DFK An Independent Member Firm of DFK Canada Inc. and DFK International

Newsletter

Summer 2009

COMMUNICATING WITH YOUR ACCOUNTANT MAKES $ENSE

Author: James K. Whittaker, CA, Partner, Teed Saunders Doyle & Co.

Communication is one of the most important factors of success. Whether it is the success of a relationship or the success of a team, if all the participants are not communicating and information is missing, the decisions that are made will tend to fall short of meeting the team's goals. Accountants and tax-payers are also a team and need to communicate. Clients who openly communicate with their accountants (not only their goals and achievements, but also their financial concerns, including debts) are more likely to benefit from simple tax planning strategies.

An example arose as I met with a couple who are owners and managers of a corporation. The company had a year-end in the early fall. Upon review, I noticed in the last couple of weeks of the year they had withdrawn a substantial amount of cash from the company in the form of dividends. This meant the amount had to be included on their personal tax returns for 2008 and much of the income was taxed at the highest tax rate. They had some excess funds in the company and figured they would pay off a personal line of credit.

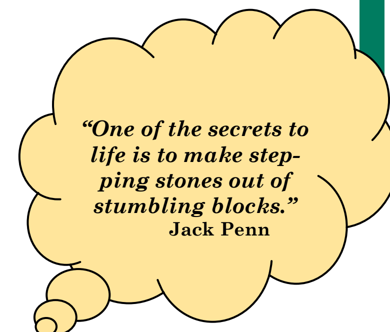
In this case, since they were both approaching the higher tax brackets before these dividends, they would have saved taxes simply by paying the balance off over two years - half when they did and the remainder in January - so that part of the income would have been included on their 2009 returns instead. The tax savings would have been between 8 to 10%. As it turns out, their interest rate on the line of credit at the time was only about 4.5%.

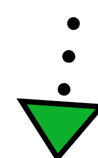
During a meeting with another client, it wasn't until we started talking about boating that I found out that he had a $40,000 loan outstanding on his boat. I was aware that he had a healthy unregistered investment portfolio. Based on this conversation and a call to his broker, we were able to access cash from his investment account through the realization of GICs and other near-cash investments and pay off his boat loan. He then set up an investment loan to put a similar amount of cash back into his portfolio, so that it could continue to grow. He now has about the same amount of debt, but the interest is deductible on his personal tax return because the related debt was incurred to finance the purchase of investments. Since he is in the highest tax bracket, the deduction gives him about a 47% tax savings on the interest he pays.

If you have not already discussed your complete financial situation with your accountant, now might be the time to do so. When you next meet, bring a summary of your debts, as well as your income and assets. If you anticipate a major purchase, you may also want to mention this. They can decide what is relevant, so be open. The more information they have, the more opportunities they have to identify for implementing tax saving strategies.

Inside this issue:

Communicating With Your Accountant Makes $ense	1
The Tax Implications of Moving	2
Income-Splitting Loans	3
Family Income Splitting	4





Special points of interest:

- ***Maximum RRSP limits:***
  2009 - $21,000
  2010 - $22,000
- ***The Harmonized Sales Tax (HST) comes into effect in B.C. on July 1, 2010. Is your business prepared?***
- ***Personal tax instalments:***
  - *September 15, 2009*
  - *December 15, 2009*
  - *June 15, 2010*

THE TAX IMPLICATIONS OF MOVING

Author: M. Earl MacLeod, CA, Partner, WBLI Chartered Accountants

With the ever-increasing mobility of the labour force, it is important to know what is and what is not eligible as a moving expense.

Deductible moving expenses are paid and incurred in respect of an eligible relocation, such as a taxpayer moving to carry on business, accept employment at a new work location, or attend a university, college, or other educational institution on a full-time basis. Both the old and new residences must be located in Canada, and the new residence must be at least 40 kilometres closer to the taxpayer's new work location than their old residence.

In addition to the costs of moving the family and household goods, eligible moving expenses include:

- Meals and lodging near either the old or new residence for a period not exceeding 15 days.
- Any costs incurred for cancelling a lease of the old residence.
- Costs in respect of the sale of the old residence.
- Legal fees and any tax, fee, or duty (not GST/ HST) imposed on the transfer or registration of title on the purchase of a new residence.
- Interest, property taxes, insurance, and utilities incurred for the old residence (max. $5,000) while it was unoccupied, not rented, and reasonable efforts were made to sell it.
- Costs related to changing addresses, replacing drivers' licenses, and utility connections and disconnections.

For taxpayers, other than students, the amount of deductible moving expenses cannot exceed the employment income from the new work location. For students, it cannot exceed the amounts received for scholarships, bursaries, or research grants in excess of research expenses.

In addition, any moving expenses reimbursed by your employer are not deductible and are not included in your income. Therefore, when negotiating with your employer, first consider the reimbursement of any moving expenses for items that are not eligible as deductible moving expenses (i.e., travel expenses related to house hunting trips, or additional travel back to the old residence in order to initiate or conclude its sale).

This planning should also be considered for non-resident employees moving to Canada for employment, because the Act only allows for deductions related to moves within locations in Canada. This may provide a means for the Canadian employer to reimburse the non-resident for these non-deductible moving expenses and not create taxable benefits.

An exception to the exclusion on international moves is available where a person, while not physically in Canada, is still resident in Canada for tax purposes. While this exception is very limited with respect to who it would apply to, it does open the door a little.

There is no requirement for the moving expenses to be deducted at the time of the change in employment. In the tax court case *Beyette v. MNR*, the taxpayer changed work locations in 1981 and physically moved in 1986. The deduction of the moving expenses was allowed even though it was several years later.

As well, in the case of *Jaschinski v. R.*, the taxpayer was able to deduct moving expenses related to his move from Calgary first to a temporary home in Mississauga and then eighteen months later to a permanent home in Campbellville. This was allowed by the courts because the taxpayer's argument was that the interim stay in Mississauga was only a stopover until a permanent home could be found.

It is important to know what is and what is not eligible as a moving expense.

INCOME-SPLITTING LOANS

Author: Dave Gautier, CA, KNV Chartered Accountants LLP

On June 3, 2009, the Canada Revenue Agency (CRA) announced that the prescribed interest rate used to calculate low interest loans will remain at 1%, effective from July 1 to September 30, 2009. The low prescribed rate makes tax planning using income-splitting loans an increasingly attractive opportunity.

Income-splitting opportunities exist when one family member is taxable at a lower marginal income tax rate than another. The goal of income splitting is to transfer income that would otherwise be taxed in the hands of the higher-rate taxpayer to the lower-rate taxpayer, resulting in the family paying less tax on an overall basis.

The *Income Tax Act* has income attribution provisions that discourage income splitting. However, if the higher-rate taxpayer were to loan the lower-rate taxpayer the money to purchase an income producing asset, with interest payable at the prescribed rate, the income earned on the investment would not be subject to the attribution rules.

The interest on the prescribed rate loan can be paid during the year and must be paid in full within 30 days of the end of the calendar year. The interest received will be taxed in the hands of the higher-rate taxpayer and the interest paid is generally tax-deductible to the lower-rate taxpayer.

For a loan advanced from April 1 to September 30, 2009, the prescribed rate will be 1% for the life of the loan. If you have an existing income-splitting loan, you may consider refinancing the loan prior to September 30, 2009.

EXAMPLE – INCOME SPLITTING USING A FAMILY TRUST

Mr. and Mrs. Jones have an opportunity to earn 8% by investing in a mortgage. They have $300,000 to invest, and both Mr. and Mrs. Jones have individual incomes over $126,265 per year from working at the family business—Jones Plumbing Ltd. They have three children living at home: Lisa, Michelle and Aaron. The Jones children have no income and are beneficiaries of the Jones Family Trust. (Note: The British Columbia maximum tax rate is used in these calculations.)

Option 1:
Mr. and Mrs. Jones invest in the mortgage.

	Mr. & Mrs. Jones
Investment income ($300,000 x 8%)	$24,000
Income tax @ 43.7%	(10,488)
After-tax proceeds	$13,512

Option 2:
Mr. and Mrs. Jones lend the money to the Jones Family Trust, and the Jones Family Trust allocates the income to the beneficiaries.

	Mr. & Mrs. Jones	Family Trust	Lisa	Michelle	Aaron
Investment income	$Nil	$24,000	$Nil	$Nil	$Nil
Interest at the prescribed rate	3,000	(3,000)	Nil	Nil	Nil
Net investment income	3,000	21,000	Nil	Nil	Nil
Income allocation		(21,000)	7,000	7,000	7,000
Income tax (Parents 43.7%; Children 20.1%)	(1,311)	Nil	(1,407)	(1,407)	(1,407)
Basic Personal Exemption	Nil	Nil	1,407	1,407	1,407
After-tax proceeds	$1,689	Nil	$7,000	$7,000	$7,000

The income-splitting loan will save the Jones family **$9,177** in taxes per year!

FAMILY INCOME SPLITTING

Author: Hugh Faloon, CA, CFP, TEP, Partner, Ginsberg Gluzman Fage & Levitz, LLP

For many years, income splitting has thrived as a basic tax planning technique by reducing a family's overall tax burden, thus increasing disposable income. The reason for this is that individuals in Canada are taxed separately, with graduated tax rates. For example, the tax on a single taxable income of $50,000 is significantly higher than the tax on two taxable incomes of $25,000. Income splitting, therefore, attempts to shift income that might be taxed at a high rate in one's hands to someone who will pay less tax.

Over the years, the Government has eliminated many of the possibilities for income splitting with income attribution rules. These rules eliminate the immediate benefits a taxpayer may achieve by transferring property to a spouse, or to a child under 18 years of age, causing the income generated from the transferred property to revert to the transferor.

If property is transferred to a corporation in which the spouse and minor children are shareholders, and the property is used in an active business, there is no attribution. However, if the property were used for investment purposes, there would be a deemed interest benefit to the transferor.

A wide range of income-splitting techniques are still available. The applicability of each one may be limited to specific family situations and objectives. Such techniques include:

- Using a family trust.
- Paying a reasonable salary to a spouse or child employed in a family business.
- Lending funds to family members for them to invest.
- Transferring property with capital growth to minor children.
- Transferring property to children over 18 years of age.
- Having Canada Pension Plan income split between spouses.
- Splitting your qualified pension income up to 50% with your spouse.
- Having the higher-income spouse pay all living expenses.
- Using Registered Education Savings Plans to save for a child's education.

Contact one of our tax experts for more information on family income splitting.

Some of KNV's participants in the 2009 Vancouver Sun Run. We are proud to have sponsored more than 50 runners and walkers representing our firm this year. We hope to have even more in 2010.

Phone: 604-536-7614
Toll Free: 1-800-761-7772
Fax: 604-538-5356

Located in:
White Rock, South Surrey, and Kelowna
www.knv.com

THE INFORMATION PROVIDED IN THIS PUBLICATION IS INTENDED FOR GENERAL PURPOSES ONLY. CARE HAS BEEN TAKEN TO ENSURE THE INFORMATION HEREIN IS ACCURATE; HOWEVER, NO REPRESENTATION IS MADE AS TO THE ACCURACY THEREOF. THE INFORMATION SHOULD NOT BE RELIED UPON TO REPLACE SPECIFIC PROFESSIONAL ADVICE.