

Marmer Penner Inc. Newsletter

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Income Splitting Opportunity

Investors who rely on fixed income securities such as guaranteed investment certificates (“GICs”), treasury bills and bonds cringe when they see the low rates facing them now upon renewal. These low interest rates, however, create a tax planning opportunity which may translate into an income splitting opportunity in family law matters.

The *Income Tax Act* (“ITA”) contains what are known as “attribution rules” that prevent a taxpayer from income splitting certain types of investment income with lower-taxed family members by transferring money to them. This applies to both gifts and interest-free loans. In such cases, the attribution rules attribute any interest or dividends earned to the transferor. The ITA does permit the transfer of funds for such purposes if it is by way of a loan bearing interest at a rate no lower than Canada Revenue Agency’s (“CRA”) prescribed rate of interest. In such a case, the transferor must include the loan interest in his income.

CRA’s current prescribed rate of interest is at an all-time low of 1%. According to the ITA’s income attribution rules, if Dad wishes to lend Junior \$100,000 interest-free to invest on Junior’s behalf, any interest or dividends that Junior earns is attributed to Dad for

income tax purposes. However, if Dad charges Junior the prescribed rate, there is no attribution. Accordingly, a parent can now lend their minor child, say, \$100,000 at 1% to permit the child to buy a longer term bond or GIC which pays 3%. Even better, the parent can lend the money to a child to purchase one of many high dividend paying securities such as Bank of Montreal and Canadian Imperial Bank of Commerce, both of which currently pay dividend yields in excess of 5%. This is not just an opportunity for all parents to income-split, but also for support-paying spouses to reduce their Line 150 income. If it is not obvious, family law practitioners should determine the source of all interest income reported on a spouse's personal tax return. If the interest income of a spouse includes income from related parties (especially minors), it may indicate this type of income splitting. In this case, it may be prudent to request details of the loan made to the related party and/or copies of the related party's personal tax returns.