GALLOWAY BOTTESELLE & COMPANY

Professional Services Group

The Abacus

ISSUE 62

PROFESSIONAL **STRENGTH** PERSONAL **SERVICE** PRACTICAL **SOLUTIONS**

New tax benefits for families with children

ON OCTOBER 30, 2014, Prime Minister Harper and Finance Minister Joe Oliver announced three new tax benefits for families with children.

TAX BENEFIT 1

Family Tax Cut

This change, announced publicly as '*income splitting*' is not actually income splitting, though it will have the same economic effect to the family unit.

Under our progressive tax system, a family's income is taxed at a higher rate if one spouse earns, say, $100,000 and the other spouse earns nothing, as opposed to each one earning $50,000.

The new Family Tax Cut is designed to reduce or eliminate this difference. It is available only to couples (including common-law partners) with children under 18. It takes effect in the 2014 taxation year.

The new rule does not actually permit income splitting. The spouse earning $100,000 cannot transfer $50,000 of that income to his or her spouse for tax purposes (as can be done with pension income since 2007). Instead, a calculation is done as if up to $50,000 of the income was earned by the lower-income spouse, and either spouse can claim a credit, reducing federal tax by up to $2,000 (typically, the higher-income spouse would claim the credit, but either spouse can).

TAX BENEFIT 2

Increased and expanded Universal Child Care Benefit

The Universal Child Care Benefit (UCCB) is a $100 monthly payment to parents of children under six. It is taxable to the lower-income spouse, or for a single parent, in the child's hands (so that no tax is normally payable). The UCCB theoretically allows parents to pay for child care, but there are no strings or conditions attached to it, and taxpayers can spend it on whatever they like.

The UCCB is being increased from $100 to $160 for children up to age six, and will be introduced as a $60 monthly payment for children age six to 17. Again, there are no conditions or restrictions on how these funds are used.

These increases of $60 per month for every child aged 0 to 17 will take effect January 2015, but will not start being paid until July. One effect of this postponement is that the higher UCCB will not affect the federal government's budget for the year ending March 31, 2015. More important politically is that parents will receive a cheque for $420 per child (accumulating seven months of payments) in July 2015, conveniently just around when a federal election is called. A family with three children under 18, for example, will get an extra $1,260 in July, and $180 each month after that, in addition to what they were already receiving.

As a result of the enhanced UCCB, the regular child tax credit will be repealed, effective for 2015. However, the **Family Caregiver Credit** that applies to infirm minor children will continue to apply.

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Moving from Canada

TAX IMPLICATIONS

IF YOU CEASE to be resident in Canada for income tax purposes, there may be significant and possibly adverse income tax consequences. The main culprit is a rule in the Income Tax Act that deems you to have disposed of most of your property for fair market value proceeds when you cease to be resident, with some exceptions as noted below. You are also deemed to re-acquire the property at a cost equal to the same fair market value.

The deemed disposition can result in capital gains or losses, depending on the current value of your property when you leave Canada relative to its cost to you. The income (or loss) resulting from the deemed dispositions is reported on your income tax return for the year of your departure from Canada. The resulting tax, if any, is sometimes referred to as Canada's '*departure tax*'.

One piece of good news is that you can usually defer paying the departure tax until you actually dispose of the property (which could be years down the road). If the income resulting from the deemed disposition is $50,000 or less, you can defer paying the tax without providing security (technically, you can defer without security if the resulting tax is less than the tax that would be applied to $50,000 of taxable income, using the highest marginal rate of tax). If the resulting income (tax) is greater, you must provide acceptable security with the CRA in order to defer the payment of the tax. Either way, you do not have to pay interest on the tax owing.

EXEMPTED PROPERTIES

As noted above, certain properties are exempted from the deemed disposition rule. Notable properties that are exempted include:

- **Real property** (real estate) in Canada (Your gain will be taxed when you later dispose of the property as a non-resident.);
- **Property used in a business** carried on through a permanent establishment in Canada (same);
- **If you were a resident of Canada** for 60 months or less in the 120 months before your departure from Canada, any property owned when you formerly became resident in Canada, and any property inherited by you during the period of residence; and
- **Certain other** '*excluded rights or interest*', such as your interests in pension plan, RRSP, RRIF, and similar plans.

However, if you make an election in your tax return, any property in the first two categories (real property in Canada, property used in a business in Canada) can be subject to the deemed disposition rule. The election could be beneficial if the deemed disposition results in a loss, which could be used against other capital gains (whether incurred in the year or as a result of the departure tax). The election can also be beneficial if the disposition of property results in a gain, if you have losses that can be applied to offset the gain, as the rule will result in a higher cost of the property for future Canadian income tax purposes.

When you later sell property that was subject to the deemed disposition rule, you may be subject to tax in your new country of residence (foreign tax) if the sale results in a gain. In such case, you can claim a foreign tax credit for Canadian income tax purposes for the foreign tax in respect of the portion of the gain that was taxable in Canada on your departure (i.e. the accrued gain up to your date of departure). The tax credit is allowed if the property is not real property and you are taxed in your country of residence that has a tax treaty with Canada. Furthermore, a tax credit is allowed if the property is real property in another country and the tax is paid to the other country, or to the country in which you are resident and that country has a treaty with Canada.

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MOVING FROM CANADA CONT'D FROM P. 2

Conversely, if you later sell the property at a loss and the property is '*taxable Canadian property*', the loss can be carried back to reduce or offset the gain that resulted from the deemed disposition of the property

on your departure from Canada. Taxable Canadian property includes items such as real property in Canada, and shares or interests in corporations, partnerships, or trusts, where the value of your shares or interests is primarily attributable to real estate or resource properties in Canada.

If you subsequently return to Canada and become resident, you can elect to effectively override the gain from the deemed disposition of property that applied on your departure. Effectively, this means that the gain from the deemed disposition is ignored, and your original cost of the property is restored.

INFORMATION REPORTING FOR YEAR OF DEPARTURE

In order to provide the CRA with information with respect to the departure tax, you may be required to file Forms T1161 and T1243 with a list of your properties by the filing due-date for the year of departure (April 30 of the following year, or June 15 if you or your spouse carry on business). Form T1161 is required only if the fair market value of your '*reportable properties*' at the time of departure exceeds $25,000. Reportable properties do not include Canadian cash, most '*excluded rights or interests*' (as described above), or personal-use property worth less than $10,000.

Incidentally, you should not think that because you have left Canada, you can safely ignore your Canadian tax obligations. If you have an unpaid tax debt, there are several ways the CRA can collect the debt. These include:

1 **Seizing any assets** or financial accounts you have left in Canada;
2 **Garnishing any debts owed** to you by anyone in Canada, including pension payments;
3 **Assessing any family member** to whom you transfer assets, including assets transferred to your heirs on your death; and
4 **Asking the tax authority** of another country to enforce the Canadian tax debt under its tax collection mechanisms, if Canada’s tax treaty with that country permits it. ■

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TAX BENEFIT 3

Increased child care expense limits

Child care expenses can generally be deducted by the lower-income spouse, up to a limit of two thirds of '*earned income*' and subject to certain dollar limits. These dollar limits have not increased since 1998 (since 2001 for disabled children):

- $10,000 per severely disabled child: ($250 per week)
- $7,000 per other child under seven ($175 per week)
- $4,000 per other child age seven to 16 — and infirm dependent children over 16 ($100 per week)

Note that the expenses do not have to be incurred for the child in question. For example, if the family has two children age three and 12, then the dollar limit is $11,000 even if all the child-care costs are paid to care for the three-year-old.

The new announcement makes small increases in these amounts:

- $11,000 per severely disabled child ($275 per week)
- $8,000 per other child under seven ($200 per week)
- $5,000 per other child age seven to16 — and infirm dependent children over 16 ($125 per week)

These changes will automatically result in increases to the '*periodic*' child-care expense limits, which apply to boarding school or camp or where the higher-income spouse can claim the expenses because the lower-income spouse is in school, prison or hospital. Those limits are 1/40th of the annual limit per week. ■

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Testamentary trusts

Last year for preferential taxation

Testamentary trusts are trusts that arise on your death, such as those made under your will.

HISTORICALLY, testamentary trusts have been taxed preferentially relative to *inter vivos* trusts (trusts set up during your lifetime). The tax preferences include:

- Testamentary trusts are subject to the same graduated tax rates that apply to other individuals (whereas *inter vivos* trusts are subject to a flat tax at the highest marginal rate). Thus, for example, if you set up multiple trusts under your will, you can engage in post-mortem income splitting;
- Testamentary trusts can have an off-calendar fiscal period and taxation year;
- They are not required to make quarterly tax instalments;
- They are allowed a $40,000 exemption under the alternative minimum tax; and
- They can flow out investment tax credits and certain other amounts to their beneficiaries.

Unfortunately, this is the last taxation year that these tax preferences will apply. Beginning in 2016, the tax preferences will not apply to testamentary trusts (other than '*graduated rate estates*', below). As such, testamentary trusts will generally be subject to the same tax rules that apply to *inter vivos* trusts.

The tax preferences will continue to apply to graduated rate estates. Basically, a graduated rate estate is the estate of an individual for up to 36 months after the individual's death. After the 36 months, the tax preferences will no longer apply. An individual can have only one graduated rate estate.

In addition, a testamentary '*qualified disability trust*' will continue to be subject to graduated tax rates. A trust can qualify as such if a beneficiary under the trust is eligible for the disability tax credit. ■

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