Specifically excluded from the definition of salary-deferral arrangements are:

- registered pension funds or plans
- disability or income-maintenance insurance plans under policies with insurance companies
- deferred profit-sharing plans (DPSP)
- employee profit-sharing plans
- employee trusts
- group-sickness or accident-insurance plans
- supplementary unemployment-benefit plans
- vacation-pay trusts
- plans or arrangements established for the sole purpose of providing education or training to employees to improve work-related skills
- plans or arrangements established to defer the salary or wages of a professional athlete
- employee bonus plans under which employees receive their annual bonuses within three years of the applicable year-end
- prescribed plans or arrangements, such as sabbatical plans or deferred-salary-leave plans (DSLPL)

Individuals who participate in a deferred-salary-leave plan must return to regular employment following a leave of absence for a period that is at least as long as the leave itself. Otherwise any deferred amounts, plus unpaid interest, immediately become taxable as employment income — whether paid out or not — during the taxation year the taxpayers realize they can't return to work for the specified period.

If employees have the opportunity to obtain additional vacation time via flex credits or payroll deductions, and that vacation time is carried forward until the next calendar year, the CRA has warned this might be considered a salary deferral arrangement for tax purposes.

Salary-deferral-arrangement taxation rules might also apply when employees take a funded leave of absence just prior to retirement due to unused credits provided under a flex plan. See your certified general accountant for details.

#### **DEDUCTIONS FROM EMPLOYMENT INCOME**

Employment-income deductions are restricted to those items specifically provided for in the *Income Tax Act*. Besides automobile and legal expenses, which are discussed in the next chapter, other deductible expenses may include:

- Expenses of up to two-thirds of earned income for attendant-care expenses necessary for a medically impaired person to earn business or employment income. Form T2201 — Disability Tax Credit Certificate is required when





Union dues do not necessarily have to be paid to a Canadian organization. Therefore, employment-related annual dues paid to a trade union outside Canada might also be tax deductible.

making this claim. (Note: this amount potentially reduces the availability of any medical-expense credit for full-time attendant care).

- Union dues and professional fees if required to maintain membership.
- Employment-related travel expenses, including parking, taxis, bus fare, etc., if required by the terms of employment and not reimbursed.
- Assistants' salaries and supplies, if required to be paid without reimbursement by the terms of employment.
- Office rent and expenses, if the employees and employers have agreed that the employees are to provide their own working environment. It must be their principal workplace or used exclusively, on a regular and continuous basis, for activities such as business-related meetings. If the qualified workspace is in the employees' homes, the employees may be allowed a pro-rata deduction for rent paid, maintenance, utilities and minor repairs. Expenses related to mortgage interest, property taxes and insurance may not be deducted (unless, in the case of property taxes and home-insurance premiums, they are related to commission sales expenses). To the extent that a claim for workspace in the home exceeds employment income, that portion of the deduction is denied in the current year; however, it may be carried forward indefinitely against future income resulting from the same employment.
- Musical instruments — capital-cost allowance (CCA) and related rental, insurance and maintenance costs — may be claimed only against income earned directly from using the musical instrument.
- Aircraft — CCA, interest expense and operating and maintenance costs related to business use.



A computer used by a professor to teach and create music was ruled to be a musical instrument and thus eligible for employment deductions, by the tax courts.

Apprentice mechanics of self-propelled motor vehicles can write off expenses for tools of the trade acquired after 2001. The amount eligible for write-off is that by which the annual cost of tools (plus the last three months of the previous year, if it represents the first year of employment) exceeds the greater of \$1,000 or five per cent of the apprentice's related income for that year. Unused amounts can be carried forward for deduction in a subsequent taxation year.

Provisions are also available for various tradespeople to claim an additional credit of up to \$500. Apprentice vehicle mechanics can deduct this amount on top of existing write-off opportunities.

Employers must complete Form T2200 — Declaration of Conditions of Employment to legitimize these deductions.



An assistant's salary might include amounts paid to a spouse or other family member if the salary is reasonable for the amount of work performed.

Employees and partners claiming expenses on their tax returns may be entitled to claim a refund for the business-use portion of the GST paid. The GST rebate must then be reported as income in the year it is received. To claim a refund, complete Form GST 370 — Employee and Partner GST/HST Rebate Application. For a copy of this form and more information, obtain the CRA's *Completion Guide and Form for Employee and Partner GST Rebate*.

Certain members of the clergy or religious organizations may be entitled to deduct an amount paid for living accommodation. They must complete Form T1223 — Clergy Residence Deduction in order to determine that amount. Special rules for expense deductions might also apply to employees, such as artists, and those who are required to move temporarily to a work camp for their jobs, like individuals involved in forestry operations.

Consult your certified general accountant for more details.



If required by your employer to work at home after business hours, deductions might be available in certain instances if employment after hours is considered by an employer and/or union to constitute a separate working arrangement.

### COMMISSION SALES EXPENSES

Commissioned salespeople, if required by contract to pay their own expenses, may be able to deduct those expenses against commission income. To do so, both the employee and employer must complete portions of Form T2200.



If your expenses exceed commission-related income, there may be alternative methods of making claims available to you. Consult your certified general accountant for advice on how to maximize tax savings.



If you are a commissioned employee, consider leasing rather than purchasing capital equipment (such as a computer) where CCA is not allowed.

Commissioned employees are allowed a broader range of deductions than other employees in areas such as advertising, promotion, meals and entertainment. Furthermore, commissioned salespeople, unlike other employees, are allowed to deduct a pro-rata share of property taxes and home-insurance premiums against commission income if their workspace is in their home. Such deductions are generally limited to offsetting the amount of commissions earned.



Commissioned life-insurance salespeople are allowed to deduct commissions earned with respect to the purchase of their own policies.



A commissioned sales employee who works in the home should ensure that a separate business telephone line exists for regular phone expenses, other than business long-distance charges, to be deductible.

Although the restrictions for commissioned employees are mainly similar to those for salaried employees, there are notable exceptions. For instance, CCA (a full description of capital cost allowance is on page 36) on an automobile or aircraft used for business may be deducted against other income to the extent that it has already been used to fully reduce commission income, with any residue allowable as a non-capital loss. The interest paid on money borrowed to purchase such an automobile or aircraft may also be deducted.

Check with your certified general accountant about the correct tax treatment to be accorded advances against commission income.



Additional expense-deduction provisions might be available to you if you sell property or negotiate contracts on behalf of your employer, provided you normally work away from the employer's office; must pay your own expenses; and are remunerated in whole or in part by commissions. Contact your certified general accountant for details.

## Other Taxable Benefits

### USE OF COMPANY CARS

An employee or shareholder using a company car for strictly business purposes does not incur a taxable benefit.

However, where the use of the automobile involves some personal use, a taxable benefit does occur. A standby charge consisting of two per cent of the automobile's original cost (one and one-half per cent for a car salesperson) or two-thirds of the lease cost, plus GST, applies for each month the automobile is available for the employee's personal use.

If personal use of the automobile does not exceed 20,000 kilometres annually, and the automobile is used for business more than 50 per cent of the time, a proportional standby-charge reduction is permitted. If, for example, a vehicle was driven 40,000 kilometres, including 25,000 kilometres for business (more than half) and 15,000 for personal purposes, the actual standby charge



The full operating benefit for personal use of an automobile applies if the employer pays any operating expenses. Therefore, it may benefit you to fully reimburse your employer for such coverage.

would be calculated as 75 per cent (15,000 divided by 20,000) of the regular standby charge.

When both the employer and employee/shareholder have contributed toward purchasing an automobile, its cost for the purposes of calculating a standby charge would be reduced by the amount paid by the employee/shareholder.

Where an employer is primarily engaged in selling or leasing luxury automobiles, special considerations involving the value of multiple automobiles might have to be taken into account when calculating the standby charge calculation. Please consult your certified general accountant for further details if this affects you.



A standby charge may not apply under certain, well-defined, circumstances. If, for instance, the employer's policy is to have you return the automobile to company premises when you embark on a business trip, the standby charge should be prorated to exclude those days. But if you voluntarily leave the automobile at your employer's premises over that period, those days will probably count toward the standby charge.

In addition to the standby charge, the employee must calculate an operating benefit, using one of two options.

In 2009, they may elect to make a general declaration of 24 cents per kilometre for personal use; 21 cents per kilometre if selling or leasing automobiles constitutes their principal source of employment (both amounts unchanged from 2008). Alternatively, if the car is used more than 50 per cent for business, the deemed operating benefit may be one-half of the standby charge, provided the employee notifies the employer in writing before the end of the year. As with other taxable benefits, GST is deemed to be included in the operating benefit.

The operating benefit may also be reduced by any amount reimbursed to the employer within 45 days of the calendar year-end.

For capital-cost-allowance (CCA) purposes, employers are restricted to \$30,000 of the automobile cost on purchases made after 2000, not including federal and provincial sales tax. The annual CCA allowance is 30 per cent on a declining-balance basis, except for the year of acquisition when the allowance is limited to one-half or 15 per cent. Each car costing more than the allowable limit at the time of purchase is included in a separate CCA class with no recapture or terminal loss available upon disposal.

(A more complete description of CCA and how it works is on page 36).

The deduction for interest on money borrowed is restricted to a maximum of \$300 per month if the automobile was purchased after 2000.

If the automobile is leased as per an agreement entered into after 2000, the maximum deduction is \$800 per month (excluding PST and GST). This limit helps to ensure that the deduction level is consistent for both leased and purchased vehicles. Another restriction prorates deductible lease costs in situations where the value of the vehicle exceeds the CCA limit.



The standby charge is calculated on the vehicle's original cost regardless of its age. If it is an older vehicle, consider purchasing the car from your employer. Note, however, that if a leased automobile is purchased at less than its fair market value, the difference is considered a taxable benefit and must be included in your income.

The employee benefit is generally calculated on the vehicle's full cost, regardless of the fact the employer is limited in the amount of capital cost, finance charges or lease payments permitted as a write-off for a passenger vehicle.

Note that some vehicles, such as those used for emergency response purposes (i.e., medical, fire or police) are not defined as automobiles for income-tax purposes.

#### **USE OF EMPLOYEE-OWNED CAR**

Employees who are required to travel on business or work away from their employer's office can use their own automobile. Employees required by terms of employment to provide their own vehicle and who want to deduct the employment-related costs of operating the car, or any other employment-related expense (see Deductions from Employment Income, page 15), must file form T2200. The employer must sign this form annually, certifying the required conditions were met during that year.



Keep a record log, in addition to relevant travel receipts, to support business mileage. Without a statistical record, a taxpayer often has a tendency to overestimate the percentage of kilometers incurred as a result of business activities.

Employees who are required to pay their own automobile expenses are entitled to deduct business-related vehicle expenses that are not reimbursed by the employer. Deductions for the capital cost or lease cost of the vehicle are limited in their extent just as they are for employer-owned automobiles.

Deductions for expenses such as gasoline, insurance, maintenance, licence, auto-club membership, leasing costs and interest on money borrowed to purchase the car are normally allowable in the same proportion as business to total kilometres driven during the year. Major accident repair costs, minus insurance proceeds or damage claims, are also fully deductible provided the vehicle was used for business, not personal, purposes at the time of the accident.

Travel between an employee's home and the employer's office is generally considered to constitute personal, rather than business, use of the automobile. In 2007, however, a taxpayer successfully appealed a CRA decision to disallow expense deductions incurred to and from the office on the grounds that their employer required them to have a car at work every day, thus preventing them from commuting using less expensive modes of transportation. Furthermore, if required to make a business stop between their home and office at the request of their employer, the entire distance travelled throughout the day may constitute business, rather than personal use.



If your employer allows you to keep an office in your home, but also requires that you travel to head office on business, related travel-expense allowances have, under certain circumstances, been ruled by the courts as being exempt from taxation.

Any proportion of an employer-paid automobile allowance that is deemed by the CRA to be unreasonably high is taxable to the employee. The maximum amount the employer may claim in 2009 has been established by the CRA at 52 cents per kilometre for the first 5,000 kilometres of business travel in a year, and 46 cents per kilometre thereafter (both amounts unchanged from 2008).

Alternatively, an employee who receives an unreasonably low allowance may choose to include that amount in income and then deduct the actual business-use expenses. However, employees cannot refuse to accept a reasonable allowance without also jeopardizing their ability to claim a deduction for automobile expenses.



A salesperson or other employee who lives and travels in a motor home might be able to deduct expenses of that motor home relative to the proportion it is used for business (i.e., distance travelled).

Traditionally, an allowance based on anything other than actual business travel on a per kilometre basis has not been considered reasonable and must, therefore, be included in the employee's income. Similarly, should the actual expenses be reimbursed, any additional allowance would be considered unreasonable and need to be treated as income.

However, in 2009, the CRA said that, under some circumstances, employer-provided travel allowances within a municipality or metropolitan area can be excluded as a taxable benefit if the primary beneficiary is the employer.

It is acceptable for an employer and employee to agree on a periodic advance based on a reasonable estimate of business kilometres driven. At the calendar year-end or termination of employment, whichever comes first, the employee and employer must reconcile that advance against the actual distance travelled on behalf of the company. If the advance was inadequate, the employer must make up the shortfall, whereas the employee must return any excess should the reverse situation occur. Once an employee receives a reasonable allowance to cover all employment-related use of the automobile, no further expenses can be claimed for tax purposes.



If you have an arrangement with your employer that involves a combination of both a flat rate and per-kilometre travel allowance for the same vehicle, the tax treatment might be complex, particularly if some automobile expenses were also reimbursed. Your certified general accountant can assist in this process.

Employer-subsidized parking must generally be included in income if the benefit is being provided primarily to the employee. However, if the parking spot is provided for the primary benefit of the employer, to allow the employee to use an automobile in the course of carrying out business-related duties during office hours or save on taxi fares when required to work late, all or a proportion of this amount might be reduced or waived.

#### LOANS TO EMPLOYEES

A loan or any other debt owed by employees to their employers potentially creates an attributed taxable benefit based on the prescribed rate of interest set quarterly by the CRA. The employers must record any difference between the prescribed and actual interest rates as employment income on the employees' T4s.

When borrowed funds are used to acquire either income-producing property or an automobile or aircraft for employment use, the interest amount actually paid or imputed may be deductible as an offsetting expense against the resulting investment or employment income.



Borrowing funds from your employer may prove to be more efficient and less expensive than other sources, even though you may pay tax on the imputed interest benefit. Note, however, that careful evaluation of borrowing alternatives may require professional advice.

The imputed benefit of a loan used for a home purchase or refinancing is calculated using the lesser of the prescribed rate in effect at the time the loan was made (refer to Appendix VII, page 136), or the prescribed rate for each quarterly period the loan remains outstanding. Employees will remain liable for this taxation benefit even if they transfer the home to a relative. All employee home-purchase loans are deemed to have a five-year maximum term, after which they are deemed to have been re-established at the prescribed rate in effect at that time.

Employees who receive a home-relocation loan from an employer for a move designed to bring them at least 40 kilometres closer to their new place of business may be eligible to deduct attributed interest on up to \$25,000 of loan principal for five years.

When the full or partial proceeds of a loan from an employer are forgiven, that amount is considered to be a taxable benefit to the employee.

The tax treatment on loans to employees might be less favourable if the employees are also shareholders of the company making the loan.



If you expect interest rates to increase, consider renegotiating an employee home-purchase loan for an additional term. If you have predicted correctly, the taxable benefit might be minimized over the next five years of that term.

## RETIRING ALLOWANCE AND TERMINATION PAYMENTS

A retiring allowance paid to an employee upon or after retirement to recognize long service or to compensate for office or employment loss must be included in income. Retirement refers to retirement from an employer, regardless of whether the employee is of normal retirement age. If the employee receives the allowance in instalments, they are taxable in the year received.

The employer is not required to withhold tax if the tax-eligible retiring allowance is contributed directly to the employee's registered retirement-savings plan (RRSP). Otherwise, if the employee receives the payment directly, tax must be withheld. Employees may then contribute to their plan up to 60 days after the year of receipt, claim that amount as a deduction on their tax return, and recover the corresponding tax withheld.



An employee who retires but retains a seat on the board of directors of a private company at nominal compensation might still be eligible to collect a retiring allowance.

In addition to an individual's normal RRSP contribution limits, retiring allowances transferred to an RRSP are allowable to a maximum of \$2,000 for each employment year prior to 1996, plus an additional \$1,500 for each employment year prior to 1989 in which the employee did not have vested rights in an employer-sponsored pension plan at retirement.

Years of past service need not have been continuous. Where there were gaps in employment and the employee has "bought back" years of service under a registered pension plan, special taxation rules may apply.

The fair market value of certain benefits of significant value received by an employee in recognition of long service will also likely qualify as a retiring allowance under the *Income Tax Act*. If, for instance, an employer buys out an automobile lease on behalf of an employee at a discount from fair market value, any resulting taxable benefit could qualify as a retiring allowance.

The payment of accumulated sick-leave credits may also qualify as a retiring allowance if such payment is made in recognition of long service or in respect of the loss of an office or employment.

The fair-market value of other property, such as shares, jewelry or life-insurance policies, which are not paid for, but instead received in respect of a loss of office or employment, may also be considered part of an employee's retiring allowance and, therefore, included in income.



In cases involving a loss of office or employment, you may receive an amount awarded as damages by a human-rights tribunal. If that amount is part of a retiring allowance, you might be able to exclude a reasonable amount of such an allowance from income for tax purposes.





Legal fees incurred in a termination case do not necessarily have to be paid to a lawyer in order to be deductible. Fees paid to another professional, such as a labour-relations consultant retained to negotiate a severance package, may also be deductible.

All or a portion of payments with respect to a loss of employment may still qualify as a retiring allowance, even if they are made before the employer/employee relationship has been formally severed. If, however, a retiring allowance initiates while an employee remains on the company's payroll there must be some evidence the cessation of that relationship, including the receipt of individual employee benefits, (i.e., they don't also extend to other former employees) is scheduled to occur at a fixed date.

The CRA stated in 2006 that if, following retirement, employees are rehired by the same employer or by an affiliated, non-arm's-length company pursuant to an arrangement made prior to retirement, they would generally not qualify for retiring allowances. However, it also identified certain exceptions where the retirement allowance might not be adversely affected, such as when retired civil servants subsequently obtain part-time employment in a different area of government, without any continuation of pension benefits, solely through their own efforts. Such cases will be examined on an individual basis.

Taxpayers who receive a retroactive lump-sum payment of at least \$3,000 as part of a lump-sum settlement related to dismissal from an office or employment (or other qualifying award) may qualify for federal tax relief. A mechanism exists to provide such taxpayers with the opportunity to deduct any excess tax liability that may result from declaring settlement proceeds all at once as they must do under the current system, rather than being able to apply it retroactively to the respective year(s) related to the settlement.



A severance amount paid to a spouse or common-law partner as a result of working in a family business such as farming may qualify as a retiring allowance regardless of past remuneration, provided an employer/employee relationship existed over that period and the proposed retiring allowance is considered reasonable by the CRA.

#### **RETIREMENT COMPENSATION ARRANGEMENT (RCA)**

A retirement compensation arrangement (RCA) might be established under which the taxpayer's current or former employer or another non-arm's-length party has contributed funds. Such payments, made prior to retirement or the loss of an office, would be designed to fund future payments in case the taxpayer vacates that office. The RCA may provide for discretionary payments prior to the loss of such office if the taxpayer can prove there has been a "substantial change" in the services required.

Examples of a substantial change in duties may include situations such as where a former officer of a company is retained as a consultant, or a professional athlete resigns as a player but continues to provide services to the sporting franchise as a member of the coaching staff or scout.

RCA plans are very specific and do not overlap with other plans such as a deferred profit-sharing plan, employee profit-sharing plan or employee trust, among others. Consult your certified general accountant for more details.

#### **LEGAL EXPENSES INCURRED**

Taxpayers can deduct legal expenses incurred and paid during the year to obtain a pension benefit or retiring allowance in respect of employment. In any single year this deduction is limited to the pension or retiring allowance received, less any related transfer to an RRSP or RPP. Expenses that are not deductible in a particular year may be carried forward seven years.

A separate provision of the *Income Tax Act* allows individuals to deduct legal costs paid to collect salary or wages. Even if they are never collected, a deduction is allowed provided the employee incurs costs to establish a right to wages or salary.

Legal expenses associated with establishing a right to collect salary or wages may be incurred from a variety of sources including, for example, a former or current employer or a professional association.

In a related matter, it used to be the long-standing administrative practice of the CRA not to tax prejudgment interest on awards with respect to wrongful dismissal. However that policy changed in 2004 and prejudgment interest relating to wrongful dismissal is now taxable. Check with your certified general accountant to determine the correct tax treatment if this situation applies to you.

#### **DEATH BENEFITS**

When an employee dies and an employer makes a payment to the surviving spouse or common-law partner or other beneficiary in recognition of the deceased's employment, the first \$10,000 of this amount is generally a tax-free death benefit.

This \$10,000 exemption first applies to the surviving spouse or common-law partner. If the surviving spouse or common-law partner receives less than \$10,000 and other beneficiaries are entitled to receive a benefit in respect of the employee, their exempt limit will be \$10,000 less any amount already claimed by the surviving spouse. The remaining exempt portion would then be shared on a pro-rata basis among the other beneficiaries.

From a tax point of view, it is possible to have more than one spouse or common-law partner (e.g., a legally married spouse and a common-law partner). If more than one spouse or common-law partner is entitled to receive a death benefit with respect to a deceased individual, the resulting benefit must be allocated on a pro-rata basis.

### **Income and Dividends from a Business and Self-Employment**

Self-employed individuals, unlike those who are employed by others, have the right to control a number of factors in their work environment, such as the hiring and firing of staff, wages or salary to be paid, and the place and manner in which work is done, including the freedom to service more than one client. They are also responsible for supplying the tools of their trade along with covering overhead and other expenses.



Self-employment might also exist in circumstances where a worker is hired through an agency for various temporary assignments.

A measure of uncertainty arises with that control. Generally speaking, self-employed individuals, unlike employees, have no guarantee of a steady income because their remuneration depends on the continuing success of their business enterprise; thus, there is a greater degree of financial risk.

The CRA Guide RC4110, entitled *Employee or Self-Employed?*, outlines detailed criteria for determining whether a taxpayer is employed or self-employed. The major themes of this booklet include an analysis of who has control over the working environment and time spent on the job; who owns the tools and equipment necessary to do the job; as well as who bears the brunt of responsibility for a potential risk/reward scenario when it comes to a financial profit or loss.

Determining whether an individual should be classified as self-employed or as an employee for tax purposes is sometimes complicated. Your certified general accountant can assist you in making this determination.

#### **ACCOUNTING FOR BUSINESS INCOME**

With the exception of farmers and fishers, self-employed taxpayers generally must declare income in the period it is earned, even if the remuneration billed for is collected in a subsequent period. Expenses incurred to earn that revenue must be matched in the same period, even if they are paid in a subsequent time frame. This is known as the accrual basis of accounting.

Under accrual accounting, for instance, construction contractors would normally declare any progress billings made, less amounts withheld pending satisfactory completion of a job, as earned income for that period. However, contractors may also elect to include such holdbacks in their income for that year, provided they administer the same accounting treatment to all contracts.

The correct tax treatment to apply in specific instances involving work in progress could differ. Your certified general accountant can assist you in this area.

#### **ACCOUNTING FOR ONLINE INCOME**

The CRA announced in July 2009 that online income earned by individual and corporate taxpayers as a result of selling items via electronic sources such as eBay Canada is taxable. The Agency said they will also conduct audits to ensure eBay sellers "have filed all required returns and accurately represented the full scope of their business income."

#### **ROYALTY INCOME**

Royalty income, such as that received by an author or musician, is generally considered to be investment income, although it might also be classified under some circumstances as business or employment income.

Because the tax treatment for royalty income can be complicated, it is best to check with your certified general accountant to determine the correct application for it.

## SALARY VERSUS DIVIDENDS

To maximize the availability of after-tax funds and minimize total corporate and personal tax, an owner/manager should consider the appropriate mix of salary and dividends to receive as compensation. Although the tax system is designed to extract approximately the same combined corporate and personal tax dollars regardless of any salary and dividend mix, perfect integration does not always occur.



When determining the optimal mix of salary and dividends, ensure that personal tax credits are fully used. Maintain desired levels of salary for purposes of CPP and RRSP contributions.

No two situations are identical and the optimum combination of salary and dividends can only be determined on an individual basis. However, the following factors should be considered:

- Whether tax credits or losses are available to reduce corporate tax otherwise payable, in which case dividends may be preferable to salary.
- Dividends can be received tax-free to the extent the company has a balance in its capital-dividend account.
- Dividends may trigger refundable taxes to the corporation, resulting in a reduction of taxes payable.
- Dividends may reduce the individual's cumulative net investment loss (CNIL) account.
- Dividends, when taken with other tax preference items, may result in alternative minimum tax (AMT). Sufficient salary or bonus may eliminate or reduce AMT.
- Salary or bonus in the current year creates earned income necessary for RRSP contributions in the subsequent year, whereas dividends do not.
- Share redemption or reduction of shareholder advances to a corporation as an alternative to paying either dividends and/or salary can result in a tax-free return of paid-up capital or debt.
- The existence of payroll-related costs, such as employment insurance (if the shareholder owns 40 per cent or less of the company) and Canada pension-plan (CPP) premiums. However, dividends are not used for the calculation of CPP and employment insurance (EI).
- There is a federal small business deduction of 17 per cent, for a reduced tax rate of 11 per cent on the active business income of Canadian-controlled private corporations (CCPC) for up to \$500,000 (up from \$400,000 in 2008). Ontario also has special provincial rates for small business corporations under its jurisdiction. The small business deduction threshold in Ontario is also \$500,000.



An entrepreneur should carefully discuss strategies involving corporate dividends with a certified general accountant, since tax planning and potential strategies in this area can be extensive.

## Related Issues Affecting Business Income and Dividends

### ESTABLISHING A MANAGEMENT COMPANY OR PROFESSIONAL CORPORATION

There may be certain tax advantages associated with establishing a management company to provide non-professional services or products to a professional at a reasonable mark-up (e.g., the CRA generally considers 15 per cent to be reasonable in many instances).

If incorporated by a professional's spouse or common-law partner, for example, a management company can be used to split income in addition to providing other incorporation benefits, such as a tax deferral. As earnings are taxed at the lower corporate tax rate, more cash may be available for working capital or the purchase of capital assets.



Because management fees paid by management companies are effectively subject to GST, professionals who are exempt from charging GST should consider directly employing administrative staff.

Those in charge of establishing management companies should ensure they are not deemed to be personal-services businesses. A personal-services business is defined by the *Income Tax Act* as a corporation through which individuals deliver services to a recipient individual, partnership or organization, etc., of which they would otherwise be considered officers or employees. As a means of discouraging individuals from delivering such services through a corporation, personal-services businesses are denied the small business deduction as well as being limited in terms of eligible expense deductions.

This restriction could, for instance, apply to a business that does not have more than five full-time employees (although additional part-time employees will be enough to qualify it for a deduction, according to a 2008 court ruling).

The goods and services tax (GST) also reduces some of the potential advantages for exempt professionals to establish management companies. For instance, while management companies must charge GST on fees and mark-ups, the exempt practitioner is unable to recover the GST as an input credit.

Some provinces allow certain professionals to form professional corporations. Note, however, that there are legal differences between management companies and professional corporations. Furthermore, professional corporations face certain restrictions compared to other corporations.

Check with your certified general accountant and lawyer to make sure you understand all the taxation, legal and other important aspects that apply to your circumstances before taking any action with respect to incorporation.



A management corporation structure might allow for greater ownership control than a professional corporation in certain situations. Consult your certified general accountant.

## BUSINESS PARTNERSHIPS

Various business partnerships may exist between two or more people. The agreement between these business principals is likely to cover a multitude of issues, including the distribution of subsequent profits and losses, which could be equal or in some other proportion reflecting the degree of their involvement in the business; the initial financial investment; proportion of risk assumed; or other criteria.

Principals also need to determine the degree to which partnership draws will be based on cash flow or income.



Make sure that any partnership agreements, including any intended taxation strategies or objectives, are in writing and can be accessed, particularly in the event a future dispute should arise that needs to be resolved in the courts.

In addition to an arm's-length partnership, it may also be possible for owners of unincorporated businesses to establish their spouses or common-law partners as partners who are eligible to share in the business's profits or losses. To qualify as partners, the spouses or common-law partners will be required to:

- contribute a significant amount of time, specified skill or training to the business, or
- invest property in the business

The allocation of partnership income or losses should be reasonable under the circumstances. Partners should be aware that a provision of the *Income Tax Act* allows the CRA to reallocate income or losses among the partners if it is determined that the primary motivation for selecting a particular allocation is to reduce or postpone tax that would otherwise be payable.

Special rules apply to limited partnerships. Consult your certified general accountant for details.



Consider introducing family members as officers or shareholders so that they may participate in dividend income, even if no direct involvement in operations was present to justify salaries.

## SHARE STRUCTURE

Owner-managers often hold corporate shares in a Canadian-controlled private corporation (CCPC). It is also possible for an individual to own shares of a holding company, which in turn owns all the shares of the operating company. Under this structure, dividends may be passed tax-free among CCPCs. By doing this, funds can be transferred away from future risks associated with the operating company without incurring additional income taxes. Provided excess funds are not personally required, this might be advantageous in certain situations.

Although investment capital accumulation in the holding company may cause complications with respect to claiming the small business-corporation (SBC) capital-gains deduction on a subsequent sale of shares, this potential problem can generally be remedied if appropriate steps are taken prior to disposition. You might want to discuss this with your certified general accountant.

In determining whether a corporation qualifies as a CCPC, it is important to ascertain not just the current share ownership but also with whom the right of control resides. If, for instance, a foreign-based minority owner has the right to either acquire shares or dilute ownership such that the company is no longer majority owned by Canadian parties, it could be denied status as a CCPC.

The size of the business may also be a factor; for example, if it does not have more than five full-time employees (i.e., five full-time employees, plus at least one part-time employee) it might be considered a specified investment business and, therefore, not qualify for the small business deduction.

Share restructuring can also be conducive toward establishing a potential estate freeze. A capital gain realized on the ultimate sale of qualifying small business shares might, for instance, be split among several family members holding shares, each with an available \$750,000 lifetime capital-gains exemption (see capital-gains deduction on page 47 for a discussion of the conditions that qualify).

Decisions handed down in several recent court cases have reinforced that family members are eligible to receive dividends, regardless of the degree of their participation in helping to establish or run a family business.

#### **LOANS TO SHAREHOLDERS**

Generally, a shareholder loan is required to be included in the taxpayer's income in the year the loan was made. However, there are certain exceptions. One is that the loan must be repaid by the end of the following fiscal year of the corporation making the loan, provided it is not part of a series of loans and repayments.

The imposition of taxable benefits on a shareholder loan is based on prescribed interest rates, as applied to the loan principal outstanding. Loan repayments are applied to outstanding balances on a first-in, first-out basis. The payment of dividends, salaries and bonuses may also qualify as legitimate repayments of a shareholder loan, provided that amount is included in the taxpayer's income.

If bona fide arrangements were made when the loans originated that repayment would take place within a reasonable period of time, that loan might not be considered income if it occurred in the ordinary course of the lender's business or was made to enable a shareholder who is also an employee that deals at arm's-length with the corporation to:

- acquire a dwelling for personal use
- purchase an automobile for use in the course of employment
- purchase fully paid shares from the corporation or a related corporation (provided such shares are held by the individual for personal benefit)

## **PRESERVING BUSINESS LOSSES**

A business with non-capital-loss carry-overs that are due to expire may increase taxable income, in order to use as much of the loss as possible, by any of the following methods:

- Reduce CCA claims and amortization of eligible capital expenditures (see section on page 36).
- Compensate employee shareholders by declaring dividends rather than pay a salary (assuming there are sufficient retained earnings).
- Sell redundant fixed assets or other capital property when this will result in a recapture of CCA.
- Reduce tax reserves, including reserves for doubtful accounts.
- Elect to capitalize interest and related costs on money borrowed to acquire depreciable property.
- Transfer losses to another corporation within the corporate group as losses may be used within that group by means of an amalgamation or wind-up, subject to restrictions if a change of control results.
- Value the business inventory at full market value. Note, however, that a change in the method of valuing inventory must result in a more appropriate way of calculating income. The minister of national revenue must also approve this change.
- Realize capital gains on investments.
- Bring capital-gains reserves into income.
- Apply losses to a corporation's part IV tax account (referred to in the *Income Tax Act* as tax on taxable dividends received by private corporations), if no other alternative is viable.

## **CHOICE OF YEAR-END**

### **PROPRIETORSHIP/PARTNERSHIP**

All sole proprietorships, professional corporations that are partnership members and partnerships (where at least one member is an individual, professional corporation or other affected partnership) are generally required to have a December 31 fiscal year-end.

If an appropriate election is made, however, some businesses may qualify to establish an alternative fiscal year-end and estimate calendar-year business income using a specified formula. The alternative method is a one-time election that must be made by the taxpayer (or in the case of a partnership, by a representative on behalf of all members). This election must be made by the filing due date of the first tax return that includes the business's income.

The alternative-method election remains in effect until it is revoked or the business no longer qualifies to apply it. Once a December 31 year-end is used for tax reporting, however, the business cannot subsequently elect to use the alternative method.

In the year an individual dies, goes bankrupt, or otherwise ceases to carry on the business, there can be no additional income inclusion under the alternative method unless, in the case of business cessation, a similar business is started in the same calendar year.



Some taxpayers in a partnership arrangement are required to fill out CRA Form T501 — Statement of Partnership Income.

The rules governing this subject are complex. Taxpayers are advised to consult a certified general accountant for more details.

#### **CORPORATION**

A corporation can choose its first year-end, which must be within 53 weeks from the date of incorporation.

In establishing an incorporated business's fiscal period, the timing of income recognition is often a major consideration; other factors, such as the normal business cycle, should also be weighed into the decision.

### **Business and Self-Employment Expenses**

Individuals may deduct all expenses incurred in the conduct of their business, provided they are undertaken to earn income, are reasonable under the circumstances, and not limited or prohibited by certain rules or regulations established with respect to specific expenses.

Examples of business expenses may include all or part of the following:

- accounting
- advertising
- amortization of capital assets
- bad debts
- business-related memberships and subscriptions
- business-related start-up costs
- business taxes, fees and dues
- certain group benefits
- collection (i.e., related to bad debt)
- convention expenses (up to two a year)
- consulting
- delivery and freight
- disability-related modification expenses
- equipment rental
- insurance (fire, theft, liability)
- interest and bank charges
- legal
- light, heat and water
- maintenance and repairs (other than for passenger motor vehicles)
- management and administration fees
- meals and entertainment expenses
- motor-vehicle expenses (such as fuel, insurance and repairs)
- home-office expenses (including postage, stationery, telephone and other supplies)

- property taxes or rent on business property
- purchases of materials and supplies
- representation costs to obtain a business-related licence, permit, franchise or trademark
- salaries and amounts paid “in kind”
- specific courses taken to improve business skills
- subcontractors’ costs
- travelling expenses (limitations apply to motor vehicles)
- workspace in the home (when appropriate)



Self-employment expenses must be documented. There are instances where the tax courts have disallowed what might otherwise have been legitimate expenses because of poor or non-existent documentation. A lack of proof to support the taxpayer’s argument in the event of a dispute with the CRA could also lead to the imposition, or upholding of penalties.

## OTHER DEDUCTIONS

Individuals who are self-employed can deduct the employer’s share of Canada pension plan (CPP) and Quebec pension plan (QPP) earned-income contributions. They can also deduct premiums paid for coverage under Ontario’s workplace safety and insurance board (WSIB).

Self-employed individuals may also, within limits, deduct health and dental premiums paid on behalf of them or immediate family members sustained under a private health-services plan (PHSP), provided they are actively engaged in the business and derive more than 50 per cent of their income from it.

## LEGITIMACY OF EXPENSE DEDUCTIONS

When determining whether a self-employment enterprise, such as a sole proprietorship or partnership, constitutes a true business with allowable expense deductions, the tax courts generally place a great deal of emphasis on determining the commercial viability of the enterprise.

Hence, taxpayers must establish that their prominent intentions are to make a profit and, in so doing, they are employing objective standards in their conduct of the business. The courts will also look at factors such as the amount of time and capital devoted to the business, the existence of a solid business plan, whether or not there is adequate capitalization, ties to professional associations, the training of its entrepreneur(s) and, depending on the nature of the enterprise, the existence of employees.

If there is a personal element associated with the business operation (e.g., if it has been established as a hobby), the expenses associated with that personal element are likely to be denied as taxable deductions. The tax courts might then turn their attention toward determining whether or not the activity was also being carried out in a sufficiently commercial manner as to constitute a source of income, in which case a proportion of its expenses might be related to commercial operations and, therefore, deductible. Somebody using artistic talents such as painting, writing or photography in a business endeavour should, for example, be especially diligent about being able to provide tangible proof the enterprise is predominantly commercial in nature.

One of the tests the courts are likely to employ in this situation is a determination regarding whether or not the business was established with, and maintains, a reasonable expectation of profit (REOP) within a reasonable period of time.

#### **DEDUCTIONS RELATED TO SALARY PAID TO SPOUSE/COMMON-LAW PARTNER OR CHILDREN**

If a spouse, common-law partner or other family member is employed by a business, whether it be incorporated, a partnership or sole proprietorship, there are potential opportunities for income splitting and reduction of the family's overall tax burden.



The salary paid to a family member may allow that individual to become eligible for CPP and RRSP contributions.

The following criteria must be met if a business is to be allowed a deduction for salary paid to a family member:

- The salary must be paid periodically, preferably by cheque for bona-fide services performed.
- An employer-employee relationship must exist.
- Any salary paid must be reasonable for the work performed

Normal payroll deductions apply for non-arm's-length employees (such as a spouse or child), except for employment-insurance (EI) premiums, which may be exempt. Consult your certified general accountant with the particulars of your situation.



You should be especially vigilant about documenting the work carried out by family members in order to help prove the compensation they received was equitable.

#### **DEDUCTIONS RELATED TO WORKSPACE IN THE HOME**

The *Income Tax Act* limits the circumstances under which a self-employed individual can deduct the costs related to a workspace in the home. They are confined to situations where the space is used exclusively to earn income from a business and on a regular and continuous basis for meeting clients, customers or patients; or if it is the individual's principal place of business.

This claim may be based on the proportionate space within the home that is used as a workplace. Eligible expenses include rent, mortgage interest, realty taxes, insurance, utilities and maintenance. It is generally not advisable to claim capital-cost allowance (CCA), (see page 36), on a portion of the home because that portion would then not qualify for the principal-residence exemption when it is ultimately sold.



A bed-and-breakfast enterprise may also qualify as workspace in the home, provided the guest rooms are located inside the owner's home and not in a separate dwelling.

Similarly, claiming 50 per cent or more business use of the home or making major structural alterations to adapt it to business use will trigger a "change in use," resulting in loss of the principal-residence exemption.

The amount a taxpayer can claim is limited to his or her business income before deductions for home workspace. Any unused amount may then be carried forward and claimed in the subsequent year against related business income. To the extent that unused amounts cannot be claimed in the following year, they can be carried forward indefinitely to be claimed at the first available opportunity.



Don't forget to include business-storage space in the basement and elsewhere, when determining the proportion of your home used for commercial purposes.

#### **AUTOMOBILE EXPENSES**

The *Income Tax Act* restricts certain expenses relating to "passenger vehicles." A passenger vehicle, which can include a van, pick-up truck or sport-utility vehicle, is defined as a motor vehicle designed to carry no more than nine people, including a driver and luggage. It does not fit this definition if:

- "All or substantially all" (generally considered to be at least 80 per cent to 90 per cent) of its use is for the transportation of goods, equipment or passengers in the course of income-earning activities; or
- More than 50 per cent of its use is for such activities and it seats not more than three people, including the driver; or
- It is a pick-up truck used for such income-earning activities at a special or remote work site situated at least 30 kilometres from an urban area with at least 40,000 people.

These rules can be complicated, so check with your certified general accountant for clarification.

The restrictions on deductible expenses and related business-use calculations are both discussed under use of company cars, on page 18.

It is impossible to provide a simple rule of thumb with respect to an automobile lease versus purchase decision. Each situation must be carefully reviewed and many factors, including interest rates, mileage allowances and expected resale value, plus income-tax implications, taken into consideration before a final decision is made.

Certified general accountants are also well equipped to help in this process.

## DEDUCTION FOR BUSINESS MEALS AND ENTERTAINMENT

The *Income Tax Act* imposes a restriction on the deductibility of business-related meals, beverages and entertainment expenses, based on a general presumption that these normally combine elements of both a personal and business nature. Only 50 per cent of such expenses are deductible with certain exceptions, such as when employees are required to work at selected special work sites or in remote locations; are travelling aboard an airplane, train or bus on business; or they are incurred at a fundraising event to benefit a registered charity, among others.

The 2007 federal budget increased this allowance to 80 per cent for long-haul truck drivers while they are working. This increase will be phased in over a five-year period. It was 60 per cent for expenses incurred on or after March 19, 2007; that allowance increased to 65 per cent on January 1, 2008; and 70 per cent on January 1, 2009.

The 50 per-cent rule also applies to meals and entertainment provided as part of a convention, seminar or similar event, where the organizer may specify a reasonable amount to cover the cost of food and entertainment. Otherwise, the fee for that event will be deemed to include \$50 a day for meals and/or entertainment. (Incidental refreshments, such as coffee and doughnuts, are exempt from this calculation.) Certain other expenses, such as transportation costs incurred to get people to attend an entertainment event, might also be subject to this 50 per-cent restriction.

Bottles of liquor or certain food items given as gifts at Christmas or on other special occasions may also fall within the auspices of this 50 per cent limitation. However, some food, beverage and entertainment-related expenses for up to six special events in a calendar year, such as Christmas parties and employee meetings, held at a particular place of business to which all of the firm's employees are invited, might be 100 per-cent deductible. Business owners with employees should, therefore, consult their certified general accountant for a clarification of these rules.

## CAPITAL COST ALLOWANCE (CCA)

Capital assets such as land, buildings, automobiles, furniture, computers, etc., provide an enduring benefit to a business. This period is generally recognized by the accounting profession as being at least one year; in practice, most capital assets provide benefits that last for several years. Capital costs also include items such as leasehold improvements and legal, accounting and other professional fees paid to acquire a capital property.

Individuals who run their own business cannot, therefore, expense or write off the cost of such assets immediately upon purchase; rather, they must spread the cost over several years. For tax purposes, this write-off is referred to as capital cost allowance (CCA) and it is subject to strict rules and limitations. Assets are grouped into approximately 50 classes where items are provided



If you dispose of one of several identical eligible capital properties with a shared value, you may use an average cost to determine the value of the individual property sold.



Specific costs incurred by employers to improve business premises' access for people who are disabled may be deducted in the year they are incurred and need not be capitalized.

with a discretionary allowance claimed annually at a fixed percentage, generally on a declining balance basis.

A small sampling of common CCA classes, a description of what is contained in those classes and their corresponding deduction rates include:

- Furniture and fixtures (class 8), 20 per cent on a declining-balance basis.
- Automobile (class 10 or 10.1), 30 per cent on a declining-balance basis.
- Manufacturing and processing machinery (class 43), 30 per cent on a declining-balance basis.
- Leasehold improvements, which may either be written off on a straight-line basis over the term of the lease (including the first renewal period), or five years, whichever is greater.

Special rules apply for Class 10.1 automobiles, classified as "passenger vehicles," if their cost exceeds a threshold of \$30,000 prior to sales taxes.



You do not have to claim all eligible CCA amounts in the year they are incurred if you believe it may be tax advantageous to carry all, or some, of that amount forward to a future year.

In most cases, only one-half of the normal allowance is available on depreciable property acquired in an arm's-length transaction in the fiscal period it is acquired. Where the fiscal period is less than 365 days, the amount that would otherwise be claimed must be prorated, based on the number of days in that period.

Special rates apply to computer equipment. The federal budget in 2004 increased the CCA rate on such items acquired after March 22, 2004, to 45 per cent from 30 per cent. The federal budget in 2007 further increased the CCA rate on such items acquired on or after March 19, 2007, to 55 per cent from 45 per cent. The rates for broadband, internet and other data-network infrastructure equipment were increased to 30 per cent from 20 per cent in 2004.

The federal budget in 2009 proposed a temporary, 100 per cent CCA rate for eligible computers and accompanying systems software acquired between January 28, 2009 and January 31, 2011, inclusive. Furthermore, the half-year restriction rule for the first year does not apply in this instance, so qualifying assets can be entirely expensed within one year.

The Ontario government has matched those changes, with the same effective dates.

New CCA classes have also been created to accommodate equipment qualifying for these accelerated rates.

Various incentives involving CCA at accelerated rates also exist for assets that contribute to the development of clean energy technologies.

The 2007 federal budget established a temporary two-year 50 per cent straight line accelerated-CCA rate to cover investment in eligible machinery and equipment acquired on or after March 19, 2007 and before 2009 and used in manufacturing or processing activities as an economic incentive to Canada's manufacturing sector.

Budget 2008 extended this by three years until the end of 2011. The straight-line depreciation was originally scheduled to apply to eligible assets purchased in 2009, with eligible assets purchased in 2010 and 2011 subject to an accelerated, but declining-balance rate of depreciation; however the 2009 federal budget extended this straight line provision through until the end of 2011.

Ontario has also followed suit regarding this provision.

Certain types of equipment can become obsolete before being fully depreciated for income tax purposes. Taxpayers may elect to place eligible rapidly depreciating equipment in a separate class. Examples of eligible property include certain computers, photocopiers, fax machines or telephone equipment costing more than \$1,000. If such property has not been disposed of after five years, it must be transferred to the general class to which it would have originally been placed.

A terminal loss could result on the disposition of such elected property should the proceeds ultimately received be less than any remaining undepreciated-capital cost (UCC). Consult your certified general accountant for details on these and other specific rules, such as the correct tax treatment associated with any subsequent recapture of CCA, as well as a full clarification of CCA classes and the multitude of items contained within each, as well as potential classification choices that may be available.



Consider purchasing employment-related assets (e.g., automobile, musical instruments, etc.) closer to year-end in order to potentially accelerate the timing of CCA claims.

#### **ELIGIBLE CAPITAL EXPENDITURES AND RECEIPTS**

Certain expenditures are capital in nature, but not included in any CCA class that qualifies them to be written off on a declining-balance basis. These include, but are not limited to, expenditures related to acquiring certain government rights; trademarks; franchises; incorporation fees; certain farm-related quotas; and goodwill.

Seventy-five per cent of such expenditures may be amortized at a rate of seven per cent per year, on a declining-balance basis.

When this type of capital asset is sold, income is generated when applied to the recapture of depreciation amounts previously written off, with any remainder treated as a taxable capital gain from a capital-property disposition. Such a sale could also generate a loss, in which case special rules apply.

Consult your certified general accountant for more details.

#### **GST INPUT TAX CREDIT**

The GST input tax credit is a credit, or refund, claimed by registrants on goods and services tax (GST) returns filed on a monthly, quarterly or annual basis. This credit covers GST paid or payable in the course of any business activity.

The following criteria must be met in order for taxpayers to be eligible to claim the input tax credit:

- The person making the claim must be registered.
- The registrant must deal with taxable supplies.
- Goods or services must be acquired or imported for consumption, use or supply in the course of a commercial activity.
- Documentation pertaining to the tax paid or payable must be retained.

Consult your certified general accountant for details about the calculation methods available for you to claim this credit (i.e., the 'quick method' of accounting for the GST may be more applicable and save both time and money), the due dates for making this claim, and other related information.

### **Farming Income and Losses and Other Special Considerations**

Farming is a very diverse and specialized industry in Canada. It encompasses a wide range of activities, including tilling the soil, livestock raising or showing, poultry raising, dairy farming, winery-related vineyard operations, tree farming, beekeeping and, in some instances, activities associated with raising fish, such as commercial shellfish, among others.

#### **DETERMINING WHETHER FARMING CONSTITUTES THE MAIN SOURCE OF INCOME**

Qualified farm property (QFP) is defined in the *Income Tax Act* as property that is owned by the taxpayer, his or her spouse or common-law partner, or in a partnership, that was used "in the course of carrying on the business of farming in Canada," under some very specific scenarios.

The CRA may take several factors into consideration when determining whether taxpayers engage in farming activities to the extent that it constitutes their chief source of income. Taxpayers for whom farming does not represent their main source of income will be limited in their ability to deduct farm-related operating losses.

The criteria used by the CRA to examine this issue include:

- Whether the farming operation has a reasonable expectation of profit (REOP).
- Whether earned profits from farming are substantial compared to the taxpayer's major source of income.
- Whether there is a family history of farming activities.



- The extent of the taxpayer's knowledge of farming.
- Whether the activity generating the taxpayer's major source of income has, to some degree, been subordinated as a result of farming activities.
- The professionalism of business activities, including the existence of a business plan, and the amount of time and capital committed.

Consult your certified general accountant for more details.

#### **BASIS OF ACCOUNTING**

To accommodate such a myriad of farming-related operations, several accounting and income tax provisions are available.

Farmers and fishers have the option of reporting income using the cash (rather than the accrual) basis of accounting. The cash basis can be advantageous to farmers because it allows them to decide when to report income by timing the sale of produce or livestock in the most appropriate year. Using the cash basis, farmers can also time expenses by paying accounts in the year they wish to make the deduction.

This timing option, which is not available to members of any other industry, can significantly increase tax-planning alternatives for the farming community.

Several additional calculations in determining farming income may also differ from those of other businesses. For instance, under the cash basis of accounting, expenses relating to a taxation year that fall two or more years after the actual payment are not allowed as deductions in the current taxation year. If, for example, in December 2009 a farmer pays insurance premiums covering 2009, 2010 and 2011, the amount deductible on the 2009 income tax return would be limited to the actual cost of insurance for 2009 and 2010 only. Costs related to 2011 will only be deductible during 2011. Also, a farmer who enters into a three-or-more-year equipment lease cannot deduct the portions that relate to lease payments beyond one year into the future (e.g., if the lease were signed in 2009 that would cover until the end of 2010).

Tilling, clearing and levelling of farmland, as well as building an unpaved road, can be expensed in the year such payments are made or any portion carried forward to future years. However, land improvements on farmland rented out to another farmer/producer do not qualify for this deferral. In such cases, land improvements can be expensed in the current year or, alternatively, added to the cost of the land.

If the farmer is actively involved in peripheral activities, such as the purchase and sale of seed, this business is not considered farming and must be reported using the accrual basis of accounting, which will include reporting inventories on hand at year-end. The CRA will consider certain non-farming activities to be part of the farming operation if these activities are undertaken on a small scale and the income from them is incidental to other farming revenue.



If you are a farmer using the cash basis of accounting, note that when an expense is paid using a credit card, the relevant date of payment for tax purposes occurs when the expense is charged to the credit card, not when the credit card is paid.

Other differences that affect the farming industry include:

- Assets purchased during the year are restricted by the CCA half-year rule, except assets such as quotas (which are eligible capital property), where the full amortization amount is allowed in the year of acquisition.
- Deceased farmers' Rights and Things include harvested crops, livestock on hand (less the basic herd), supplies on hand, inventory and receivables (if the deceased used the cash basis of accounting).
- No GST is charged on sales of most farm commodities. Registered farmers must, however, charge GST on items such as land and quota rentals and firewood sales that do not fall under the exception list provided by the CRA. Asset purchases and sales specifically exempt include tractors over 44.74 kW (60 PTO hp) and most harvesting, tillage, haying and grain-handling equipment. Consult the CRA list for further details.

Farmers and fishers should also be aware that:

- Payments received out of the agricultural income disaster assistance (AIDA) and the Canadian agricultural income stabilization (CAIS) programs are taxable when received.
- Advance payments for a crop are considered to be a sale of that crop and are, therefore, taxable when received. However, advances under the *Agricultural Marketing Programs Act* (AMPA) are considered loans and are not taxable when received. In this case, income is triggered when the crop is sold and the loan repaid.
- A farmer who plants an orchard must capitalize the cost of the trees by adding it to the adjusted cost base (ACB) of the land. Therefore, those trees would not qualify for capital cost allowance (CCA). However, replacement trees can be expensed when purchased.



Expenses for dogs and cats located on the farm are deductible if those expenses relate to their use for rodent, or other wild-animal control, or for security.

#### **MANDATORY INVENTORY ADJUSTMENT (MIA)**

Whenever cash-basis accounting results in a farming loss, a mandatory inventory adjustment (MIA) must be performed with respect to purchased inventory on hand at year-end. The MIA is calculated by adding to income the lesser of the loss amount and FMV of the purchased inventory, such as livestock, feed, fertilizer, fuel and other supplies still on hand at year-end.

For MIA purposes, inventory is generally valued at the lower of its original purchase price and FMV. Specified animals are valued at their original purchase price, less 30 per cent per annum on a diminishing-balance basis, unless the taxpayer elects to value them at a greater amount that does not exceed their original cost. All horses are specified animals; cattle registered under the *Animal Pedigree Act* may also be treated as specified animals at the taxpayer's option.

## OPTIONAL INVENTORY ADJUSTMENT (OIA)

Farmers can elect to report an optional inventory adjustment (OIA) at year-end to help reduce wide swings in net income that sometimes occur under the cash basis of accounting. The OIA is calculated on an individual, rather than a partnership, basis. Using the OIA, the taxpayer may elect to decrease expenses by an amount up to the full FMV of inventory on hand at year-end. The OIA claimed in one year then becomes an increase in expenses the following year.



Crops in the ground qualify for the optional inventory adjustment.

## RESTRICTED LOSSES

Taxpayers who are engaged in farming activities, but for whom farming is not deemed by the CRA to be their "chief source of income" — either by itself or in combination with some other economic activity — may be restricted in any loss they can claim against other income. Recent court cases appear to take a more liberal approach as to whether farming, in combination with some other endeavour of the taxpayer, represents a major source of income.

That claim is limited to the first \$2,500 of farm losses, plus one-half of the next \$12,500 of such losses, for a maximum claim of \$8,750 in one year. Any loss in excess of that claim is identified as a "restricted farm loss," which can be carried back up to three years or forward up to 20 years, for losses incurred and credits earned in taxation years that end after 2005 (up from 10 years previously), and applied against farming income.

The same carry-back and carry-forward provisions pertain to regular farm losses.

Farmers cannot use restricted farm losses to create or increase a capital loss on the sale of farmland. However, any portion of outstanding restricted farm losses may be added to the adjusted cost base (ACB) of farm property in order to reduce the capital gain realized upon disposition. The allowable portion of such losses applied is limited to the property taxes and interest on money borrowed to purchase land.

A full-time farmer who has to take a part-time outside job to support the farm should be able to claim all of his/her farm losses for tax purposes without application of the restricted farm loss rules.

## INVESTMENT TAX CREDIT (ITC) RELATED TO FARMING OPERATIONS

A scientific-research and experimental-development (SR&ED) investment tax credit may be claimed on that portion of the farmer's "checkoff," "assessment" or "levy" — terms that are used for determining SR&ED eligibility by the commodity boards.

Individuals qualify for a 20 per cent investment tax credit on the amount that is considered applicable to SR&ED expenditures by, for example, the wheat and corn boards. The boards then usually issue a statement or letter to the producer identifying the proper amount to claim.

Individuals claiming this ITC must fill out CRA Form T203 — Investment Tax Credit Corporations.

#### FARM DISPOSITIONS AND CAPITAL GAINS

Farm-property dispositions may qualify for the \$750,000 lifetime capital-gains exemption available (effective March 19, 2007, up from \$500,000), subject to certain restrictions. If, for example, the farm was purchased before June 18, 1987, the property must have been used principally in a farming business during at least five years it was owned by the taxpayer or his or her ancestor(s).

If the farm was purchased after June 17, 1987, the taxpayer must have owned it for at least 24 months and the gross revenue from farming must have exceeded income from all other sources for at least that 24-month period. A farmer who acquired the farm before June 18, 1987, but made the election available in 1994 to report accrued capital gains on the farm was deemed, in 1994, to have disposed of that property and reacquired it at the proceeds of disposition designated in the election. This “deemed reacquisition” means the farmer must now follow the rules applicable to farms acquired after June 17, 1987.

A farmer is permitted to claim a reserve on that portion of the farm sale that is not yet payable, according to certain restrictions. If the farm is sold and a mortgage taken back from the purchaser, the vendor must report capital gains on the greater of: 20 per cent of the gain each year; or the amount of proceeds received. This can spread the tax from that capital gain over a period of up to five years. For a non-arm’s-length sale, from a parent to a child for example, the minimum amount changes from 20 per cent to 10 per cent of the gain and enables the vendor to effectively spread the tax over a period of up to 10 years.

Alternative minimum tax (AMT) — see description on page 107 — does not apply to a capital gain from the sale of eligible capital property (quota, for example). Nor does the AMT apply to any deemed dispositions in the year of death.

There are special, complicated rules for transferring farmland, eligible capital property and depreciable property of a prescribed class to a spouse/ common-law partner or child during a taxpayer’s lifetime or upon death. Interested readers should refer to the CRA’s interpretation bulletins, IT268R4— Inter-Vivos Transfer of Farm Property to a Child and IT349R — Intergenerational Transfer of Farm Property on Death.

Currently, all transfers of farmland situated in Ontario made into a family-farm corporation are exempt from the Ontario land-transfer tax (LTT). The Ontario government has expanded this provision to include qualified transfers of farmland between family members, as well as transfers from family-farm



A child beneficiary of a trust who has never farmed could still possess qualified farm property, provided a relative — i.e., parent, grandparent or great-grandparent — satisfied the gross revenue test in previous generations when they owned and operated the farm on a regular, continuous basis.

corporations to individual family members for transactions that take place after March 25, 2008.

Given the complexities involved, it might, therefore, be prudent to consult a certified general accountant and/or lawyer on matters related to the transfer or sale of farmland.

#### **ONTARIO RETAIL SALES TAX**

Farm implements, machinery and equipment designed for farm use, such as tractors, milking machines, farm wagons, etc., can be purchased without Ontario retail sales tax (RST) by people in the business of farming. Repairs to these items also qualify for exemption. A purchase-exemption certificate must be signed and given to suppliers on items that are not generally made exclusively for farming use, such as hand tools.

There is a point-of-sale exemption for the purchase of farm-building materials. Purchases associated with certain post-harvest activities are also included in the RST exemption.

General guidelines covering both tax-exempt and taxable items can be obtained from the Ontario Ministry of Finance's Retail Sales Tax Guide 807.

### **Other Measures**

#### **AGRISTABILITY AND AGRINVEST**

The AgriStability and AgriInvest programs are designed to provide Canadian agricultural producers with long-term, whole-farm risk-management tools, which provide protection for farming operations from both large and small declines in farm income.

For details about these programs, consult Agriculture and Agri-Food Canada; call 1-866-367-8506; contact the Ontario Ministry of Agriculture, Food and Rural Affairs; or consult with a certified general accountant who is familiar with them. In Ontario, these programs are administered by Agricorp.

These programs replace the old Canadian agricultural income stabilization (CAIS) program.

#### **CROP ADVANCES**

Farmers are eligible for up to \$100,000 in interest-free cash advances for stored crops under the *Agricultural Marketing Programs Act*. Advances of up to \$400,000 are also available at market interest rates. This crop must be in storage in a non-processed form, while the producer must retain title to the crop and also be responsible for marketing it. This advance is considered a loan and it is not taxable when received. Income is triggered when the crop is sold and the loan repaid.



Because the CRA considers crop advances to be loans, in a better than average year, consider storing all or part of the crop and then taking an advance against it. This advance, which must be applied for early in the year, serves as an effective planning technique for farmers using the cash basis of accounting.

## CANADIAN FARM BUSINESS ADVISORY SERVICES (CFBAS)

A financial-management counselling program, named the Canadian farm business advisory services (CFBAS), is available for Canadian farmers who are experiencing agriculture-related financial problems. For a fee of \$100, farmers can receive confidential counselling services to deal with problems, such as decreased margins or cash-flow difficulties.

Other specialized business-planning services, at variable costs, are also available through the CFBAS.

Farmers in drought-stricken regions of Canada — which have been particularly prevalent in some venues in recent years—or areas that have received excessive moisture, may also qualify for temporary income tax relief for certain aspects of their operation. Consult Agriculture and Agri-Food Canada for details regarding current designated regions and the agricultural activities affected.



Many local and provincial programs exist that may financially benefit farmers. As these programs and the requirements to qualify for them change frequently, a taxpayer who is affected should visit the local provincial ministry of agriculture, food and rural affairs offices once or twice a year for updates.

## Investment Income and Expenses

### INTEREST: ANNUAL ACCRUAL

The interest income on compound-interest obligations, such as Canada savings bonds (CSB) or other instruments like guaranteed investment certificates (GIC), must be reported on an annual accrual basis from the anniversary date. Investment issuers are obligated to provide taxpayers with annual information slips (T5) reporting this income, although it is the taxpayer's responsibility to ensure all interest is recorded.

### DIVIDENDS

Taxpayers who receive eligible dividends from a public Canadian corporation (and certain private, resident corporations that must pay Canadian tax at the general corporate rate) are subject to an enhanced-dividend tax-credit rate that includes a 45 per cent gross-up (up from the previous 25 per cent), offset by a federal-dividend tax credit, which reduces federal income-tax payable, worth roughly 19 per cent (18.97 per cent) of the total grossed-up amount (the actual reduction is 11/18ths of the 45 per cent gross-up). This equates to a dividend tax credit worth 27.5 per cent of actual dividends.

This enhanced dividend tax credit rate covers eligible dividends paid since January 1, 2006. Both public and private corporations whose dividends are subject to the enhanced rate must notify their shareholders of this status.

Ineligible dividends from Canadian-controlled private corporations (CCPC) not subject to the general corporate tax rate will continue to be subject to the 25 per cent gross-up and 16.67 per cent dividend tax credit, (or 13.33 per cent reduction to the total grossed-up amount).

Ontario now has a two-tier dividend structure similar to that of the federal government. Dividend tax credits on eligible dividends from public Canadian corporations and other private, resident corporations that pay Canadian tax at the general corporate rate are received at 7.4 per cent of eligible taxable dividends in 2009 (up from 7.0 per cent in 2008). Dividends from other CCPCs receive a credit of 5.13 per cent of the grossed-up amount (unchanged from 2008).

Although dividends from non-resident corporations must also be included in income, they are not subject to either the gross-up or dividend tax credit. Where foreign currency is involved, such dividends must be converted to Canadian dollars at the average rate of exchange for the year.

Stock dividends are generally treated as ordinary taxable dividends. This dividend amount also represents the cost of the new shares. If the stock dividend is in shares of the same class, it may affect the shareholder's average cost for future sales.

Common shareholders of a public corporation are sometimes entitled to apply their dividend proceeds toward the purchase of additional corporate shares at a discount from market price under a dividend-reinvestment plan (DRIP). This will, in turn, incrementally increase the cost base of their investment.

Although such shareholders will, under a strict interpretation of the *Income Tax Act*, incur a taxable benefit equal to the discount amount when such shares are purchased, in practice the CRA does not assess a benefit where the amount paid for the additional shares is at least 95 per cent of its fair-market value and all shareholders are accorded the same reinvestment rights. Taxpayers are, however, still liable for tax otherwise payable on their dividends in the year such dividends have been reinvested.

Stock splits are not taxable.



If your spouse or common-law partner does not pay enough tax to use the dividend tax credit, consider transferring the taxable Canadian dividends to your income so you can claim this credit if that provides a greater tax advantage.

## **CAPITAL GAINS AND LOSSES**

A capital gain results from a sale or deemed disposition of a capital property, such as an investment-related instrument (e.g., stock), when it is sold for more than its ACB, less any disposition expenses incurred, like commissions. Unlike ordinary income however, only 50 per cent of the gain is included in income.

When investors experience a loss, the 50 per cent "allowable capital loss" amount must first be used to offset any capital gains they may have in the same year. Any unused allowable capital loss amount may be carried back up to three years, or forward indefinitely, to reduce taxable capital gains of other years.

The inclusion rate for capital gains and losses has not always been 50 per cent. In 2000, for instance, the inclusion rate was decreased twice, from 75 per cent to 66.67 per cent, then to 50 per cent. Individuals may, therefore, need to make complex adjustments when applying capital losses of one year against capital gains of another.

The proceeds of disposition from capital property have sometimes been ruled by the courts to be ordinary income or losses rather than capital gains or losses if there is strong evidence that the substantive nature of such a transaction was purely speculative — i.e., the property was purchased with the short-term intent to sell. Other factors, such as the number of transactions; duration of holdings; amount of time devoted to carrying them out; means of financing; and expertise of the taxpayer, may also weigh into the decision. The CRA addresses some of these factors in its bulletin IT-459 — Adventure or Concern in the Nature of Trade.

Special rules exist for capital gains and losses originating from certain foreign-currency transactions where there is a fluctuation in foreign exchange rates. Your certified general accountant can help determine whether these rules apply to you.

#### **CAPITAL GAINS DEDUCTION**

Capital gains from dispositions of qualified farm and fishing property, as well as small business-corporation (SBC) shares, may be eligible for a taxpayer's lifetime exemption of up to \$750,000 effective on or after March 19, 2007, (increased from \$500,000 prior to that date). At a 50 per cent inclusion rate, this represents a taxable amount of \$375,000 (up from \$250,000).

An individual's ability to claim the capital-gains deduction may be reduced by past claims for capital-gains deductions, allowable business-investment losses (ABIL), see page 49, or for a cumulative-net investment loss (CNIL), also see page 49.

#### **RESERVES**

If a property sale results in a capital gain and a portion of the proceeds is not due until after the year-end, taxpayers may claim a reasonable reserve for the unrealized portion of that gain. At least one-fifth of the capital gain must be included in income each year unless it arises from the sale of a farm, qualified fishing business or shares in an SBC to the taxpayer's child. In that case at least one-tenth of the gain must be included in income annually.

A reserve for the unrealized portion of an ordinary income gain may be claimed for up to 36 months from the date of the sale (unless the proceeds become due earlier) if:

- The sale of land results in an ordinary income gain and a portion of the proceeds is not due until after the taxation year-end; or
- The sale of property, other than land, results in an ordinary income gain and a portion of that gain is due more than two years after the sale date.

A reserve claimed in one year must be taken into income the next year and a new reserve, if still applicable, claimed at the end of that year.



## SHARES OF A SMALL BUSINESS CORPORATION (SBC)

A small business corporation (SBC) is a CCPC in which all or substantially all of its assets (generally representing at least 90 per cent of FMV) at the time of sale were:

- Used in an active business carried on primarily in Canada (more than 50 per cent) by a corporation or any related corporation(s); or
- Shares or debt of one or more connected corporation(s) which also qualify as an SBC.

A connected shareholder is generally defined by the *Income Tax Act* as one who owns at least 10 per cent of the issued shares of any class of stock in a corporation (or related corporation). The CRA also takes into account the right of an individual to acquire additional shares when making this calculation.



Consider transferring non-active assets to a separate company to maintain qualified SBC status.

To qualify for the \$750,000 lifetime capital-gains exemption, shares of an SBC (including connected corporations, which are considered to be associated and, therefore, part of the same unit) must meet several requirements.

Throughout the 24 months immediately prior to disposition, for instance, the shares must have been owned either by the taxpayer or a related person or partnership. Over that same period, more than 50 per cent of the FMV of a corporation's assets must have been used in an active business carried on in Canada and/or be shares or debt of a qualified connected corporation.

The requirement to hold shares for 24 months does not apply to treasury shares issued as consideration for other shares or the assets used in an active business. A special provision also applies for qualified SBC shares when the company goes public. Taxpayers may elect to dispose of their small business shares immediately prior to the corporation going public. Where the shares' FMV exceeds their ACB, investors may specify any amount between those values as proceeds of disposition and then recognize a capital gain, to be offset by the available capital-gains deduction.

Individuals may defer the tax on capital gains from eligible small business investments, provided such proceeds are reinvested in another eligible small business. Eligible small business investments include newly issued shares in an SBC whose assets do not exceed \$50 million. An eligible reinvestment can be made at any time during the year of disposition or within 120 days after the end of the year.

In practice, the classification of an SBC and applications involving its subsidiaries can sometimes be complex. Consult your certified general accountant for guidance in this area.



If you transfer qualified small-business-corporation shares into a self-directed RRSP, the time such shares are held inside the RRSP count toward the 24-month holding-period restriction.

## ALLOWABLE BUSINESS INVESTMENT LOSS (ABIL)

A loss realized from the arm's-length sale of shares or qualifying debt of an SBC may qualify as a business investment loss. Similarly, a loss upon the deemed disposition of an uncollectible debt of an SBC or the shares of a bankrupt SBC may also qualify. Taxpayers might also be able to claim, via an election on their tax return, an allowable business investment loss (ABIL) if they continue to hold shares or debt in an SBC that has become insolvent.

A business-investment loss is calculated the same way as a capital loss, except that it may be applied against all income, not just capital gains. One-half of the business-investment loss may be applied against other income in the year the loss is realized. Unused portions of an allowable business-investment loss may be carried back three years, with the balance carried forward 10 years. If any unapplied ABIL balance remains at the end of ten years attributable to losses sustained after 2003 (or at the end of seven years for losses attributable prior to 2004), it then becomes a net capital loss, which can be used to reduce taxable capital gains thereafter.

The deductible amount of an individual's ABIL must first be reduced by any previously claimed capital-gains deduction. If any allowable business-investment loss is deducted from income, an equal amount of taxable capital gains must be realized and reported as income in subsequent years before the capital-gains deduction becomes available.

Where a corporation is insolvent and neither it nor a corporation controlled by it carries on business, the taxpayer will be allowed to elect a disposition for tax purposes and realize the loss. If that corporation or another controlled by it commences carrying on business within 24 months, the taxpayer must recognize a gain equal to the loss claimed in the year that business recommences.

An election must be made under the *Income Tax Act* to claim a loss on debt, or shares of an insolvent company. This requirement also applies to claiming capital losses where the company is public.



Keep all documentation related to an allowable business investment loss. It may be required as proof to substantiate your claim.

## CUMULATIVE NET-INVESTMENT LOSS (CNIL)

A taxpayer's cumulative net-investment loss (CNIL) at the end of a year is defined as the amount by which the total of investment expenses incurred after 1987 exceeds the total of their investment income for those years.

The cumulative gains limit for purposes of the capital-gains deduction will be reduced by the amount of an individual's CNIL balance at the end of a taxation year.

## INCOME TRUSTS

Income trusts are investment instruments that distribute cash from revenue-generating assets directly to unit holders in a tax-efficient manner — often without having to pay any tax at the corporate level.

The activity of such trusts, now also formally known as specified-investment flow-through (SIFT) trusts, has been sharply curtailed, however, after Canada's finance minister announced significant changes to the income trust taxation structure in October 2006. These have resulted in the distributions from such trusts being taxed more like dividends from corporations.

The structural changes announced took effect in 2007 for certain trusts, such as new trusts, that were not publicly traded until after October 2006; they will not apply until the 2011 taxation year for other trusts that were publicly traded prior to November 2006 and whose growth in the intervening period does not exceed what the Department of Finance defines as "normal growth."

Certain real-estate-investment trusts (REIT) meeting specified criteria are exempt from the new rules.

Income trust structures that are still allowed under the new rules might appeal to investors who are interested in a steady cash flow return. Such investors should note, however, that a component of the cash flow from income-trust investments might constitute a return of capital, as opposed to income. This return of capital results in a lower cost base, thus leading to a larger capital gain when such investments are disposed.

Due to the complexity of income-trust taxation and the new restrictions placed upon such structures, and to be informed about updates to the transitional rules, it is best to check with your certified general accountant if income trusts are part of your investment strategy.

#### **INTEREST EXPENSE DEDUCTIBILITY**

Interest expenses on borrowed funds between arm's-length parties who are engaging in transactions at commercial interest rates are deductible provided the taxpayer uses those funds to produce income from a business, investment or property. The same provisions might also apply as a result of a loan between non-arm's-length parties provided FMV is received and the recipient pays interest on the loan.

Interest expense on funds borrowed to make an interest-free loan might also be eligible for deduction in certain instances where it can be proven that such funds are ultimately used to earn, or enhance income-earning capability.



Provided interest on borrowed funds meets all of the criteria necessary to be deductible for income-tax purposes, it does not matter whether the funds originate from Canadian or foreign sources.



In certain instances where a loan is secured for business purposes but its use will involve both business and personal needs – i.e., if a mortgage is secured to cover a parcel of land that will contain commercial real estate property as well as a personal residence, all of the interest might be deductible. Check with your certified general accountant if this situation applies to you.



Don't forget that interest expense may include elements of both simple and compound interest.



Carrying charges for purchasing Canada savings bonds (CSB) through a payroll-deduction plan are eligible for the interest-expense deduction.

A taxpayer can also deduct fees (but not commissions) paid for advice received with respect to the purchase, sale and administration of specific investments, such as shares or securities, provided those fees are paid to a professional whose principal business involves managing such investments.



If you need to finance your business, consider establishing a line of credit with your financial institution. The interest incurred on a line of credit used exclusively to finance business purchases is tax deductible.

Decisions handed down by the Supreme Court of Canada (Singleton, Ludco Enterprises Ltd.) in September 2001 reinforced the right of taxpayers to deduct interest when borrowed money was used for the purpose of earning income from a business or property. Lower courts had earlier denied the taxpayers their respective deductions.

The Supreme Court ruled that in the absence of evidence of a sham, window-dressing, or other similar circumstances, the courts could not question whether other "economic realities" served as motivation behind a subsequent transaction (Singleton), nor could they question the sufficiency of the income expected or received (Ludco).

However, this remains a very sensitive area of tax law and court rulings since then, where there have been extenuating factual circumstances (e.g., Lipson), have not necessarily been consistent with those results. Therefore, consult your certified general accountant for advice about appropriate tax strategies involving complex transactions.



If you use your credit card for both personal and business purchases, keep accurate records of the proportion spent on business expenses because any corresponding interest is tax deductible.



In order to establish a direct link between the interest that is payable on borrowed funds for investment purposes, consider practices such as keeping separate bank accounts for business and personal funds.

## SUPERFICIAL LOSSES

The *Income Tax Act* contains specific rules with respect to the treatment of superficial losses. The superficial-loss provision — which begins 30 days before and ends 30 days after the disposition of a property — exists to prevent taxpayers from executing a transaction that creates a loss while they, or an affiliated person or corporation, retain or acquire control of the same or an identical property that created the loss.

Consult your certified general accountant for details about which types of dispositions would constitute superficial losses.

## PRINCIPAL RESIDENCES

The gain realized by an individual on a principal residence disposition is not included in income and is, therefore, tax-exempt.

A principal residence includes the immediately adjacent land, generally considered to be up to one-half hectare (about 1.24 acres), unless any excess land can objectively be demonstrated to have contributed to the use and enjoyment of the housing unit as a residence. As the determination of any additional exempt portion for the purpose of this gain is complex, you are advised to contact your certified general accountant to assist with this calculation.

Before 1982, individuals were able to arrange their affairs such that if they owned two properties (e.g., a residence and a cottage), the residence could be registered in the name of one spouse and the cottage in the other's name. This resulted in the couple enjoying the benefit of owning two principal residences, while avoiding taxation on the disposition of either property.

For 1982 and subsequent years, a family unit has only been permitted one principal residence for purposes of this exemption. A couple who owned two principal residences prior to 1982 and still own both could possibly enjoy the benefit of two principal-residence exemptions on gains that had accrued up until December 31, 1981.

It is also still possible to obtain the benefit of two principal-residence exemptions by transferring one of the properties (preferably one that has not appreciated substantially in value) to a son or daughter 18 or older, who currently does not own a principal residence. When that property is subsequently disposed of, adult children may claim the principal-residence exemption and avoid taxation on disposition, provided it qualifies as their residence. A complex calculation to determine which property generates the higher exempt capital gain may be required. Your certified general accountant can help with this.

Because a principal residence is considered personal-use property, taxpayers cannot realize a capital loss if, when they sold their home, its value had depreciated from the time it was purchased.



When selling your principal residence, you would be prudent to complete a CRA form T2091—Designation of a Property as a Principal Residence by an Individual, especially if there could be any doubt with respect to any part of the amount you are claiming.

In some instances, certain individuals who are involved in the business of selling homes may be denied the principal-residence exemption if the CRA deems that resale was a motive in the acquisition of a particular property. A dispute could arise with the CRA regarding whether a house sold constitutes a principal residence or is part of a business transaction, based on factors such as the length of ownership; type of property being sold; frequency of home purchase/sale; and the taxpayer's original intent when purchasing the property.

Couples who are involved in divorce proceedings might enter into a settlement that involves transferring ownership in a house and/or cottage. This could, in turn, involve issues such as the timing of the principal-residence designation — especially for a cottage — and the adjusted cost base at which the transfer takes place.

Consult your certified general accountant, especially in situations where complex questions arise about the principal-residence designation.



A principal residence can include a house, apartment, condominium, duplex unit, cottage, mobile-home trailer or houseboat.

#### **PERSONAL-USE PROPERTY**

There are two main categories of personal-use property. One is also termed "personal-use property." The other is "listed personal property" (LPP). While both categories refer to property that is held primarily for personal enjoyment, and not for commercial use, items characterized as LPP are specific and include:

- print, etching, drawing, painting, sculpture or other similar work of art
- jewellery
- rare folio, rare manuscript or rare book
- stamps
- coins

From a tax perspective, both types of personal-use property are considered to have both an ACB, as well as proceeds upon disposition of at least \$1,000. As a result, they cannot produce a capital gain unless disposed of for greater than \$1,000. Most personal-use-property losses are considered personal expenses and are, therefore, not deductible. Only LPP can produce a capital loss, subject to strict rules. For example, capital losses arising from LPP can only be offset against capital gains specifically arising from LPP. If LPP losses cannot be offset by LPP gains in the same year, they can be applied against previous LPP gains not already offset up to three years back; or against future gains for up to seven years.

Consult your certified general accountant for more details.

## Personal Deductions

### CHILD CARE EXPENSES

A claim may be made for expenses incurred on behalf of eligible children to allow individuals or their spouses or common-law partners to:

- Earn income from employment or self-employment.
- Spend at least 12 hours per month studying in an educational program lasting at least three consecutive weeks at a secondary school, college, university or other designated educational institution.
- Conduct research or similar work for which either spouse or common-law partner received a grant.

Generally, the parent with the lower net income claims the least of:

- The actual amount paid.
- Two-thirds of that parent's earned income.
- \$10,000 for each child on whose behalf a disability tax credit may be claimed, regardless of age; plus \$7,000 for each other eligible child under seven at year-end; plus \$4,000 for each other eligible child between seven and 16, inclusive (extending past 16 only for children who have a physical or mental infirmity and remain dependent on the taxpayer or spouse).



Although one condition of being able to deduct child-care expenses involves earning a living, this deduction might still be available during periods in which temporary, extenuating circumstances, such as a strike or other labour stoppage, prevent you from working. Furthermore, there may be other instances when child-care expenses remain deductible because the services provided help enable a parent to earn a living or attend classes, even though the services were not provided at the exact time they were at work or school.

Eligible children include the taxpayer's, his or her spouse's or common-law partner's natural or adopted children, or one for whom the individual had custody and contributed to the support; who was under 16 at any time in the year; or dependent by reason of mental or physical infirmity.

For parents of children with a disability, there is no requirement that the parent claiming the child-care expenses for eligible services, such as baby-sitting, or those provided at a day nursery or day-care centre, among others, be the one who claims the disability tax credit (DTC) on behalf of an eligible child. In many cases it will be advantageous for the other parent to claim the DTC. In some cases the child, after having attained the age of majority, might be able to claim the DTC.

A maximum of \$250 per week can be claimed for all children 16 or younger for whom anyone is entitled to claim a DTC.

Under certain conditions, the supporting person with the higher income will be able to claim child-care expenses, up to \$175 per week for each child under seven or who has a severe disability, plus \$100 per week for other eligible children. For example, in two-parent families where one spouse or common-law partner is working while the other is studying full- or part-time,



The child-care portion of fees paid to a private school that provides both educational and child-care services (such as before or after-class supervision) might also be deductible as child-care expenses.

the higher income spouse is eligible to claim a deduction (for part-time education the corresponding amounts eligible for deduction are \$175/\$100 per month, respectively).

Parents who have shared custody for a child over the course of a taxation year might each be entitled to claim a deduction for eligible expenses incurred while that child resided with them.

Payments made to a boarding school or camp, including a sports school that requires lodging qualify up to a maximum of \$175 per week per child under seven and a maximum of \$100 per week for other eligible children between seven and 16, inclusive.

The deductibility of summer day camps, sports schools or other recreational activities may depend on factors such as the child's age, the program's sophistication (i.e., if it is oriented more toward achieving a progressive, measurable improvement in skills, rather than serving as a recreational sporting activity, the CRA would generally not equate that to child-care), and whether such expenses are incurred to allow the parent or supporting person to carry on earning a living. Court cases have also emphasized that the expenses incurred should relate primarily to guardianship, protection and child-care.

Child-care expenses claimed might reduce the amount eligible for the taxpayer to claim as a child tax benefit.

Check with your certified general accountant to determine which options apply to you.



A grandparent who supports grandchildren may be able to claim child-care expenses as the primary caregiver.

## **SPOUSAL SUPPORT PAYMENTS**

Spousal support payments, which were more commonly referred to as alimony and maintenance payments, are deductible by the payer and taxable to the recipient, defined as the "spouse or common-law partner or former spouse or common-law partner of the payer," provided certain conditions are met. Generally, the payer and recipient must be living apart as a result of the relationship breakdown, both when payments are received and for the balance of that year; also, payments must be an allowance made periodically, either directly or to a third party under a written agreement or court order.

A lump-sum payment stipulated in any legal arrangement would not constitute a periodic payment and, therefore, probably not qualify as being



tax-deductible by the payer. However, where the legal agreement specifies that a periodic payment take place and the payer makes a lump sum payment in respect of arrears, or as an advance under that agreement, then that payment would probably qualify as being tax deductible by the payer, with the recipient having to include it in taxable income.

Payments made before a written agreement or court order has been issued are also deductible to the payer and taxable to the recipient if the agreement or order specifically provides that payments made earlier in the year or the immediately preceding year qualify.

Expenses specifically determined by a court order or written agreement as being payable directly to a third party for spousal support are also deductible and taxable to the respective parties.

### **CHILD SUPPORT PAYMENTS**

Child support payments are treated differently than spousal support payments. Recipients do not include child support payments in their income, nor does the payer deduct those payments for tax purposes, if they are made as a result of a written agreement or court order made on or after May 1, 1997. The same treatment may apply to a written agreement or court order before that date, or an amendment to that original agreement or order after May 1, 1997, provided payments commence on or after May 1, 1997.

Prior to that date, child support paid pursuant to a written agreement or court order was deductible by the payer and taxable to the recipient. Parents with existing agreements made before May 1, 1997, with payments which commenced prior to that day, have the option of filing a joint election with the CRA to apply the new tax treatment to payments made after April 30, 1997. Once the tax treatment has been changed, however, parties will not be permitted to return to the old rules.

In order for an allowance to qualify as child support, it should generally be payable on a periodic basis (typically weekly or monthly), with provisions to continue for either an indefinite period or until the occurrence of a specified future event, such as a child attaining the age of majority.



Be aware that if you go to court and obtain an amending order to an existing agreement involving child-support payments, the income-tax rules attributable to each may be different, particularly if the original agreement was made prior to May 1, 1997, and the amendment occurred on or after that date.

### **ISSUES RELATED TO SPOUSAL AND CHILD SUPPORT**

Legal fees incurred to establish spousal or child support are deductible. Should a portion of the legal fees paid in a divorce settlement be for obtaining child support, the onus is on the taxpayer to establish the proportion of fees directly related to child support.

Legal costs incurred to enforce pre-existing rights to interim or permanent support amounts; to increase spousal and/or child support once an original court-imposed settlement has been passed; or to defend against (but not for)



Legal agreements should specify the breakdown, if any, between support payments that are for spousal support and child support. Otherwise, it will be assumed for tax purposes they are all for child support and treated accordingly by the CRA.

the reduction of support payments (whether child support or otherwise) are all deductible, provided they are not incurred against an estate.

The CRA used to rule that legal fees incurred in establishing the right to spousal support amounts were not deductible because such costs were for personal or living expenses. However, the CRA has changed its position and now considers legal costs incurred to obtain spousal support under the *Divorce Act* or applicable provincial legislation in a separation agreement to have been incurred as a result of enforcing a pre-existing right to support and, therefore, deductible.

Support payments can be made directly to a child at the spouse's discretion.

Taxpayers must also be cognizant of any relevant provincial laws with respect to support or maintenance that might apply to them.



You may claim eligible support payments made to a payee living outside Canada if you have adequate proof of payment; in most cases, the CRA will ask for a court order and/or written agreement and payment receipts to allow this deduction. Retain these documents to support your claim.

## MOVING EXPENSES

Taxpayers may claim eligible moving expenses to change residences within Canada, provided the move brings them at least 40 kilometres closer (i.e., using the shortest normal route) to a new job, business location in Canada, or post-secondary institution at which they enter full-time attendance.

The claim amount is limited to income from the new business or employment, or prizes and research grants, either in the year of the move or the following year. For individuals who are reimbursed in whole or in part, the full amount of the moving expense can only be claimed as a deduction if the reimbursement amount is also included in calculating income.

Students who were in full-time attendance at a post-secondary educational institution in Canada and who move at least 40 kilometres within Canada for employment purposes may also claim moving expenses against income earned from a full- or part-time job (including a summer job) the year the



You do not necessarily need to have a job at your new location to become eligible to deduct moving expenses against earned income when you eventually find and begin work within a reasonable period of time. An example of this could be where a taxpayer moves from one geographic location to another in Canada where employment opportunities are better.



The Tax Court of Canada ruled in 2009 that a person who accepted a new full-time position in a different department, but at the same hospital where she previously worked part-time, was eligible to claim expenses for a move that brought her more than 40 kilometres closer because that helped enable her to work full-time hours.

move took place or the following year. This also applies the year after graduation.

Eligible moving expenses include such items as:

- Travel costs, including reasonable amounts for meals and accommodation to move the individual and members of the household.
- Costs for up to 15 days of temporary board and lodging near either residence.
- Storage costs for household effects.
- The cost of connecting or disconnecting utilities as a result of the move.
- The cost of cancelling a lease or selling the old residence.
- Legal fees.
- Reasonable selling costs directly related to the sale of the home.
- Transfer taxes or taxes upon registration of title to the new residence only if a former residence has been sold.

Additional related expenses with respect to maintaining a vacant former residence, such as mortgage interest, property taxes, insurance premiums, maintenance of heat, power and utility connections, along with certain personal costs to revise legal documents to reflect the new address, are also deductible. The deductible amounts are limited to the lesser of actual costs involved in maintaining the former premises, or \$5,000.

Taxpayers who rent out a former home in their original location prior to moving because they are unable to sell it might be able to claim rental income and losses in connection with that property.

Limited tax-free compensation may be available where employers reimburse employees to cover a loss or diminishment in the value of their former home. Compensation of up to \$15,000 for an eligible housing loss is tax-free. If the compensation exceeds \$15,000, half that excess is taxable.

Under certain circumstances, a taxpayer who is required to move into a temporary home before moving a second time into a permanent home might be able to deduct expenses related to both moves. In determining whether a home is considered temporary or permanent in nature, the tax courts are likely to look at a variety of factors such as if certain of the taxpayer's material belongings remain in storage and if family members have relocated with the taxpayer.

Furthermore, taxpayers who move to a new location and work there for only a short period of time (i.e., a few months), before moving a second time for employment reasons — perhaps back to their original venue — might be able

to claim expenses for two moves provided they can prove they were “ordinarily resident” in terms of being settled into the daily routine of life, while in both places.

Moving expenses might also be deductible in certain circumstances that involve a move in or out of Canada, provided the taxpayer is, and remains, a Canadian resident.



If a former home is sold for a loss in a year after relocation, a taxpayer might be able to select in which of those two years it is best to claim that loss for tax purposes. Consult your certified general accountant if this situation applies to you.

### TRAVEL-EXPENSE CLAIMS

Taxpayers have the option of using a simplified method to calculate certain non-reimbursed travel expenses, specifically related to a move, medical treatment or for northern-resident deductions. Such travel can, for example, occur by automobile, bus, train or airplane, and cover such items as hotel or motel accommodation, meals and other incidental expenses. This simplified method includes a flat rate of \$17 per meal (to a maximum of \$51 per day) per person.

Special rates apply to transportation-sector employees, who can use the rate of \$17 per meal (up to a maximum of \$51 per day). In addition, transportation-sector employees, such as those involved in the trucking, railroad, bus or airline industries to transport people and/or goods, can use the Canadian equivalent of U.S. \$17 per meal (up to a maximum of U.S. \$51 per day) while travelling and incurring meal expenses in the United States.

Receipts do not have to be submitted when claiming these flat rates, although taxpayers should keep their receipts in case the CRA asks for proof of the claim. Employees who elect to claim actual meal expenses must keep their receipts in order to claim.

The *Income Tax Act* allows employees to deduct 50 per cent of meal expenses, regardless of whether they elect to do so via fixed or actual rates.

The simplified method also includes a fixed amount to be claimed per kilometre of travel in each province or territory (where inter-provincial/territorial travel is involved, the venue from which the journey began is used for calculation purposes). The applicable rate established by the CRA for the 2008 taxation year in Ontario was 55.5 cents per kilometre. Changes for the following year are typically published by the federal government either late in the old calendar year or early in the new one; therefore, possible updated rates for the 2009 taxation year were not yet available when this booklet went to press.



Foot and bicycle couriers, along with rickshaw drivers, also qualify for a meals deduction of up to \$17 daily, without receipts.

## NORTHERN RESIDENTS DEDUCTIONS

Special deductions relating to residency and travel are available to taxpayers who reside in designated northern areas defined as either a “prescribed northern zone” or a “prescribed intermediate zone” (which collectively encompass all three territories, plus parts of Canadian provinces with the exception of those in the Maritime region) for a continuous period of not less than six months beginning or ending in the year. Such venues are listed in CRA form T4039 — Northern Residents Deductions — Places in Prescribed Zones.

Taxpayers in a prescribed northern zone are eligible for a basic residency deduction of up to \$8.25 per day, or \$16.50 if they are claiming on behalf of the entire household, even if there is only one member in that household.

Taxpayers in a prescribed intermediate zone are eligible for one-half the amount of the northern deduction — \$4.13 for individual taxpayers, and \$8.25 per household.

In some instances, these deductions might help offset the inclusion in income of a cost-of-living differential, or premium, paid to certain taxpayers who reside in places such as Canada’s three territories. Such premiums are designed to compensate for living in more isolated areas that have a higher cost of living and require greater travel expenses.

Supplementary housing benefits are also available for residents in prescribed zones that do not have a developed rental market.

Taxpayers claiming northern residents deductions must fill in CRA form T2222 and attach it to their income tax return.

## Part Two: Tax Planning Issues

### Income Splitting

Income splitting with a spouse or other family member in situations where this is legally permitted can be an effective way of saving the family unit tax — sometimes a very substantial amount. However, there are stringent rules in place designed to prevent income splitting in certain instances, so it is necessary to know where these opportunities exist and where they do not in order to carry out proper tax planning.



If you earn more than your spouse, you could reduce your family's combined tax bill by paying your spouse's expenses, thus allowing him or her to save some money for investment purposes. The income and gains from these investments would then be taxed in your spouse's hands at a (presumably) lower tax rate. This strategy will also help you even out future retirement income if you have been able to invest in a tax-deferred retirement plan and your spouse has not.

#### ATTRIBUTION RULES

The *Income Tax Act* includes rules that cause income to be attributed to and taxed in another person's hands in specific instances. For example, income earned from money or other property loaned to a spouse or common-law partner, related minor, or trusts of which they are beneficiaries, is attributed to lenders except in defined circumstances.

Low interest or interest-free loans made to a non-arm's-length adult, such as an adult child, may result in income attribution if one of the main reasons for the loan is to reduce or avoid tax. Such rules also apply to income from loaned property.

To further discourage income splitting with minor children, a special tax at top marginal rates applies to certain income received by minor children under 18. Generally, this special tax applies to the receipt of dividends and other shareholder benefits from private corporation shares as well as income received from a partnership or trust that provides property or services to a business in which a relative of that child participates.



If you earn less than your spouse, keep a clear record of the source of your investment funds to ensure that your investment income is attributed to you. This could be accomplished by, for instance, depositing your personal income into a separate bank account rather than a joint account. Then those funds could be used to make investments in your name.



Income earned from Canada child-tax-benefit (CCTB — see chapter additional tax considerations) payments invested in the child's name will not be attributed to the parents.



Be careful how trust property is used to benefit minors. In one decision handed down by the Tax Court of Canada, three child beneficiaries were found to be joint and severally liable for a trust's taxes owing after a parent used some of the trust's proceeds to pay for their private-school tuition and summer-camp fees.

#### **ATTRIBUTION OF CAPITAL GAINS**

Attribution generally applies to any capital gain realized by a spouse or common-law partner on property loaned or transferred at less than FMV. Therefore, when there is a gain on the disposition of such a property, reinvestment of the full proceeds constitutes a substituted property and all gains from the new property would also be attributed to the owner of the original property.

However, a capital gain realized by a child or other related minor is not subject to attribution, except for certain farm property transferred under a tax-deferred rollover. Attribution will also not apply where capital gains have been earned in an irrevocable trust established for a child (minor or otherwise).

Parents often contribute to investment accounts held in trust for their children. To avoid attribution of capital gains in that instance, take care that such "in trust for" accounts qualify as irrevocable trusts. To qualify, the terms and conditions of the account must serve to divest, deprive or dispossess the parents of title to deposited funds. If the parents have the right to withdraw those funds for their personal benefit, the account will not qualify as an irrevocable trust.

#### **TRANSFERS FOR FAIR VALUE**

Transferred property for which fair market value (FMV) consideration is received is not subject to attribution rules. A taxpayer who transfers property to a spouse or common-law partner must elect that spousal rollover rules do not apply in order to avoid being subject to attribution rules. Through this election, the transferor may report any accrued gain up to that time. The spouse will then report any future gain realized.

Where property is sold to a related person for less than its FMV, the seller is deemed to have received consideration equal to its FMV. Moreover, the family unit might ultimately pay double tax on a portion of any accrued capital gains. That is because the recipient will be taxed on any gains made on top of the original purchase price, part of which — the amount necessary to hike the selling price back up to FMV — will have already been reported by the seller.



Be aware that if you have any tax liabilities outstanding at the time you transfer property in a non-arm's-length transaction — i.e., to a spouse or other family member, especially where you have received less than FMV consideration in return, they might, under some circumstances, be deemed by the tax courts as being joint and severally liable and, therefore, partially responsible for your liability.

## LOANS FOR FAIR VALUE

If a loan is made, or transferred property is settled with a loan, attribution rules do not apply provided:

- Interest is charged on the loan at the lesser of a normal commercial rate or CRA's prescribed rate.
- Interest in respect of that year and each preceding year has been paid no later than 30 days after the end of each year.

If a taxpayer loans funds to a spouse or common-law partner, with interest payable at least annually at the lesser of prescribed or commercial rates and the spouse or common-law partner invests those funds to achieve a yield exceeding the rate of interest charged, that excess income will be taxed in the spouse's or common-law partner's hands, not attributed to the taxpayer.

## LOANS TO EARN BUSINESS INCOME

The *Income Tax Act* clearly distinguishes between business and property income. Attribution rules do not apply to income earned from a business — either as a proprietorship, partnership or through an SBC. Attribution will apply, however, if the borrower is a limited partner or a partner who is not actively engaged in the activities of the partnership or a similar business.

Loans to family members, if used in an active business, will not result in attribution of the proceeds of any subsequent business income or gains.

## REINVESTMENT OF ATTRIBUTED INCOME

In situations where earned income is attributed to the lender, the reinvestment of that income is for the recipient's account and will not be subject to attribution.



A loan may be preferable to an outright transfer, since after realizing the gain the transferee could repay the loan and invest the gain, free of future attribution. If cash is not readily available, consider lending investments. Note, however, that these rules can be complex; for instance, if the entire proceeds from the sale of the investment are reinvested, attribution will still apply. Seek advice from your certified general accountant.

## STATUTORY INCOME SPLITTING

CPP benefits of up to 50 per cent of an individual's total benefit may be assigned for spousal payment provided each spouse or common-law partner is at least 60. The percentage eligible for assignment is subject to certain considerations.

One spouse or common-law partner's assignment will automatically result in an assignment, in the same proportion, of the other spouse or common-law partner's direct benefit. Attribution rules do not apply to CPP benefits assigned in this manner.



If you have a higher taxable income than your spouse or common-law partner, which places you in different tax brackets, splitting CPP benefits may achieve some tax savings.



## PENSION INCOME SPLITTING

A taxpayer is allowed to split pension income with a spouse or common-law partner, by allocating up to one-half of the qualified income. See also pension income credit on page 95.



Pension income splitting might be a good strategy to minimize overall family taxes if the spouse to whom the funds are being transferred has low, or no other sources of income.

## SPOUSAL REGISTERED RETIREMENT SAVINGS PLANS

For details on how the spousal registered retirement savings plan (RRSP) can be used for long-term tax-planning purposes, including future income splitting, see the section on spousal RRSPs, page 73.

## REGISTERED EDUCATION SAVINGS PLANS (RESP)

Registered education savings plans (RESP) are usually established for children by a parent or grandparent, to help save for post-secondary education.

Contributions are not deductible for tax purposes and are not taxable when withdrawn. All contributions can be paid to the subscriber or beneficiaries at any time, subject to the terms and conditions of the issuer.



A flying school might qualify as an educational institution that provides post-secondary instruction for the purposes of applying RESP savings.

An RESP under which the sole beneficiary is entitled to the disability tax credit (DTC) in the 32nd year of the plan's existence is called a specified plan.

Contributions to an RESP are allowed for a maximum of 31 years after the plan is established; 35 years if the plan is a specified plan. The income earned within an RESP may be sheltered from tax for a maximum of 36 years — up to 41 years if the plan is a specified plan. It is not taxable until paid out, at which time it will be included in the recipient's income. Since many students have little or no other income, they can usually withdraw the RESP income tax free.

There is no annual contribution limit for an RESP. However, total lifetime contributions are restricted to a maximum of \$50,000 per beneficiary.

Educational-assistance payments (EAP) are taxable distributions to a beneficiary of accumulated income and government contributions. Students may



Former students may still be able to receive income from their RESP for a brief period after leaving school. A beneficiary is entitled to receive EAPs for up to six months after ceasing enrollment, provided the payments would have qualified as EAPs if made immediately before the student's enrollment ceased.



If you are a subscriber to an RESP and you do not expect the beneficiary will qualify for payments before the plan's mandatory expiration, consider temporarily foregoing your RRSP contribution. This will allow you to build up contribution room in the RRSP to permit a transfer of the accumulated income from the RESP.

start receiving EAPs as soon as they are enrolled in a post-secondary education program. Programs may be either full-time or part-time, require attendance or be delivered through distance education courses, as long as they meet the requirements for program length and hours of course work. (See tuition fee and education credits, page 92.) Part-time students must be at least 16 to receive EAPs.

Subscribers may change the named beneficiaries or designate more than one, subject to the plan issuer's restrictions, although take care to avoid causing a taxable over-contribution. If the new beneficiary is a brother or sister of the former beneficiary, and is under 21, or, if both beneficiaries are connected by blood or adoption to an original subscriber, and both are under 21, there will be no tax consequences to replacing a beneficiary.

Should subscribers designate more than one beneficiary, each must be related to the subscriber and be less than 21 at the time of being named. Under these so-called "family plans," one sibling's share may be paid to another sibling. In other words, subscribers are able to maximize contributions for, say, two children, but one child can receive all the accumulated government contributions and income. Contributions under a family RESP cannot be made for beneficiaries after they turn 31.

RESP income can be paid to a subscriber if the RESP is at least 10 years old and all of the beneficiaries have reached 21 and are not currently eligible to receive an EAP, or if the RESP has existed for 36 years (41 years if the RESP is a specified plan), or if all of the beneficiaries are deceased. The first two conditions may be waived if the beneficiary is mentally impaired.

Under those conditions, up to \$50,000 in RESP income may be transferred to a subscriber's or spousal RRSP provided there is contribution room. Otherwise, the accumulated income will be included in the subscriber's income and a 20-per-cent tax will apply, in addition to regular taxes.



RESPs allow adults to grow their education savings tax-free too. You can name yourself or another adult as the sole beneficiary of an RESP, as there are no age limits for RESPs established for only one individual.

#### **CANADA EDUCATION SAVINGS GRANT (CESG)**

For every dollar a parent, grandparent or other person contributes toward the RESP of a child up to 18, the federal government will contribute an additional 20 cents, up to an annual limit of \$500 for a \$2,500 contribution (up from \$400 for a \$2,000 contribution in 2006 and prior years) through the Canada education-savings grant (CESG). Special rules apply to contributions made on behalf of 16- and 17-year-olds.

Families with net family income of up to \$40,726 in 2009 are entitled to a higher annual CESG grant of 40 cents for every dollar on their first \$500 of RESP contributions. Families with net family income between \$40,726 and \$81,452 are eligible for a higher grant of 30 cents per dollar each year on their first \$500 of contributions.

For 2009, the maximum annual amount of CESG (basic + additional) that can be paid in any year is \$600 for current contributions, and \$1,100 if there is unused grant room from previous years. Unused grant room accumulates at a rate of \$500 a year, (up from \$400 in 2006 and prior years).

The maximum lifetime CESG that a child is eligible for remains \$7,200.

#### **REGISTERED DISABILITY SAVINGS PLAN (RDSP)**

A registered disability savings plan (RDSP) is designed to provide savings for the long-term financial security of a child or adult with a disability. This plan, which has a similar design to the RESP, began in the 2008 calendar year.

As with an RESP, earnings generated on contributions are tax exempt while they remain in the plan. Contributions are not tax deductible and not included in income when paid out. All other amounts paid out of the plan are included in the beneficiary's income. Unlike an RESP, the holder cannot directly access the non-taxable contributions, as only the beneficiary or the beneficiary's estate is entitled to receive payments from an RDSP.

Anyone can contribute to an RDSP with the permission of the holder, and contributions are permitted until the end of the year in which the beneficiary reaches 59. Contributions are limited to a lifetime maximum of \$200,000 with no annual limit.

To augment funds in the RDSP the government will contribute, in the form of Canada disability savings grants (CDSG), funds equivalent to between 100 per cent to 300 per cent of RDSP contributions, to a maximum of \$3,500 annually, and \$70,000 over the lifetime of the beneficiary, depending on the beneficiary's family income. The federal government will also contribute up to \$1,000 annually in Canada disability savings bonds (CDSB), to a maximum of \$20,000; depending on the beneficiary's family income. Lower-income families may qualify for payments from the CDSB program without having to make a contribution to an RDSP. Beneficiaries must be 49 years or younger at the end of the year to be eligible for a CDSG or CDSB.

The deadline for making contributions and applying for the matching grant and the income-tested bond for the 2008 contribution year was extended to March 2, 2009 from December 31, 2008. The 2009 RDSP contribution year began March 3, 2009 and ends December 31, 2009.

Generally, only the beneficiary can open an RDSP. If the beneficiary is a minor or has reached the age of majority but is not competent, a parent or certain other individuals can open the RDSP and become its holder.

When amounts are paid from an RDSP, all CDSGs or CDSBs paid into the plan in the preceding 10 years must be repaid.

Only individuals who are residents of Canada and eligible for the disability tax credit (DTC) can be beneficiaries under an RDSP. If beneficiaries improve to the extent they no longer qualify for the DTC, proceeds of the RDSP (less any repayment of CDSGs and CDSBs) must be paid to them and the plans collapsed.

Lifetime disability-assistance payments (LDAP) are annual payments made from an RDSP that are subject to annual minimum and maximum limits. They may begin at any age but must commence by the end of the year in which the beneficiary turns 60. Once started, they must continue until the plan is terminated or the beneficiary dies.

Disability-assistance payments (DAP) are any lump sum payments to a beneficiary or to the beneficiary's estate. They may be requested at any time. If the total of government contributions made before the beginning of the year exceeds the total of private contributions made, the DAP will be subject to restrictions based on the LDAP formula. These restrictions may be relaxed if a medical practitioner certifies that the beneficiary is not expected to live longer than five years.

Contributions and payments from RDSPs will not impact eligibility for federal government benefits or Ontario social assistance.

## Tax-Advantaged Investments

The term tax shelter is commonly used when referring to investments and/or other arrangements with tax advantages, but it also has a very specific meaning for tax purposes. The definition is complex, but generally an investment or "gifting arrangement" may be considered a tax shelter under the ITA if:

- It is promoted as offering tax savings; and
- It is reasonable to consider that the losses, deductions or credits resulting from the investment or arrangement would, within the first four years, be equal to or more than the net cost of the original investment.

Taxpayers face a number of limitations with respect to tax-shelter deductions and credits. Such deductions and credits can, for instance, result in alternative minimum tax (AMT), see page 107, or be limited by at-risk rules, which state that individuals may not write off more than the cost of their investment.

Deductions and credits will also be limited if loans related to tax shelters are considered limited-recourse debt, as defined by the *Income Tax Act*. To avoid being considered limited-recourse debt, money must be borrowed with bona fide arrangements to repay the principal within 10 years. Interest must be payable regularly at prescribed rates, with the investor at full risk for the loan. Limited-recourse debt is not included in the ACB of an investment.



Obtain the benefit of tax-shelter deductions in advance. Apply to your CRA district taxation office for permission to reduce income taxes at source to reflect tax-shelter deductions.

Taxpayers must specifically identify any tax-shelter-investment deductions or credits, accompanied by a shelter-identification number, on their tax return. Tax-shelter promoters should provide the necessary filing forms and relevant details, such as the amounts for losses or deductions. An investment or arrangement can be considered a tax shelter even if the promoter has not specifically represented it as a tax shelter or obtained an identification number. However, if an investment or arrangement is found to be a tax shelter and an identification number was not obtained all deductions and claims relating to the tax shelter will be denied.

Tax opinions of accountants and lawyers provided by the promoter of a tax shelter, or the existence of a tax-shelter identification number, do not indicate that the CRA has confirmed that deductions or credits related to the tax shelter will be allowed. It is common for the CRA to disallow deductions from tax shelters, often reassessing years where they had previously allowed them. Therefore, before you invest in a tax shelter, it may be wise to seek independent tax advice from your certified general accountant to assess the potential risks and benefits.

#### **LIMITED PARTNERSHIPS (LP)**

Limited partnerships (LP) provide limited liability while allowing the investor a flow-through of tax losses directly to them. LP investors are taxed on their share of income or loss in the partnership. Cash distributions represent partnership drawings and reduce the limited partner's ACB but do not represent taxable income.

For partnership interests acquired after February 22, 1994, a capital gain must be reported where limited or passive partners have a negative ACB in their partnership interest at the end of a fiscal period. This provision will prevent tax-shelter arrangements where tax-deductible losses are claimed and the investors subsequently receive cash distributions exceeding the partnership interest costs. Only the income or loss for a prior (not the current) period will be taken into account in determining the ACB of a partnership interest.

In addition, losses allocated to a limited partner in a taxation year are restricted to that limited partner's at-risk amount at the end of the fiscal period of the partnership, minus certain other deductions. For most investors, their share of a partnership's losses and their at-risk amount will be the amounts reported on the information slip provided by the partnership.

Matchable-expenditures rules introduced in 1996, and further restrictions added in 2001, have eliminated mutual-fund and film limited-partnership tax shelters. However, "grandfathering" provisions apply for certain agreements made in writing prior to September 18, 2001. Consult your certified general accountant for specific details.

#### **RENTAL REAL ESTATE AND REAL ESTATE LIMITED PARTNERSHIPS**

Rental real estate used for commercial purposes might provide taxpayers with the ability to leverage capital, write-off expenses, earn capital-cost allowance (CCA) sheltered rental income, and enjoy capital appreciation on their investment. Investing in rental real estate through a limited partnership may slightly escalate the rate at which CCA can be claimed because the partnership claims the CCA and the investor deducts the financing costs. If the investor acquired the property directly, the financing costs would increase the rental expenses and potentially reduce the permitted CCA claim.



Profits and losses from rental property can affect your RRSP deduction limit, as well as possible entitlement to certain means-tested government benefits.

Rental income received from real estate might, under certain circumstances, be considered by the CRA to be either income from a business or income from property. That is a key distinction because the two are sometimes treated differently from a tax standpoint.

In most cases, rental income will be considered income from property if it is earned by renting space and providing only basic services. If additional services are provided, the rental income may be considered business income. The more services provided, the greater the chance the rental operation is a business. However, as the differences between business and property income are not clearly defined in the *Income Tax Act*, it is best to check with your certified general accountant to get clarification.

Expenses incurred to repair or improve a home or a portion thereof, in preparation for or in the course of renting it out, may qualify as either current expenditures or, depending on factors such as the significance and permanence of those improvements, as capital expenditures.

Market considerations aside, some tax aspects associated with rental real estate could potentially reduce its appeal. For example, while CCA in respect of a rental property may be claimed to shelter net rental income from tax, it may not be claimed to create or increase a loss. The fact that when the property is sold any recapture will be added to the investor's income (to the extent proceeds of disposition exceed the undepreciated capital cost) further diminishes the potential advantages of claiming CCA on rental real estate.

If you are a Canadian resident who owns foreign property that is being rented or leased, consult your certified general accountant to help you determine the correct tax treatment and any elections that might be required with respect to that property.



If you are renting out a property that you also use personally, such as a cottage, be sure that you keep separate, meticulous records of expenses incurred for personal use and rental use of that property.

#### **LABOUR-SPONSORED VENTURE-CAPITAL CORPORATION (LSVCC)**

Labour-sponsored venture-capital corporations (LSVCC) are investments sponsored by labour organizations that allow individuals to pool their money to purchase a diversified portfolio of small- and medium-sized businesses. Taxpayers can register their LSVCC purchase as an RRSP and receive the normal RRSP tax deduction as well as the federal and provincial tax credits.

The federal government provides a maximum credit of 15 per cent on a \$5,000 investment under this program; thus there is a federal tax credit of up to \$750 available. Ontario offers a labour-sponsored investment fund (LSIF)



If you have a shortage of cash, consider borrowing for your RRSP contribution and investing in a LSVCC. If you were in the highest tax bracket (46.41 per cent in Ontario in 2009), your tax savings from a maximum \$5,000 federal investment would be \$2,321 from the RRSP, plus \$1,500 from the LSVCC tax credits, for a total tax saving of \$3,821. You can then use your tax savings to repay most of the loan

credit on up to 15 per cent of \$7,500, or \$1,125. Some "research-oriented" investment funds qualify for an additional five per cent Ontario credit, to a maximum of \$375, bringing the total Ontario credit to \$1,500.

There is, therefore, the potential for a combined federal/provincial tax credit of \$2,250. However, Ontario's LSIF is scheduled to be phased out in 2010 and 2011. (See section on LSIFs, page 118 .)

Investments made in an LSVCC in the first 60 days of the year will qualify as contributions for either the previous or current tax year.

LSVCC shares redeemed during the month of February or on March 1 of a (non-leap) calendar year are treated as having been redeemed 30 days later. This means shareholders who are 30 or fewer days short of holding their investment for the requisite number of years will avoid clawback of the tax credit. They will also have the opportunity to acquire new LSVCC shares during the first 60 days of a year using proceeds from the redemption of existing shares, thereby making them eligible to claim a tax credit for the previous year.

This tax credit does not reduce the ACB of the shares held, but will reduce any capital loss realized on their disposition.

To avoid a tax-credit clawback, LSVCC investments must be held for at least eight years (five years if they were purchased prior to March 6, 1996). In case of death, the LSVCC can be redeemed immediately, without clawback of the tax credits.



If you own units of an LSVCC purchased in 2001 or earlier, check the terms of your fund. In some cases it may be possible to redeem the units of a fund and reinvest them in the same fund (or another one) to obtain another tax credit. Under federal rules, fund units must be held for a minimum of five years if purchased before March 6, 1996, or eight years if purchased after March 5, 1996. The equivalent provincial rules vary by jurisdiction. Also, before redeeming your units, be sure to check the terms of the prospectus of the fund you purchased as redemption fees imposed by the fund company may also apply.

#### **FLOW-THROUGH SHARES AND OIL, GAS AND MINERALS**

Special tax incentives exist to encourage individuals to risk capital for the exploration and development of oil, gas and minerals. These incentives are offered through flow-through shares, joint ventures and limited partnerships. Through such vehicles, individuals may be eligible to deduct specific exploration expenses and other resource-related incentives.

Flow-through shares allow issuing companies to renounce certain deductions in favour of the investor. The initially acquired shares are priced at a premium to market value so the company can participate in the tax savings. Investor deductions generally reduce the cost base of the shares to zero, resulting in a capital gain equal to the entire proceeds when the shares are sold.

In addition to deductions for expenses, there is a 15 per cent non-refundable mineral-exploration tax credit available to individuals who invest in qualifying flow-through shares. To be eligible the flow-through share agreement must be made on or before March 31, 2010.

Ontario residents who qualify for the aforementioned federal credit with respect to expenses incurred for mineral exploration in Ontario may also qualify for a five per cent provincial tax credit through the Ontario-focused flow-through share (OFFTS). The Ontario portion of this credit is refundable.

Enhanced tax incentives also exist with respect to the availability of flow-through shares for investors in certain renewable energy and energy-conservation projects.

Joint ventures are similar to limited partnerships except that at-risk rules do not apply. Partnerships and joint ventures may also be eligible for additional tax benefits in the form of provincial crown royalty-tax-rebate programs.

Consult your certified general accountant for details.

#### **UNIVERSAL LIFE (UL) INSURANCE POLICIES**

Exempt universal-life (UL) insurance policies offer many tax advantages. Under an exempt UL policy, for instance:

- Premiums paid in excess of the mortality cost and premium tax are accumulated and invested. Income tax on the returns of investments held within the accumulation fund is deferred until withdrawals are made from the policy.
- When the policyholder dies, beneficiaries generally receive both the face value of the life insurance and full amount of the accumulation fund tax-free, resulting in permanent tax savings.

Furthermore, UL can be used to fund retirement needs. Individuals can, for example, borrow from their policy or pledge it as security for a loan, subject to the terms of the policy, with the loan providing a cash flow to fund retirement. Because this cash has resulted from a loan, rather than income, it is not taxable. Also, if repayment of the loan is deferred until the death of the policyholder, the loan will effectively be partially repaid out of pre-tax dollars.

UL insurance is, however, a complex product and should only be purchased with professional advice, including a full explanation of the plan's terms, underlying investments, costs and tax treatment.



Don't confuse insurance-policy dividends with corporate dividends. Insurance-policy dividends are not a distribution of corporate profits; they are a return of premiums and as such are not taxable so long as they do not exceed the adjusted cost base of the insurance policy.



## Deferred Income Plans

Deferred income plans allow taxpayers to earn investment income on which they can defer paying tax while it remains in the plan. Some deferred income plans also allow a tax deduction, within specified limits, for contributions made.



Contribute to your RRSP early in the year. If, for example, you contribute \$21,000 – the maximum possible annual contribution amount for 2009 – at the beginning of the year instead of at the end, over a 25-year period, assuming a five-per-cent rate of return, you would have an extra \$122,800 in your RRSP.



If you are an employee who is making regular RRSP contributions, request that the amount of income tax withheld on your paycheque be reduced in order to reflect the savings those contributions will bring. This is a more efficient way to manage your money than overpaying tax up front, then waiting for a refund the following year.

### REGISTERED RETIREMENT SAVINGS PLANS (RRSP)

Registered retirement-savings plans (RRSP) are registered plans into which individuals contribute savings or eligible investments for future use — typically, but not necessarily exclusively, for retirement. Taxpayers can have several different RRSPs and invest each in a variety of eligible vehicles (See section on self-directed registered retirement savings plans, page 74, for examples.)

Eligible RRSP contribution amounts reduce taxpayers' taxable income and thus save tax. However, any RRSP withdrawal will trigger an income inclusion for that taxation year, regardless of whether some — or all — of the amount withdrawn is re-contributed to the plan later that year.

Taxpayers may be required to pay certain RRSP-related administrative or management fees outside of their plan. Such fees are not tax-deductible.

### REGISTERED RETIREMENT SAVINGS PLANS' CONTRIBUTION LIMITS

The annual RRSP contribution limit is 18 per cent of the previous year's earned income to the allowable maximum dollar limit (see below); less the previous year's pension adjustment (PA) as reported on the T4, plus unused contribution room carried forward from previous years. The PA for a year is a measure of the total value of the benefit earned for the year under a registered pension plan (RPP) or deferred profit-sharing plan (DPSP). Past service pension adjustments, if any, are also deducted. The contribution limit also takes into account total pension-adjustment reversals (PAR). PARs restore lost contribution room to individuals leaving RPPs or DPSPs before retirement.



Individuals with low earned income that precludes their owing any tax should still consider filing a tax return in order to create RRSP contribution room for future use because 18 per cent of earned income from the previous year is eligible to be contributed to an RRSP.

The definition of “earned income” includes:

- employment earnings, net of union dues and employment expenses
- research grants (net of related expenses)
- net income from self-employment and active partnership income
- disability pensions under the C/QPP
- royalties
- net rental income
- alimony or separation allowances received
- employee profit-sharing plan allocations
- supplementary unemployment-benefit plan payments (not EI)

Less:

- the current year’s loss from self-employment or an active partnership
- deductible alimony and maintenance payments
- current year rental losses

The maximum annual dollar limit has been increased to \$21,000 for 2009, up from \$20,000 for 2008. That ceiling is scheduled to increase to at least \$22,000 for 2010, after which the annual maximum contribution rates will be indexed to reflect increases in average wage growth.

The CRA reports individuals’ RRSP contribution limits for the current tax year on the notice of assessment they receive after filing their previous year’s tax return. Eligible contributions must be made either during the calendar year or within 60 days of the calendar year-end, in order to be deductible for the previous tax year. Unused RRSP limits that have accumulated since 1991 are eligible to be carried forward by the taxpayer.

Contributions to a personal RRSP may be made until the end of the calendar year in which the taxpayer turns 71.



You don’t have to deduct an RRSP contribution the year in which it is made; instead, you can carry it forward for deduction in a future period when you have income placing you in a higher-tax bracket. Be sure you have used all personal tax credits before deducting your RRSP contribution.

#### **SPOUSAL REGISTERED RETIREMENT SAVINGS PLANS**

Taxpayers can contribute to their own RRSP, the RRSP of the spouse or common-law partner, or both, provided they do not exceed their maximum deductible amount. Spousal contributions become the property of the spouse or common-law partner. Although spousal contributions reduce the contributors’ RRSP limits, they do not affect the recipient spouses’ contribution limits for their own RRSPs.

Spousal RRSP contributions have no more immediate tax benefits than contributing toward personal RRSPs. The future tax savings could be substantial, however. Contributing to spousal RRSPs gives taxpayers and the spouse or common-law partner the opportunity to equalize retirement income and reduce their future tax liability.

If, for instance, one spouse or common-law partner belongs to a good registered pension plan and the other does not, it may be beneficial for the spouse or partner with the pension plan to contribute to a spousal RRSP. Then during retirement, a potential scenario might be for that spouse to draw on that pension and either leave funds in the spousal RRSP or withdraw them in amounts that would be non-taxable or taxed at lower rates.

Contributors should be aware, however, that some or all of the income withdrawn from a spousal plan might be taxable in their hands if spousal contributions were made in either the year of withdrawal or the two preceding years. If, on the other hand, the spouse or common-law partner converts the RRSP to an annuity or a registered retirement-income fund (RRIF), withdrawing only the minimum RRIF payment required, there would be no attribution to the contributor.

Contributions to a spousal RRSP may be made until the end of the year in which the spouse or common-law partner turns 71, even if the contributor is older than 71.



If you have both a regular and a spousal RRSP and are the annuitant for each, you can transfer the proceeds of one plan into the other prior to maturity if you believe that will provide certain advantages, such as administrative ease or a reduction of RRSP fees. The combined new plan would then be classified as a spousal plan.

#### SELF-DIRECTED REGISTERED RETIREMENT SAVINGS PLANS

Investing in an RRSP through banks, trust companies, life-insurance companies and mutual funds is usually the most convenient way to start an RRSP. But when the size of an RRSP portfolio and the number of RRSPs individuals own become larger, a self-directed RRSP could allow more flexibility and control over the investments within their plan. It also provides plan-holders an opportunity to consolidate these investments.



If you don't have enough cash to top up your RRSP, consider making a contribution in lieu of cash or "in kind" as it is commonly phrased. The asset transferred must be a qualified investment. Be aware, however, of the tax consequences when transferring investments to your RRSP. The CRA treats such transfers as a sale of the investment. Moreover, while capital gains triggered by a transfer to an RRSP are taxable, capital losses are not deductible.

The list of RRSP-eligible investments is quite extensive. Generally, it includes cash, term deposits, GICs, publicly listed and some private company shares, mortgages, bonds, mutual funds, and some gold and silver, among other investments. The restriction on foreign property held inside an RRSP was lifted as of 2005.

Be careful that you only place qualified investments into your self-directed RRSP, however. The *Income Tax Act* imposes a one-per-cent per-month penalty tax on the value of non-qualified investments placed into an RRSP.

For instance, shares traded on over-the-counter markets generally do not qualify as RRSP-eligible investments.

Check with your certified general accountant if you have any questions about the RRSP-eligibility of your investments.



Beware of the superficial loss rules when purchasing investments within your RRSP. For instance, if you sell a money-losing investment and purchase the same investment in your RRSP within 30 days, the resulting loss may be a superficial loss rather than a capital loss. (See superficial losses, page 52.)

### **SPECIAL REGISTERED RETIREMENT SAVINGS PLANS' CONTRIBUTIONS**

Individuals are allowed to transfer retiring allowances (which may include severance pay and accumulated sick-leave credits) directly into their RRSPs, within certain limits. For years of service between 1989 and 1995 inclusive, the limit is \$2,000 per year. For years prior to 1989, an additional \$1,500, for an annual total of \$3,500, may be contributed for each year of service that the employee did not have a pension plan.

No special contributions are allowed for years of service from 1996 onwards.

Directly transferring such lump-sum payments to an RRSP will eliminate withholding-tax deductions. Individuals who directly receive those lump-sum payments still have 60 days after year-end to contribute to their RRSPs and obtain deductions for the year of receipt. They cannot carry forward unused special RRSP contributions to future years. (See retiring allowance and termination payments on page 23.)

### **CREDITOR-PROOFING RRSPS**

In the event of bankruptcy, creditors have traditionally been able to seize funds from most RRSP plans held at financial institutions. However, RRSPs held through an insurance policy that is properly structured in terms of beneficiaries, etc., are generally exempt from creditors under the federal *Bankruptcy and Insolvency Act*. Therefore, most individuals — particularly if they are self-employed and face a potentially greater risk of bankruptcy — should consider creditor proofing at least a portion of their RRSP portfolio in this fashion. Your certified general accountant can help you set this up.

Amendments to the *Bankruptcy and Insolvency Act*, which had received Royal Assent in December 2007, came into force in September 2009. Such amendments expand creditor protection to RRSP contributions made more than 12 months prior to bankruptcy (though the legislation allows that provinces may provide more immediate protection). Registered retirement income funds (RRIF) are also protected under this legislation. Check with a trustee in bankruptcy for details if this is an area of concern.

### **RRSP OVER-CONTRIBUTIONS**

Over-contributions to an RRSP that are in excess of \$2,000 are assessed a penalty of one per cent per month. Taxpayers may deduct all or a portion of the excess balance in a subsequent year, provided the deduction amount is within their normal contribution limits for that year. Subsequent deduction of

the excess may also occur after the year an individual turns 71 or in years after the plan has matured — provided the individual has sufficient contribution room to absorb it.

Taxpayers who owe tax on over-contributions to their RRSP must pay this tax and file Form T1-OVP — Individual Tax Return for RRSP Excess Contributions no later than 90 days after the end of the year in which they had taxable over-contributions. If they file this form late, CRA will charge a penalty of five per cent of the balance owing, plus one per cent for each month the return is late, to a maximum of 12 months. The late-filing penalty may be higher if they were also charged a late-filing penalty on a Form T1-OVP return for any of the three previous years. Furthermore, if they do not pay tax by the deadline, they may also have to pay arrears interest on any unpaid amount.



Over-contributions to an RRSP can be designated as a repayment of an outstanding Home Buyers' Plan (HBP) loan. Therefore, if you have over-contributed more than \$2,000, you can avoid penalties that might otherwise apply by using that amount to pay down an HBP loan.

### **RRSP EDUCATION WITHDRAWALS**

Taxpayers are able to withdraw money from their RRSPs for qualifying full-time education and training for either themselves or their spouses or common-law partners, but not both at the same time, on a tax-free basis. (For individuals with disabilities, this provision covers both full- or part-time education and training).

This provision is known as the lifelong-learning plan (LLP).

LLP withdrawals may not exceed \$10,000 in a year and \$20,000 over a four-year period. Taxpayers can participate in the plan as many times as they wish, but may not start a new plan before the end of the year in which all repayments are made for previous withdrawals. Withdrawals are generally repayable in equal instalments over 10 years, commencing no later than 60 days after the fifth year marking the date of the first withdrawal (or sooner if the student fails to remain in the program full time).

Withdrawals can also be repaid earlier than required. Amounts that are not repaid as scheduled will be added to taxable income.



Students in medical residency programs that last for at least three months and qualify for the tuition-fee tax credit may also participate in the life-long learning (LLP) program.

### **HOME BUYERS' PLAN (HBP)**

Individuals may withdraw up to \$25,000 from their RRSPs (up from \$20,000 effective January 28, 2009), without attracting immediate taxation, to assist in acquiring an owner-occupied home. The home must be acquired by October 1 of the year following the withdrawal, which is made using CRA Form T1036 — Home Buyers' Plan (HBP) Request to Withdraw Funds from an RRSP.

An ordinary RRSP contribution made less than 90 days before a withdrawal cannot be deducted.

Withdrawn amounts are repayable in equal annual sums over 15 years, beginning no later than the second year following the year of withdrawal (although they can also be made more quickly). Repayments due in a specific year may be made during that year or within 60 days after the year-end. If, during a particular year, individuals do not repay the scheduled amount or repay only part of it, the unpaid portion will be included in their income for that year.

To participate, a prospective homebuyer cannot have occupied a home as a principal residence that was owned by them, or their spouse or common-law partner, at any time from the beginning of the fourth calendar year before the withdrawal year, to 31 days before the withdrawal. Those who wish to withdraw in 2009, for example, must not have owned a home after 2004.

There are special withdrawal rules with respect to purchasing homes for the benefit of a person with a disability who qualifies for the disability-tax credit (DTC). These allow for previous home ownership and multiple withdrawals.

#### **REGISTERED RETIREMENT INCOME FUNDS (RRIF), ANNUITIES AND RETIREMENT OPTIONS**

Individuals are required to terminate their RRSP plans by the end of the year during which they turn 71. When terminating an RRSP, there are three alternatives. Plan holders may:

- Withdraw the funds, in which case the total amount withdrawn is included in their annual income.
- Purchase an annuity that provides a regular income for a defined period, which may include their lifetime; the joint lifetime of both they and their spouse or common-law partner; a fixed period; or combinations thereof. The annuity payments will be taxed as received.
- Transfer an RRSP into a registered retirement-income fund (RRIF), which is similar to an RRSP in that the plans' funds and income earned remain untaxed until withdrawn. Although the funds are held in a trust, taxpayers may continue to exercise authority over investment decisions. They must withdraw a minimum amount from the plan each year, based on their age or that of a younger spouse or common-law partner, upon which they are then taxed. The minimum withdrawal amount, expressed as a percentage of the value of assets within the plan, increases each year until 94 when it becomes fixed at 20 per cent annually until the plan is depleted.



When deciding whether to convert your RRSP into an RRIF, retirement annuity or a combination of both, there are a number of factors to consider. If you are holding an RRIF, for instance, you are able to remain active in making investment decisions. With an annuity, however, you are transferring autonomy of the underlying investment portfolio to financial professionals who, in turn, assume the risk and provide you with a steady income for a fixed period of time or the rest of your natural life. Also, while you can convert all or part of your RRIF funds to a retirement annuity at any time, once annuities have been established, they are permanent.

Within an RRIF, individuals also have the option of withdrawing amounts in excess of the minimum although any excess withdrawn amounts will also become taxable in that year.

#### **REGISTERED PENSION PLANS (RPP)**

In addition to having an RRSP, many employees also belong to a registered pension plan (RPP) through their employer.

The maximum allowable contribution for a money purchase RPP has been increased to \$22,000 for 2009 (from \$21,000 for 2008); in future, they will be indexed annually to account for the average wage growth.

Annual money-purchase plan RPP contribution limits are 18 per cent of pensionable earnings (the same as RRSPs), up to the limits stated above.

The maximum pension limit for defined-benefit registered pension plans (RPP) increased to \$2,444 for 2009 from \$2,333 for 2008; in future they will be indexed on an annual basis to reflect increases in average wage growth.

The age limit at which contributors must stop contributing to RPPs is 71.

Money-purchase RPP proceeds are allowed to pay out pension benefits, using the same income stream permitted under an RRIF (i.e., minimum payments beginning no later than age 72).

#### **OTHER REGISTERED PENSION PLAN FEATURES**

Deductions for RPP contributions, in respect of both current and past services rendered after 1989, are allowed during the year the contribution was made provided the contribution was made in accordance with the plan's registered terms. This applies whether contributions are mandatory or optional.

The deduction amount for past-service contributions rendered before 1990 depends on whether or not taxpayers contributed to any RPP in the year to which the past service applies. If they were not a contributor during that period, they may account for \$3,500 times the number of years of eligible service; however, the maximum amount deductible in any one calendar year is only \$3,500.

For years of service during which the employee was a contributor, the maximum available deduction is also \$3,500, reduced by any current year or past deductions (including those claimed for prior years while not a contributor to any RPP).

Any remaining balance may be carried forward for deduction in subsequent years provided the taxpayer has the available contribution room.

Individuals who make past service contributions to their RPP in instalments will probably pay accrued interest charges. The interest paid for years after 1989 is considered a past-service contribution.

Within limitations, the *Income Tax Act* provides for the transfer of benefits accrued under a defined-benefit RPP to a money-purchase RPP, RRSP, or

RRIF. Likewise, the proceeds of a money-purchase pension plan can be transferred to another money-purchase RPP, RRSP, or RRIF.

Furthermore, funds previously transferred from a money-purchase RPP into an RRSP or RRIF can be transferred back into the money-purchase pension plan, where they are subject to the same payout requirement as the RRIF.

Employees may also deduct, within limits, additional voluntary contributions (AVC) under a money-purchase plan. The amount deducted will, however, affect their RRSP limit the following year.

The CRA now recognizes registered pension plans that provide survivor benefits to same-sex partners.

Beginning in 2008, certain defined-benefit pension-plan holders who are at least 55 may receive up to 60 per cent of their pension, while still being permitted to accrue further benefits.

#### **INDIVIDUAL PENSION PLANS (IPP)**

Another retirement option, best suited to certain older, high-income individuals such as managers of owner-operated businesses and corporate executives who have consistently been able to contribute the maximum amount to their RRSP on an annual basis, might be an Individual Pension Plan (IPP). The annual contribution amount to an IPP, which is a defined-benefit plan, depends on an actuarial calculation which determines how much is required to fund a pre-established pension amount. This minimum amount increases with age.

IPP funds are used to fund retirement through various options, including the owner: withdrawing a prescribed annual pension amount; transferring the commuted value of accrued pension benefits to a locked-in plan; or purchasing a life annuity; the taxpayers' spouses might also be eligible to receive an annuity if they are survivors.

As with RRSPs, contributors get tax deductions for their contribution amounts, and the invested funds are allowed to grow on a tax-deferred basis until they are ultimately withdrawn. Like an RPP, IPP contributions create a pension adjustment amount.

The IPP is also generally creditor proof.

Talk to your certified general accountant if you think this retirement instrument, which has very complex rules with respect to issues such as the treatment of surplus amounts; transfer of plan assets to another retirement fund; and disposition of proceeds upon death; among others, might be beneficial to you.

#### **LOCKED-IN ACCOUNTS**

When individuals leave their place of employment, they often have the option of either receiving a pension at retirement or transferring the commuted value of their deferred pension. Pension legislation usually requires that the commuted value cannot be paid to the individual employees, but must instead be either transferred directly to another pension plan or locked-in plan, or used to purchase a life annuity.



Locked-in plans are just RRSPs or RRIFs with an extra layer of rules found in pension-benefits legislation. The federal government and the provinces (except PEI) each have their own pension benefits legislation and, hence, the requirements for locked-in plans vary by jurisdiction. Locked-in plans are governed by legislation affecting the pension plan from where the funds originate, which might not necessarily be the jurisdiction where an individual currently resides. Locked-in plans should not be confused with a fixed-term investment inside an RRSP, such as a GIC.

There are important differences between various types of locked-in plans as well as between plans listed under the same name that are governed by the legislation of different jurisdictions. Consult your plan administrator to help you sort this all out.

The commuted value of a pension regulated by the *Ontario Pensions Benefit Act* may be transferred to a locked-in retirement account (LIRA). Unlike a regular RRSP, withdrawals can only be made from a LIRA in very limited circumstances. At retirement — which can generally occur as early as 55 or as late as 71 — the LIRA funds must be transferred to a life annuity or a new life-income fund (New LIF). New LIFs are subject to the same annual minimum withdrawal limits as RRIFs and also to maximum withdrawal limits determined by pension legislation.

The New LIF was introduced in Ontario in 2008 to replace the old life-income fund (Old LIF) and locked-in retirement-income fund (LRIF), which are no longer available. Existing Old LIF and LRIF holders may switch to a New LIF plan or maintain their current plans.

Until December 31, 2009, New LIF owners have a one-time opportunity to withdraw in cash or transfer to an RRSP or RRIF, up to 25 per cent of the total market value of the plan's assets. In 2010 only, owners will also have a one-time opportunity to withdraw or transfer an additional 25 per cent of assets that were transferred to their plan on or before December 31, 2009.

As well, from January 1, 2009 onwards, owners have a one-time opportunity to withdraw or transfer 50 per cent of new assets transferred to their plan. An application to withdraw or transfer new funds must be made within 60 days of their transfer to the New LIF.

In May 2008, the federal Minister of Finance announced that major changes with respect to federally regulated locked-in plans were in effect. Taxpayers who are at least 55 years of age are entitled to transfer locked-in assets to a restricted life-income fund (RLIF). RLIFs allow for the one-time transfer of up to 50 per cent of the plan's holdings into an RRSP or RRIF. This option must be exercised within 60 days of the creation of the plan.



Don't forget that significant taxation implications, a potential change in eligibility for various means-tested federal benefits, as well as the possible loss of creditor protection, might result from withdrawing funds out of various locked-in accounts.

Individuals who are at least 55 years of age, with up to a combined total of \$23,150 in 2009 in federally regulated locked-in holdings can also wind up their LIF, RLIF, or restricted locked-in savings plan (RLSP) accounts (but not locked-in RRSP), or transfer them to a tax-deferred savings vehicle such as an RRSP or RRIF.

Under federal and Ontario laws, extraordinary withdrawals in circumstances involving financial hardship, reduced life expectancy, or a situation where a taxpayer ceases to be a Canadian resident are also permitted.

#### **TAX-FREE SAVINGS ACCOUNT (TFSA)**

The new Tax-Free Savings Account (TFSA) allows Canadians who are 18 and older to save tax-free.

Unlike an RRSP, investors are not able to deduct contributions to a TFSA for tax purposes; however investment income, including capital gains earned within the TFSA, will not be subject to tax, even when the funds are ultimately withdrawn.

The 2009 contribution limit is \$5,000. After 2009, the annual limit will be indexed to inflation, and rounded to the nearest \$500. Unused TFSA contribution room will carry forward indefinitely to future years. The amount of withdrawals made from a TFSA in the year will be added to the contribution room at the beginning of the following year. The CRA will report individuals' TFSA contribution room for the current tax year on the notice of assessment they receive after filing their previous year's tax return. Excess contributions to a TFSA are subject to a tax of one per cent per month.



Speak with your certified general accountant to determine how TFSAs might fit into a retirement strategy also involving RRSPs or RRIFs, or an education-funding strategy using RESPs.

Generally, the same type of investments permitted in an RRSP can also be held in the TFSA.

As with RRSPs, taxpayers may contribute "in kind" to a TFSA. Such property will be considered to have been disposed of at FMV. Any capital gains will be taxable, but capital losses will not be tax deductible.

TFSA funds are permitted to be withdrawn at any time, in any amount, and for any reason without affecting taxable income or eligibility for federal means-tested benefits or tax credits. Spouses and common-law partners may also loan or give their partners funds to contribute to a TFSA without having the income earned from that contribution subject to attribution rules. TFSA assets can also be transferred to a spouse or common-law partner's TFSA upon death and, under certain conditions and limitations, this transfer might not affect the spouse or common-law partner's own TFSA contribution room.

Taxpayers who subsequently become non-residents of Canada can maintain their TFSA account, and will not be taxed on subsequent earnings or withdrawals. However, they may not make any further contributions, nor accumulate additional contribution room as long as they remain non-residents.

A TFSA may be carried by the holder indefinitely; there is no time limit to close this account.



TFSA's might be an effective means for couples with disparate income levels to split income, with the higher income spouse providing funds to the partner to contribute to his/her own TFSA.



Be careful that you only hold qualified investments in your TFSA. When non-qualified investments are acquired by a TFSA, the *Income Tax Act* imposes a penalty tax of 50 per cent of the FMV value of the non-qualified investments.

## Part Three: Tax Credits and Related Items

### Federal and Ontario Provincial Non-Refundable Tax Credits

Federal tax credits reduce the amount of basic federal tax payable. In addition, each of Canada's provinces and territories has its own independent tax structure, with rates that apply to these credits and help further reduce the overall tax payable.

The federal credit is determined by multiplying a gross dollar amount by the lowest federal tax rate, currently 15 per cent for 2009. The gross amount of most tax credits, such as the basic personal, age and spousal credits, are indexed annually by a formula that takes into account increases in the consumer-price index (CPI).

Ontario also indexes selected non-refundable tax credits based on its own CPI formula. For a summary of federal and Ontario tax credits, see Appendix I, page 123.

Unused non-refundable federal- and provincial-tax credits cannot be transferred to another taxation year.

#### BASIC PERSONAL CREDIT

Federally, taxpayers are entitled to claim the basic personal credit of 15 per cent on \$10,320, for a credit of \$1,548 (up from \$9,600, for a credit of \$1,440 in 2008).

Provincially, Ontario taxpayers are entitled to claim a basic personal credit of 6.05 per cent on \$8,881, or \$537 (up from \$8,681, or \$525 in 2008).

#### CANADA EMPLOYMENT CREDIT

The Canada Employment Credit is available on 15 per cent of \$1,044, for a credit of \$157 in 2009 (up from \$1,019, or \$153 in 2008).

#### SPOUSAL CREDIT

Individuals supporting a spouse or common-law partner whose net income is less than \$10,320 (up from \$9,600 in 2008) may claim the federal spousal credit. They may claim the maximum credit of 15 per cent on \$10,320, for a credit of \$1,548, if the spouse or common-law partner's income is nil. That credit is reduced if the spouse or common-law partner's net income is more than nil but less than \$10,320, where the credit is eliminated.

Provincially, Ontario taxpayers supporting a spouse or common-law partner whose net income is less than \$8,295 (compared to \$8,108 in 2008) may



If you lived separate and apart from your spouse for all or any part of a year for reasons other than a marriage break-down, you may still be entitled to claim the spousal credit.

claim the spousal credit. They may claim the maximum credit of 6.05 per cent on \$7,541, or \$456, if the spouse or common-law partner's income was \$754 or less (compared to \$737 in 2008). That credit is reduced if the spouse or common-law partner's net income is more than \$754 but less than \$8,295, where the credit is eliminated.

Special rules may apply to individuals' claims if their status changed during the year.



You may claim an amount for your dependent spouse or common-law partner even if he or she did not live in Canada during the year. To do so, you must supply proof of that support, such as a cancelled cheque or money order receipt, etc., in the name of the eligible payee. The documents submitted should also contain detailed information, such as the recipient's name, address and date of transfer.

#### **AMOUNT FOR AN ELIGIBLE DEPENDANT CREDIT**

Taxpayers may claim the amount for an eligible dependant credit if at any time during the year they were single, divorced or separated and supported a qualified relative, including a child, who lived with and was dependent on them. The eligible dependant credit is calculated in the same manner as the spousal credit.



If you were entitled to the amount for an eligible dependant claim at the beginning of the year, you maintain that entitlement for the full year. Even if you marry during the year, that entitlement remains, provided you don't claim the spousal credit.

The following restrictions apply:

- The dependant, other than a child, must be a Canadian resident.
- A dependent child must be either under 18 at any time in the year, or any age if dependent by reason of mental or physical infirmity.
- The claim may only be made in respect of one eligible dependant at a time.
- Where two or more individuals are otherwise entitled to a credit in respect of the same person, only one is able to claim the credit.
- The credit cannot be claimed for an individual on behalf of whom the taxpayer is required to pay a support amount.

To qualify, the dependant need not have lived with or been supported by the taxpayer throughout the entire year.



If more than one person is eligible to claim this equivalent-to-spouse credit on behalf of another individual, such as a child, it is important that a formal agreement be reached as to which taxpayer will do so because otherwise nobody will be able to claim it.

## AGE CREDIT

Individuals 65 or older in the year are entitled to a federal credit of 15 per cent on \$6,408, or \$961. This gross amount is reduced by 15 per cent of net income over \$32,312, thereby eliminating the entire credit when income of \$75,032 is attained.

Provincially, Ontario taxpayers 65 or older are entitled to a credit of 6.05 per cent on \$4,336, or \$262. This gross amount is reduced by 15 per cent of net income over \$32,280, thereby eliminating the entire credit when income of \$61,187 is attained.



You may be able to claim the unused portion of your spouse or common-law partner's age credit.

## DISABILITY TAX CREDIT (DTC)

A 15 per cent federal disability tax credit (DTC) on \$7,196 or \$1,079 is available to any individual whom a Canadian medical doctor certifies on Form T2201 is suffering from severe and prolonged mental or physical impairment. The Ontario provincial portion of this credit is 6.05 per cent on \$7,175 or \$434.

Once Form T2201 is on file with the CRA, it doesn't need to be resubmitted annually.

Other professionals may also certify specific disabilities. For instance, an optometrist can certify sight impairment or an audiologist can certify a hearing disability. Occupational therapists and psychologists can also certify a taxpayer's physical or mental disability, respectively.

This impairment is considered severe if the disability markedly restricts the individual in physical daily-living activities, such as walking, speaking, feeding, dressing, or mental activities, such as perceiving, thinking and remembering, among others; and prolonged if the disability lasts, or is expected to last, for a continuous period of at least 12 months. The courts have also often taken a compassionate, common-sense approach toward defining whether a person is restricted in the activities of daily living and, in so doing, have considered the overall impact that a disability has had on that person's life.

In 2002, for instance, the Tax Court of Canada ruled that although an individual suffering from chronic fatigue syndrome was not markedly restricted from performing any one of the CRA's specified basic activities of daily living, she nevertheless qualified for the credit because of the cumulative restrictive effects that illness had on her ability to function.



If you qualify for Canada pension-plan (CPP) disability benefits, remember to check to see whether you also qualify for the DTC.

The disability tax credit (DTC) also extends to individuals who have been certified by a medical doctor to require therapy at least three times a week, averaging a total of at least 14 hours, to deal with a marked restriction in their ability to perform a basic activity of daily living.



You may be able to claim an eligible dependant credit for a person by reason of an infirmity even if that person does not qualify for the DTC. The CRA considers a person to be infirm if that individual is dependent on the services of another for a considerable period of time.

#### **DISABILITY TAX CREDIT SUPPLEMENT**

A federal DTC supplement of up to \$630 (15 per cent of \$4,198) is also available for caregivers of children under 18 who have severe disabilities that require full-time home care. Annual child-care and attendant-care expenses in excess of \$2,459 claimed on behalf of that child will reduce this supplement, eliminating it completely once such expenses reach \$6,657.

For Ontario taxpayers, the maximum DTC supplement is \$253 (6.05 per cent of \$4,185). Annual child-care and attendant-care expenses in excess of \$2,451 claimed on behalf of that child will reduce this supplement, eliminating it completely once such expenses reach \$6,636.

#### **CHILD-DISABILITY BENEFIT**

A federal child-disability benefit (CDB) was introduced in the 2003 federal budget for the benefit of parents whose children qualify for the DTC. For additional details about the CDB, see page 105 in the chapter on additional tax considerations.

#### **CHILD TAX CREDIT**

The federal budget of 2007 introduced an annual non-refundable child tax credit, effective January 1, 2007, that pays parents \$2,000 for each child under 18 at the end of a taxation year. In 2009, this indexed federal credit is 15 per cent of \$2,089, or \$313 per child.

When a child resides with both parents throughout the year, either parent may claim this credit, with any unused portion being transferable between spouses or common-law partners. In instances where a child does not reside with both parents, the parent eligible to make that claim will be the one who is also eligible to claim the wholly dependent-person credit in respect of that child.

This credit applies for the full year, no matter which date a birth, adoption or death may occur during that year.

#### **INFIRM DEPENDANT CREDIT**

Where a relative 18 or older is dependent on the taxpayer by reason of mental or physical infirmity, the taxpayer may claim, as the federal portion of this credit, 15 per cent of \$4,198 less the dependant's income in excess of \$5,956, for a maximum credit of \$630. The maximum available credit is eliminated entirely when the dependant's income reaches \$10,154.

The Ontario portion of this credit is 6.05 per cent of up to \$4,186, less the dependant's income in excess of \$5,950, for a maximum credit of \$253. The maximum available credit is eliminated entirely when the dependant's income reaches \$10,136.

To qualify, individuals must have supported the relative at some time during the year. The relative must be either a child or grandchild of the taxpayer or spouse or common-law partner or, if residing in Canada at any time throughout the year, could also be the taxpayer's or spouse's or common-law partner's parent, grandparent, brother, sister, uncle, aunt, niece or nephew.

#### **CAREGIVER TAX CREDIT**

The caregiver tax credit reduces federal tax by up to \$630 (15 per cent of \$4,198) for individuals 18 and over who are responsible for the in-home care of an infirm, dependant relative or parent/grandparent (including in-laws) who are at least 65. The maximum available credit is reduced by the dependant's net income in excess of \$14,336 and eliminated entirely when the income reaches \$18,534.

The Ontario provincial tax credit involves a maximum of \$253 (6.05 per cent of \$4,186), which is reduced by 6.05 per cent of net income in excess of \$14,321 and eliminated entirely when the income reaches \$18,507).

Eligibility for this credit (as well as for the DTC and DTC supplement, and infirm-dependant credits) includes spouses or common-law partners of individuals who are dependent because of mental or physical infirmity; support may also be provided by certain caregivers living apart from their dependent relatives.

This credit is not available on behalf of individuals for whom the equivalent-to-spouse credit or infirm-dependant credit has already been claimed.



If you take time off work to care for a gravely ill or dying family member, including a parent, spouse or child, you are eligible to be provided with employment-insurance (EI) benefits for up to six weeks.

#### **ADOPTION TAX CREDIT**

The 2005 federal budget introduced an adoption tax credit to cover up to \$10,000 worth of eligible adoption expenses for a child of the taxpayer, including non-reimbursed items such as fees paid to an adoption agency that is licensed in a province or territory; court costs; legal and administrative expenses; and reasonable travel and living expenses required to secure an adoption, among others.

With indexing, the federal amount is \$10,909 in 2009, at a rate of 15 per cent, for a credit of \$1,636.

The Ontario government also has a corresponding provincial adoption tax credit. With indexing, the amount is \$10,835 in 2009, at a rate of 6.05 per cent, for a provincial credit of \$656.



## MEDICAL EXPENSE CREDIT

Individuals may claim a credit for any non-reimbursed medical expenses. The federal portion of this credit for the 2009 taxation year consists of 15 per cent of expenses in excess of the lesser of: \$2,011; or three per cent of the individuals' net income for the year. Such expenses may be incurred on the taxpayers' own behalf or that of their spouse or common-law partner, or their child under 18.



A taxpayer and spouse can apportion the medical expenses claimed on behalf of each other to best minimize their overall tax liability. In some cases, it might be advantageous for the lower-income spouse to claim allowable medical expenses.

Medical and disability-related expenses may also be claimed by caregivers who are looking after an adult child 18 or over or somebody other than a spouse or common-law partner or dependant child; the amount they can claim is the lesser of: \$10,000; or the amount by which expenses paid exceed \$2,011; or three per cent of net income.

The Ontario portion of the medical-expense credit consists of 6.05 per cent of expenses in excess of the lesser of: \$2,010; or three per cent of the individual's net income for the year.

Generally, medication must be prescribed by a registered physician or dentist (nurse practitioners are also allowed to prescribe certain medication), and dispensed and recorded by a qualified pharmacist, if such expenses are eligible to be claimed for the medical-expense tax credit. Payments may also be issued indirectly to a medical practitioner, i.e., through an institution that provides medical services on their behalf.

Receipts must support expenses claimed. Normally, these expenses can be claimed for any 12-month period ending in the year but should the return be prepared for a deceased taxpayer, that period is expanded to encompass claims for any 24-month period, including the individual's date of death.



A parent or other guardian who does not live with, and/or have legal custody of, a child might still be able to claim certain medical expenses on the child's behalf. Even if the child is not wholly dependent on the taxpayer, if the taxpayer is providing for essential needs, factors such as support payments and expenditures for security and education will also be taken into account when the CRA decides whether the expenses qualify to be deducted.

## ELIGIBLE MEDICAL EXPENSES

The list of expenses eligible for the medical-expense tax credit includes, but is certainly not limited, to:

- Full-time attendant care for individuals with severe and prolonged mental or physical impairments, including all expenses with no maximum.
- Supervision of an individual eligible for the DTC who is residing in a Canadian group home devoted to the care of people with a severe and prolonged impairment.



A pharmacist is also considered to be a medical practitioner. Therefore, if your pharmacist provides such services as running a disease management clinic or other activities for which a fee is payable, this may qualify as a deductible medical expense.



In some Canadian jurisdictions, practitioners in so-called “alternative treatment” fields, such as naturopathy, acupuncture and massage therapy, might qualify as authorized medical practitioners. Check to determine whether expenditures for the services you are receiving in Ontario are covered for tax purposes.

- Part-time attendant care — up to \$10,000 federally (indexed at \$12,280 for the Ontario portion of this credit), increasing to \$20,000 (indexed at \$24,561 in Ontario) if the individual died during the year.
- A block, or annual fee, paid to a medical centre or physician to cover uninsured medical services.
- 50 per cent of the cost of an air conditioner needed for a severe chronic ailment, to a maximum of \$1,000.
- 20 per cent of the cost of a van that is, or will be, adapted for the transportation of an individual using a wheelchair, to a maximum of \$5,000 (indexed at \$6,142 in Ontario).
- Expenses incurred for moving to accessible housing, to a maximum of \$2,000 (indexed at \$2,459 in Ontario).
- A device such as a wheelchair to assist an individual with a mobility problem.
- Sign-language interpreter fees.



You may include premiums paid for private health insurance in your medical-expense claim.



You may deduct reasonable travel expenses if required to seek specialized medical treatment outside Canada. To qualify, you must have an existing medical condition or illness and seek the care of health professionals.

- Voice-recognition software necessary to assist a person with a disability.
- Various medical devices, along with accessories, required to assist with impaired seeing or hearing.
- Tutoring services from a non-related person for individuals with a certified learning disability or mental impairment.
- Certain costs related to attending an educational facility with specialized personnel, equipment or facilities to address a physical or mental handicap.



The cost of full-time care in a nursing home might also include care that is provided by professionals other than those on staff.

- A portion of reasonable expenses relating to certain construction or renovation costs incurred to assist individuals with a severe disability gain access to, or be mobile or functional within, their principal residence.
- Reasonable expenses for driveway alterations made to enable a mobility-impaired individual to access a bus.
- Reasonable travel expenses incurred to obtain medical services not available in the vicinity of the patient's home, to the extent these have not been reimbursed by a provincial health plan, or other source. See also travel expense claims, page 59.

The list of expenses eligible for the medical-expense credit is lengthy. For a review of eligible medical expenses, and certification that might be required to be eligible to make such claims, refer to CRA publication IT519R2—Medical Expense and Disability Tax Credits and Attendant Care Expense Deduction, or other related documents.



A stroller designed specifically for a child with special mobility needs is considered equivalent to a wheelchair and, therefore, deductible as an eligible medical-expense item for tax purposes.



Future parents who are in the process of adopting a child might still be able to claim eligible medical expenses for that child prior to the actual adoption date — provided they become totally responsible for the child's care and supervision before the arrival and ultimate adoption takes place later that year. This situation could be especially relevant in a case involving an international adoption.

#### OTHER MEDICAL CREDITS

A refundable tax credit of up to \$500 is available to individuals with high medical expenses and low annual income. There are also broad rules governing income earned by a trust established for the benefit of a person with a disability, as well as for duty-free goods for an individual with a disability.

Some taxpayers may also qualify for a federal refundable medical-expense supplement of up to \$1,067 (up from \$1,041 in 2008). The actual supplement amount is the lesser of: \$1,067; or 25 per cent of attendant-care expenses claimed under the disability-supports deduction (see below), plus 25 per cent of allowable expenses claimed under the medical-expense tax credit.

To qualify for this supplement, taxpayers must be 18 or older and have total business and employment income of at least \$3,116 for the year. This supplement is reduced by five per cent of family net income in excess of \$23,633.

## DISABILITY SUPPORTS DEDUCTION

The 2004 federal budget introduced a new disability supports deduction. It includes attendant-care expenses, plus other disability support expenses that have not otherwise been reimbursed and have been incurred to enable eligible individuals to work, or attend secondary school or a designated educational institution. Under this provision the maximum deduction is the lesser of: eligible non-reimbursed expenses; and earned income for the year. If attending school, it is the lesser of: eligible non-reimbursed expenses; and the least of three amounts — the amount by which total income exceeds earned income; \$15,000; and \$375 times the number of weeks they are in attendance at that school.

Expenses claimed under the disability supports deduction, which include various devices and services to deal with vision, hearing, speaking and mobility restrictions, among others, cannot also be claimed under the medical-expense tax credit.

## OTHER POINTS RELATED TO DISABILITY AND MEDICAL EXPENSES

Use of the DTC on the tax return of a deceased individual may still be applicable in the year of death if a medical doctor certified before death that the individual had a "severe and prolonged mental or physical impairment," which was reasonably expected to last for at least 12 months.

For 2002 and subsequent taxation years, seniors living in a retirement home, who also qualify for the DTC, may claim attendant-care expenses of up to \$10,000 per year (their estate may claim \$20,000 for the year of death).

The attendant-care component of fees paid to a retirement home includes the salary and wages paid to employees with respect to the following services provided to a senior, including:

- health care
- meal preparation
- housekeeping in the resident's personal living space
- laundry for the resident's personal items
- a transportation driver
- security, where applicable

The retirement home must provide the taxpayer or caregivers with a receipt showing the applicable amounts paid for attendant care. Eligible seniors who wish to request an adjustment for the 2002 taxation year may do so either through a letter to the CRA, which includes the senior's social insurance number (SIN), address, daytime phone number, and supporting documentation by completing form T1-ADJ — T1 Adjustment Request; or online via [www.cra-arc.gc.ca/myaccount](http://www.cra-arc.gc.ca/myaccount).

The attendant-care provision may also apply to taxation years prior to 2002 if a notice-of-objection ruling is still outstanding or can still be filed.

Generally, expenses paid to a nursing home qualify as tax-deductible medical expenses, while those paid to a personal-care institution do not, because the care provided to patients in a nursing home tends to be more extensive.

However, there may be exceptions to that rule. All or part of the remuneration paid to a personal-care facility might, for instance, be deductible in situations where an individual with a severe and prolonged impairment requires specialized equipment, facilities or personnel.

Caregivers are also able to deduct reasonable expenses associated with the cost of training required to care for dependent relatives with mental or physical infirmities.

Patients who are incapable of travelling without the assistance of an attendant may be able to deduct a full range of reasonable travel expenses on behalf of the person required to assist them travel to a facility at least 80 kilometres away from home to seek proper medical treatment.

Certain expenses incurred for the purpose of providing care to a person with a disability are exempt from the goods and services tax (GST) and harmonized sales tax (HST). These include a government-funded homemaker service provided to individuals in their place of residence, various medical devices and some recreational programs. For a complete list, consult CRA's guide RC4064, Information Concerning People with Disabilities.

#### **TUITION FEE AND EDUCATION CREDITS**

Post-secondary students who are not otherwise reimbursed for the cost of their courses, or who have received financial assistance such as a grant, benefit, or other allowance, are generally entitled to a credit for the cost of the courses and certain related school fees that they or their families must pay.

Full-time students must generally be taking courses of at least three consecutive weeks involving at least 10 hours of study per week for the duration of the course at a designated educational institution. Typically, this is at a university, college, or other school in Canada that offers courses at a post-secondary level, or internationally at a university or in a university-related course that leads to a degree.

These students may claim a federal tuition credit of 15 per cent of eligible tuition fees, plus an education credit of 15 per cent of \$400 per month, or \$60 in 2009, with the education credit allowable only if they are attending a designated educational institution as defined by the federal government.

In Ontario, this education credit is indexed; students may claim a monthly provincial credit of up to 6.05 per cent of \$478, or \$29 in 2009.

To qualify for these credits, students need not attend full-time, but only be enrolled as full-time students. Students with disabilities may also be enrolled part-time to qualify for a full-time credit.

Students who are engaged in part-time studies — defined as a minimum of three consecutive weeks involving at least 12 hours of course work per month at a designated educational institution in Canada only (although exceptions might apply for part-time students who live in Canada and commute to a listed school in the U.S.) may also claim the tuition fee credit of 15 per cent of eligible fees. They may also deduct \$120 a month toward eligibility for the 15 per cent federal education credit, which in 2009 is \$18; and 6.05 per cent of 92

\$143 per month (indexed) toward eligibility for the Ontario education credit, worth \$9 in 2009. The same transfer and carry-forward provisions applicable to full-time students also apply to part-time students.

#### ADDITIONAL POINTS RELATING TO TUITION FEE AND EDUCATION TAX CREDITS

People with disabilities who are enrolled in human resources and skills development Canada (HRSDC) or equivalent provincial/territorial-approved training programs can deduct those related expenses. Under this adult basic-education (ABE) deduction, such courses may, for instance, allow taxpayers to finish secondary school, improve their literacy skills or upgrade existing educational credentials, in order to improve their employment chances. (Note: the ABE deduction is retroactive and might apply to financial assistance received during taxation years after 1996 and before this announcement in 2001).



Mandatory computer-service fees eligible for the tuition credit may also include use of a laptop computer and applicable software.

The 2004 federal budget expanded provisions of the education credit to include students who are pursuing career-related post-secondary education at their own expense. Note, however, that courses taken outside a university, which are designed to improve personal skills, would not likely qualify for the tuition credit. The *Income Tax Act* states that to qualify for this credit, such courses must be designed to improve occupational skills and be held at a certified place of instruction.

Students who are enrolled in two designated educational institutions in order to achieve a combined course load equivalent to that of a full-time student may be entitled to the full-time education credit provided at least one of the designated institutions issues the appropriate T2202 or T2202A form if a Canadian institution, or TL11A, TL11C, or TL11D form (all of these forms are variations of the Tuition, Education and Textbook Amounts Certificate) if outside the country, to indicate that the courses taken at both schools qualify them for that status.



If you reside in Canada near the U.S. border and are registered in, and commute to, a designated educational institution in the U.S., you might be able to claim and/or transfer a tuition credit for a course of any duration.

There are some mandatory ancillary charges, such as fees for computer services, labs, health and athletics that are also eligible for the tuition credit. Tuition fees at a qualified Canadian educational facility must exceed \$100 per institution (this requirement is waived for foreign universities provided the full-time student is attending a course of at least 13 weeks duration leading to a degree) and be claimed on a calendar-year basis. Courses must be taken at a post-secondary level or be for occupational skills provided by a qualified educational institution for students 16 or older.

The 2006 federal budget introduced a textbook credit for students eligible for the full-time and part-time education credits. In 2009, the federal textbook



Tuition fees paid to obtain up to 110 hours of instruction for a commercial pilot's license or to become a professional flying instructor also qualify as eligible tuition fees provided they are taken at a certified flying school or club.



All or a portion of the fees charged in an internship program may be eligible tuition fees for purposes of the tuition tax credit, provided they relate to the process of academic instruction and do not constitute a placement fee.

credit is 15 per cent of \$65, or \$10 per month for full-time students, and 15 per cent of \$20, or \$3 for part-time students.

That budget also fully exempted from taxation all scholarship, fellowship or bursary income with respect to post-secondary education or occupational training, provided it applies to enrolment in a program that entitles the student to claim the education credit. Previously, only the first \$3,000 of such income was exempt.

Those with access to the education credit include taxpayers who are receiving financial assistance for their post-secondary education through the EI or a similar provincial program.

Furthermore, students need not necessarily be in physical attendance at a qualified institution in Canada to claim either the tuition or education tax credits. Recent court rulings have interpreted the *Income Tax Act* differently with respect to whether students must physically attend a designated institution outside Canada in order to claim the tuition credit. However, there now appears to be a general acceptance that they do not. Therefore, online course participation through, for example, the internet website of a recognized post-secondary institution, either in Canada or internationally, may also qualify the taxpayer for both tax credits.



Fees for your child's extracurricular classes may also be eligible for the tuition credit if your child is at least 16; the classes are taken through a certified educational institution; and the program provides occupational skills. Dance or skating lessons are examples of classes that might qualify. If your child is under 16, certain courses may still qualify provided they are post-secondary equivalency-level courses taken through a certified educational institution. A music academy might be a good example.



The CRA has ruled that students may deduct tuition fees paid to an accredited post-secondary institution for audit/hearer courses in which they attend lectures, but do not write examinations or receive credit.

## TRANSFER OF CREDITS

Unused tuition, education and textbook credits may be carried forward indefinitely to offset students' income taxes in future years. Alternatively, students may transfer unused federal credits of up to \$5,000 (an indexed \$6,141 for the Ontario portion of this credit), reduced by their income in excess of personal credits, to a supporting person such as a parent or grandparent, but the transferred credits must be claimed in the year incurred.

Students who are attending an accredited institution outside Canada — generally in a university-level course of at least 13 consecutive weeks duration leading to a degree — are eligible to transfer their unused credits provided they owe Canadian income tax. All, or at least a substantial portion, of their income must be considered taxable income earned in Canada during the year the tuition fees were incurred.

Consult your certified general accountant if you attend a higher education facility outside Canada.

## STUDENT LOAN INTEREST TAX CREDIT

A 15 per cent federal tax credit and a 6.05 per cent Ontario provincial tax credit are available on the repayment of interest on federally or provincially approved student loans.

To be eligible, however, students must consolidate their loans with an authorized lender after graduating and assume responsibility for paying interest by the first day of the seventh month following completion of their studies.

Students have the option of applying that non-transferable credit to either the current year or carrying it forward to any one of, or spread over, the next five taxation years.

## PENSION INCOME CREDIT

The federal government allows a 15 per cent federal tax credit on up to \$2,000 of eligible pension income (non-indexed). In 2009, this amounts to a maximum of \$300. Provincially, a 6.05 per cent Ontario tax credit on up to \$1,228 of eligible pension income (indexed from a base of \$1,000), is available for the 2009 taxation year, which amounts to a maximum credit of \$74. Taxpayers may also transfer to their return any unused pension-income credit belonging to spouses or common-law partners.

Eligible pension income includes, for example:

- Life annuity receipts from a superannuation or pension fund, regardless of the recipient's age.
- Annuity receipts under an RRSP or DPSP, amounts received from an RRIF and certain other non-government annuities, provided the recipient is at least 65 by the end of the year or the amounts are received as a consequence of a spouse or common-law partner's death.



If you are 65, consider creating pension income by converting part of your RRSP to a life annuity or an RRIF if your financial circumstances warrant such a move.



- Foreign-source pensions, such as United States social security and United Kingdom pension income, to the extent such income cannot be excluded as a result of an existing tax convention between Canada and a foreign country.

Payments to an LRIF, or similar locked-in tax instrument, which are treated like RRSPs and RRIIFs for tax purposes, may also qualify for a pension income deduction.

Ineligible pension income includes, for instance:

- Canada Pension Plan (CPP), and Quebec Pension Plan (QPP)
- Old-Age Security (OAS) and the Guaranteed Income Supplement (GIS)
- lump-sum payments from a pension or superannuation plan
- death benefits
- retiring allowances
- amounts received under a salary-deferral arrangement
- payments received out of a retirement-compensation arrangement
- any other qualifying income that has been rolled over to an RPP or RRSP

Since 2007, the federal government allows taxpayers to split qualified pension income with a spouse or common-law partner, by allocating to them up to one-half of such qualified income. When pension income has been allocated in such fashion, both partners must make a joint election on Form T1032 — Joint Election to Split Pension Income.

Amounts transferred to spouses under 65 might not be eligible for the pension deduction.



Contributing to a spousal RRSP also creates potential pension income for your spouse or common-law partner.

#### **CHARITABLE-DONATION CREDIT**

The federal charitable-donation tax credit is calculated as 15 per cent on the first \$200 of eligible donations, plus 29 per cent of any amount in excess of \$200. The corresponding provincial tax credit for Ontario residents is 6.05 per cent of the first \$200 and 11.16 per cent of any amount over \$200.

A credit can be claimed for donations made in the current and/or the preceding five years (if not already claimed), based on an annual limit — generally 75 per cent of net income. That increases to 100 per cent in the taxpayer's year of death and for the preceding year.



Make sure you request a tax receipt from the organization to which you are making a tax-deductible donation. The receipt should include the charitable organization's registration number with the CRA, among other information. You don't need to send receipts if you are completing an electronic return, but you will need to maintain them for your records in case they are requested.



You may also claim donations made by your spouse or common-law partner. To maximize the charitable-donation credit, consider combining both your donations if they total more than \$200. If not, it may be best to defer claiming these deductions, subject to the five-year carry-forward limitation, to get above the \$200 threshold.

Donations of appreciated capital property giving rise to capital gains also benefit from higher limits of up to 100 per cent of net income. Note, however, that the federal government introduced a rule, effective December 5, 2003, which limits the value of a gift of property for charitable-donation purposes to the donor's cost of the property, where such property has been donated within three years of acquisition. Check with your certified general accountant for more details.

Where a donation other than cash has been made to a registered charity, the charity must issue a receipt for the FMV of the property at the time the gift was made.

A taxpayer may claim a credit for charitable donations made to an organization outside Canada, provided a donation has also been made to that same organization by the federal government, or representatives of the government, during either the current or preceding years.

The income inclusion rate on capital gains arising from donations of publicly traded securities made to recipients other than private foundations was previously 25 per cent. The 2006 federal budget entirely eliminated the income-inclusion rate for such donations, effective May 2, 2006. It also eliminated any tax inclusion for qualifying charitable donations of listed publicly traded securities acquired with employee stock options as well as, in certain instances, where taxpayers donate ecologically sensitive land, also effective May 2, 2006.

Special rules may also apply for donations of certain securities to private charitable foundations on or after March 19, 2007.

Consult your certified general accountant if you have questions about the proper tax treatment of charitable donations you make, particularly if these involve donations of property.



Additional savings may result from reduced provincial surtaxes when the higher-income spouse or common-law partner makes the charitable-deduction claim.

#### **CREDIT FOR PUBLIC TRANSIT PASS**

A federal non-refundable tax credit is available for taxpayers who purchase eligible weekly (involving at least four consecutive weekly passes per month), monthly, or longer transit passes. In some instances, even shorter duration passes or electronic payment cards might be acceptable if they accumulate to allow for equivalent travel over a month or longer. Public transit could include transit of various modes, such as local bus, streetcar, subway, commuter train or bus, or local ferry. This credit applies at the rate of 15 per cent for 2009.

This credit is transferable to a spouse or common-law partner, as well as to parents of dependent children 18 or younger.



Save applicable public-transit passes and purchase receipts to verify the expenses you are claiming for this tax credit.



If, during the course of your commute, you need to take your automobile on a ferry for which you pay monthly or longer fees, you may claim a public-transit credit for the ferry costs relating directly to the transport of you and/or other family members, but not those for your automobile.

#### **CREDIT FOR ENROLMENT IN CHILDREN'S FITNESS PROGRAMS**

To encourage greater involvement in physical-fitness programs, the 2006 federal budget introduced a fitness tax credit of up to \$500 against eligible fees paid for children under 16 who are enrolled in certain sports and physical-fitness program activities.

This credit, which took effect January 1, 2007, requires that "substantially all of the activities (undertaken) must include a significant amount of physical activity that contributes to cardio-respiratory endurance plus one or more of: muscular strength, muscular endurance, flexibility, or balance."

The CRA lists several supervised children's programs as examples of recreational activities eligible for this tax credit, including hockey, skating, soccer, karate, football, basketball, folk dancing, swimming, hiking, horseback riding and sailing.

The programs must be ongoing. For example, the prescribed programs of physical activity include: a weekly program involving a minimum of eight consecutive weeks' duration "in which all or substantially all of the activities include a significant amount of physical activity." They also include programs of at least five consecutive days, provided more than 50 per cent of that time is devoted to physical activity, such as a summer or day camp program. Similarly, membership in a club, association or other organization for eight consecutive weeks or longer may also qualify provided more than 50 per cent of the activities, or the time scheduled for such activities, is devoted to programs deemed eligible for this credit.

A pro-rated credit is available to cover membership and registration fees for programs in which 50 per cent or fewer of the activities are eligible.



If you pay family membership fees in a program that involves eligible fitness activities, mixed with other activities, you might be able to apply a prorated portion to the children's fitness credit. Make sure you get a receipt from the organization clearly stating the amount that is eligible for a credit.

For children who are eligible for the DTC, the fitness tax credit applies if they are under 18; plus there is a separate \$500 credit, for a total of \$1,000, available to them provided at least \$100 is spent on registration fees for an eligible program.

The taxable benefit for a \$500 credit in 2009, at 15 per cent, is \$75. For a \$1,000 credit, this benefit is \$150.

#### **FIRST-TIME HOME BUYERS' TAX CREDIT (HBTC)**

The 2009 federal budget introduced a new non-refundable First-Time Home Buyers' Tax Credit (HBTC) for first-time home buyers who purchase qualifying homes on or after January 28, 2009. They are eligible for a credit of up to 15 per cent on \$5,000, or \$750.

To participate, prospective homebuyers or their spouse/common-law partner cannot have owned and lived in another home in the calendar year they make the purchase, or the four years previous to that. If they purchase a home in 2009, for example, they must not have owned and lived in a home after 2004. The time and first-home requirements are waived for acquisitions of a home by or on behalf of a taxpayer with a disability who is eligible for the DTC, if the home is purchased for the purpose of providing a more accessible environment, or is one better suited for the personal needs.

Any unused portion of an individual's first-time HBTC may be claimed by the spouse or common-law partner, but the total of all claims cannot exceed the maximum credit of \$750.

#### **TEMPORARY HOME-RENOVATION TAX CREDIT FOR 2009**

The 2009 federal budget proposed a temporary home-renovation tax credit (HRTC) of 15 per cent on eligible expenditures in excess of \$1,000, and up to \$10,000 for work performed or goods acquired in relation to certain home (including cottage) renovations of an enduring nature incurred between January 28, 2009 and January 31, 2010, inclusive.

The Department of Finance has, however, specified that the expenditure for work performed or goods acquired during this period is not eligible for this credit if it "is made pursuant to an agreement entered into before January 28, 2009."

This credit, worth up to a maximum of \$1,350 (\$9,000 X 15 per cent), will only apply to the 2009 taxation year. Expenditures incurred in January 2010 must be claimed on the taxpayer's 2009 tax return.

The CRA has listed various examples of eligible and ineligible expenses for purposes of the HRTC on their website, in English at [www.cra-arc.gc.ca/tx/ndvdlsgmnts/hmwnr/hrtc/lgbl-xpns-eng.html](http://www.cra-arc.gc.ca/tx/ndvdlsgmnts/hmwnr/hrtc/lgbl-xpns-eng.html) and in French at [www.cra-arc.gc.ca/tx/ndvdlsgmnts/hmwnr/hrtc/lgbl-xpns-fra.html](http://www.cra-arc.gc.ca/tx/ndvdlsgmnts/hmwnr/hrtc/lgbl-xpns-fra.html).



Eligible expenses for both a home and cottage property may qualify for a HRTC in 2009, within the total maximum spending limit of \$10,000, provided both are owned and used by members of your family. This limit applies per family, including spouses/common-law partners and children under 18.

Eligible expenditures will not reduce any other tax credits or grants the taxpayer might be entitled to, such as the medical expense tax credit.

Taxpayers are asked to keep their receipts and other supporting documentation related to the HRTC claim in case the CRA requires them for verification purposes.

#### **CANADA PENSION PLAN (CPP) AND EMPLOYMENT-INSURANCE (EI) PREMIUMS CREDIT**

Individuals who are paying Canada pension plan (CPP) and/or employment-insurance (EI) premiums may claim a 15 per cent federal tax credit and 6.05 per cent provincial tax credit on the amount paid.

Self-employed individuals who are paying both the employee and employer portion of CPP premiums may claim a non-refundable credit for one-half the full 9.9 per cent contribution amount — in effect, the employee portion of the CPP (which amounts to 4.95 per cent) — and a deduction from income for the employer's half (also 4.95 per cent). However, self-employed taxpayers do not pay EI premiums related to self-employment income.

For 2009, the maximum federal tax credit available for CPP premiums paid is 15 per cent of \$2,119, or \$318. For EI premiums paid it is 15 per cent of \$732, or \$110.

For Ontario, the corresponding rates are 6.05 per cent of CPP premiums of \$2,119, or \$128; and 6.05 per cent of EI premiums of \$732, or \$44.

### **Other Tax Credits**

#### **GOODS AND SERVICES TAX (GST) CREDIT**

Beginning in July 2009, eligible individuals received a goods and services tax (GST) credit that increased to \$248 per adult and \$130 per qualified dependent child under 19, subject to an income test based on family net income. A supplementary goods and services tax credit (GSTC) is also available for individuals with no spouse or common-law partner.

For taxpayers without dependants, this supplement is phased in at two per cent of net income in excess of \$8,047, up to a maximum of \$130 (with the total credit being reduced by five per cent of family net income in excess of \$32,312). Single parents automatically receive the full \$130 GST supplement, without any phase-in dependent on income.

The GST credit and supplement are fully indexed for inflation on an annual basis every July 1.

Only one spouse or common-law partner can claim the GST credit on behalf of both spouses or common-law partners and any dependants.

GST credits are paid separately, on a quarterly basis, in July, October, January and April. When the total credit is less than \$100, only one annual payment is made, during July.

The GST credit responds to changes in family circumstances, such as the birth of a child, alteration in marital status, or the taxpayer's becoming 19, in the quarter following such an event. In order for the CRA to respond expeditiously to the taxpayer's personal changes, however, the relevant information must be relayed to the agency on time.



You must file an income-tax return in order to be eligible to receive the GST credit. Claim \$248 (rather than \$130) for a dependant claimed as an "eligible dependant."

#### **POLITICAL CONTRIBUTION TAX CREDIT**

Contributions to a registered federal political party or a candidate in a federal election are eligible for a tax credit against federal income tax payable in the year the contribution was made, provided they are supported by valid receipts.

The federal tax-credit calculation takes into account:

- 75 per cent of the first \$400 contributed; plus
- 50 per cent of the next \$350; and
- 33 1/3 per cent of contributions between \$750 and \$1,275.

At \$1,275 of political contributions, the maximum annual credit of \$650 will have been reached.

Similar credits are also available in Ontario. See Ontario political contribution tax credit, page 118.



To maximize the political-contribution tax credit, consider spreading contributions over several years, if you wish to donate more than the maximum allowable annual amount for tax purposes.

#### **FOREIGN TAX CREDIT (FTC)**

Canadian residents are taxable in Canada on world income from all sources. Income from foreign jurisdictions may also be subject to tax in that jurisdiction.

Foreign tax paid may be claimed as a foreign tax credit against Canadian taxes, subject to limitations. Foreign income that is exempt from tax in a foreign jurisdiction pursuant to, say, a tax treaty might not be included in the foreign-income base for purposes of the tax-credit calculation. Although this income may be exempt in a foreign jurisdiction, it must still be included in the taxpayer's world income for Canadian tax purposes.

The onus is on Canadian residents who receive income from foreign sources to ensure that any tax withheld from their pay pursuant to a tax treaty currently in effect between Canada and that country is withheld in the correct amount and percentage.

A separate credit calculation is required for both business and non-business income of each source country. Using Form T1135 — Foreign Income Verification Statement, taxpayers are also required to annually report specified foreign assets, whose total cost exceeded \$100,000 at any time during the previous taxation year.

Social-security taxes paid to a foreign government are not eligible for Canadian foreign tax credits, with the exception of certain taxes paid in the U.S. that are covered by provisions in the Canada-United States income tax convention.

#### **OVERSEAS EMPLOYMENT TAX CREDIT (OETC)**

Canadian residents who perform substantially all employment duties outside of Canada in the course of a taxation year, while employees of specified employers to whom they are at arm's-length (also usually a resident of Canada), or sub-contractors thereof, may qualify for the overseas-employment tax credit (OETC).

Specified employers must carry on business in the same country where employees, including professional, administrative and other support staff, perform their duties. Such jobs are generally held in connection with an overseas natural resource, construction, installation, agricultural or engineering project.

This credit potentially shelters from federal tax up to 80 per cent of overseas employment income — including salary, wages and other remuneration, such as gratuities, taxable benefits and stock options — netted off by a reasonable proportion of allowable employment deductions, to a maximum of \$100,000 (i.e., sheltering up to \$80,000). In 2009, Ontario residents may deduct 38.5 per cent of the federal OETC.

To qualify for the OETC, the CRA specifies that taxpayers must work overseas for at least six consecutive months either in one calendar year or overlapping the previous or next year. However, a 2002 court decision (Rooke) also ruled that as long as taxpayers performed all, or substantially all, of the work outside Canada over the course of a particular taxation year, they would be entitled to the deduction.

"All or substantially all" generally refers to at least 90 per cent of employees' income being derived from eligible activities during the qualifying period for the OETC.

During this period taxpayers can still take leave for vacation time and other activities, such as returning to Canada to meet with their employers and/or work briefly here, without prejudicing their status in terms of qualifying for the OETC — provided they continue to perform a substantial amount of their employment duties outside Canada.



Activities performed under contract with the United Nations might qualify taxpayers for an OETC credit.

An individual who would otherwise be employed by a foreign company, but instead incorporates a Canadian company, which in turn contracts with the foreign company to provide services, cannot claim this amount. This credit is also disallowed if the Canadian company does not employ more than five full-time employees (i.e., five full-time employees, plus at least one part-time employee) and the taxpayer is a specified shareholder, or is related to a specified shareholder, who owns at least 10 per cent of the shares together with non-arm's-length parties of the business.

An amendment to this provision of the *Income Tax Act* has been proposed whereby at least 10 per cent of the qualified employer's shares, or the value of any partnership interests, must be held by people resident in Canada.

The CRA recognizes the government of Canada as a specified employer. Therefore, federal-government employees might qualify for the OETC if employed overseas as the result of a government contract, although services provided under a prescribed international development-assistance program by the federal government are excluded.

Income used by the taxpayer to calculate the OETC may not be used in the calculation of the foreign-tax credit.

#### **SCIENTIFIC RESEARCH AND EXPERIMENTAL DEVELOPMENT TAX CREDIT (SR&ED)**

Generous tax incentives exist to encourage investment in certain research and development (R&D) activities. A scientific-research and experimental-development investment tax credit (SR&ED ITC) is, for instance, available on qualified capital and current expenditures. This SR&ED ITC can reduce tax payable and/or result in a cash refund.

Canadian-controlled private corporations may be eligible for SR&ED ITCs at a rate of 35 per cent on the first \$3 million of annual eligible expenditures and 20 per cent thereafter (although the \$3 million expenditure limit might be reduced as taxable income for the previous taxation year rises above \$500,000 when that taxation year ends after December 31, 2008 (up from \$400,000), and as taxable capital of the previous year exceeds \$10 million). Other Canadian companies, along with individuals, are eligible for SR&ED ITCs at a rate of 20 per cent. SR&ED ITC eligible activities must be business-related and carried on in Canada; this could also include areas considered part of the country's exclusive economic zone, including its airspace, seabed or subsoil.

The upper limit for the \$3 million ITC phase-out is \$800,000 of taxable income for a previous taxation year that ends after December 31, 2008 (up from \$700,000); and \$50 million of taxable capital. If the previous fiscal year straddles December 31, 2008 the new and old phase-out limits will be prorated based on the number of days before and after that date.



Carefully monitor the use of related materials that comprise a portion of your SR&ED ITC. Such costs are only permitted in the ITC calculation to the extent they are actually applied in the research and development process, as opposed to some other commercial use.





You need not have incurred the SR&ED expenditures during the year in which a related deduction is claimed.

Investment tax credits can be carried back up to three years and carried forward up to 20 years for losses incurred and credits earned in taxation years after 1997.

To apply for a claim to this credit, businesses and individuals must complete Form T661 — Scientific Research and Experimental Development (SR&ED) Expenditures Claim, which has been simplified of late. Individuals must also complete Form T2038 (IND) — Investment Tax Credit (Individuals), while corporations must complete Form T2SCH31 — Investment Tax Credit — Corporations.

SR&ED claims must be filed within 12 months of the filing due date of the taxpayer's income tax return.

Ontario also offers a number of R&D-related tax incentives. These include:

- A tax exemption on the federal SR&ED investment tax credit.
- Effective January 1, 2009, a 4.5 per cent non-refundable Ontario research and development tax credit.
- A 20 per cent refundable tax credit for R&D expenditures performed at eligible research institutes in Ontario.
- A 10 per cent refundable provincial tax credit for eligible small- and medium-sized companies performing R&D.
- A 100 per cent deduction for the cost of intellectual property, such as patents and licences.

Check with your certified general accountant to see if and how this credit might apply to certain activities and expenditures related to your business.



The salary of a Canadian who is engaged in SR&ED eligible activities outside the country, but which support eligible activities within Canada, might also constitute eligible expenditures.



Because the opportunity for an SR&ED ITC will generally be lost if the claim is not filed on time, it is a good idea for an individual or business that wishes to make a claim to do so well in advance of the final due date. It is best to provide the CRA with enough time to review the claim and confirm that everything required has been received. The CRA says a claim filed "at least 90 days before the reporting deadline" will provide sufficient time for them to review it and advise the claimant of any deficiencies in advance of the deadline.

## Additional Tax Considerations

### CANADA CHILD TAX BENEFIT

The Canada child tax benefit (CCTB) is an income-tested benefit with two components: the CCTB base benefit for low- and middle-income families; and the national child benefit (NCB) supplement for low-income families. It involves a monthly non-taxable payment made to a custodial parent of children under 18.

The CCTB and NCB supplements are both fully indexed for inflation on an annual basis every July 1.

The base value of the CCTB stands at \$1,340 beginning July 2009 (up from \$1,307), with a \$93 supplement (up from \$91) added for a third and subsequent qualified child.

The CCTB benefit begins to be phased out at two per cent of family net income above \$40,726 (up from \$37,885 in 2008) for one dependent child, and four per cent of family net income above that threshold for two or more children.

Effective July 2009, the NCB supplement increased to \$2,076 for the first child, \$1,837 for the second child and \$1,747 for each subsequent child (from \$2,025, \$1,792 and \$1,704, respectively). The NCB supplement begins to reduce as net family income rises above \$23,710 (up from \$21,280).

As a result of the above changes, maximum annual combined CCTB benefits and NCB supplements increased to \$3,416 for the first child, \$3,177 for the second child and \$3,180 for additional children (from \$3,332 for the first child, \$3,099 for the second child and \$3,102 for each subsequent child).

The threshold level of net family income at which the NCB supplement is fully phased out has increased to \$40,726 (from \$37,885).

Both spouses or common-law partners must file income tax returns in order to receive the CCTB and NCB supplements.

Parents who are separated or divorced might each be eligible to receive a portion of the annual CCTB allotment on behalf of their dependent children if they share custody or even if the non-custodial parent temporarily resides with the children for at least one month during the year. The parent with whom the children resided on the first day of that month is generally considered to be responsible for their care and upbringing and, therefore, eligible for the benefit.

Special rules might apply to certain situations involving foster parents.

Please see Appendix II on page 127 for details.

### CHILD DISABILITY BENEFIT

The federal government introduced a child disability benefit (CDB) in its 2003 federal budget. Effective July 1, 2009, it provides parents of children who

have a disability with a supplement to the CCTB of up to \$2,455 annually (up from \$2,395 for the previous 12 months) per qualified child. In order to be eligible to receive this credit, their child must have a medical condition that qualifies them for the disability tax credit.

The full \$2,455 benefit for the first eligible child is phased out at two per cent of family income in excess of the NCB supplement threshold limit of \$40,726 (up from \$37,885 for the previous 12 months). Thus, families who have one child who qualifies for both the full NCB supplement and CDB will receive a total annual CCTB benefit of \$5,870 on behalf of that child for the 12 months beginning July 1, 2009.

The CDB is eliminated completely when the net income of a family responsible for one child who has a disability reaches \$163,476. That limit will be higher if more children with disabilities are being cared for in the family.

The CDB may also be claimed with respect to certain dependants, provided they don't require the credit to reduce their own tax liability after claiming personal, age, pension credits and any credits relative to EI and CPP premiums paid.

The list of relatives to whom the unused portion of the individual's disability tax credits may be transferred under certain circumstances includes a parent, grandparent, child, grandchild, brother, sister, aunt, uncle, nephew, or niece of the individual or the spouse/common-law partner, provided the individual with a disability is living with the supporting person and is at least partially dependent.

#### **UNIVERSAL CHILD CARE BENEFIT (UCCB)**

The 2006 federal budget presented Canadians with a universal child-care benefit (UCCB). The UCCB, which took effect July 1, 2006, provides all families in Canada with \$100 per month, or \$1,200 per year, for each child under six. It is taxable in the hands of the lower-income spouse or common-law partner. Amounts received under the UCCB will not adversely affect income-tested federal benefits receivable such as old-age security (OAS) or EI.

Families with eligible children who already receive the CCTB automatically receive the UCCB benefit. Those who do not will have to apply to the CRA.

#### **WORKING INCOME TAX BENEFIT (WITB)**

In 2009, the refundable working income tax benefit (WITB) provides up to \$522 for individual taxpayers 19 or over without dependants, whose earned income exceeds \$3,000. This credit is reduced by 15 per cent of net family income in excess of \$9,923, which would fully eliminate this benefit at net family income of \$13,403. The WITB is \$1,044 for families, including couples or single parents 19 or over, with earned income in excess of \$3,000, reduced by 15 per cent of net family income in excess of \$15,145, which would eliminate this benefit at \$22,105.

The WITB is calculated at the rate of 20 per cent of each dollar of earned income in excess of \$3,000, therefore, reaching a maximum benefit at \$5,615 of earned income for individuals and \$8,225 of earned income for families.

Individuals who are not classified as dependants; who are eligible for the DTC; and have at least \$1,750 in earned income, will also receive an additional disability supplement that will provide up to a maximum credit of \$261. This disability supplement is reduced by 15 per cent of net family income in excess of \$13,404 for single individuals and \$22,108 for families, which would fully eliminate this benefit at net family income of \$15,144 for single taxpayers, and \$23,848 for families.

Full-time students with no dependants are not eligible for this WITB.

#### **OLD AGE SECURITY (OAS) PENSIONS**

The maximum old-age security (OAS) pension amount payable to senior citizens in 2009 is approximately \$6,204. However, a clawback provision reduces OAS pensions for individuals with net income exceeding \$66,336. The clawback rate of 15 per cent eliminates the entire OAS benefit at \$107,696 of net income.

The OAS is available to most Canadians at 65. Check the Service Canada website at [www.servicecanada.gc.ca/eng/sc/oas/pension/oldagesecurity.shtml](http://www.servicecanada.gc.ca/eng/sc/oas/pension/oldagesecurity.shtml), and [www.servicecanada.gc.ca/fra/sc/sv/pension/securitedelavieillesse.shtml](http://www.servicecanada.gc.ca/fra/sc/sv/pension/securitedelavieillesse.shtml) in French for a complete description regarding eligibility requirements.

#### **GUARANTEED-INCOME SUPPLEMENT (GIS)**

The guaranteed-income supplement (GIS) is paid to individuals 65 or over who qualify based on low income. GIS receipts are included in net income, affecting tax calculations, although an offsetting deduction allows individuals to exclude GIS benefits from taxable income.

In Ontario, old-age supplements are paid under the provincial guaranteed annual income system (GAINS) for seniors. The GAINS benefit, which is a supplement to the federal GIS, only assists seniors with very low incomes.

#### **ALTERNATIVE MINIMUM TAX (AMT)**

Individuals are generally subject to alternative minimum tax (AMT) in situations where the AMT exceeds ordinary taxes payable. AMT is computed on adjusted taxable income in excess of \$40,000 at the lowest federal tax rate of 15 per cent (with credits allowed for certain personal amounts), plus the applicable provincial tax.

In Ontario, the AMT rate for 2009 is calculated at 40.33 per cent of the corresponding federal AMT. This amount is added to the provincial tax.

Individuals may be liable to pay AMT if the following items are on their tax return:

- taxable dividends
- a federal political contribution
- the overseas employment tax credit
- a labour-sponsored-fund tax credit
- taxable capital gains
- a loss from a multiple-unit residential building (MURB) or certified film where CCA is taken

- net losses from resource properties
- employee stock options or share deductions
- an employee home-relocation deduction
- any losses or carrying charges arising from limited partnerships or investments identified as tax shelters.

AMT paid in excess of ordinary tax in one year is eligible to be carried forward seven years and deducted against tax payable in excess of the AMT liability in future years.

An individual who makes quarterly tax instalments is required to take the AMT into account for the purpose of determining instalments payable. This minimum tax is not applicable in the year of death.

Check with your certified general accountant if you think AMT might apply in your situation.

### **FOREIGN PENSIONS**

Individuals who reside in Canada must normally pay Canadian tax on any pension income received from a foreign country in excess of CDN \$1,000. Certain deductions may be allowed to avoid double taxation with the host country, as determined by the existence of any tax conventions between Canada and that other country. Other conditions might also apply. For instance, Canada's tax agreement with Germany stipulates that social-security benefits cannot be taxed more in the receiving country than had the recipient resided in the paying country.

Canada has tax conventions with about 85 countries around the world. Taxpayers with ties to another nation who have questions about their tax status should consult their certified general accountant.

### **UNITED STATES FILING REQUIREMENTS**

The United States imposes tax and/or filing requirements on Canadians in certain circumstances. Canadians who are considered residents for U.S. income-tax purposes are subject to U.S. tax on their world income.

U.S. residency is determined on the basis of either immigration status or physical presence. The substantial-presence test uses a formula taking into account the number of days individuals are present in the country during the current year, along with a fraction of the days they were present during the two preceding years.

Canadians who are considered U.S. residents under the substantial-presence test, but are not in the U.S. for more than 182 days during the year, can avoid being considered residents for tax purposes by filing a closer-connection statement. To qualify, individuals must show that closer connections to



The international location of a permanent home or business establishment will significantly affect both personal and corporate taxes. Therefore, a tax accountant and/or lawyer should be consulted if there is any ambiguity.

Canada exist, substantiated by the location of a permanent home, or business establishment, as well as factors such as family and other social relationships.

Even taxpayers who maintain significant residential ties to the U.S. or another country might still be considered to be a Canadian resident for tax purposes, depending on a number of factors such as their length of stay in Canada — whether it is for a substantial period of time, or is occasional or intermittent, for instance; physical and/or financial property owned; maintenance of health coverage; driver's licence; existence of a bank account; and personal or business connections here.

The Canada-United-States tax treaty determines residency for U.S. tax purposes for Canadians who are present in the U.S. in excess of 182 days. Taxpayers with dual citizenship in both Canada and the United States may also be subject to special rules. In certain instances, an apportionment of income earned in both countries might be required.

Complex taxation rules might also apply in situations where an individual is moving from one country to the other.

Check with your certified general accountant to determine your income-tax-filing requirements if you have ties to both countries. Most recently, the fifth protocol to the Canada-United States Tax Convention entered into force on December 15, 2008; there might be some provisions related to that update which affect you.



An increasing number of Canadians own vacation property in the United States. Several complex tax issues, including estate-related matters, could result on both sides of the border depending on factors such as joint ownership with a spouse and/or others (i.e., time sharing), especially if there is any commercial use associated with that property. Consult your certified general accountant to sort these matters out.

## **INSTALMENTS**

Instalments are required from self-employed taxpayers, or those whose taxes have not otherwise been withheld by the employer, if the difference between tax payable and amounts withheld at source is greater than \$3,000 in both the current and either of the two preceding years (for farmers and fishers, both of the two preceding years). Quarterly instalments are due on the 15th of March, June, September and December (for farmers and fishers, one instalment only is due on December 31).

The total required instalment amount is equal to the preceding year's tax payable or estimated current year's tax payable, if lower. (For farmers and fishers, the instalment payable is two-thirds of this amount).

The CRA sends instalment reminders based on a formula — with the first two instalments based on half of the second preceding year's net tax payable plus CPP contributions payable and the last two instalments based on the preceding year's net tax payable and CPP (minus the first two instalments already paid during the current year). Alternatively, taxpayers may choose to pay all

four instalments on the basis of the preceding year's net tax payable if they think that is more advantageous.

Interest is compounded daily and charged on late or deficient instalments at a prescribed rate. (Refer to Appendix VI, page 120, as well as Appendix VII, page 136.) If the interest on deficient instalments is more than \$1,000, an additional penalty of 50 per cent on that excess may apply. If instalments are paid according to the CRA's instalment reminders, no liability for interest or penalty will be assessed.



If your instalment has been late or deficient in the past, consider prepaying or overpaying future instalments. The CRA will offset interest on early or excess instalments against interest charged for the same year (although interest on any net balance will not be paid).

#### **PENALTIES AND INTEREST CHARGES ON OVERDUE TAXES**

Individual taxpayers who do not file their returns by April 30 of the subsequent year (June 15 if they or the spouse or common-law partner have self-employed income) may be required to pay a late-filing penalty. This penalty is five per cent of the balance owing, plus one per cent for each month the return is late up to a maximum of 12 months (with a maximum potential penalty of 17 per cent).

An additional penalty applies when returns are filed late and taxpayers have already received a late-filing penalty during any of the three preceding years. This repeater penalty is equal to 10 per cent of the tax owing at the due date plus two per cent each month the return is late, up to 20 months (and a maximum potential penalty of 50 per cent).

Interest is charged on unpaid tax and penalties from the due date. Where there is self-employment income, the due date of the tax return is deferred to June 15; however, the balance of tax remains due on April 30 and interest will be charged on any balance owing from that date. This interest, charged at a prescribed rate, is compounded daily. (Refer to Appendix VI, page 133, as well as Appendix VII, page 136.) Penalties and interest paid are not tax deductible.

Interest received from the CRA for overpayments is taxable in the year of receipt.



To avoid penalties, file your return on time even if you are unable to pay the tax balance due.

#### **NOTICE OF OBJECTION**

Taxpayers who disagree with the assessment they receive on their income-tax return can formally object to the findings by writing to the chief of appeals at their tax services office or tax centre. Alternatively, they can fill out a Form T400A Objection — *Income Tax Act*. The time limit for individual taxpayers to

file this objection is the later of: 90 days after the mailing date of the notice of assessment, or one year after the taxpayer's filing due date, accompanied by a written application, made on a timely basis, to the CRA.

For GST objections, taxpayers can complete and mail Form GST159, Notice of Objection (GST/HST) to the chief of appeals at their tax services office. This must be done within 90 days of the mailing of their notice of assessment or notice of determination.

The Tax Court of Canada (TCC) is the first judicial level to which a tax dispute can be taken. Subsequent appeals of a TCC judgment must then be made to the Federal Court of Appeal (FCA) within 30 days of the decision being announced (excluding July and August). The final potential spot to resolve a dispute is with the Supreme Court of Canada; however, the supreme court must first approve the cases it hears and, in practice, only a small percentage of applications will be allowed to present to the nation's highest court.

Information about taxpayer objection and appeal rights is also online; see document P148, entitled *Resolving Your Dispute: Objection and Appeal Rights under the Income Tax Act*, accessible through the main CRA website.



Taxpayers who wish to file a notice of objection with respect to a CRA assessment must do so in writing, providing all relevant details. It is also vitally important to adhere to all deadlines established by the CRA.

#### **TAXPAYER RELIEF PROVISIONS**

This series of legislation, previously known as the fairness package, allows the CRA to use discretion under certain circumstances in the following areas:

- With respect to the acceptance of late, amended, or revoked elections.
- To waive or cancel part or all of a penalty or interest where taxpayers have not complied with a requirement under the *Income Tax Act* or applicable regulation because of extraordinary circumstances beyond their control.
- To reassess or make a redetermination on an income tax return to give a refund or to apply a refund against amounts owing beyond the normal three-year period.

Details are outlined in CRA Information Circular IC07-1, Taxpayer Relief Provisions, which replaces and consolidates the information in previous information circulars IC92-1, 92-2, and 92-3. This can be found online at URL: [www.cra-arc.gc.ca/E/pub/tp/ic07-1/README.html](http://www.cra-arc.gc.ca/E/pub/tp/ic07-1/README.html), or in French at [www.cra-arc.gc.ca/F/pub/tp/ic07-1/](http://www.cra-arc.gc.ca/F/pub/tp/ic07-1/).



Relief provisions might apply to certain areas in Canada when a natural disaster affects taxpayers' ability to file their returns on time.





Retain electronic financial records, preferably along with backup, for audit purposes, even if you have already printed hard copies of such documents. Check with the CRA regarding the appropriate minimum retention period.

The period in which a taxpayer may make a request to the CRA for relief under the above provisions is limited to 10 years from the end of the calendar year corresponding to the tax year or fiscal period in question.

Taxpayers can make their requests in writing to a district office or taxation centre with all relevant information, including their name, address, social insurance number, the applicable taxation year(s) and documents to support the application, including records of dates, times and names of people from whom information was received. If they believe the agency has not exercised its discretion in a fair and reasonable manner, they may request — in writing — that the director of the district office or taxation centre review their situation.

The CRA website at [www.cra-arc.gc.ca](http://www.cra-arc.gc.ca) contains a link to the CRA's voluntary disclosures program (VDP), which provides a description of the program, including the circumstances upon which VDP relief from penalty and persecution may be considered.

The CRA also provides an online service called My Account, which is accessible through the main site. This allows individuals to access their personal income tax-related information. They can access this site by providing their date of birth, social insurance number, income from their tax return and special web-access user name and password.



A taxpayer who would like to authorize a third party, such as another family member or a professional financial advisor like a certified general accountant, to deal with the CRA on his/her behalf, including online, can do so by filling out Form T1013—Authorizing or Cancelling a Representative. It can also be done online by logging on to [www.cra-arc.gc.ca/eservices/tax/individuals/myaccount/menu-e.html](http://www.cra-arc.gc.ca/eservices/tax/individuals/myaccount/menu-e.html) in English or [www.cra-arc.gc.ca/eservices/tax/individuals/myaccount/menu-f.html](http://www.cra-arc.gc.ca/eservices/tax/individuals/myaccount/menu-f.html) in French.

#### TAX-ALERT INITIATIVE

The CRA's tax-alert initiative appears on the website [www.cra-arc.gc.ca/gncy/lrt/menu-eng.html](http://www.cra-arc.gc.ca/gncy/lrt/menu-eng.html) in English and [www.cra-arc.gc.ca/gncy/lrt/menu-fra.html](http://www.cra-arc.gc.ca/gncy/lrt/menu-fra.html) in French. This program offers concentrated information on a variety of tax-related topics, including unsavoury tax-avoidance schemes; the serious consequences associated with tax evasion; tax shelters and havens; and a description of how the underground economy hurts Canadians.



The CRA website lists registered charities, including those that have recently registered or whose listing has been revoked or annulled. Prospective donors can use the CRA's search engine to investigate a charitable organization.

The website also contains tips on how to become an informed donor to charities; information about how the CRA conducts audits and investigations, including what taxpayers need to know if they are being audited; and a description of fairness and taxpayer rights, among a multitude of other topics.

#### **TAXPAYER BILL OF RIGHTS**

In May 2007, the CRA and federal Department of Finance announced the release of a taxpayer bill of rights, which includes 15 rights about issues ranging from service, privacy, and procedures dealing with tax disputes, among others, plus an additional five commitments to small businesses in Canada.

The establishment of a taxpayers' ombudsman, to "operate independently and at arm's-length from the CRA" was also announced. Among other duties, the mandate of this office is to "conduct impartial and independent reviews of service-related complaints about the CRA."

Details about both the taxpayer bill of rights and taxpayers' ombudsman are available on the CRA website [www.cra-arc.gc.ca/menu-e.html](http://www.cra-arc.gc.ca/menu-e.html) in English and [www.cra-arc.gc.ca/menu-fra.html](http://www.cra-arc.gc.ca/menu-fra.html) in French.

#### **ESTATE PLANNING**

An individual is deemed to have disposed of all assets owned, at FMV, on the date of death. Estate planning can minimize tax consequences at death by implementing specific tax-deferral measures in advance. Such measures include inter-spousal rollovers of assets, rollovers to corporations, the creation of family trusts, and estate freezes.

Because estate-tax planning is complex and beyond the scope of this tax-planning booklet, do consider seeking professional advice from your certified general accountant. For additional information on estate planning, refer to CGA Ontario's *Executorship: A Guide for Those Called upon to Act as an Estate Trustee* booklet. To receive your complimentary copy, call 416-322-6520, ext 8254, or view it online at [www.cga-ontario.org/Publications/Information\\_Booklets.aspx](http://www.cga-ontario.org/Publications/Information_Booklets.aspx).

## Part Four: Ontario

### Ontario Provincial Tax

Although the CRA handles income tax administration for Ontario, the province operates using an autonomous tax-on-income (TONI) system, under which provincial income tax rates are levied on net income. In 2009, those rates are as follows: up to \$36,848, 6.05 per cent; between \$36,848 and \$73,698, 9.15 per cent; and in excess of \$73,698, 11.16 per cent.

Provincial surtaxes are applied as follows during the 2009 taxation year:

- 20 per cent of Ontario income tax in excess of \$4,257, plus 36 per cent of Ontario income tax, for a total of 56 per cent in excess of \$5,370.
- Taxpayers who lived in Ontario on December 31 of a particular year are normally deemed to be Ontario residents for the entire tax year and thereby subject to provincial tax.

### NEW HARMONIZED SALES TAX

The Ontario government announced in its 2009 budget that it intends to adopt a harmonized sales tax (HST) on July 1, 2010. The HST will be 13 per cent, combining the provincial retail sales tax of 8 per cent, with the federal goods and services tax (GST) of 5 per cent.

### ONTARIO TAX REDUCTIONS

Ontario residents are entitled to calculate a basic \$205 reduction in 2009, supplemented by a \$379 reduction for each eligible child 18 or younger. An additional \$379 reduction is also available for each dependant with a disability.

These tax reductions, which must be applied before provincial tax credits, are lowered by one dollar for every three dollars of Ontario tax payable in excess of the reduction amount. They are eliminated entirely when the gross provincial tax payable exceeds available tax reductions by 150 per cent.

Taxpayers are required to determine their Ontario-tax reduction before claiming available foreign-tax credits.

### ONTARIO CHILD BENEFIT

The 2007 provincial budget introduced an Ontario child benefit (OCB), effective July 1, 2007, for each child under 18. The initial OCB payment through to and including June 30, 2008 inclusive was \$250 (in addition to social-assistance or Ontario child-care supplement [OCCS] for working families' payments), reduced by 3.4 per cent of adjusted family net income over \$20,000. That payment increased to \$1,100 on July 1, 2009 (which is up from \$600 for the year beginning July 1, 2008). It is reduced by eight per cent of adjusted family net income in excess of \$20,000.

The OCB will eventually replace the OCCS benefit as well as most child-related social-assistance benefits, although if a family's OCCS entitlement exceeds that for the OCB, they also receive the difference. This consolidation process began in 2008. Remaining excess entitlements under the OCCS will begin to be phased out over a seven-year period beginning in 2011.

The OCB payment timetable has been accelerated by two years. It was originally supposed to rise to an annual maximum of \$1,100 per child by July 2011. Now the government has committed to increasing the OCB annual maximum to \$1,310 per child by approximately December 31, 2013.

Parents must file income tax returns and be registered for the Canada child tax benefit to receive the OCB.

#### **ONTARIO CHILD CARE SUPPLEMENT (OCCS) FOR WORKING FAMILIES**

Ontario's former refundable tax credit for lower-income families incurring qualifying child-care expenses for each child under seven was incorporated into the Ontario child-care supplement for working families (OCCS), which is now, in turn being incorporated into the Ontario child benefit (OCB). See section above.

The maximum annual OCCS benefit prior to the phase-in with the OCB was \$1,100 for each child under seven in a two-parent family. The maximum annual benefit for single parents was \$1,310 for each child under seven.

Benefits were calculated as a percentage of a family's earnings from work (including self-employment) in excess of \$5,000, depending on the number of children under age seven. The benefits were 21 per cent of earnings in excess of \$5,000 for a family with one child under seven; 42 per cent for a family with two children under seven; and 63 per cent for a family with three or more children under seven. Benefits were reduced by eight per cent of family net income in excess of \$20,750.

The OCCS required families to apply for annual benefits by June 30, with receipts supporting all claims. Check with the Ontario ministry of revenue toll-free at 1-866-668-8297 if you have questions about your current status in regard to the OCCS and how benefits are being coordinated with the OCB.

#### **PROPERTY TAX CREDIT**

The Ontario property tax credit is generally available to taxpayers over 18, but may also be available to those between 16 and 18 who paid rent or property tax (or had it paid on their behalf) for a principal residence, and did not reside with a person eligible to claim a CCTB on their behalf.

This credit is limited to a maximum of \$250 (\$625 for taxpayers 65 or older), plus an additional 10 per cent of occupancy costs. The aggregate total is combined with the eligible sales-tax credit; then reduced by two per cent of total income in excess of \$4,000 [for taxpayers 65 and over who reside with a spouse or common-law partner, the comparable amount before this clawback begins is four per cent of total income in excess of \$24,750 in 2009].

The total income for this calculation includes the combined net incomes of both spouses or common-law partners. If both are under 65 and have not separated, either is eligible to claim this credit, although only one may do so. Special rules apply for couples who married or separated during the year.

The property tax credit is available only for principal residences. If the taxpayer's property is owned, 100 per cent of property-tax payments are eligible as occupancy cost. Special rules apply in instances where a co-operative is declared a principal residence. Also, property tax claimed for a farm is limited to the taxpayer's principal residence plus one acre of land.

If the property is rented, 20 per cent of the rent paid is eligible as an occupancy cost. (Superintendents who pay reduced rent in lieu of services rendered may be eligible to claim an imputed rent amount as part of their property tax claimed).

A student living in a prescribed residence (usually affiliated with a university, college, or nursing school) will have a deemed occupancy cost of \$25 for the applicable portion of the year. Rental payments made by residents of nursing homes also qualify for the Ontario property-tax credit without impairing any tax-deductible medical expenses claimed in connection with that residency.

Non-related individuals who share a principal residence and pay rent or property tax may allocate occupancy cost on a prorated basis relative to their proportionate share of accommodation.

Seniors and people with a disability who own residential property and are deemed to be low income may be eligible for relief from property-tax increases resulting from assessment reform. It is the responsibility of each municipality within the province to determine who qualifies for tax relief.

The 2008 provincial budget introduced a new senior homeowners' property tax grant, beginning in 2009, to assist low- and moderate-income seniors offset their property taxes. This grant is worth up to \$250 in 2009; and will increase to \$500 in 2010 and subsequent years.

#### **SALES TAX CREDIT**

Taxpayers over 18 (or between 16 and 18 and not residing with anyone eligible to receive a CCTB on their behalf) may be eligible for a \$100 Ontario sales tax credit. Another \$100 credit may be available for cohabiting spouses or common-law partners, with an additional \$50 credit available on behalf of each dependent child for whom taxpayers or cohabiting spouses or common-law partners are eligible to receive child tax benefits.

The sales tax credit and property tax credit are combined and applied as described above, under property tax credit, page 115. The maximum combined benefit for seniors in 2009 is \$1,125. This is a refundable tax credit that can be received even if the taxpayer owes no tax.

If both spouses or common-law partners are under 65, either may be eligible to claim the sales tax credit on behalf of the other and any dependent children, but only one may do so. The spouse or common-law partner who claims the property-tax credit must also claim the sales-tax credit.

If one spouse or common-law partner is 65 or older, that spouse or common-law partner must claim the property and sales-tax credit on behalf of both.

Two new separate, property and sales tax credits, both payable quarterly to qualified taxpayers, are proposed to take effect in July, 2010.



Individuals who turn 16 during the tax year are eligible to claim their own provincial sales- and property-tax credits if nobody is claiming them as a dependant or has received the CCTB on their behalf. Young taxpayers in that situation should complete their own tax returns and claim these benefits.

#### **LAND TRANSFER TAX REFUND PROGRAM**

The province's 2007 fall economic outlook and fiscal review expanded the provisions of Ontario's existing land transfer tax refund program, available to first-time purchasers of newly constructed homes, to also encompass first-time homebuyers of resale homes for agreements entered into after December 13, 2007. Thus, first-time purchasers of both types of homes are eligible for a provincial-government refund on up to \$2,000 of the land transfer tax paid for their new home.

#### **ONTARIO HEALTH PREMIUM**

Taxpayers pay a personal health premium in Ontario based on their taxable income, at the following rates:

<b>Taxable Income</b>	<b>Premium</b>
Up to \$20,000	\$0
\$20,000 – \$25,000	six per cent of income greater than \$20,000
\$25,000 – \$36,000	\$300
\$36,000 – \$38,500	\$300 plus six per cent of income > \$36,000
\$38,500 – \$48,000	\$450
\$48,000 – \$48,600	\$450 plus 25 per cent of income > \$48,000
\$48,600 – \$72,000	\$600
\$72,000 – \$72,600	\$600 plus 25 per cent of income > \$72,000
\$72,600 – \$200,000	\$750
\$200,000 – \$200,600	\$750 plus 25 per cent of income > \$200,000
More than \$200,600	\$900

The first income band has a \$5,000 cushion through which the first \$300 payment is fully phased in. Each of the subsequent income bands, with the exception of \$36,000 to \$38,500, has a \$600 cushion through which the next \$150 increment is fully phased in.

The Ontario health premium is included as part of Ontario's payroll withholding tax. Self-employed individuals who pay by instalment can elect to increase quarterly payments to account for this premium.

## **ONTARIO POLITICAL CONTRIBUTION TAX CREDIT**

To encourage participation in the political process, contributions to registered Ontario political parties, candidates or constituency associations are eligible for an Ontario political contribution tax credit. This amount is calculated as follows:

- 75 per cent of the first \$372 contributed, plus
- 50 per cent of the next \$868, between \$372 and \$1,240; and
- 33 1/3 per cent of contributions of the next \$1,581, between \$1,240 and \$2,821.

At \$2,821 of political contributions, the maximum annual credit of \$1,240 will have been reached. This tax credit is refundable, meaning taxpayers receive the credit even when they pay no income tax.

Either spouse or common-law partner may claim the total political-contribution credit (which is only available in the current taxation year) for both.

## **LABOUR-SPONSORED INVESTMENT FUNDS (LSIF)**

The federal government allows a credit of 15 per cent on up to \$5,000 for investments in labour-sponsored venture-capital corporations (LSVCC); plus the Ontario government allows a 15 per cent credit on up to \$7,500 under its labour-sponsored investment fund (LSIF) program.

As a result, the combined annual maximum federal and provincial tax credits for both LSVCCs and LSIFs total up to \$1,875, subject to the LSIF phase-out schedule outlined below.

Eligible provincial labour-sponsored investment funds (LSIF) must be held for a minimum of eight years. As unused LSIF credits cannot be carried over to another year, the taxpayer might wish to seek professional advice in order to use other potential deductions or credits for carry-forward to avoid losing this credit.

The LSIF is able to offer a 20 per cent tax credit — an additional five per cent — where it can be demonstrated that a significant portion of the LSIF's capital is invested in research-and-development-oriented companies. An LSIF able to meet that standard is referred to as a research-oriented investment fund (ROIF).

The 2004 provincial budget presented a moratorium on new LSIF registrations after May 18, 2004.

The provincial government also announced in September 2005 that it intends to phase out the LSIF and corresponding ROIF tax credits in 2009 and 2010. The 2007 economic outlook extended this limit by one year such that the LSIF will now be eliminated for tax years after 2011. This updated phase-out is scheduled to proceed as follows:

- maintaining the 15 per cent tax-credit rate until the end of the 2009 tax year
- reducing the credit to 10 per cent for 2010

- further lowering the credit to 5 per cent in 2011
- eliminating it entirely for tax years after 2011

#### **COMMUNITY SMALL BUSINESS INVESTMENT FUNDS (CSBIF)**

The Ontario government allows qualifying individual investors and corporations to receive a tax credit of up to 15 per cent on a minimum \$25,000, to a maximum \$500,000 investment in an eligible community small business investment fund (CSBIF). Thus, the maximum credit available is \$75,000.

Seven-and-one-half per cent of this credit is available at the time of investment in a CSBIF; the remaining seven-and-one-half per cent is available when the CSBIF invests in an eligible small business.

#### **EMPLOYEE-OWNERSHIP (EO)**

Employees who establish an employee-ownership labour-sponsored venture-capital (LSVCC) corporation program are eligible for an employee-ownership (EO) credit. This could involve, for instance, circumstances where employees invest in, or buy out, a business from their current employer. Two pools of deductible tax credits are created. Pool 1 is calculated annually as follows:

- 20 per cent of the first \$3,500 of investment
- 30 per cent of the balance between \$3,501 and \$15,000 of investment, to a maximum of \$4,150 in tax credits

Credits may be deducted to the extent of available Ontario taxes payable.

Any credits from Pool 1 that are unused in the current year drop down into Pool 2, where they carry forward for five years and, if unused, then expire. The maximum amount of tax credits that may be deducted in a single year is \$4,150 (from Pool 1) plus the entire balance of Pool 2.

Taxpayers who wish to contribute more than the amount required to qualify for the maximum \$4,150 annual credit should consider seeking professional advice.

Employees of a business qualifying under the EO-LSVCC program may make a lifetime investment of up to \$150,000 in that business. Regardless of the amount invested, a maximum of \$15,000 a year becomes available for conversion to tax credits. This balance is carried forward. Thus, tax credits arising from a \$150,000 contribution made in one year can be deducted over 10 years.

Credits deducted for LSIF and EO-LSVCC investments will be added to taxes payable if the related shares are sold or invested funds returned within eight years.

#### **ONTARIO INNOVATION TAX CREDIT (OITC)**

The Ontario innovation tax credit (OITC) provides a 10 per cent refundable tax credit to qualifying publicly listed and private corporations that invest up to \$3 million in annual qualifying expenses for SR&ED activities in Ontario (the 2008 provincial budget increased this from \$2 million to parallel federal changes) that are eligible for the federal investment tax credit.



The full OITC is available where Ontario taxable paid-up capital in the previous taxation year did not exceed \$25 million and federal taxable income was not more than \$500,000. This \$3 million limit is reduced with respect to provincial paid-up capital between \$25 million and \$50 million, and federal taxable income between \$500,000 and \$800,000 if the taxation year ends after 2008 (up from \$400,000 and \$700,000, respectively). If the previous fiscal year straddles December 31, 2008 the new and old phase-out limits will be prorated based on the number of days before and after that date.

See the section outlining the federal scientific-research and experimental-development tax credit program on page 103.

#### **APPRENTICESHIP TRAINING TAX CREDIT**

Ontario's apprenticeship training tax credit (ATTC) is a 25 per cent refundable tax credit of up to \$5,000 covering a maximum 36 months worth of salaries and wages paid to eligible apprentices in designated industries and trades. Small businesses with total salaries and wages of \$500,000 or less can claim up to 30 per cent of those expenses.

The ATTC was originally intended as a temporary measure until the end of 2014; however the 2009 provincial budget made this tax incentive permanent. Furthermore, for expenditures incurred on or after March 27, 2009, it: increased the coverage period to 48 months; increased the maximum tax credit to \$10,000; and enhanced the rates to 35 per cent (45 per cent for small businesses).

#### **SMALL BUSINESS DEDUCTION THRESHOLD**

Ontario's small business deduction-threshold rate is \$500,000. This is the amount of active business income that Canadian-controlled private corporations (CCPC) are able to earn at a preferential tax rate.

## Conclusion

Tax planning is always necessary — particularly under an income tax system such as Canada's, which incorporates a progressive rate schedule with rules that allow or disallow specific transactions and courses of action.

Furthermore, new federal and provincial laws and policies are constantly being introduced; these often have a direct effect on specific tax strategies, because new opportunities may arise and old approaches may no longer be appropriate or valid as a result. It is, therefore, incumbent upon taxpayers to remain aware of contemporary tax rules that are applicable to specific actions being contemplated.

For these reasons, it is also a good idea to review any tax-planning proposals with a certified general accountant.

### ACCOUNTANT REFERRAL SERVICE

The Certified General Accountants of Ontario offers an accountant referral service, free of charge to Ontario residents and businesses that would like to hire a professional accountant for help with financial planning, tax returns, financial statement preparation and other accounting services. CGA Ontario will match clients' specific needs to a CGA Ontario practitioner's preferred area of practice.

To access CGA Ontario's online accounting referral service, visit [www.cga-ontario.org/Public/Selecting\\_an\\_Accountant/Accountant\\_Referral\\_Service.aspx](http://www.cga-ontario.org/Public/Selecting_an_Accountant/Accountant_Referral_Service.aspx) or for more information, call CGA Ontario at 416-322-6520 or toll-free at 1-800-668-1454.

240 Eglinton Avenue East  
Toronto ON M4P 1K8

[cga-ontario.org](http://cga-ontario.org)

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## Appendix I:

### Personal Tax Credits

Description	Federal Rates		Ontario Provincial Rates	
	2009 Federal Amount	Maximum Federal Credit <sup>(1)</sup>	2009 Provincial Amount	Maximum Provincial Credit <sup>(1)</sup>
Basic credit	\$10,320	\$1,548	\$ 8,881	\$ 537
Employment credit	1,044	157	0	0
Spousal credit <sup>(2)</sup>	10,320	1,548	7,541	456
– reduced by net income over \$0 (federally)				
– reduced by net income over \$754 (provincially)				
Amount for an eligible dependant <sup>(2)</sup>	10,320	1,548	7,541	456
– reduced by net income over \$0 (federally)				
– reduced by net income over \$754 (provincially)				
Age credit – over 64 <sup>(3)(4)</sup>	6,408	961	4,336	262
– reduced by net income over \$32,312 (federally)				
– reduced by net income over \$32,280 (provincially)				
Disability credit <sup>(5)</sup>	7,196	1,079	7,175	434
Disability supplement for child under 18 <sup>(2)</sup>	4,198	630	4,185	253
– reduced by child-care and attendant-care expenses over \$2,459 (federally)				
– reduced by child-care and attendant-care expenses over \$2,451 (provincially)				
Infirm dependants 18 and over <sup>(2)</sup>	4,198	630	4,186	253
– reduced by net income over \$5,956 (federally)				
– reduced by net income over \$5,950 (provincially)				
Caregiver amount <sup>(2)</sup>	4,198	630	4,186	253
– reduced by net income over \$14,336 (federally)				
– reduced by net income over \$14,321 (provincially)				
Adoption amount	10,909	1,636	10,835	656

Child tax credit (under 18)	\$ 2,089	\$ 313	\$ 0	\$ 0
Children's fitness	500	75	0	0
Eligible medical expenses, each 100 less three per cent of net income to a maximum of \$2,011 (federally) and \$2,010 (provincially)		15	100	6.05
Tuition credit <sup>(6) (7)</sup>	each 100	15	100	6.05
Education credit per month of qualified attendance <sup>(7)</sup>				
– full time	400	60	478*	29
– part time	120	18	143*	9
Textbook credit per month of qualified attendance				
– full time	65	10	0	0
– part time	20	3	0	0
Student loan interest credit	each 100	15	100	6.05
Pension income received to a maximum of <sup>f(4)</sup>	2,000	300	1,228*	74
Donations				
– first \$200	each 100	15	100	6.05
– excess <sup>(8)</sup>	each 100	29	100	11.16
Public transit pass	each 100	15	0	0
First-time home buyers' tax credit	5,000	750	0	0
Home renovation tax credit (2009 only)	9,000**	1,350	0	0
CPP (premiums paid) <sup>(9)</sup>	2,119	318	2,119	128
EI (premiums paid) <sup>(10)</sup>	732	110	732	44

\*\* the home renovation tax credit is only for expenses in excess of \$1,000.

Most personal tax credits, including the basic, spousal and amount for an eligible dependant, medical dependency, disability and age tax credits, are fully indexed to the annual inflation rate, as determined by the applicable consumer price index (CPI) rates for both Canada and Ontario. Indexation is designed to prevent Canadian taxpayers from being in a higher tax bracket solely because of an inflation-induced increase in salary.

Items marked with an asterisk (\*) are indexed in Ontario only.

1. Federal credits calculated at 15 per cent of gross amount, except donations over \$200, which are calculated at 29 per cent. Ontario credits calculated at 6.05 per cent of gross amount, except donations over \$200, which are calculated at 11.16 per cent. Both credits apply to reduce basic tax, before surtaxes and have a higher real value if surtaxes otherwise apply.

2. Where the dependant's net income is in excess of the indicated threshold, such excess will decrease the gross amount for purposes of calculating the credit.

The federal portion of the spousal and eligible dependant credits is eliminated when net income reaches \$10,320. The provincial portion of these credits is eliminated when net income reaches \$8,295.

The federal portion of the disability supplement for children under 18 is eliminated when child-care and attendant-care expenses reach \$6,657. The provincial portion of this credit is eliminated when net income reaches \$6,636.

The federal portion of the infirm-dependant credit is eliminated when net income reaches \$10,154. The provincial portion of this credit is eliminated when net income reaches \$10,136.

With the caregiver amount, the federal credit is eliminated when net income reaches \$18,534. The provincial portion is eliminated when net income reaches \$18,507.

3. The federal credit-for-age amount is reduced by 15 per cent of net income over \$32,312. The federal portion of this credit is, therefore, eliminated when net income reaches \$75,032. The provincial credit-for-age amount is reduced by 15 per cent of net income over \$32,280. The provincial portion of this credit is, therefore, eliminated when net income reaches \$61,187.
4. Age and pension credits may be transferred to a spouse or common-law partner to the extent not required by the taxpayer.
5. Disability credits may be transferred to a supporting person to the extent not required by that individual.
6. Must exceed \$100 per institution.
7. Federal tuition and education credits to a maximum of 15 per cent of \$5,000 and provincial tuition and education credits to a maximum of 6.05 per cent of \$6,142 (indexed) may be transferred to a spouse or common-law partner, parent or grandparent to the extent not required by the student. Alternatively, unused credits can be carried forward indefinitely by the student, although the outstanding balance must be reduced in future years as soon as adequate income is earned to absorb the credits.
8. To a maximum of 75 per cent of net income for all donations, including those made to the Crown or Crown agencies, except in the year of death or the immediately preceding year, when the ceiling is 100 per cent of net income.
9. Employee and employer contribution rates for CPP pensionable earnings in 2009 are each assessed at 4.95 per cent of pensionable earnings, up to a maximum of \$46,300 (up from \$44,900 in 2008), less a basic \$3,500 exemption. Self-employed individuals must pay both the employer and employee halves of this payment (a total of 9.9 per cent), but are entitled to a non-refundable tax credit for one-half of the premiums paid and a deduction from income for the other half.
10. The employee portion of EI premiums is assessed at \$1.73 per \$100 of insurable earnings in 2009, to a maximum of \$42,300 (up from \$41,100 in 2008).

## Appendix Ia: Ordering of Federal Non-Refundable Tax Credits

The *Income Tax Act* requires that the federal non-refundable tax credits be claimed in the following order:

- personal tax credits (i.e., basic personal tax credit, spousal- and eligible dependant tax credits and dependant/caregiver tax credits)
- age credit for an individual who has reached 65
- credit for employee contributions to CPP and employee premiums for EI
- credit for an individual who receives certain pension income
- credit for Canada employment income
- credit for adoption expenses
- credit for eligible long-term transit passes
- credit for child-fitness tax credit
- credit for severe and prolonged mental or physical impairment of:
  - (i) an individual; or
  - (ii) a dependant
- credit for unused tuition, education and textbook tax credits
- tuition credit for fees of a student enrolled at a designated educational institution
- the tax credit for a student enrolled in a qualifying educational program at a designated educational institution (i.e., enabled through the payment of child-care or attendant-care expenses)
- education and textbook tax credits
- credit in respect of unused tax credits for tuition, education or textbooks that are transferred to the student's parent or grandparent
- credit in respect of unused tax credits for tuition, education, textbooks, age, pension and mental or physical impairment of an individual that are transferred from the individual to the individual's spouse or common-law partner
- credit for medical expenses
- credit for charitable donations
- credit for interest on student loans
- credit in respect of the tax on dividends (see page 45, in chapter on Investment Income and Expenses).

**Appendix II:**  
**Components of the Canada Child Tax Benefit**

	<b>Maximum Benefit Effective July 1, 2009</b>
<b>Base Benefit</b>	
Basic amount per child	\$1,340
Additional benefit for third child and subsequent children	93
<b>NCB Supplement</b>	
First child	2,076
Second child	1,837
Third child and subsequent children	1,747
<b>Total CCTB benefit – Child seven years and over</b>	
First child	3,416
Second child	3,177
Third child and subsequent children	3,180
<b>Changes to the Income Thresholds of the Canada Child Tax Benefit</b>	
<b>Base Benefit</b>	
Start phase-out	40,726
<b>NCB Supplement</b>	
Start phase-out	23,710
End phase-out	40,726
<b>Child Disability Benefit (CDB)</b>	
Start phase-out	40,726



## Appendix III:

### Marginal Tax Rates – Federal and Ontario – 2009 and 2010\*\*

#### Marginal Tax Rates – Federal – 2009<sup>(1)</sup>

Taxable Income	Tax	On Next
\$ 0	\$ 0 +15%	\$ 40,726
40,726	6,109 +22%	40,726
81,452	15,069 +26%	44,812
126,264	26,720 + 29%	remainder

#### Marginal Tax Rates – Ontario – 2009<sup>(2)\*</sup>

Taxable Income	Tax	On Next
\$ 0	\$ 0 +6.05%	\$ 36,848
36,848	2,229 +9.15%	36,850
73,698	5,601 +11.16%	remainder

#### Marginal Tax Rates – Federal – 2010<sup>(1)</sup>

Taxable Income	Tax	On Next
\$ 0	\$ 0 +15%	\$ 40,970
40,970	6,146 +22%	40,971
81,941	15,159 +26%	45,081
127,022	26,880 + 29%	remainder

#### Marginal Tax Rates – Ontario – 2010<sup>(2)\*</sup>

Taxable Income	Tax	On Next
\$ 0	\$ 0 +5.05%	\$ 37,106
37,106	1,874 +9.15%	37,108
74,214	5,269 +11.16%	remainder

\*Not including Ontario surtax of 20 per cent on provincial tax between \$4,257 and \$5,370, and an additional 36 per cent, for a total of 56 per cent, on provincial tax above \$5,370, in 2009. These amounts will reduce to \$3,978 and \$5,091, respectively, in 2010.

See also Appendices IV and V.

\*\*Note that the calculated tax payable amounts are considered to be net of any personal deductions, including non-refundable tax credits, etc.

- (1) The increased tax bracket limits above assume a federal CPI formula-based adjustment of 0.6 per cent in 2010.
- (2) The increased tax bracket limits above assume a provincial CPI formula-based adjustment of 0.7 per cent in 2010.
- (1)(2) The indexation factor for 2010 is the percentage change in average CPI levels from October 1, 2008, to September 30, 2009, relative to the average CPI level between October 1, 2007, and September 30, 2008.

## Appendix IV:

### Top Combined Federal/Provincial Tax Rates – 2009

Province	Combined Top Marginal Rate <sup>(1)</sup>				
	Provincial/ Territorial Rate	Ordinary Income	Capital Gains	Eligible Dividend*#	Non-Eligible Dividend*##
Alberta	10.00%	39.00%	19.50%	14.55%	27.71%
British Columbia	14.70	43.70	21.85	19.92	32.71
Manitoba	17.40	46.40	23.20	23.83	38.21
New Brunswick	17.00	46.00	23.00	21.80	34.21
Newfoundland & Labrador	15.50	44.50	22.25	22.89	32.71
Northwest Territories	14.05	43.05	21.53	18.25	29.65
Nova Scotia	17.50	48.25	24.13	28.35	33.06
Nunavut	11.50	40.50	20.25	22.24	28.96
Ontario	11.16	46.41	23.20	23.06	31.34
PEI	16.70	47.37	23.69	24.44	38.15
Quebec	24.00	48.22	24.11	29.69	36.35
Saskatchewan	15.00	44.00	22.00	20.35	30.83
Yukon	12.76	42.40	21.20	17.23	30.49

\*Calculated on actual dividends, not grossed-up amount for tax purposes. These rates take into account changes based on the two-tier dividend tax structure that Ontario and other provinces have implemented. Check with your certified general accountant to confirm which dividend rates apply to you.

# Eligible dividends include those received from a public Canadian corporation and certain private, resident corporations that must pay Canadian tax at the general corporate rate.

## Non-eligible dividends include those received from Canadian-controlled private corporations (CCPC) that are not subject to the general corporate tax rate.

Provincial and territorial rates listed in this grouping are calculated independently of federal tax rates. In each case, lower rates apply to the lower income brackets. Note that Quebec residents receive an abatement of 16.5 per cent of the basic federal tax.

(1) Combined rates reflect the following provincial surtaxes:

Alberta – no provincial surtaxes

British Columbia – no provincial surtaxes

Manitoba – no provincial surtaxes

New Brunswick – no provincial surtaxes

Newfoundland & Labrador – no provincial surtaxes.

Nova Scotia – 10 per cent on provincial tax in excess of \$10,000

Ontario–20 per cent on provincial tax between \$4,257 and \$5,370, inclusive, and an additional 36 per cent, for a total of 56 per cent on provincial tax in excess of \$5,370

PEI–10 per cent on provincial tax in excess of \$12,500

Quebec–no provincial surtaxes

Saskatchewan–no provincial surtaxes

Northwest Territories–no territorial surtaxes

Nunavut–no territorial surtaxes

Yukon–five per cent on territorial tax in excess of \$6,000

Note: all Canadian provinces and territories, except Quebec, have adopted a “tax on income” (TONI) system of calculating provincial or territorial personal income tax. Quebec administers its own provincial taxes, as it has since 1954.

## Appendix V: Combined Federal and Ontario Marginal Tax Rates for 2009 and 2010

### Combined Federal and Ontario Marginal Tax Rates — 2009<sup>(1)(2)</sup>

Taxable Income*	Ordinary Income	Capital Gains	Eligible Dividend*#^	Non-Eligible Dividend***
At \$36,848	24.15	12.08	(3.21)	7.11
At \$40,726	31.15	15.58	6.94	15.86
At \$64,881**	32.98	16.49	7.45	16.86
At \$73,698	35.39	17.70	10.94	19.88
At \$76,442**	39.41	19.70	12.91	22.59
At \$81,452	43.41	21.70	18.71	27.59
At \$126,264	46.41	23.20	23.06	31.34

^ eligible dividend range of -3.21% to +2.54% at taxable income of \$36,848

### Combined Federal and Ontario Marginal Tax Rates — 2010<sup>(1)(2)</sup>

Taxable Income*	Ordinary Income	Capital Gains	Eligible Dividend*#^	Non-Eligible Dividend***
At \$37,106	24.15	12.08	(3.21)	7.11
At \$40,970	31.15	15.58	6.94	15.86
At \$65,038**	32.98	16.49	7.45	16.86
At \$74,214	35.39	17.70	10.94	19.88
At \$76,664**	39.41	19.70	12.91	22.59
At \$81,941	43.41	21.70	18.71	27.59
At \$127,022	46.41	23.20	23.06	31.34

^ eligible dividend range of -3.21% to +2.54% at taxable income of \$37,106

\*\*provincial surtaxes apply

\*Calculated on actual dividends, not grossed-up amount for tax purposes. These rates take into account the two-tier dividend tax structure. Check with your certified general accountant to confirm which dividend rates are applicable to you.

# Eligible dividends include those received from a public Canadian corporation and certain private, resident corporations that must pay Canadian tax at the general corporate rate. Note that negative rates of return for certain lower taxable income amounts, which may represent tax credits or refunds, are approximate figures only because federal tax and provincial/territorial tax are calculated separately and cannot typically be offset against one another.

## Non-eligible dividends include those received from Canadian-controlled private corporations (CCPC) that are not subject to the general corporate tax rate.

(1) Tax rates before personal credits are applied, except for Ontario surtax, denoted as a double asterisk (\*\*), which is net of the basic personal credit only. See the section on Federal and Ontario Non-Refundable Tax Credits, beginning on page 83, as well as Appendix I, beginning on page 123, for tax credit information. It is assumed each bracket is composed of ordinary income. The rate indicated is the marginal rate for additional income of the type noted.

(2) The increased tax bracket limits for 2010, on the previous page, assume a federal CPI adjustment of 0.6 per cent and a provincial CPI adjustment of 0.7 per cent in 2010.

The prior tables take into effect Ontario rates, using the TONI system introduced by the government in 2000. In 2009 and 2010, they are as follows:

<b>Taxable Income</b>	<b>2009</b>
To \$36,848	6.05%
Between \$36,848 and \$73,698	9.15%
\$73,698+	11.16%

<b>Taxable Income</b>	<b>2010</b>
To \$37,106	5.05%
Between \$37,106 and \$74,214	9.15%
\$74,214+	11.16%

The tables also take into account Ontario surtaxes of both 20 per cent (at income of \$64,881 in 2009 and \$65,038 in 2010) and 56 per cent (at income of \$76,442 in 2009 and \$76,664 in 2010).

Taxable income brackets are indexed annually by a formula based on the federal and provincial CPI increases. The above rates are, therefore, subject to change as a result of both that and measures brought forth in budgets introduced after the publication date.

## Appendix VI:

### Canadian Tax Planning and Filing Deadlines for Ontario Residents – 2010

#### First Quarter

January 15	<p>Deadline for employees who acquired qualified publicly listed shares under employee stock-option plans in 2009, to file a letter indicating their intention to defer related benefits.</p> <p>Deadline for employers to remit Ontario employer health-tax (EHT) instalment, covering December 2009.</p>
January 30	<p>Pay intra-family loan interest related to previous taxation year, to avoid income attribution.</p>
February 14	<p>Reimburse employer for company car operating costs, to reduce operating benefit for the previous calendar year (optional). Since February 14, 2010 falls on a Sunday, it would be prudent to complete this task no later than Friday, February 12.</p>
February 15	<p>Deadline for employers to remit Ontario employer health-tax (EHT) instalment, covering January 2010.</p>
February 28	<p>Last day to report personal use of car for previous calendar year if personal distance travelled was not greater than 20,000 kilometres and at least 50 per cent of the distance was for business purposes, in order to reduce standby charge for company car (optional). Since February 28, 2010 falls on a Sunday, it would be prudent to complete this task no later than Friday, February 26. For practical purposes, however, taxpayers who choose to make this report should really do so by mid-February.</p> <p>Last day to issue T4s, T4As and T5s to people and CRA. As February 28, 2010 falls on a Sunday, this deadline will automatically be extended until Monday, March 1.</p>
March 1	<p>Last day to make personal- and spousal-RRSP contributions applicable to previous taxation year.</p>
March 15	<p>First-quarter instalments due from taxpayers who are required to remit quarterly.</p> <p>Deadline for employers to remit Ontario employer health-tax (EHT) instalment covering February 2010.</p>
March 31	<p>File trust-income tax return for trusts with a December 31 year-end.</p>

## **Second Quarter**

- April 15      Deadline for employers to remit Ontario employer health-tax (EHT) instalment covering March 2010.
- April 30      File personal income-tax return for previous taxation year and remit balance due, if any, to CRA.
- File GST-rebate application for employee-related expenses deducted in previous taxation year.
- May 15      Deadline for employers to remit Ontario employer health-tax (EHT) instalment, covering April 2010. As May 15, 2010 falls on a Saturday, this deadline will automatically be extended until Monday, May 17.
- June 15      Second quarter instalment due from taxpayers who are required to remit quarterly.
- Due date for personal tax returns of individuals with self-employed business income, or spouses or common-law partners of taxpayers with self-employed business income. (Payment of tax balance still due April 30.)
- Deadline for employers to remit Ontario employer health-tax (EHT) instalment, covering May 2010.

## **Third Quarter**

- July 15      Deadline for employers to remit Ontario employer health-tax (EHT) instalment, covering June 2010.
- August 15      Deadline for employers to remit Ontario employer health-tax (EHT) instalment, covering July 2010. As August 15, 2010 falls on a Sunday, this deadline will automatically be extended until Monday, August 16.
- September 15      Third-quarter instalment due from taxpayers who are required to remit quarterly.
- Deadline for employers to remit Ontario employer health-tax (EHT) instalment, covering August 2010.

## **Fourth Quarter**

- October 15      Deadline for employers to remit Ontario employer health-tax (EHT) instalment, covering September 2010.

November 15	Deadline for employers to remit Ontario employer health-tax (EHT) instalment, covering October 2010.
December 15	Fourth-quarter instalment due from taxpayers who are required to remit quarterly.  Deadline for employers to remit Ontario employer health-tax (EHT) instalment, covering November 2010.
December 31	Annual tax instalment due from individuals whose chief source of income is farming or fishing and who choose not to remit quarterly.  Deadline for taxpayers 71 (born in 1939) to ensure 2010 contributions to their RRSP are made. It is also the deadline for such individuals to convert their RRSPs to either RRIFs or life annuities. (People in that situation should, however, consult a certified general accountant who practises personal financial planning, well in advance of that date, to discuss the various options available to them).  Deadline for taxpayers who qualify to have the operating-cost benefit with respect to an automobile used for employment, calculated as half the amount of the annual standby charge, to notify their employer in writing of such intentions.  Ensure tax-deductible fees (e.g., accounting, investment counsel, interest carrying charges and safety-deposit-box), expenses, (e.g., employee-related moving expenses) and credits (e.g., for charitable donations and medical expenses) for the current taxation year have been paid.



Appendix VII:  
 Prescribed Canada Revenue Agency Interest Rates on Overdue  
 and Unpaid Income Taxes

		Federal		
		Receiver General To	Payments From	All Other Purposes
2008 –	1st quarter	8%	6%	4%
	2nd quarter	8	6	4
	3rd quarter	7	5	3
	4th quarter	7	5	3
2009 –	1st quarter	6%	4%	2%
	2nd quarter	5	3	1
	3rd quarter	5	3	1
	4th quarter	5	3	1

## Appendix VIII:

### Glossary of Abbreviations and Acronyms

ABE	adult basic education
ABIL	allowable business-investment loss
ACB	adjusted cost base
AIDA	agricultural income-disaster assistance
AMPA	Agricultural Marketing Programs Act
AMT	alternative minimum tax
APF	agricultural policy framework
ATTC	apprenticeship training tax credit
AVC	additional voluntary contribution
CAIS	Canadian agricultural income-stabilization program
CCA	capital-cost allowance
CCPC	Canadian-controlled private corporation
CFBAS	Canadian farm business advisory services
CRA	Canada Revenue Agency
CCTB	Canada child tax benefit
CDB	child-disability benefit
CDNX	Canadian venture exchange
CDSB	Canada disability savings bond
CDSG	Canada disability savings grant
CESG	Canada education savings grant
CNIL	cumulative net-investment loss
CPI	consumer-price index
CPP	Canada pension plan
CRCE	Canadian renewable and conservation expenses
CSBIF	community small-business investment fund
DAP	disability-assistance payments
DOF	department of finance
DPSP	deferred profit-sharing plan
DRIP	dividend-reinvestment plan
DSLP	deferred salary-leave plan
DTC	disability tax credit
EAP	educational assistance payments
EHT	employer health tax
EI	employment insurance
EO	employee ownership
FCA	Federal Court of Appeal
FMV	fair-market value
FTC	foreign tax credit
GAAR	general anti-avoidance rule
GAINS	guaranteed annual-income system for seniors
GIC	guaranteed-investment certificate

GIS	guaranteed-income supplement
GST	goods and services tax
GSTC	goods and services tax credit
HBP	home-buyers' plan
HBTC	home-buyers' tax credit
HRTC	home renovation tax credit
HST	harmonized sales tax
IC	information circular
IPP	individual pension plans
IRS	Internal revenue service (U.S.)
ITC	investment tax credit
LDAP	lifetime disability-assistance payments
LIF	life-income fund
LIRA	locked-in retirement account
LLP	lifelong-learning plan
LP	limited partnership
LRIF	locked-in retirement-income fund
LSIF	labour-sponsored investment fund
LSVCC	labour-sponsored venture-capital corporation
LTT	land-transfer tax
MIA	mandatory inventory adjustment
MURB	multiple-unit residential building
NCB	national child benefit
OAS	old-age security
OCB	Ontario child benefit
OCCS	Ontario child-care supplement
OFFTS	Ontario focused flow-through share
OETC	overseas employment tax credit
OITC	Ontario innovation tax credit
OIA	optional inventory adjustment
PA	pension adjustment
PAR	pension adjustment reversal
PHSP	private health-services plan
PRIF	prescribed retirement-income fund
PSPA	past-service pension adjustment
PST	provincial sales tax
QFP	qualified farm property
QPP	Quebec pension plan

R&D	research and development
RCA	retirement-compensation arrangement
RDSP	registered disability savings plan
REOP	reasonable expectation of profit
RESP	registered education savings plan
RLIF	restricted life-income fund
RLSP	restricted locked-in savings plan
ROIF	research-oriented investment fund
RPP	registered pension plan
RRIF	registered retirement-income fund
RRSP	registered retirement-savings plan
RST	retail sales tax
SBC	small-business corporation
SIFT	specified investment flow-through
SIN	social-insurance number
SR&ED	scientific research and experimental development
TCC	Tax Court of Canada
TFSA	Tax-free savings account
TONI	tax on income
UCC	undepreciated capital cost
UCCB	universal child-care benefit
UL	universal life
VDP	voluntary-disclosures program
WITB	Working income tax benefit
WSIB	Workplace safety and insurance board

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## Certified General Accountants of Ontario

240 Eglinton Avenue East

Toronto, ON M4P 1K8

416-322-6520 or

1-800-668-1454

Email: [info@cga-ontario.org](mailto:info@cga-ontario.org)

[cga-ontario.org](http://cga-ontario.org)

[cga-yourcareer.org](http://cga-yourcareer.org)