

2009 Year End Tax Planning Considerations

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The end of another year is upon us once again. And while tax planning is a year-round activity and a vital component of the financial planning process, now is the time to pay special attention to various tax issues in advance of the end of the 2009 taxation year. The following outlines some common tax planning ideas and items that may need to be addressed, as well as some considerations for 2010.

Personal Planning Opportunities

- Year End – Tax Loss Selling
- Registered Plans
- Personal Payments
- Transit Pass Tax Credit
- Home Renovation Tax Credit
- Mutual Fund Purchases
- Non-deductible Interest on Your Loans
- Allocating Pension Income to your Spouse
- Estate Planning
- Stock Option Deferral
- Tax Shelters

Corporate Planning Opportunities

- Shareholder Loans
- Capital Gains Exemption
- Allowable Investment loss (ABIL)
- Salary
- Business Income Reserve
- Capital Gains Rollover

Note: These points are general and brief, and not applicable to all situations. Consult with your own tax advisor before implementation of any of these strategies to determine if any of these options are relevant and prudent as it pertains to your own specific situation.

Year End -Tax Loss Selling:

1. Tax loss selling to crystallize Unrealized Capital Losses:

As we approach the end of the 2009 personal taxation year, it is just about that time to review your portfolio in an effort to identify positions currently trading at a loss that may be sold in order to take advantage of the associated tax benefit. This is the time for you to sell positions that may be used to offset taxable gains.

Note: Canada's tax rules require sellers to wait at least 30 days before repurchasing the same security in order to be able to claim the full amount of the capital loss.



2. Utilizing previous Realized Capital Losses:

The simplest remedy to offset Capital Gains is with realized Capital Losses within your portfolio. Capital Losses are generated by selling securities and/or mutual fund units for less than the cost at which they were acquired. If these losses are currently available, then they can be used to directly offset the capital gains generated from other stock in your portfolio. As a rule, Capital Losses do not expire and thus can be carried forward indefinitely and applied to offset capital gains generated in the future, or back to prior years.

3. Transferring Unrealized Capital Losses from spouse or common-law partner:

A more complex version of tax loss selling is using the Unrealized Capital Losses of a spouse or common law partner. This might be an attractive option if an individual does not have Capital Losses themselves. In short, to be able to access Capital Losses of a spouse (or a common law partner) the capital loss can be transferred by selling the security on the open market at fair market value, and then having your spouse reacquire the same security. Although a superficial loss will be triggered, your spouse will be able to use this loss on his/her own tax return. Given that the mechanics of this type of transaction has a higher degree of complexity and requires that certain conditions be met and adhered to, we strongly advise that you contact your own tax accountant/tax advisor for more details of this strategy in order to find out if this alternative is a suitable option for you.

4. Utilizing Future Capital Losses:

In the event that investors have no Capital Losses to utilize, you should keep in mind that Capital Losses can be carried back three years to offset any capital gains in those years and recover some of the taxes already paid. Thus, if in the coming years you have Capital Losses, they can be carried back and used against the capital gain realized in the 2009 taxation year. It is important to note that dispositions of securities by individuals that are repurchased by their RRSP will be subject to the superficial loss rules.

Remember, in order to maximize any of the above-mentioned tax loss selling strategies, consider deferring sales of securities with gains until January 2010 (this strategy could also be used to defer tax in instances where there are no accumulated losses).

Year End Securities Trading Considerations:

- Final trade date for security transactions for Toronto trades is December 24, 2009.
- Final trade date for securities transactions through New York is December 28, 2009.
- Key: Settlement must take place not later than December 31st.
- Consider delaying the purchase of annual pay/accrual fixed income securities (e.g. 1 year T-Bill or annual pay GIC) until 2010, thereby deferring the taxation of the income by a year.
- Election to defer the income inclusion of stock option benefits must be filed with the individual's employer by January 15, 2010 (Form T1212).



Registered Plans:

- Deadline for 2009 RRSP contributions is March 1, 2010.
- **Reminder:** The annual contribution limit for 2009 is the lesser of 18% of 2008 earned income up to a maximum of \$21,000, less the Pension Adjustment for 2008. The 2008 Notice of Assessment will indicate the allowable amount along with any unused amounts from prior years.
- If the annuitant turns 71 in 2009, RRSPs must be terminated and, to avoid being fully taxable in 2009, converted to a RRIF and/or annuity by December 31.
Note: Contributions to the plan must be made by December 31 - not 60 days after year end - as the plan won't exist after December 31. Where the individual still has contribution room, contributions can continue to be made to a spousal plan if the individual's spouse is not over 71.
- The RRSP limit for 2009 will be \$21,000.
- The over contribution limit is \$2,000. If this is exceeded the penalty is 1% per month.
- As of January 2, 2009, residents of Canada aged 18 and older can save up to \$5,000 every year in a Tax Free Savings Account (TFSA). All income (interest, dividends and capital gains) earned in your TFSA is tax-free for life. You can withdraw from your TFSA at any time, for any reason and all withdrawals are also tax-free. Consider maximizing the remaining amount of contribution room for 2009 and take steps to make an additional \$5,000 contribution anytime after Jan 1st 2010 for the 2010 taxation year.
- Contribute to RESPs no later than December 31 to maximize the income deferral and benefit from the Canada Education Savings Grant (20% of contribution to maximum of \$500 per year if beneficiary is under 18).
Note: The maximum lifetime contribution limit is \$50,000 per beneficiary.

Personal Payments

- Final tax installment payment for 2009 is December 15.
- Remember: In addition to non-deductible interest on late or deficient installments (currently 5%), if your installment interest charges are more than \$1,000 the penalty is calculated by first determining which is higher, \$1,000 or one-quarter of the installment interest. Then the higher amount is subtracted from the installment interest and the difference is divided by two.
- Interest on intra-family loans (generally at the prescribed rate) must be paid by January 30, 2010 to avoid income attribution. Consider new arrangements while the prescribed rate is low – currently 1%
- Charitable donation payments must be made before the end of the year. The maximum annual claim is 75% of net income. Unused amounts can be carried forward up to five years. Where publicly listed shares are donated, the gain is no longer taxable.
- Eligible medical expenses can be claimed for any 12 month period ending in the calendar year. Only amounts in excess of the lesser of 3% and \$2,011 are eligible.
- A Reminder for parents of children under the age of 16, who are entitled to a non-refundable tax credit of up to \$500 for each child registered in an eligible program of physical activity.



- Other payments that must be made by December 31 to be considered in the 2009 tax return include:
 - Investment management & custody fees
 - Loan interest
 - Safety deposit box
 - Alimony/maintenance payments
 - Political contributions
 - Tax shelter payments
 - Moving expenses
 - Tuition fees
 - Child care
 - Professional fees
 - Review family trusts for any action that's required by December 31 2009.

Transit Pass Tax Credit

A non-refundable tax credit is issued for the cost of public transit passes (yearly, monthly, weekly and cost-per-trip electronic cards) provided that certain conditions are met. The amount claimed is multiplied by the lowest personal income tax rate for the year (currently 15%) and then deducted from the amount of taxes otherwise payable.

Home Renovation Tax Credit

Earlier this year, the federal government introduced a new tax credit called the "The Home Renovation Tax Credit" (HRTC) which is based on eligible expenses for improvements to your house, condominium or cottage. It can be claimed on your 2009 income tax return and applies to eligible purchases made only after January 27, 2009, and before February 1, 2010.

The HRTC applies to eligible expenses of more than \$1,000, but not more than \$10,000, resulting in a maximum non-refundable tax credit of 15% which is equal to a tax savings of \$1,350. The HRTC will not be reduced by other government tax credits, grants, or incentives that you may be entitled to.

Mutual Fund Purchases:

Defer the purchase of non-registered mutual fund units near the year-end to avoid having to report year-end distributions.

Non-deductible Interest on Your Loans:

If you have investments outside a RRSP or RRIF, consider liquidating some of the investments (calculating the tax cost first) and use the proceeds to pay down the debt. Then re-borrow to replace the investments.



Allocating Pension Income to Your Spouse:

You are able to allocate up to one-half of your income that qualifies for the existing pension income tax credit to your resident spouse/common-law partner. This may result in greater after tax income from your retirement plans.

Pension eligible income will vary depending on age:

For people age 65 and older,

Eligible Pension Income: includes payments from a registered pension plan (RPP – a pension from an employer-sponsored defined benefit plan or a defined contribution plan), income from a registered retirement savings plan (RRSP) annuity, a registered retirement income fund (RRIF), a LIF (a locked-in RRIF), or a deferred profit sharing plan (DPSP) annuity.

For individuals younger than 65:

Eligible Pension Income: includes only payments from a registered pension plan (RPP – defined benefit or defined contribution).

Note: Ineligible Pension Income: includes guaranteed income supplement (GIS), old age security (OAS), RRSP withdrawals and income from retirement compensation agreements (RCAs).

Estate Planning

Do you need to update your Will? Do you know what taxes your estate will be burdened with upon your death? Why wait to make it a New Year's resolution to get your estate planning in order, take the initiative now, and consult with your legal advisor.

Stock Option Deferral

Stocks acquired (through stock option plans) but not sold during 2009 can have the benefit deferred on amounts up to \$100,000 in total fair market value (based on the fair market value at the time the options were granted) Your employer must be notified of your wish to defer before January 15, 2010.

Tax Shelters

Tax shelters are by their very nature a known means of reducing income taxes. More importantly as the year end approaches, many of these shelters are aggressively marketed to many Canadians. The most important aspect of a tax shelter is the quality of the product and not the immediate tax savings that may be had. Thus before making any decisions about investing in a tax shelter, no matter how simplistic they seem and no matter how enticing they are, you should consult with your own tax professional before doing so.



Corporate Planning Opportunities:

If you are an owner/manager of a Canadian private corporation, there are some planning opportunities uniquely available to you.

Shareholder Loans:

Shareholder loans not repaid before the year-end may result in the full amount of the loan being fully taxable on your 2009 tax return. If the loan was made to help with the purchase of a home, automobile for work, or corporate shares an exemption would apply.

\$ 750,000 Capital Gains Exemption (LCGE)

Shares of a qualified small business corporation, fishing property and farm property (including shares of a corporation or partnership interest) still qualify for the lifetime capital gains exemption. This exemption has been increased from \$500,000 to \$750,000 for taxable capital gains after March 18, 2008. You should consult with your own tax advisor/professional since if you have any outstanding cumulative net investment loss (CNIL) or active business investment losses (ABIL) may affect the amount and use of the capital gains exemption.

Allowable Business Investment Loss (ABIL)

If you have an ABIL, you will be able to reduce your overall taxable income. An ABIL is simply a loss on shares and/or debt you own of a small business corporation. The benefit of an ABIL versus a capital loss is that an ABIL can be used to reduce one's overall income as opposed to a capital loss that can only be used to reduce capital gains.

Be mindful that the administration, paperwork and requisite documentation including the overall financial details must be in place prior to claiming the ABIL on your tax return. As with most tax filings, prudent preparation and planning will go a long way to ensuring that the ABIL is claimed properly on your tax return and readily accepted by CRA.

Salary

Review with your tax advisor on the optimal mix of salary and dividends for you (and if applicable) other family members for 2009 taxation year. Pay a reasonable salary to a spouse or child who is in a lower tax bracket that provides services to your business.

Business Income Reserve

If you sold goods in 2009, but don't receive the proceeds of the sale of those goods until after the end of the year, you may be in a position to claim a reserve over a maximum of three years.



Capital gains rollover

If you sold or will be selling eligible small business investments in 2009, invest the proceeds in other eligible small business investments by April 30, 2010 to be eligible to defer all or part of the capital gain.

Note

It is strongly recommended that you engage your own tax advisor/accountant to review the above-noted corporate planning considerations before strategically engaging in the implementation of any of them.

The commentary and/or information provided herein should not be construed as legal or tax advice. Clients are strongly encouraged to seek the expertise of independent professionals, such as tax, legal and accounting experts prior to the final implementation of any strategy. Only after a diligent analysis of the client's needs, objectives and financial position and tolerance for risk can an appropriate recommendation be made.

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