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PERSONAL TAX

74(1)

CLAWBACK PLANNING

The clawback of Old Age Security ("OAS") for 2005 applied on income of \$60,806, with the full clawback at \$98,850.

Persons who have faced the clawback on their 2005 personal tax return may want to undertake some planning to avoid this extra cost in future years such as:

(a) **Income Splitting**

The OAS clawback applies to each spouse separately. Attention should be paid to income splitting possibilities with a spouse. One approach is applying for a division of Canada Pension Plan ("CPP") where the higher income spouse is receiving more CPP than the lower income spouse.

(b) **Transfer Assets**

Seniors with significant investment income may wish to transfer some of their capital to children or grandchildren, whether directly or through a Trust. Such a strategy should be carefully thought out, both to ensure the transferor retains enough assets for their spending requirements and to ensure any transfers do not create new tax problems. Alternatively, a senior could transfer

income-earning assets to an alter-ego or joint spousal trust, or to a corporation.

(c) **Avoid Dividends**

A \$100 dividend adds \$125 to net income, so it increases clawback by \$18.75 instead of \$15.00 (15 per cent). The 2006 Federal Budget proposals exacerbate this problem by causing the same \$100 cash dividend on a publicly traded security to add \$145 to income, and \$21.75 to clawback. If a senior can arrange to realize their investment income in the form of capital gains instead, only including half of the gains in income, their clawback could be reduced. (See 74(3) for more information.)

(d) **Shifting Income**

Perhaps the senior could arrange his/her finances to receive less income in some years, and more in others, to minimize clawback.

Similarly, dividends or salary from your own corporation could be structured to alternate between high and low income years.

(e) **Discretionary Deductions**

Where a senior has discretionary deductions, such as RRSP contributions or reserves on gains, consider claiming these in years where they will reduce the clawback.

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(f) **Apply Late**

When a person applies for OAS, they can receive payments for a few months prior to their application. A high income senior might wish to delay his/her application if his/her income is such that all the OAS would be clawed back in any case.

EMPLOYMENT INCOME

74(2)

TREASURY BOARD NON-TAXABLE TRAVEL ALLOWANCES

Effective December 5, 2005, the Treasury Board per kilometre rates are:

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	Effective Dec. 5, 2005	Effective Oct. 1, 2005	Effective Apr. 1, 2005	Effective July 1, 2004
Alberta	45.5	49.0	44.0	43.5
British Columbia	45.5	49.0	44.0	43.0
Manitoba	44.0	47.0	42.0	40.5
New Brunswick	45.5	49.5	44.5	43.5
Newfoundland and Labrador	49.0	52.5	47.5	47.5
Northwest Territories	52.5	54.5	49.5	49.0
Nova Scotia	46.0	49.5	44.5	44.0
Nunavut	52.5	54.5	49.5	49.0
Ontario	47.0	50.5	45.5	45.5
Prince Edward Island	45.5	49.0	44.0	44.0
Quebec	50.0	53.5	48.5	47.5
Saskatchewan	43.0	46.0	41.0	40.0
Yukon	55.0	57.0	52.0	50.5

The total meal and incidental allowance is \$74.65 per day.

For details see website http://www.tbs-sct.gc.ca/pubs_pol/hrpubs/TBM_113/tb-dv-c_e.asp.

Editor's Comment

This could be a starting point for providing travel allowances to employees.

EMPLOYEE BENEFITS

A summary of some low or non-taxable employee benefits listed in the CRA T4130 Guide include:

1. Board, lodging and transportation provided to an employee who works at a special or remote worksite (temporary duties).
2. Cellular telephones provided to an employee primarily to assist the employee in employment are non-taxable. However, the personal-use portion should be included in the employee's income.
3. Employee counselling services are not taxable if they relate to the wellness, mental or physical health of an employee or a relative, an employee's re-employment, or an employee's retirement.

4. Benefits provided to employees who have a disability are generally not taxable such as transportation costs between the employee's home and work location.
5. Merchandise sold to employees at a discount provides non-taxable benefits unless it is an arrangement to buy merchandise at less than cost.
6. Up to two non-cash gifts and awards per year are not taxable to a maximum of \$500 for gifts and \$500 for awards (including taxes).
7. Internet service provided at an employee's home is not taxable as long as the employer is the primary beneficiary of the service.
8. Moving expenses reimbursed when an employee is transferred are not taxable.
CRA considers a non-accountable allowance for incidental relocation moving expenses of \$650 or less to be a reimbursement and not taxable.
9. Payments under a Private Health Services Plan are not taxable.
10. If an employer pays professional membership dues on behalf of an employee, there is no taxable benefit to the employee if the employer is the primary beneficiary of the payment.
11. The use of a recreational facility or

- club is not taxable if it can be shown that the membership is principally for the employer's advantage.
12. The reimbursement of a spouse or common-law partner's travelling expenses is not taxable if he/she went at the employer's request and was mostly engaged in business activities during the trip.
 13. Subsidized meals are not taxable if the employee pays a reasonable charge that covers the cost of the food, its preparation, and service.
 14. Overtime meals, or a reasonable allowance for overtime meals, are not taxable if the employee works three or more hours of overtime after his/her scheduled hours of work and the overtime is infrequent and occasional (less than three times a week).
 15. A reasonable travel allowance for a salesperson is not taxable.
Also, not taxable is an allowance for travelling away from the municipality where the employee regularly reports to work.
 16. Training costs when the training is mainly for the employer's benefit are not taxable.
 17. Distinctive uniforms to be worn while carrying on employment duties or, special clothing (including safety footwear) designed to protect from employment hazards, are non-taxable. Reimbursed laundry or drycleaner services to clean these uniforms and clothing are also not taxable.
 18. Premiums paid to a wage-loss replacement plan or an income maintenance plan that are group plans are not taxable.

Caution: Owner-managers must receive these benefits in their capacity as employees - not shareholders.

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BUSINESS/PROPERTY INCOME

74(3)

NEW 2006 DIVIDEND PROPOSALS

Some points to consider with respect to the November 23, 2005 and the May 2, 2006 Federal Budget tax proposals on dividends from public companies and from high rate private company income after January 1, 2006 include:

1. the 45% gross-up and enhanced dividend tax credit could result in almost \$65,000 in dividends being received tax-free if there is no other income.

This assumes that the provinces follow the federal rules.

2. A disadvantage is that if a person receives Old Age Security, or other credits or income that are clawed back based on income, the enhanced gross-up on the dividends will increase income, thereby increasing the clawbacks.
3. The new rules are also proposed to apply to dividends paid after 2005 by Canadian-Controlled Private Corporations ("CCPCs") to the extent that their income is subject to tax at the general corporate income tax rate - and is not investment income eligible for a refundable dividend tax on hand. CCPCs may have to reconsider the practice of bonusing out income in excess of the annual business limit - \$300,000 for federal purposes.

This may result in CCPCs having two pools of earnings with different tax rules on dividends from each pool.

OWNER-MANAGER REMUNERATION

74(4)

CREDITOR PROOFING

Persons that are potentially subject to claims by third parties such as directors or professionals should consider, along with insurance, asset protection techniques such as:

1. loans made to corporations should be secured,
2. repayment of a loan should be several (not joint and several),
3. loans should be non-recourse,
4. a partner should be a limited, not a general partner,
5. real estate and other significant business assets should be owned by a sister corporation to the operating corporation that has the risk,
6. shares of an operating company should be held by a holding company so that dividends can be paid to remove the operating company's surplus and limit its exposure to creditors, and
7. if possible, a partnership activity should be carried out through a limited liability partnership.

2006 FEDERAL BUDGET

74(5)

On May 2, 2006, the Honourable Jim Flaherty, Minister of Finance, presented his first Budget to the House of Commons.

HIGHLIGHTS

A. PERSONAL INCOME TAX

Canada Employment Credit

For 2006, an individual will be entitled to deduct in computing tax the lesser of employment income and \$250, multiplied by the appropriate percentage for the

taxation year. (The \$250 increases to \$1,000 for 2007 and subsequent years.)

Capital Gains of Fishers

For a disposition on or after May 2, 2006 by an individual of a fishing property, a share of the capital stock of a family fishing corporation, an interest in a family fishing partnership or a qualified fishing property, the provisions of the Act relating to eligible capital property gains, capital gains reserves, replacement property rollovers, intergenerational rollovers from an individual to a child of the individual, trust rollovers from a spousal or common-law partner trust to a child of the individual and the lifetime capital gains exemption will apply to these fishing properties.

Tradespeople's Tool Expenses

An individual may deduct from employment income as a tradesperson, tool costs in excess of \$1,000, for eligible tools acquired on or after May 2, 2006.

Textbook Tax Credit

For the 2006 and subsequent taxation years, an individual who is entitled to the education tax credit will be entitled to claim a textbook tax credit equal to the product obtained when the appropriate tax rate percentage for the year is multiplied by \$65 for each month in the year in which the individual was entitled to claim the education tax credit as a full-time student, or \$20 for each month in which the individual was entitled to claim the education tax credit as a part-time student.

This is worth about \$80 per year for a full-time student.

Scholarship and Bursary Income

For the 2006 and subsequent taxation years, the total of all amounts received in the year on account of scholarships, fellowships, and bursaries may be excluded from income, if these amounts are received in connection with the

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individual's enrolment at a designated educational institution in a program in respect of which the individual may claim the education tax credit.

Pension Income Amount

For the 2006 and subsequent taxation years, the pension income on which the pension tax credit is calculated will be increased to \$2,000 from \$1,000.

Tax Credit for Public Transit Passes

For the 2006 and subsequent taxation years, an individual will be entitled to deduct an amount equal to the product obtained when the appropriate tax rate percentage for the year is multiplied by amounts paid in respect of eligible public transit passes in respect of transit on or after July 1, 2006 for the use of the individual, the spouse or common-law partner, or a child of the individual who has not before the end of the taxation year attained the age of 19 years. This includes a public transit pass that is valid for a period of at least one month of public transit.

Dividend Tax Credit

The federal dividend gross-up will be increased to 45 per cent and the individual tax credit will be adjusted to 11/18ths of the gross-up in respect of certain taxable dividends ("eligible dividends") paid after 2005. (See 74(3) for more information.)

Donations of Publicly Listed Securities and Ecologically Sensitive Land

These gifts made by a taxpayer to a qualified donee on or after May 2, 2006 will not be subject to taxable capital gain treatment.

B. BUSINESS INCOME TAX

General Corporate Income Tax Rate

This rate will be reduced to 19 per cent

from 21 per cent by 2010.

Corporate Surtax

This surtax will be eliminated for taxation years that end after December 31, 2007, with proration for taxation years that include that date.

Small Business Deduction Limit

The small business income eligible for the 12% tax rate will be increased to \$400,000 from \$300,000 as of January 1, 2007.

Small Business Rate

The small business deduction rate will be reduced for taxation years that end after 2007 to 11.5% in 2008, and 11% after 2008.

Federal Capital Tax

This tax will be eliminated effective January 1, 2006.

Apprenticeship Job Creation Tax Credit

For the 2006 and subsequent taxation years, a taxpayer will be allowed an investment tax credit in respect of each eligible apprentice employed in the business after May 2, 2006 equal to the lesser of \$2,000 and 10% of eligible salary and wages payable in respect of the employment.

The Budget also proposes a new \$1,000 grant for first and second year apprentices effective January 1, 2007.

Farming

Budget 2006 provides \$1.5 billion in 2006 including \$500 million for farm support, plus a one-time investment of \$1 billion to assist farmers in the transition to more effective programming for farm income stabilization and disaster relief.

C. EXCISE TAX ACT

GST Rate Cut

The 7% Goods and Services Tax ("GST")

will be cut to 6% effective July 1, 2006.

GST Transitional Rules

The Budget includes transitional rules for transactions occurring close to or straddling the July 1, 2006, implementation date.

Repealing the Excise Tax on Jewellery

Budget 2006 proposes to repeal the excise tax on jewellery effective May 2, 2006.

Reducing Excise Duties for Canadian Vintners and Small Brewers

Budget 2006 proposes to provide excise duty relief to wines made from 100-per cent Canadian-grown product. Excise duty reductions for small brewers are also proposed.

These measures will be effective July 1, 2006.

D. UNIVERSAL CHILD CARE

Families

Budget 2006 introduces the Universal Child Care Benefit as of July 1, 2006. This new benefit will give families \$100 per month per child under age 6. This will be taxed in the hands of the spouse with the lower income but, will not reduce federal income-tested benefits.

Families who receive the Canada Child Tax Benefit ("CCTB") will receive the new benefit automatically.

Families who do not receive the CCTB will be able to apply for the new benefit by submitting a completed CCTB application form to the Canada Revenue Agency.

Children's Fitness Tax Credit

The Budget proposes to introduce, effective January 1, 2007, a tax credit to promote physical fitness among children. For each child under 16, the credit will be provided on up to \$500 in eligible fees for

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programs of physical activity.

ESTATE PLANNING

74(6)

SPOUSAL RRSP

In a June 30, 2005 External Technical Interpretation, CRA notes that where funds are withdrawn from a Spousal RRSP and the annuitant's spouse has contributed to a Spousal RRSP for that person in the year of withdrawal or in the two previous years, the amount withdrawn attributes back to the contributor.

However, where the funds from the Spousal RRSP are rolled into a Registered Pension Plan, the attribution rules will not apply. Also, periodic retirement benefits from the RPP will not attribute back.

BULLION AS A QUALIFIED INVESTMENT

In a December 5, 2005 External Technical Interpretation, CRA notes that new Regulations permit investments in gold and silver bullion coins, bars and certificates for RRSPs and other deferred income plans after February 22, 2005 if certain conditions are met.

MARRIAGE BREAKDOWN

74(7)

SUPPORT PAYMENTS

In December, 2005, CRA released Guide P102 - Support Payments.

The Guide reviews the tax rules on support payments, registering your Order or Agreement, source deduction adjustments, specific purpose payments, payments to and from non-residents, and reporting requirements.

If there is no court order or written agreement, the spousal support payments are not included in income by the recipient

or deductible by the payer.

Also, child support agreements made after April, 1997 will not be deductible/taxable to the payer/recipient. Pre-May 1997 agreements will also have this non-deductible/non-taxable status if both persons elect to have this occur or the Order or Agreement is changed after April, 1997 to increase or decrease the child support amounts.

A unilateral change by the parents may not be sufficient as the parties cannot unilaterally waive the rights of a child.

GST

74(8)

GST/HST WEB REGISTRY

As part of their obligations under the GST/HST, registrants are required to ensure that Input Tax Credits are claimed only where suppliers are registered for GST/HST. Previously, the sole means available to verify this was to contact Canada Revenue Agency.

The February 23, 2005 Federal Budget proposed a publicly accessible web-based GST/HST Registry. This has now been activated and the link is:

https://www.businessregistration-inscriptionentreprise.gc.ca/ebci/brom/registry/registryPrompt_en.jsp

After entering a GST/HST number, business name, and date of transaction, the system will tell you whether the person was registered for GST/HST on that particular date.

This could also be valuable for real property transactions where a vendor needs to confirm that the purchaser is registered so that the vendor will not be required to collect GST/HST on the sale.

WEB TIPS

74(9)

HEALTHY EATING

You might want to check out this quick health link for diet and fitness information www.fitday.com.

Included in this website are:

- a diet & fitness journal,
- a calorie & nutrition counter,
- a weight loss tracker.

When using this free system, you are able to select the items that you have eaten during a given day. The program will then provide a break down of the different types of fats, carbs, proteins and alcohols in your system and compare it to items such as your age, weight, and daily physical activity level. From this you will be able to track your daily intakes by category and find the right patterns for healthy eating and/or weight loss.

DID YOU KNOW...

74(10)

CROSSING THE BORDER WITH \$10,000 OR MORE

Under new legislation, a person has to report to Canada Border Services Agency ("CBSA") amounts equal to or greater than Can. \$10,000 or its equivalent in a foreign currency, that you are bringing into or taking out of Canada by completing Form E677, Cross-Border Currency or Monetary Instruments Report - Individual.

If the currency or monetary instruments are not your own, you must complete Form E667.

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If you are sending \$10,000 or more into or out of Canada through the mail, you must complete Form E667.

If you are sending the \$10,000 by courier, the courier must have the person in charge of the conveyance complete Form E668 and attach it to Form E667.

Failure to report the transfer may include forfeiture and penalties ranging from \$250 to \$5,000.

CBSA sends the Forms to the Financial Transaction and Reports Analysis Centre of Canada (FINTRAC) for assessment and analysis. See www.fintrac.gc.ca or call 1-

800-461-9999.

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