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Navigating Your Tax Return

Taxation Bulletin – *February, 2008 Version*

introduction

By Doug Brodhead, Assistant Director of Public Policy, PLAN

As families across Canada brace themselves for tough economic times, it has become even more important to capitalize on any deductions, credits, and rebates that you may be eligible to receive. The wind down from the holiday season often forces many of us to begin looking at ways to save money, and filing your 2008 tax return can be a great way to put more money in your pocket.

2008 brought two new registered plans. The Registered Disability Savings Plan (RDSP) was launched on December 1st, 2008. This tax-deferred savings plan designed specifically for people with disabilities is now available across the country. To be eligible, you must receive the Disability Tax Credit, or be in the process of applying. This bulletin outlines the DTC and process to open an RDSP.

The Tax Free Savings Plan (TFSA) was launched January 1, 2009 and will give Canadians the opportunity to save up to $5,000 annually in a tax-free plan.

These plans are an essential part of tax planning. By exploring the options outlined in this 2008 Tax Bulletin, we hope you can capitalize on everything you are entitled to receive.

The Federal Government will **contribute as much as $4500/ year to an RDSP.** The deadline for 2008 contributions has been extended to March 2, 2008. Visit www.rdsp.com

PLAN would like to thank **HLB Cinnamon Jang Willoughby Chartered Accountants** for their advice and support in creating this Bulletin.

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What's *NEW* for 2008

The Registered Disability Savings Plan (RDSP)
The Registered Disability Savings Plan has now become an official savings plan available to all Canadians who are eligible for the Disability Tax Credit. This plan, launched in December of 2008, will allow people to save for their future, receive significant contributions from the federal government through a Grant and Bond, and withdraw money with no restrictions. The RDSP is an exciting new tool for families to use and will help approximately 500,000 Canadians save for the future. For more information on the RDSP visit www.rdsp.com

The Tax Free Savings Account (TFSA)
The Tax Free Savings Account is a new plan that will allow individuals to put away $5000 in savings a year, and these savings will accumulate tax-free with no taxation on withdrawals. If you cannot put in the full $5000 a year, the TFSA will allow you to carry forward any unused contribution room. There is no limit on the amount someone can contribute into a TFSA over the lifetime of the plan, but the beneficiary must be over the age of 18 to contribute into the plan.

The TFSA would be considered an asset under all provincial disability income assistance programs. Until they have been exempted, they will be of limited value as a savings tools for Canadians who receive disability assistance.

The Medical Expense Tax Credit
The list of medical expenses that you can claim on this particular tax credit has been extended to include: altered auditory feedback devices; electrotherapy devices; standing devices; and pressure pulse therapy devices. As well, you can now claim some expenses for service animals that are specially trained to assist someone who is severely affected by autism or epilepsy.

Other changes relating to personal income tax and GST/HST:

- Rewording of the Income Tax Act s. 118.2(2)(n) to ensure that the cost of non-prescription medications will not be considered eligible medical expenses after February 26, 2008. The revision to the Income Tax Act s. 118.2(2)(n) provides that for drugs to be eligible medical expenses, they must be drugs *"that can lawfully be acquired for use by the patient* ***only if prescribed*** *by a medical practitioner or dentist"*. Thus, if the patient is able to purchase the drugs off the shelf, the cost will not be an eligible medical expense.
- **Registered Education Savings Plans**—the time they remain open will be extended to 35 years from 25 years, and the contribution period will be increased by 10 years.
- Eligible expenses under the **medical expense tax credit** will be expanded. See Health-related tax measures on the CRA website.
- The residency component of the **northern residents deduction** will be increased by 10%.
- GST/HST will no longer be payable on costs of training to help individuals cope with disabilities or disorders, such as autism.
- The list of GST/HST-free medical and assistive devices will be expanded, to include other items, such as service dogs.
- Tax Back Guarantee—$2 billion in annual interest savings by 2009-10 will be dedicated to ongoing personal income tax reductions.

QUICK REFERENCE

Child care expenses	**Line 214**
Disability supports deduction	**Line 215**
Amount for an eligible dependant	**Line 305**
Amount for infirm dependants age 18 or older	**Line 306**
Caregiver amount	**Line 315**
Disability amount (for self)	**Line 316**
Disability amount transferred from a dependant	**Line 318**
Tuition, education, and textbook amounts	**Line 323**
Amounts transferred from your spouse or common-law partner	**Line 326**
Medical expenses for self, spouse or common-law partner, and your dependent children born in 1990 or later	**Line 330**
Allowable amount of medical expenses for other dependants	**Line 331**
Refundable medical expense supplement	**Line 452**
Working income tax benefit (WITB)	**Line 453**

TOP 10 TAX TIPS: TAKE ADVANTAGE OF TAX CHANGES TO SAVE MONEY ON YOUR FILING.

Reprinted with permission from Tax Expert Jamie Golombek, Financial Post. Published: **Wednesday, December 31, 2008**

For 2009, here are my 10 resolutions for saving more taxes:

Resolution #1: Open a TFSA. The new tax-free savings account, launched Jan. 1, is the ideal place to put up to $5,000 of savings and earn tax-free income and/or gains for life. Any withdrawals are not taxed, do not negatively affect eligibility for government-tested benefits and can be re-contributed the following calendar year.

Resolution #2: Maximize RRSP contributions. The RRSP limit for 2009 is the lesser of 18% of 2008 earned income or $21,000. Get a head start on your 2009 contribution today.

Resolution #3: Set up a spousal RRSP. The primary benefit of a spousal RRSP is that funds withdrawn can generally be taxed in the hands of the (hopefully) lower-income spouse.

Resolution #4: Earn tax-efficient investment income. For those who have maxed out their RRSP and TFSA contributions, consider tax-efficient investment income outside of these tax-sheltered plans by investing in Canadian dividends, which are eligible for the dividend tax credit, and capital gains, which are only half-taxable.

Resolution #5: Open up RESPs for kids. Don't forget to make at least $2,500 of contributions to each child's registered education savings plan (RESP) this year to take advantage of the $500 Canada Education Savings Grant. You may also be able to catch up on missed CESGs from prior years.

Resolution #6: Investigate pension splitting if you've received pension income in 2008, be sure to investigate whether splitting up to half of that income with your spouse or partner makes sense when you file your 2008 tax return this spring.

Resolution #7: Consider income splitting. A spousal income-splitting strategy whereby the higher-income spouse or partner loans funds to the lower-income spouse or partner to invest may be ideal given the record low prescribed rate, which is set at 2% this quarter.

Resolution #8: Donate "in kind" to charity. When planning your charitable giving for 2009, consider donating appreciated securities directly to your charity of choice and eliminating all tax on any accrued capital gains.

Resolution #9: Plan now to avoid a tax refund. If you regularly get a large tax refund each spring, consider applying for a reduction of tax at source using CRA Form T1213. This needs to be repeated each year.

Resolution #10: Consider opening an RDSP for a disabled person. If you or someone you care about has a disability, consider opening up a registered disability savings plan. Contributions to RDSPs, limited to $200,000 over the disabled beneficiary's lifetime, may be augmented by up to $90,000 in Canada Disability Savings Grants and Bonds.

Late last month, the government extended the deadline for opening an RDSP, making contributions and applying for the 2008 Grant and Bond to March 2.

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Children...

The Canada Child Tax Benefit and the Child Disability Benefit

The Canada Child Tax Benefit is a tax-free monthly payment made to help you with the cost of raising your children. If your child is under the age of 18 and you are the primary person responsible for their care, you may be able to receive the benefit. The basic benefit is $1,307 ($108.91 a month) for each child under age 18, and will vary depending on the number of children you have, the province you live in, your family's net income, and whether your child is eligible for the Child Disability Benefit. The basic benefit is reduced if your family net income is more than $37,885.

The Child Disability Benefit is paid monthly to people who receive the Canada Child Tax Benefit. This benefit will provide up to $2,395 per year ($199.58 per month) for your family if you care for a child under the age of 18 who has a severe and prolonged impairment in mental or physical functions. The Child Disability Benefit starts being reduced when your family net income is more than $37,885.

In order to receive both of these benefits, you will need to fill out Form T2201 *(Disability Tax Credit Certificate)* and Form RC66 *(Canada Child Benefits Application)*, and send them in with your tax return.

The Child Care Expense Deduction (line 214)

If you are a parent and working or going to school, you may be able to claim some of your child care expenses. If your child is eligible for the disability tax credit, it may be possible for you to claim up to an additional $10,000 for care of your child. Expenses that you can claim include payments made to provide child care, a day nursery or child care centre, a day camp, a boarding school, or an educational institution that provides child care services. You do not claim these costs as a tax credit, but instead deduct them from income on line 214 of your personal tax return. The parent who has the lower income should claim this deduction.

Children's Fitness Tax Credit (line 365)

Starting with the 2007 tax year, the Government of Canada allows a non-refundable tax credit based on eligible fitness expenses paid by parents to register a child in a prescribed program of physical activity. The children's fitness tax credit lets parents claim up to $500 per year for eligible fitness expenses paid for each child who is under 16 years of age at the beginning of the year in which the expenses are paid.

If a child qualifies for the disability tax credit, parents can claim up to $500 per year in eligible fitness expenses paid for the child who is under **18 years of age** at the beginning of the year. Also, if at least $100 in eligible fitness expenses has been paid for the child, an **additional** amount of $500 can be added to the eligible fitness expenses actually incurred.

GST/HST CREDIT AND REBATE

If you have a low income, the GST/HST Credit program will return part of the GST/HST you have paid throughout the year. These credits are calculated based your net income added that of your spouse (if you have one), as well as the number of dependent children.

To receive the rebate, you have to file an income tax return for 2007, even if you have no income to report. On your return you will be given the option of checking a "Yes" box in the GST/HST credit application area.

WEB RESOURCES

PLAN: www.plan.ca *(for links to specific articles on Canada Revenue Agency's website)*

RDSP: www.rdsp.com

Taxtips: www.taxtips.ca

Canada Revenue Agency: www.cra.gc.ca

www.disabilitytaxcredit.ca

www.trustlawyers.ca

www.davis.ca

www.cjw.com

Disability Tax Credit: Q&A

What is the Disability Tax Credit?
The Disability Tax Credit is a non-refundable tax credit that reduces a person's income taxes and is available for individuals who have a disability.

This credit is useful because, if an individual has little income, they still have the option to transfer all or part of it to a spouse, common-law partner or other supporting person.

That means, if you have a son or daughter of any age who is not claiming the Disability Tax Credit, then you may be able to claim some or all of the credit.

If you have missed a claim, you can file for the past ten years. This is worth exploring—it could be worth thousands of dollars returned to you.

This credit is also important because it is an eligibility requirement for establishing a Registered Disability Savings Plan.

What is the Disability Tax Credit worth?
The value of the Disability Tax Credit is a federal amount of $7,021 and a provincial amount of between $4,596 and $12,466 for the 2008 taxation year. This translates into a tax savings of between $1,402 and $2,300 depending on the province.

Note that the Disability Tax Credit claimed by an individual in connection with a disabled dependent child under 18 may be more than the amounts noted above given supplemental disability credits may be available. If you have a child under 18, who qualifies for the Disability Tax Credit, they may be eligible for the Child Disability Benefit. (See page 8.)

There may be limitations to the amount of disability credit that may be claimed if expenses in connection with attendant care or care in a nursing home are also being claimed.

How do I claim the Disability Tax Credit?
A person with a disability claims the disability amounts on the Schedule 1: Federal Tax Calculation and a provincial form. In BC it is, Form BC 428 British Columbia Tax Calculation, but each province will have its own form for claiming the provincial amount.

The person should also attach Form 2202, the Disability Certificate. Once the Disability Certificate is obtained and accepted by the Canada Revenue Agency, it will continue to be valid for each subsequent tax year until the person's condition changes. Therefore, it is not necessary to obtain a new Disability Certificate each year, unless so requested by the Canada Revenue Agency.

What if the person is a child?
A dependent child (less than 18 years), may transfer all or part of the Disability Tax Credit to a parent so that the parent can claim it. You may claim the disability credit for the child only if nobody else doing so or if no one else is claiming the child as a dependent.

Can I still claim the Disability Tax Credit when my child turns 18?
A parent may claim the unused portion of the Disability Tax Credit from a son or daughter if the person lives at home with the parent or if the person is dependent on the parent by reason of the disability, and nobody else is claiming any other non-refundable tax credits (i.e. spousal amount, amount for eligible dependent, medical expense tax credit) in connection with the son or daughter with a disability.

Note: In some circumstances, you can continue to claim the Disability Tax Credit even when an adult son or daughter does not live with you.

To claim the Disability Tax Credit for an adult son or daughter, you must also have claimed (or been eligible to claim) the Equivalent to Spouse Credit, the Care Giver Credit or the Dependent Tax Credit. To claim the Equivalent to Spouse Credit, the person must not be married. To claim the Care Giver or Dependent Tax Credits the person must be a son or daughter, grandchild, parent, grandparent, brother, sister, aunt, uncle, nephew or niece.

Disability Tax Credit Supplement for Children (line 316)
Families caring for children with disabilities (under 18 years) can also claim the Disability Tax Credit Supplement for Children, which is a federal credit of $4,095 and a provincial credit of from $2,402 to $9,355 for 2008. This translates into a tax savings between $778 and $1,550

These amounts are in addition to the Disability Tax Credit discussed above but are reduced if you also claimed child care expenses (at line 214) or attendant care expenses (as a medical expense on line 330 or 331).

THE GREY LIST Facing the Challenges of Qualifying for Disability Tax Credits

By Doug Lagasse

The application process for Disability Tax Credits (DTC) should be simple and straightforward but like many other things in life, reality can trump expectations. In the case of DTC applications, the best way to overcome the challenges of qualifying is to know that there are grey areas in the application process and to understand how they apply to your situation. This article is not about what types of medical conditions qualify for a DTC, but rather to enhance your awareness of the application process and your chances of qualifying.

In many cases, where the disability is severe and is unquestionably what the tax department calls a 'marked restriction on daily living activities', the challenges of qualifying will be less extreme.

This grey list is not theoretical but based on years of experience. Each topic was chosen because these were some of the repeated issues that have affected numerous applications. It is offered in the spirit that "**getting it right the first time**" is more important than ever. Recent federal government initiatives that support further tax reduction possibilities (potential income splitting) and the life enhancing new Registered Disability Savings Plan are dependent on a successful DTC application.

- *Uniqueness*
  The effects of a prolonged medical condition that are experienced by each individual are unique and it is the effects of the condition that CRA will look at when reviewing an application. The grey area here is, "When does a disability become severe enough to qualify for a DTC?" How do good days and bad days matter? Does ability to work matter? How about likelihood of improvement? What matters most, is that the description of the effects of a condition are clearly stated.

- *Doctors Role*
  Does your doctor, however well-intentioned, have a good understanding of what the tax department requires to successfully qualify a DTC applicant? Do you? The DTC application form (T2201) has changed numerous times in the last five years—once quite dramatically. Is your doctor up to date? Most doctors are extremely busy and that can't be good for their enthusiasm of completing forms. If the application form is vague, missing information or is contradictory, the tax department will likely respond by sending a questionnaire to the doctor asking for clarification in some areas. This should be avoided. The modern trend of 10 minute appointments does not help doctors to fully understand the effects of a patient's condition. Be sure your doctor understands your condition, knows how long you have been affected and that they have ***all*** of your medical records.

- *Loving the Tax Department*
  Each tax centre has a tendency to have different management guidelines and protocols. As well, each officer who reviews the applications has a unique understanding of the intent of the legislation. Obviously, what that means is that the same application may be treated differently depending on whose desk it lands. To avoid gambling with your application, make sure to pay close attention to your application process, so that the decision for them is easy to make and it is the one you want! Then you can love them too.

- *Sideways*
  Regretfully, even though a medical condition may normally qualify an applicant, DTC applications can be denied because of a technicality in the application process. Certainly, CRA allows for objections that can go as far as court challenges and usually this means your doctor would be involved. However, a way to look at it sideways is to re-apply in a succeeding year. Although it is now an uphill battle, this is allowed. CRA will be aware that you have previously been turned down and they will look very closely at your application and ask, "What is different this time?" In this scenario diligence in understanding what went wrong in the first place, will go a long way. Professional help is likely crucial.

- *The Financial Results*
  A successful DTC application is the most important goal, but stay focused on maximizing financial results as well. Canada has a self assessing tax system and you must tell the tax department what to do or they may not take action. In this case, the grey area is assessing all the options of properly transferring the DTC credits (and refunds) to a family member if they cannot be used completely by the person with the disability.

- *Grey Advice*
  Like a mouse asking a cat for the best place to hide, it may not always be in your best interest to depend solely on advice from the tax department. Calling the toll free line and asking for advice can be hit or miss. It is not that they intend to mislead you, but different interpretations can come into play. In other words, getting the correct answers not only depends on your questions, but whether the officer from CRA knows the right questions to ask you about your situation.

- *Being Successful*
  The DTC is an important document. The most productive approach is to treat it as your responsibility, not your doctors. Always get a copy of your DTC application from your doctor or representative. The chances of success are improved by including supporting documentation with your application. You or your representative (not your doctor) should submit your application. Can we pull out and highlight as 'Tax preparation tip'?

Remember, the tax department has no choice but to focus on the details. Since a DTC application is most often a one-time application, it can mean significant value year after year, so your interests are best served with a similar focus. Leave as little to chance as possible.

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QUALIFYING FOR THE DISABILITY TAX CREDIT?

To qualify for the Disability Tax Credit a person must have "an impairment in physical or mental functions which is both severe and prolonged".

A **"severe impairment"** means: even with therapy and the use of devices and medication, the person is restricted all or substantially all of the time. The effects must fall into one of the following:

- Markedly restricted in the basic activity of daily living
- Vision
- Life-sustaining therapy
- The combined effect of restrictions (for patients who are significantly restricted in two or more of the basic activities of daily living neither of which on its own meet the criteria for markedly restricted) is equivalent to being markedly restricted.

"Markedly restricted" means that most of the time:

- a person is not able to perform one of the activities of daily living or
- it takes an inordinate amount of time to perform one of the activities of daily living

"Significantly restricted" means that although a person does meet the criteria for markedly restricted his or her ability is still substantially restricted.

The activities of daily living are:

- speaking
- hearing
- walking
- feeding
- dressing
- bowel or bladder functions
- mental functions necessary for everyday life

What are "mental functions necessary for daily life"? In addition, for greater certainty, mental functions necessary for everyday life will be defined as including:

- Memory—the ability to remember the following: simple instructions; basic personal information such as name and address; or material of importance or interest.
- Problem-solving, goal-setting and judgement—the ability to solve problems, set and keep goals, and make appropriate decisions and judgements.
- Adaptive functioning—abilities related to self-care, health and safety, social skills and common, simple transactions.

The latter were recently adopted, so if a claim was rejected prior to 2005 then it might now be accepted.

Medical Expenses Tax Credit

Medical Expenses Tax Credit (line 330/1)

You might not think to look at the Medical Expense Tax Credit to claim items related to disability. You should! There are many disability related expenses that can be claimed. These expenses range from attendant care to symbol boards, from speech recognition software to renovation costs, and from medications to dental work.

If you have sustained significant medical or disability expenses for yourself or your relative, you may qualify for the Medical Expense Tax Credit.

You can claim for yourself or your spouse and children under 18 years ***and you can claim for other dependants.***

A ***dependant*** is a person who, at any time in the year, is dependent on you for support. Dependents could be a son or daughter (even over the age of 18 years), a child or grandchild or a parent, grandparent, brother, sister, uncle, aunt, niece, or nephew of the individual or the individual's spouse or common law partner.

Support is not specifically defined for income tax purposes and, therefore takes its ordinary meaning. In general terms, support involves the provision of the basic necessities of life such as food, shelter, and clothing.

Notes about the Medical Expense Tax Credit:

- If you claim medical expenses for a dependant, their net income reduces your claim.
- Medical expenses can be claimed for any 12 month period ending in the taxation year (or 2008).
- You cannot claim any expenses for which you have been reimbursed.
- Amounts claimed should be supported by proper receipts. A receipt should indicate the purpose of the payment, the date of the payment, the patient for whom the payment was made and, if applicable, the medical doctor or practitioner, dentist, pharmacist, nurse, or optometrist who prescribed the purchase or gave the service. A cancelled cheque is not acceptable as a substitute for a proper receipt.

Attendant Care Expense Deduction (line 330/1)

You can claim the attendant care expenses of an attendant if your relative was at least 18 years and if your relative qualifies for the Disability Tax Credit or has a mental or physical impairment. To demonstrate a mental or physical impairment, you must provide a letter from a medical practitioner certifying that the person:

- is likely to continue to be dependent on others for his or her personal needs and care for the long-term;
- needs a full-time attendant because of a mental or physical impairment; and
- needs the equipment, facilities, or personnel available in the establishment.

TAX PREPARATION TIPS:

Whether you are preparing your tax return or paying a professional, when making a claim for medical expenses you need to keep your receipts well organized. Keeping your receipts organized in chronological order will make it easier to claim the medical expenses, since this will facilitate the determination of which 12 month period ending in the taxation year is more beneficial for you.

If you are claiming a substantial amount of medical expenses, it is probably better to paper file your return since the Canada Revenue Agency will likely request the medical receipts to substantiate the claim and delay the assessment of the return. If you paper file and enclose a copy of the receipts, it will provide the Canada Revenue Agency with the necessary information to assess the return and issue any refund faster.

Attendant care is care provided by an attendant who performs those personal tasks which the person with a disability is unable to do for himself or herself. Depending on the situation, such tasks could include meal preparation, housekeeping services, laundry services, transportation, and personal services, such as banking and shopping. Attendant care would also include providing companionship to the person with a disability.

You can claim your share of salaries or wages paid to all employees performing the following duties:

- food preparation
- housekeeping services
- laundry services
- health care (registered nurse, practical nurse, certified health care aide, personal support worker);
- activities (social programmer)
- transportation (driver).

QUALIFYING MEDICAL EXPENSES:

- Renovations and alterations to dwellings
- Transportation and travel expenses of patient and accompanying individual to or from a hospital
- Care in a self-contained domestic establishment
- Care of individual with mental or physical impairment
- Payments to medical practitioners and hospitals
- Care in an institution and care in a training institution
- Artificial limbs, aids and other devices and equipment
- Guide and hearing dogs and other animals
- Rehabilitative Therapy
- Bone Marrow or organ transplants
- Devices and equipment prescribed by regulation. (For example: orthopaedic shoes or an insert for a shoe made to order; mechanical devices designed to assist an individual to enter or leave a bathtub or shower or to get on or off a toilet; devices designed to assist an individual in walking; electronic speech synthesizers)
- Preventative, diagnostic and other treatments
- Drugs, medicaments and other preparations or substances
- Premiums to private health services plan
- Eyeglasses
- Oxygen tents

If your relative qualifies for the Disability Tax Credit, you have two options:

1. Claim the disability tax credit and attendant care expenses up to $10,000.

2. Do not claim the disability tax credit. In this case, there is no maximum for the amount of attendant care expenses that can be claimed.

TAX TIP: The federal Disability Tax Credit is $7,021. Therefore, if your total medical expenses (including attendant care expenses) exceed $17,021, it is better to claim all medical expenses but not claim the Disability Tax Credit. In this case, the Disability Tax Credit neither be claimed by the taxpayer nor transferred to anyone else.

Refundable Medical Expense Supplement (Line 452)

The Refundable Medical Expense Supplement is available to people with lower incomes who have paid medical expenses, or disability supports expenses. To be eligible for this supplement you must:

- be 18, and
- have employment or self-employment income exceeding $3,040.

The maximum supplement is the either $1,041 for 2008, or 25% of both medical expenses and disability supports expenses (whichever one is less). This credit is harder to qualify for, but may be worth taking the time to fill out.

Taxation of Trusts

By Halldor K. Bjarnason, Lawyer, and Philip J. Dougan, Lawyer

Wiser folks than us have said: "There are only two certainties in life: death and taxes". This maxim definitely applies to trusts. With respect to death, in British Columbia, a trust normally has a maximum lifespan of 80 years. With trust taxation, it is much more complex. The following is a summary of key income tax issues that affect trusts where the beneficiary is a person with a disability.

For taxation purposes, a trust is treated as a separate taxpayer (but without the personal deductions available to a human being). As a result, each year the trustees must file an income tax return (a T-3 Return) for the trust and pay tax on all of the recorded income.

Inter Vivos Trusts

For *inter vivos* or "living" trusts, trusts that are created while the settlor or creator is alive, the tax filing date is 90 days after the December 31 year-end (March 30). The trust pays tax at the highest marginal rate—currently, a little over 43%—on all income earned by the trust.

Testamentary Trusts

Tax-wise, a testamentary trust has greater flexibility. A testamentary trust comes into effect upon the settlor's death—usually through a will. The testamentary trust has a flexible year-end, in that the trustee(s) can set the date when the trust is established. As well, a testamentary trust is taxed at a graduated rate, much like a living person. For the first $34,397 of income, a testamentary trust is taxed at the lowest marginal rate—currently 20.7%. The tax rate gradually increases until the highest marginal rate—currently, a little over 43%—applies to trust income over $120,000.

While the tax rates for a testamentary trust are clearly preferable to those of an *inter vivos* trust, the trustee needs to be very careful to not "taint" the testamentary trust. If funds, or other assets, from a source other than the deceased are ever added to the testamentary trust—for example, gifts or inheritances from other relatives—the trust is deemed tainted by the Canada Revenue Agency. As a result, all income of the trust is taxed at the highest marginal rate.

Payments to and from the trust can also have income tax implications. When capital assets, such as stocks or vacation property, are transferred into a trust, the transfer constitutes a "disposition of assets". The settlor will be required to pay tax on all capital gains that have accrued on the property prior to the transfer to the trust. Similarly, when a capital asset is transferred from the trust to a beneficiary or another trust, income tax is payable on all capital gains that accrued while the asset was in the trust.

When the trust transfers income to the beneficiary, or uses trust income on behalf of the beneficiary, the income can be taxed in the beneficiary's hands, at the beneficiary's marginal tax rate. For a beneficiary whose only source of income is their disability assistance, this invariably means paying less income tax. Of course, the risk is that paying trust income directly to the beneficiary will typically affect his or her eligibility for benefits, pursuant to the Disability Assistance legislation.

Preferred Beneficiary Election

One potentially useful tax-saving tool that is only available to trustees of trusts with a disabled beneficiary is the Preferred Beneficiary Election. The *Income Tax Act* provides that if a trust is for the benefit of a person with a disability (ie. someone who qualifies for the Disability Tax Credit) and the trust has been settled by the person with a disability, or his/her spouse, parent, grandparent, or great-grandparent, the trustee can opt to use the Preferred Beneficiary Election. The Preferred Beneficiary Election permits the trustee to declare that the trust income is to be taxed in the beneficiary's hands, at his or her marginal tax rate, while keeping the income within the trust for reinvestment purposes.

The Preferred Beneficiary Election must be filed within 90 days of the trust's year-end, with both the trustee and the preferred beneficiary (or his/her guardian or representative) signing it. The Preferred Beneficiary Election does not have the same potential negative affects on a beneficiary receiving disability assistance as does a direct payment of income. However, the Ministry of Health has indicated that they DO consider amounts claimed under a Preferred Beneficiary Election as income of the beneficiary. This can result in people who receive home care facing an increase in daily user fees. Therefore, it becomes important to weigh the benefits of using the Preferred Beneficiary Election.

Caregivers...

21–year Deemed Disposition Rule

We said at the beginning of this article that trusts have a maximum life expectancy. The reality is many trusts do not make it past their 21st birthday. This is because of the 21-year deemed disposition rule. In order to keep people from "hiding" capital property in a trust, the federal government introduced a rule which states that every 21 years, a trust is deemed to dispose of all of its capital property, and immediately reacquire it at market value. This deemed disposition triggers capital gains, and requires the payment of tax on all such gains. For example, if you put a $100,000 summer cottage into the trust, and 21-years later, it's worth $250,000, even though it hasn't been sold, income tax is still owed on a $150,000 capital gain. This can be a nightmare for a trust which does not have substantial cash assets, and often means that the trust must sell the property in order to pay the tax bill.

Principle Residence Exemption

A helpful exception to the deemed disposition rule is the principle residence exemption. Where a trust owns a property which is the principle residence of a beneficiary or a child or spouse of a beneficiary, the *Income Tax Act* allows the trust to claim the same benefit as when an individual owns their own principle residence: Capital gains on the principal residence are exempt, and no tax is payable. This can provide significant financial relief as the 21-year deemed disposition creeps up on the trust.

The foregoing is a summary and we strongly recommend your next steps involve advice from a chartered accountant or tax lawyer. For more information visit **www.trustlawyers.ca**

The Infirm Dependent Credit (line 306)

The Infirm Dependent Credit recognizes that many families take care of relatives with a physical or mental health condition, but may not necessarily live in the same residence as them. As long as your relative is dependent on you, or on you and others, for support you may be able to claim this credit.

Can I claim it?

You qualify if your dependent relative is 18 and older, and has a physical or mental impairment. It is not essential that your relative qualify for the Disability Tax Credit in order to receive it, but you must submit a signed statement from a medical doctor that gives the nature, commencement, and duration of your loved one's impairment. As well, their net income must be below $9,906 to qualify. They must also be dependent on you for most of the year, and this dependency must be brought about solely because of their particular infirmity.

How do I apply?

Simply fill out line 306 of your Federal Tax Return by entering your relative's net income.

What is it worth?

The credit is based on the net income of your relative. It is comprised of a federal amount of $4,095 and a provincial amount from $2,402 to $9,355, depending on your province. The resulting tax savings range from $778 to $1,550.

You will receive the full amount of the federal credit, if your relative has an income equal to or below $5,811. When your relative's net income exceeds $ 5,811, the amount deducted from your taxes begins to decrease, and is eliminated when their net income exceeds $9,906.

The Caregiver Credit (line 315)

The Caregiver Credit and the Infirm Dependent Credit are very similar. The Caregiver Credit is available to you if you provide in-home care for your relative, and your relative has a physical or mental health condition. This credit does not cover your family member if they do not live in your primary residence.

The credit is based on the net income of your relative. It is comprised of a federal amount of $4,095 and a provincial amount ranging from $2,402 to $9,355 depending on which province you live in. The resulting tax savings range from $778 to $1,550.

This credit also begins to decrease as soon as their income exceeds $13,986, and will be eliminated when their net income exceeds $18,081.

To apply for the Caregiver Credit, fill out line 315 on your federal tax return and attach schedule 5 (provides details for each dependent).

TAX TIP: Both the Caregiver Credit and the Infirm Dependent Credit allow you to split the return amongst any persons supporting your relative.

Death and Taxes

By Sadie Wetzel, Lawyer and Ryan Green, Articled Student—Davis LLP

There is a popular saying that the only two certainties in life are death and taxes. What is the link between death and taxes? Is there anything we can do to reduce the amount of taxes that will be triggered on death?

Clients often ask if Canada has estate tax. The answer is "no". Canada does not have estate tax or inheritance tax like some other jurisdictions (such as the United States). However, that does not mean that in Canada there are no tax consequences associated with death.

Under the *Income Tax Act* (the "Act"), a personal representative (most commonly the executor) must file a "terminal return" for the year in which a taxpayer dies to report the deceased's income up to the date of death. In addition to those amounts that would ordinarily be considered income to the deceased (such as employment income), the Act contains special rules requiring certain amounts to be reported on the terminal return. While there are a number of other tax consequences associated with death, the ones we typically see involve principal residences, recreational properties, stock portfolios, RRSPs and RRIFs.

Principal Residences, Recreational Properties and Stock Portfolios

Under the Act, principal residences, recreational properties and stock portfolios are generally considered to be "capital property" and as such are deemed to be sold immediately before death.

In other words, according to the Act, you sell all of your capital property the second before you draw your last breath. This "deemed disposition" rule is significant because it effectively triggers a capital gain on all of your capital property that has appreciated in value from the purchase date.

Unless the property qualifies as your principal residence, or for some other specific exemption, one-half of the capital gain will be included in your income and will be taxed at the applicable marginal tax rate (at today's current rates, the effective tax on capital gains for a taxpayer in the highest tax bracket is approximately 22%).

John dies in 2009. His only assets were:

- his house, which he bought for $350,000 and which is now worth $750,000;
- a vacant lot, which he bought for $75,000 and which it is now worth $125,000; and
- a stock portfolio which has a cost base of $50,000 and is currently worth $250,000.

John is considered to have sold all of his assets immediately before his death. The capital gain associated with his house will be exempt from tax because it was John's principal residence. However, the capital gain associated with the lot and the portfolio will be subject to tax. One-half of the total gain, or $125,000, will be included in John's income on John's terminal tax return and will be taxed at the applicable marginal tax rates.

This general "deemed disposition" rule can impose a large tax burden on an estate. To limit the hardship that this may cause for a surviving spouse, there is an exemption when a taxpayer leaves his or her property to his or her spouse, or to a trust for the spouse's benefit. When a taxpayer dies and leaves his or her assets for a spouse, or to a spousal trust, the capital gain that would typically be triggered on the taxpayer's death may be deferred until the spouse sells the property or dies.

RRSPs and RRIFs

Other important rules in the Act pertain to RRSPs and RRIFs. Generally, when you die, the entire amount of your RRSP or RRIF is included in your income and will be taxed on the applicable marginal rate.

However, as with capital properties, the general rules surrounding RRSPs and RRIFs are subject to a number of exceptions. For example, if certain conditions are met, RRSP proceeds may be left to a financially dependant child and the proceeds can be taxed in the hands of the child (at his or her marginal rates) or can be used to buy a term annuity. However, this type of planning may have adverse consequences for a child if the child is receiving provincial disability benefits.

Consequently, we strongly recommend seeking professional advice before designating a disabled child as the beneficiary of a RRSP or RRIF.

Probate Fees

In addition to income taxes, when you die, your estate may also attract probate fees. Probate is the process by which the Court confirms an individual's Will as his or her last Will by issuing a document called a

"Grant of Probate". The Grant of Probate identifies the estate's executors as the personal representatives of the estate, and effectively proves to third parties that the person named as the executor actually has power to act for the estate and to deal with the deceased's assets.

To obtain a Grant of Probate, an estate must pay a probate filing fee. The amount of probate fees applicable to an estate vary from jurisdiction to jurisdiction. For example, the probate fees in Alberta are nominal. However, in British Columbia, probate fees may be significant. In BC, the fee is currently $208 to initiate the probate proceeding plus $6 for every $1,000 of the gross value of the estate assets in excess of $25,000 and $14 for every $1,000 of the gross value of the estate passing in excess of $50,000. In other words, in BC, a $1,000,000 estate will have to pay $13,658 to obtain a Grant of Probate.

In certain cases, it may be possible to reduce the amount of probate fees. **In BC, probate fees only apply to property that passes to the estate's personal representative.** This means that assets that pass *outside* of an estate do not attract probate fees. Situations where property is not transferred to a deceased's personal representative and is consequently passed outside a Will include:

- properties held in joint tenancy;
- life insurance policies with named beneficiaries;
- RRSPs and RRIFs with named beneficiaries;
- annuities and pensions with named beneficiaries; and
- assets held in a trust.

While it may be advisable to organize your affairs so as to minimize the probate fees that may be applicable to your assets on your death, doing so may inadvertently create other problems. For example, we often see an elderly parent transfer their principal residence into joint tenancy with their adult child because they have heard that this is an effective way to reduce probate fees when the parent dies. While this technique may be effective for reducing probate fees, holding your house jointly with another person may compromise your ability to take full advantage of the principal residence exemption (as discussed above). For this reason, you should seek professional advice before transferring property into joint tenancy with another person.

Foreign Taxes cut this if not enough space

In addition to Canadian income taxes, you may also be subject to foreign taxes if you own assets in other jurisdictions or if you are a citizen of a country other than Canada. For example, if you own vacation property in the United States, when you die, you may be subject to US estate tax.

The US estate tax rules are very broad and they apply to Canadians who own vacation property in the US, *even if you are not a resident or citizen of the US.* If you are subject to US estate tax, the *entire* value of your US assets will be subject to 45% tax (2009 rate). While an offsetting credit may be available in certain cases, US estate tax can create a serious tax burden for Canadians who own property in the US.

Similarly, if you are an US citizen, you may be subject to US estate tax, *even if you do not own property in the US.* US citizens living in Canada are subject to both the Canada and the US tax regimes and are required to file tax returns in Canada and the US. When a US citizen dies, the US calculates estate tax based on the entire value of the deceased's estate, *regardless of where the assets are situated.* Once again, certain credits and exemptions may be available if specific conditions are met. Given the complexity, and the significance, of the US estate tax rules, you should seek assistance from a professional experienced in cross border issues if you own assets in the US or if you are a US citizen. Similarly, if you own property in, or are a citizen of, a jurisdiction other than the US, you should consult a professional in that jurisdiction to determine what, if any, taxes that jurisdiction will apply to your estate when you die.

Conclusion

Death can result in significant tax consequences. If assets need to be sold to pay your tax bill, there will be less property available to distribute to your beneficiaries. With a carefully designed estate plan, some of the tax consequences associated with death can be eliminated or postponed.

Odds 'n Ends

Working Income Tax Benefit (line 453)

The Working Income Tax Benefit (WITB) is a refundable tax credit intended to provide tax relief for eligible working low income individuals and families who are already in the workforce and to encourage other Canadians to enter the workforce.

You can claim the WITB on line 453 of your 2008 Income Tax and Benefit Return if your working income is over $3,000, and you meet all the eligibility criteria .

What is the disability supplement (Line 316)?

If you are eligible for the WITB and the disability amount (line 316), you may also be eligible to claim an annual disability supplement of up to $261 for 2008.

To be eligible for the disability supplement, your working income must be over $1,750 and you must be eligible for the Disability Tax Credit.

What are WITB advance payments?

Eligible individuals and families have the option to apply for WITB advance payments. The WITB advance payments correspond to a maximum of 50% of the WITB refundable tax credit (including the disability supplement, if applicable) that you expect to claim on your 2009 Income Tax and Benefit Return. Any WITB that you are entitled to and did not receive as advance payments will be paid to you when your 2009 Income Tax and Benefit Return is assessed.

The annual maximum amount you can receive in WITB advance payments is:

- $261 for single individuals without eligible dependant(s); or
- $522 for families (individuals with an eligible spouse, common-law partner or eligible dependant).

The annual maximum WITB advance disability supplement you can receive is $130.50 for an individual. If more than one individual per household is entitled to the disability supplement, we will only pay one individual the supplement in advance payments. The other individual will claim the supplement on his/her Income Tax and Benefit Return by completing Schedule 6.

When should you apply for the WITB advance payments?

To receive the WITB advance payments for 2009, you need to apply between January 1 and August 31, 2009 by completing Form RC201, Working Income Tax Benefit Advance Payments Application for 2009. **Applications for advance payments received after August 31, 2009 will not be processed.**

Disability Supports Deduction (line 215)

Up to $15,000 in disability supports expenses (including attendant care expenses) may be claimed as a deduction from income by persons with mental or physical impairments who have incurred the expenses in order to: earn employment income or attend an educational institution.

You cannot claim expenses for which you were otherwise reimbursed (unless the reimbursement is claimed as income) nor can you claim more for expenses than your earned income.

When a person has incurred the disability supports expenses in order to attend an educational institution, an additional amount may be claimed.

TAX TIP: Another option is to claim these expenses under the Medical Expense Tax Credit, where expenses can be claimed by either spouse. When claimed as a Disability Supports Deduction, the claim reduces a person's payable tax at the person's marginal rate. When claimed under the Medical Expense Tax Credit, however, the tax reduction is at the lowest tax rate.

Federal Gasoline Tax Refund Program

The Federal Excise Gasoline Tax Refund Program refunds a portion of the federal excise tax on gasoline bought for use by certain eligible individuals or organizations. This program allows you to claim a refund of part of the excise tax on gasoline at the rate of $0.015 per litre or $0.0015 per kilometer.

In order to receive this tax refund as an individual, you must have a permanent mobility impairment that makes it hard for you to use public transportation safely, and you must have confirmation from a certified medical practitioner.

You do not have to claim this amount when you file your income tax. To claim, you must complete an Application for Refund of Federal Excise Tax on Gasoline.

GST Exemptions

If you modified a vehicle to transport a person using a wheelchair (e.g. added a wheel chair lift) or adapted a vehicle to permit a person with a disability to drive, you shouldn't have to pay GST.

GST Rebates

If you purchased a vehicle that was already modified to transport a person using a wheelchair or adapted to permit a person with a disability to drive, you can get the GST on the value of the modifications back. To claim, you must complete a GST/HST Specially Equipped Motor Vehicle Rebate Application.

TAX TIP: You can also claim 20% of the cost of an accessible vehicle or payments to adapt a vehicle to transport or be driven by a person with a disability for a Medical Expense Tax Credit on your income tax. You can claim the Medical Expenses Tax Credit for yourself, your spouse or your dependent children who are 18 year or younger.

INCOME SPLITTING: BEWARE!

Starting with the 2007 tax year, seniors are able to split some pension income with their spouse. Up to half of this eligible income can be allocated to the taxpayer's spouse. Funds are not actually transferred but taxable income of one spouse is reduced resulting in a tax savings. The exact pension income that can be split depends on age, but includes life annuity payments from a pension plan and payments from a RRIF.

This can save couples a significant amount in taxes, but you need to be careful with it. The spouse's income will increase and this may affect the cost of services that are income tested. For example, if the spouse is in a seniors' care home that is income tested, then the cost of that service might increase significantly—in some cases more than the tax savings that were gained.

PLAN seminar showcase

Visit www.plan.ca for a full list of seminars

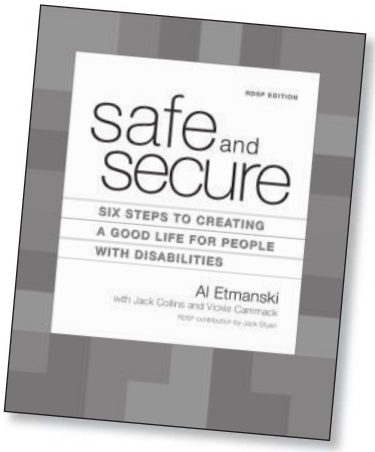
Registered Disability Savings Plan Telephone Seminars—dial in from anywhere on all the details of the RDSP and how it can benefit your relative with a disability. Free, but space limited—registration required. Canada-wide.

Wills, Trusts & Estates Online Workshop—practical information to secure the future of your loved one, the course is packed full of easy-to-use forms, videos, discussion and connection to a facilitator to answer your questions. BC only.

PLAN Orientation—family-guided orientation on the values and work of PLAN, this session is for families interested in finding more about how PLAN helps to secure your relative's future. Please call the office to register.

Safe and Secure—RDSP Edition to be released March 2009!!! **6 Steps to Creating a Good Life for People with Disabilities.**

A new book from The PLAN Institute for Caring Citizenship and Planned Lifetime Advocacy Network by Al Etmanski, with Jack Collins, Vickie Cammack, RDSP Contribution by Jack Styan.



To find out where you can obtain your free copy of Safe and Secure RDSP Edition, please visit **www.plan.ca, www.planinstitute.ca or www.rdsp.com**

Does your province or state need Safe & Secure? **Contact Jack Styan to find out how: jstyan@plan.ca**