

# COMMENT

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## Charitable Donation That Offers Double Dip

It is always nice to get something for half price or to get twice as much for the same expenditure. While this does not happen very often in tax planning, when it does it makes sense to review the final after-tax or economic position of the taxpayer.

One such example of being able to get more for less is when a private corporation makes a gift of appreciated stocks listed on a prescribed stock exchange to a charitable organization, a public foundation or a private foundation. In addition, shares of private corporations could also be donated but the tax relief in that case is only offered with respect to gifts to charitable organizations and public foundations, not private foundations.

A gift as described above will generate two tax benefits. The first tax benefit is that the inclusion rate for calculating the taxable capital gain on the disposition of the shares is zero. The second tax benefit is that the private corporation is entitled to a credit to its capital dividend account equal to the non-taxable portion of the capital gain. In this case, this is 100 per cent of the capital gain (since no part of the gain was includable in income for tax purposes).

While the current investment environment may not hold a lot of accrued capital gains for many investors, some portfolios may contain some insurance company shares that were part of the demutualization process where the adjusted cost base is zero. Consider the

example of a donor who decides to complete her charitable pledge by causing her holding company to donate \$250,000 of such shares to her favourite charity.

- The donation of the shares will entitle the corporation to a charitable receipt in the amount of \$250,000. Care will have to be exercised with respect to the valuation of the shares in order to make sure the charitable receipt is valid. A gift of private company shares would probably be followed by the charity asking for a redemption of these shares.
- If the corporation is primarily an investment holding company, the tax shield generated by the charitable receipt should be between 44.67 per cent to 50.67 per cent, which is the combined federal and provincial tax rate applicable to investment income depending on the corporation's province of residence in 2008. Let's assume the tax saving is \$119,175, which is the average between the lowest province at \$111,675 and the highest province at \$126,675.
- In addition, the corporation will be able to credit its capital dividend account in the amount of \$250,000, which would be the capital gain generated on the disposition of \$250,000 worth of shares with a zero adjusted cost base. The value of a credit in a corporation's capital

dividend account is the ability to pay tax-free dividends to its shareholders, who would be able to avoid personal tax of between 26.46 per cent and 37.40 per cent in 2008. Let's assume the value of the tax savings on these dividends is \$79,825, which is the average between the lowest province at \$66,150 and the highest province at \$93,500.

- With proper tax planning, the bottom line is that a gift of \$250,000 would only cost the taxpayer about \$51,000.

Rather than leave the taxpayer in a "cost" position, the \$79,825 of tax savings could be used to fund a life insurance program that would recover the value of a \$250,000 gift back

to the family. A corporate-owned life insurance program would by itself generate a third benefit, which would be another credit to the corporation's capital dividend account. A couple aged 65, both non-smokers, should be able to fund a \$250,000 joint last-to-die life insurance program for approximately \$79,000.

Tax planning is normally about keeping taxes to a minimum or reorganizing a taxpayer's situation without triggering tax, but when planning can accomplish more tax savings than usual, the taxpayer can benefit from a double dip.

I/R 1600.00

## RRSP Maturity Options

A registered retirement savings plan (RRSP) has to mature by December 31<sup>st</sup> of the year the annuitant turns age 71. An RRSP can also be matured earlier by the annuitant as part of planning for retirement income.

An annuitant has four options with respect to maturing his or her RRSP:

- 1) withdraw the funds;
- 2) transfer the funds to a registered retirement income fund (RRIF);
- 3) use the funds to purchase an annuity for life; or
- 4) use the funds to purchase an annuity spread over the number of years to age 90.

The option chosen should be based on the needs of the annuitant and not on just the income tax consequences of the alternative.

A complete withdrawal may make sense if the annuitant needs the funds or the RRSP is relatively small. A complete withdrawal of funds could generate a significant income tax liability because the withdrawal would be taxable in the year. However, if the annuitant needs the funds this may be the only choice. Also, a withdrawal may be part of a plan to

maximize the receipt of the annuitant's old age security by lowering taxable income in the future (i.e., because the income from the registered plan has been eliminated).

A RRIF may make sense if the annuitant wants to maintain control over his or her principal or income levels or needs to minimize income. A RRIF prescribes a minimum withdrawal amount based on the balance in the RRIF as at January 1<sup>st</sup> of each year and the annuitant's (or spouse's age) as at January 1<sup>st</sup> of each year. An annuitant may want to minimize his or her overall income so electing to receive the RRIF minimum withdrawals will match these needs. An annuitant can control his or her income levels above the RRIF minimums by requesting whatever withdrawal pattern will meet those needs.

A life annuity may make sense if the annuitant wants to guarantee a fixed (or indexed) amount of income for his or her lifetime or the joint lifetime of the annuitant and his or her spouse. Guarantees can be very important for some annuitants because they provide peace of mind with respect to investment risk and longevity risk. Once established, an annuity payout is not generally subject to investment volatility.

A term certain annuity would provide a level (or indexed) income for a fixed period of time until

the annuitant's age 90 (or a younger spouse's age 90, if so elected). A term certain annuity may make sense if the annuitant does not feel that his or her life expectancy is beyond age 90 and would like to have the slightly higher income amount compared to a life annuity.

The RRSP maturity options can provide a wide range of income options. Another facet of analysis is the amount left over that will pass onto the annuitant's family. Even though residual registered money would be taxable in the deceased's final return, some annuitants want to ensure that there is something left for their beneficiaries. A complete withdrawal could create a leftover amount if the annuitant kept the after-tax amount invested. A RRIF could leave a residual amount depending on investment returns and the amounts previously withdrawn. A life annuity and term certain annuity can leave a residual amount depending on the guarantee period of the life annuity or the time remaining in a term certain annuity.

If an annuitant has attained age 65 and does

not receive other income eligible for the \$2,000 pension income amount on the income tax return, it may be advisable to purchase an annuity or RRIF starting at \$2,000 per year. Where the taxpayer's spouse has also attained age 65 and the spouses elect to split pension income, the annuity or RRIF income can be increased to \$4,000. The remaining funds may be left to accumulate in the RRSP until age 71. In fact, if one or both of the spouses have RRSP contribution room, the funds received can be contributed to RRSPs for another tax deduction.

One of the most important observations about the choices facing an annuitant is that he or she is not limited to one alternative, but may be better off choosing a combination of several alternatives. A combination approach would allow the annuitant to achieve the advantages of several alternatives and minimize the risk of any one alternative.

I/R 5401.00

## Moving

Moving may be very taxing from the point of view of boxing up the contents of the old house, loading and unloading the moving truck, and finally setting up the new household. But moving may also bring some income tax relief in terms of a deduction from income.

To be deductible, the move must make the taxpayer 40 kilometres closer to work, whether that is with an employer or as a self-employed person. The 40-kilometre distance would be measured as the difference between the travel from the old home to the old work location and travel from the new home and the new work location (if different). In addition, both the old home and the new home would have to be in Canada.

In addition to moving for work, students also qualify for the moving expense deduction. Such a move must be made to attend full-time studies at a university, college or other educational institution. A student is allowed moving expenses even if one end of the move

was outside Canada.

Over the years, the 40-kilometre distance has been the subject of interpretation. The issue has been resolved by the Federal Court of Appeal to be the distance as measured using the shortest normal travel route available to the travelling public.

Moving expenses are deductible against income earned in the new location. If the move is near the end of the year, there might not be sufficient income earned in the new location to absorb the moving expense claim. In such a situation, the moving expenses would be deductible in the following year against income earned in the new location. For students, income would include employment income as well as scholarships, fellowships, bursaries or research grants received in the new location.

The moving expenses that qualify for deduction are listed and detailed in the Income Tax Act

to include:

- (a) travel costs between the old home and new home, plus a reasonable amount expended on meals and lodging during travel;
- (b) the cost of transporting or storing household effects from the old home to the new home;
- (c) the cost of meals and lodging near the old home or the new home, but not for a period exceeding 15 days;
- (d) the cost, if any, of cancelling the lease or a mortgage discharge payment on the old home;
- (e) the cost of selling the old residence, such as sales commission, advertising, legal expenses, etc.;
- (f) the legal costs and any fee or duty imposed to transfer or register title on the new home;
- (g) interest, property taxes, insurance premiums and the cost of utilities in respect of the old home to a maximum of \$5,000 if the taxpayer has vacated the old home and reasonable efforts are being made to sell the old home; and
- (h) the costs of revising legal documents, replacing driver's licences, connections and disconnections in respect to changing residences.

Any reimbursement from an employer would reduce the amount of deductible moving expenses. A planning idea to maximize a taxpayer's position is to have the employer reimburse only non-deductible expenses, thereby maximizing the taxpayer's overall financial position. This strategy is specifically addressed in the Canada Revenue Agency's Interpretation Bulletin IT-178R3. Care would have to be taken to ensure what type of expenses would be reimbursed by the taxpayer's employer.

While moving may be taxing, there can be some tax benefits to the move that every taxpayer should take the time to maximize in order to preserve the most favourable financial position.

I/R 7401.00

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