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Your Guide to Tax-Saving Strategies

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TAXSTRATEGY

A New Year

Tax Planning and the Spirit of Giving

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Another year seems to have flown by and we are in the swing of holiday giving. So, with that holiday spirit in mind, my gift to you are some last minute tax planning tips to cut your tax bill for 2022. But hurry up, as the next month will surely fly by if this year is any indication.

Last-Minute Income Splitting

Income splitting with low-bracket family members is always a good way to trim your tax bill. The following are some income splitting strategies which may be relevant at year end:

- You can split income

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with low-bracket family members by making a loan to them (e.g., a spouse, common-law partner or a child under the age of 18), provided that Can-Rev's "prescribed rate" is charged on the loan - the rate is adjusted quarterly (currently it is at 3 per cent for the last quarter of 2022). Interest must be paid within 30 days after the end of each year, otherwise the "attribution rules" may apply with the result that the income is taxed in your hands. Make sure that the interest payment is properly documented, e.g., by a cheque deposited to your account.

Occasionally, you might want to purposely trigger the attribution rules. For example, if the investment is generating losses (which in this year, may be the case), the attribution rules may allow you to claim

them on your return. In this case, a strategy may be to purposely miss the interest-payment deadline. However, if this is done even once, the "prescribed rate loan" exemption will no longer apply to investments made from that loan on a go-forward basis. As a result, you may have to start fresh with a new prescribed rate loan (and who knows where the prescribed rate will be then).

- If you have a family trust and you want to ensure that the low-tax rate beneficiaries are taxed on the income distributed from the trust, it is necessary that the income be either paid or made payable by the end of the calendar year. If actual payments are not made, then promissory notes or other evidence that there is a legal obligation to pay should be in place. To the extent that funds are actually paid, ensure that they are paid to the actual beneficiaries and deposited to their account. Proper trust documentation should also be in place reflecting the income being paid or payable to the particular beneficiaries.

- The higher-bracket spouse should pay all household expenses (including the lower-bracket spouse's income tax), permitting the lower-bracket spouse to invest his or her income. The income earned on the investments will be taxed on the lower-bracket spouse's tax

return – i.e., at a lower tax rate.

• Retired couples can split CPP benefits. Consider splitting CPP if one spouse/common-law partner has a significantly lower income, which can produce tax savings.

• Couples that are 65 of age or older can also pool their retirement pension income. In order to do so, both the recipient of the eligible pension income and the spouse must agree to the allocation in their tax returns for the year in question.

Defer Tax on Interest

The Income Tax Act allows a deferral of tax on an interest-bearing investment for one year after its purchase, unless the interest is paid or credited to a taxpayer's account in the meantime. Accordingly, for investments on which interest payments are deferred (e.g., payments that occur once or twice a year), it may make sense to make the purchase early in the new year, rather than late in the current year, so that at least a portion of the interest payments will be “kicked over” to the next year.

Trigger losses before year end

If you are holding on to investments that are in a loss position, and you expect to have other capital gains for 2022 from other investments, consider whether now is the time to dump your “loser stock.” This can trigger a capital loss to offset any other capital gains in your portfolio.

Even if you don't have current capital gains for 2012, your capital loss can be carried back three years to offset any previous capital gains, so this strategy is still relevant if you had capital gains in 2021, 2020 or 2019.

Claim an Allowable Business Investment Loss (ABIL)

While capital losses can only be used to reduce capital gains, 50 per cent of an ABIL can be used to reduce all types of income. Therefore, if you're a shareholder or creditor of an unsuccessful private corporation, consider selling your shares or debt by year end.

To claim an ABIL, the investment must be in a private Canadian corporation. The general rule is that, at the time of the loss sale, the company must have been a “small business corporation” – CanRev requires that 90 per cent or more (in value) of the company's assets must be used principally in an active business carried on primarily in Canada. One final restriction: The loss reverts to an ordinary capital loss to the extent that you have claimed the capital gains exemption in a previous year.

To claim an ABIL, the sale must not be to a person who is not “at arm's length.” This means you can't sell to persons who are related to you for tax purposes, including a spouse or common-law partner, child or grandchild, sibling, or a controlled corporation, for example. There is also a test: It is

possible that CanRev could say the purchaser does not deal at arm's length with you if you were the directing mind or you acted in concert with the purchaser. Accordingly, if a large loss is involved, care must be taken. (Alternatively, the loss may be available in situations where the company has gone out of business).

Keep in mind that if the investment was made by way of a loan to a company that you control (or considered “related” to under the Income Tax Act), then that loan should be interest-bearing. Otherwise, the ABIL will not be available to you.

And if you're wondering why I'm focusing on the technicalities, it's because ABIL claims are generally put under the microscope by CanRev. At the very least, you should expect a review of your claim by CanRev – a standard questionnaire is normally sent to you asking for details on the investment, as well as asking you to back up the company's status as a “small business corporation.” So before you decide to claim an ABIL, make sure your ducks are in a row.

Be kind and donate

If you expect to have other income for 2022, then during this season of giving, consider making a donation to a registered charity. Not only will you be spreading the wealth among those in need, you will also create a tax credit to offset against your other income. So, with this strategy, everyone benefits! □