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COMMENT

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PREPARING FOR TAX SEASON

As we enter a new year, the process of planning for the 2018 personal tax return season becomes top of mind for many. The primary objective is to ensure that the least amount of income tax is paid within the legal framework. The following are a few of the more commonly missed items when taxpayers are submitting their income tax returns.

Medical Expenses: Qualifying medical expenses can be claimed for a non-refundable tax credit. Expenses could include orthodontics, prescriptions, prescription eye glasses, dentures, etc. Eligible medical expenses not previously claimed for any twelve-month period ending in 2017 can be claimed on the 2017 tax return. It is a chronological 12-month period, which allows the taxpayer to alter the choice of the 12-month period in order to optimize the value of the credit.

For example, the earliest date for which expenses can be claimed may begin sometime in the 2016 calendar year and end 12 months later, in 2017. Taxpayers may claim medical expense paid in respect of themselves, their spouse or common-law partner, as well as dependent children of the taxpayer or taxpayer's spouse who are under the age of 18. The formula for calculating the federal tax credit is 15 percent of the qualifying medical expenses in excess of the lesser of three percent of the taxpayer's net income and $2,268 for 2017.

The formula is designed to create a minimum threshold below which the legislators consider expenses to be normal expenses that should be paid out-of–pocket, without tax assistance. In addition, the taxpayer may claim medical expenses related to certain non-arm's-length individuals who are dependent on the taxpayer. The definition of this group of dependants is more far-reaching than anywhere else in the *Income Tax Act.*

Dependants for this credit include the children of the taxpayer or taxpayer's spouse who are over the age of 18, parents, grandparents, aunts, uncles, nieces or nephews. Dependency is based on the facts of the situation but the Canada Revenue Agency (CRA) will look for evidence that the taxpayer is providing the dependant with the basic necessities of life such as food, shelter and clothing, on a regular and consistent basis.

The breadth of this opportunity should not be overlooked. Seldom do we see the recognition of a dependant relationship to such a great extent.

The federal tax credit for this second group of individuals is calculated as 15 per cent of the amount of the medical expenses in excess of the lesser of $2,268 (2017 figure) and three per cent of the dependant's net income. This second calculation is completed for each dependant, with medical expenses being claimed by the taxpayer.

The medical expense tax credit is not refundable and can only reduce the individual's overall income tax liability. This means that couples should review their situation and claim this credit on the tax return that generates the most tax savings.

Charitable donations: Qualifying charitable donations made in the 2017 calendar year (or unclaimed donations made in any of the previous five years) can be claimed by the taxpayer for a tax credit. There is an annual limit that caps the amount of charitable donations that may be claimed in a year at 75 percent of the individual's net income.

For many years, the top federal marginal tax rate was 29%, and the federal government generously applied this top marginal tax credit to all donations over $200. However, with the introduction of the new federal marginal tax rate of 33%, the government opted not to apply the 33% across all donations above $200. Instead, they created a notched formula that provides a 33% tax credit for donations made by individual's whose income falls within the 33% tax bracket.

The result is a formula that appears more complex than it actually is. The federal tax credit for 2017 is calculated as:

Step 1: 15% of the first $200 of donations

Step 2: 33 % of donations equal to the lesser of:
- (a) Amount of taxable income in excess of $202,800; and,
- (b) Amount of donations in excess of $200

Step 3: 29% of total donations not included in steps 1 and 2.

For example, assume an individual with taxable income of $212,800 in 2017 donates $12,200 also in 2017.

Step 1: 15% x $200
= $30

Step 2: 33% x the lesser of:
(a) $212,800 – $202,800 = $10,000; and
(b) $12,200 – $200 = $12,000
= 33% x $10,000
= $3,300

Step 3: 29% x ($12,200 - $200 (step 1 donation) - $10,000 (step 2 donation) = 29% x $2,000
= $580

Total federal credit = $30 + $3,300 + $580
= $3,910

In addition to the federal tax credit, the taxpayer will be eligible for a provincial donation tax credit. While Canada's tax system is written in a way that requires each individual taxpayer to claim his/her own donations, the CRA's administrative position generally allows one spouse to claim the donations made by the taxpayer and his/her spouse or common-law partner.

A charitable donation receipt is required to prove that a gift was completed. The receipt should identify the donor, the date of gift, the charity and the charity's registration number.

Public transit pass: This tax credit was eliminated in the 2017 federal budget; however, it is still available for qualifying expenditures made from January 1 to June 30, 2017. Eligible passes include:

- Passes that allow unlimited travel on public transit systems within Canada;
- short-term passes that entitle the user to unlimited
- travel for five consecutive days and the user buys at least 20 days' worth during a 28-day period; and
- electronic payment cards issued by a public transit authority who tracks and provides a receipt if the user travels at least 32 one-way trips over a 31-day period.

Interest expense and carrying charges: In simple terms, interest on money borrowed to earn business or investment income is generally tax deductible; however, interest expense on money borrowed to generate a capital gain is not tax deductible. It is important to review the investments for which the money was borrowed to ensure that there is no prohibition, in respect of the investment, to pay dividends or interest as this is generally an indication that the investment was more likely to be capital in nature rather than for investment income purposes.

Child care expenses: Generally, the deduction is claimed by the lower income spouse except when the lower income spouse is attending post-secondary education on a full-time basis.

The deduction is equal to the lesser of three amounts:

- the total qualified child care expenses incurred;
- $8,000 per child under age seven plus $5,000 for each child over age six but under age 16 and $11,000 for each child for whom the taxpayer has claimed the disability tax credit; and,
- two-thirds of the earned income of the spouse making the claim.

Child care expenses generally include payments in respect of caregivers, day nursery schools, day care centres, and day camps where the primary goal is to care for the children. Eligible child care expenses do not include amounts paid to a parent of the child for whom the amount is being claimed or a person under the age of 18 who is related to the taxpayer making the claim.

Carry forward information: The CRA sends all taxpayers a notice of assessment after they have filed their income tax return. The notice of assessment from the prior year contains a wealth of valuable information that should be reviewed as the current year's return is being prepared.

The notice of assessment should include the taxpayer's RRSP contribution limit and any carry-forward amounts such as capital losses. Tax return preparation should begin by reviewing last year's tax return together with last year's notice of assessment. It is important to locate and have on hand all income reporting receipts together with receipts for all deduction and credits being claimed.

While the electronic processing of income tax returns means taxpayers are no longer required to submit receipts at the time the return is filed (paper filers still submit all receipts), it is common for the CRA to systematically audit electronic returns, at a later date, by asking taxpayers to submit select receipts for verification.

If a taxpayer owes money when the income tax return is complete, the only way to delay the payment is to consider delaying the filing until the April 30th deadline. Alternatively, if the taxpayer is owed money, then it is to the taxpayer's benefit to file as early as possible.

CLEARANCE CERTIFICATES FOR AN ESTATE

In order to protect the Canada Revenue Agency's (CRA) ability to collect income taxes owing, the *Income Tax Act* contains a provision that requires an estate's executor/executrix or administrator to apply for a clearance certificate from the CRA before distributing assets from the estate.

Failure to obtain a clearance certificate leaves the executor personally liable for any outstanding income tax liability that the CRA cannot collect from the estate that otherwise would have been available.

A clearance certificate certifies that all amounts for which the estate is liable under the *Income Tax Act* have been paid or adequate security has been posted. In determining the amount of the liability, the executor is responsible for the actual income tax liability as calculated plus the liability that could reasonably be expected. The liability would include the actual income taxes owing, plus any interest and penalties that may apply.

An estate representative requests a clearance certificate by filing CRA form TX19, Asking for A Clearance Certificate. The form requires an extensive amount of information including, for example:

- Details about the deceased's identity - full legal name, social insurance number, date of death and last address of the deceased;
- Documents to support estate distribution instructions - complete and signed copy of the taxpayer's will, including any codicils, renunciations, disclaimers, and all probate documents, if applicable;
- The document appointing an administrator if the taxpayer died intestate (without a will);
- Documents to substantiate who has authority as the estate's legal representative;
- Details of all assets that were owned by the deceased at the date of death – lists of assets held personally by the deceased as well as assets held jointly, registered retirement savings plans and registered retirement income funds. Even though some assets may pass to heirs by way of joint ownership or beneficiary designations, these assets are still required to be included in the list provided to the CRA. The application requires each asset's fair market value and adjusted cost base as of the date of distribution from the estate;
- Details about distributions made and proposed from the estate;
- Details about all beneficiaries receiving property other than cash - names, addresses, and social insurance numbers; and,
- Authorization if the CRA is to communicate with someone other than the estate's legal representatives – include completed Form T1013, Authorizing or Cancelling a Representative.

If after receiving a clearance certificate the executors discover another asset, they must file for another clearance certificate in respect of the newly discovered asset. This process ensures that the CRA has full knowledge of an estate's tax liabilities, details of the estate's assets and is fully aware of beneficiary details.

The clearance certificate is an important part of being an executor. The process is detailed and may require extensive research into the affairs of the deceased and the beneficiaries of the estate.

COMMENT

GOVERNMENT PENSION PLANS: BENEFITS AND CONTRIBUTIONS FOR 2018

Contributions and benefits under government pension plans are adjusted periodically to reflect increases in the Consumer Price Index or the average Canadian wage. The new amounts, commencing January 1, 2018, are shown in the table below. Each benefit is subject to income tax when received, with the exception of the Guaranteed Income Supplement and the Allowance. All benefits shown are paid monthly unless otherwise indicated, and are the maximum amounts.

	CPP	QPP	OAS
CPP / QPP Benefits (for new beneficiaries)			
Retirement pension (at age 65) Post-Retirement benefit (at age 65) Retirement Pension Supplement	$1,134.17 $28.35 n/a	$1,134.17 n/a $21.58	
Disability pension	$1,335.83	$1,335.80	
Disabled contributor's child benefit (each child)	*$244.64	*$77.67	
Survivor's*** pension			
• under age 65	**$614.52	**$910.48	
• age 65 or over	$680.50	$680.50	
Surviving child's benefit (each child)	*$244.64	*$244.64	
Death benefit (lump sum)	$2,500.00	$2,500.00	
Annual CPP contribution			
Self-employed (9.9%)	$5,187.60		
Employee (matched by employer) (4.95%)	$2,593.80		
Annual QPP contribution			
Self-employed (10.8%)		$5,659.20	
Employee (matched by employer) (5.4%)		$2,829.60	
Old Age Security (OAS)			
January to March 2018			$586.66
Guaranteed Income Supplement (GIS)			
January to March 2018			
Spouse/common-law partner receives OAS or Allowance			$527.48
Single person (or spouse/common-law partner receives neither OAS or Allowance)			$876.23
Allowance			
January to March 2018			
Age 60 to 64, and spouse/common-law partner receives OAS and GIS			$1,114.14
Age 60 to 64, survivor's*** Allowance			$1,328.08

Notes: * flat benefit amounts
** these amounts may vary depending on whether the survivor is under age 45, disabled, or with or without children
***a survivor is the spouse or common-law partner of a deceased individual

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