

| FINANCIAL PLANNING |

Save this tax season

Changes to the *Income Tax Act* could turn a return into a refund

In the short time the minority federal Conservative government has been in power, it has certainly put its stamp on the *Income Tax Act* with some significant changes for this tax season.

1. SPLITTING PENSION INCOME

Starting in 2007, you can split up to half of certain pension income with your spouse on your tax return. For example, income from a registered pension plan (with a defined contribution and a defined benefit plan) can be split at any age. That makes them more effective than RRSPs for income splitting before 65, unless you have a spousal RRSP, that is, which can also be split before 65.

After 65, the following additional types of income can be split: Registered Retirement Income Funds (RRIF) income and RRSP income that has been converted to an annuity.

What will these new rules provide? Likely a lower combined tax amount because you can utilize the tax rate of the spouse with the lower income.

It also potentially reduces the clawback of Old Age Security (OAS) of the higher earning spouse. When the recipient's net income exceeds \$63,511, OAS is normally clawed back or reduced by 15 per cent of the excess. In some instances it may make sense to RRIF at 65 so as to make use



of the income splitting rules.

The income splitting rules do not apply to OAS and CPP income, however; although spouses who are both at least 60 years of age can already share up to half of their CPP retirement benefits based on the number of years the couple has lived together while contributing to CPP.

Canadian residents who are also U.S. citizens should consider the U.S. income tax implications of splitting income as this may create adverse tax consequences.

2. CONVERSION AGE FOR RRSPS TO RRIFs

From 2007, the age at which you can convert your RRSPs to RRIFs has been extended from 69 to 71. This will allow you to make two additional years of contributions, and the deferral of minimum contributions for two years. However if income splitting with a spouse is a priority, then early conversion to an RRIF might make sense.

3. REGISTERED EDUCATION SAVINGS PLAN (RESP)

Good news for parents facing increasing future tuition costs for

their children: the \$4,000 annual RESP contribution limit has been eliminated and the lifetime RESP contribution limit has been increased from \$42,000 to \$50,000.

The maximum annual Canadian Education Savings Grant (CESG) is also increased from \$400 to \$500 beginning in 2007, which means that the contribution on which the CESG can be obtained increases from \$2,000 to \$2,500. The maximum lifetime CESG remains at \$7,200.

The elimination of the \$4,000 RESP annual limit and the increase of the total contributions to \$50,000 has some interesting planning opportunities if cash is available and funding education is a priority. However, the lump sum contribution should be done in conjunction with the maximization of the CESG.

4. INCREASE OF LIFETIME CAPITAL GAINS EXEMPTION

The lifetime capital gains exemption on the sale of qualified farm or fishing property or qualified small business corporation shares increased from \$500,000 to \$750,000. Structures should be reviewed to ensure that the additional \$250,000 exemption per taxpayer can be utilized.

5. GIFTING OF LISTED SHARES TO A PRIVATE FOUNDATION

The tax on capital gains arising from the donation of publicly listed securities to private foundations has been eliminated. This brings donations to private foundations in line with those to public charities.

This tax exemption creates significant tax savings when corporate gifting, as it increases the capital dividend account (CDA), which can be paid out tax-free. This has special application for flow through shares as the addition to the CDA is normally close to 100 per cent of fair market value.

There are many new opportunities to save on money this tax season. If you have any questions, be sure to talk to a financial adviser. 🍀

Robert Radloff

CA, CFP, CLU, is vice-president and technical director of Investaflex Financial Group, in Vancouver, B.C. Born in South Africa, he moved to Canada in 1994.

