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# 2014 YEAR-END TAX REVIEW AND TIPS

As 2014 draws to a close, it is important to think about your overall financial situation to ensure you have considered year-end tax issues and strategies. We suggest that you review all of the following items to see if any of them apply to you or a family member.

## New in 2014

**Family Tax Cut** – The federal family income splitting plan is a non-refundable tax credit of up to $2,000 for couples with children under 18 years of age. This credit will allow the higher income earning spouse to transfer up to $50,000 of income to a lower income earning spouse for a tax savings up to $2,000. This credit will be available for 2014 tax year.

**Ontario Tax Rates** – Ontario has introduced two new tax brackets. 12.16% on taxable income between $150,000 and $220,000 and 13.16% for income greater than $220,000. These changes are effective for the 2014 tax year. These new brackets will ***not*** be adjusted for inflation.

**Ontario Provincial Retirement Savings** – The Ontario government's July 2014 budget includes a plan for an Ontario Retirement Pension Plan (ORPP) that will be introduced in 2017. The plan will require a 1.9% annual contribution (from both employer and employee) up to a maximum earning threshold of $90,000. Similar to CPP, benefits are earned as contributions are made. It will be mandatory except for the self-employed, those already enrolled in workplace pension plans, and for federally-regulated workplaces.

## RRSPs and Tax-Deferred Plans

| Maximum contribution limits for tax-deferred plans for 2014 and 2015 are as follows: | | | |
|---|---|---|---|
| **Year** | **Registered Retirement Savings Plan (RRSP) Limit** | **Defined Contribution (DC) Registered Pension Plan (RPP) Limit** | **Deferred Profit Sharing Plan (DPSP) Limit** |
| **2014** | $24,270 | $24,930 | $12,465 |
| **2015** | $24,930 | $25,370 | $12,685 |

- **Contribution Deadlines:**
  - The final day to contribute to an **employer's RPP** is **December 31st, 2014**.
  - The final day for **RRSP contributions** for deduction in 2014 is **March 2nd, 2015**.
  - **March 2nd, 2015** is also the final day to contribute to a surviving spouse's RRSP for a deduction on the final tax return of a deceased taxpayer.
  - Note that **December 31st, 2014** is the final day for contributions to your RRSP if you turn 71 this year (see below).

- **If you turn 71 in 2014**, you must convert your **RRSP/LIRA** to a RRIF/LIF/LRIF by **December 31st, 2014**. Note that the beneficiary designation for your RRSP/LIRA *does not* automatically transfer to your newly established RRIF/LIF/LRIF. If you want your spouse, partner, or someone else to be the specific beneficiary of your new account, this must be indicated on your application. If you have contribution room available, make your contribution prior to conversion. *Individuals turning 71 this year DO NOT have the extra 60 days after year-end to make a contribution to their own RRSP*.

- **If you have a spouse or partner who is younger than you**, you may base the minimum required annual withdrawals from your **RRIF/LIF/LRIF** on his/her age.

- **Another benefit of having a younger spouse or partner** is that, even if you are older than 71 and consequently can no longer have your own RRSP, you may continue to contribute to his/her spousal RRSP until the end of the year in which *he/she* turns 71, with the amount contributed being based on *your* RRSP limit. You will have the tax deduction for your spousal contribution, and your spouse may also contribute to his/her own RRSP, if applicable.

- **If you turn 71 in 2014 and do *not* have a younger spouse or partner**, you may wish to consider making an over contribution to your RRSP in December 2014, just before converting the RRSP to a RRIF. This strategy can work if you have used all your contribution room in 2014 ***and*** have earned income in 2014 that will create contribution room for you in 2015. The over contribution will be subject to a penalty tax of 1% just for the month of December 2014, but the over contribution situation is eliminated in January when the 2015 contribution room begins to apply. The un-deducted contribution is carried forward, and is deductible in 2015 or a later year. The 1% penalty is a small price to pay to get a deduction next year at your applicable tax rate, as well as allowing the additional amount to work for you sheltered in the new RRIF.

- If you are required to take a minimum annual withdrawal from your RRIF/LIF/LRIF, and you would prefer not to sell particular assets, you can **make an 'in kind' transfer to your non-registered investment account.** The market value of the assets transferred out will be taxable as a withdrawal, but you will then be able to retain the investment in your non-registered account. If you are considering this, we recommend that you check with your financial institution to ensure they can accommodate your request.

- **Transferring assets into an RRSP or TFSA (contributions in kind) –** You may transfer assets into your RRSP or TFSA as a contribution, and the contribution will be valued at the market value on the date of the transfer. **Note** that any gain on assets transferred into your RRSP or TFSA will be taxable to you in the year of the transfer.

  However, losses realized on contributions in kind may not be claimed. Therefore, selling such assets first and then contributing the cash to the RRSP or TFSA will preserve the capital loss. Just remember not to repurchase identical assets within 30 days, or the Superficial Loss rules [explained on page 5] will negate the loss. These rules apply to purchases inside or outside of your RRSP or TFSA, *and* to purchases inside or outside of the RRSP or TFSA of your spouse or another 'affiliated person'.

- **Home Buyers' Plan** – If funds were withdrawn from an RRSP prior to 2013 under the Home Buyers' Plan, a repayment equal to 1/15 of the amount withdrawn must be made by **March 2nd, 2015**. Failure to do so will result in the required repayment amount being included as taxable income for 2014. The repayment is not deductible since the withdrawal was not taxable. A repayment is made by making a contribution to the RRSP, and in addition you may make a further contribution using the regular RRSP rules.

## Investments

- **Non-registered GICs** – If you have GICs maturing in late 2014, defer reinvesting the proceeds in a new GIC until January 2015. The interest on a GIC purchased in December 2014 will be taxable in 2015, while the interest on a GIC purchased in January 2015 will be taxable in 2016.

- **Non-registered mutual funds** – If you invest in a mutual fund (outside of your registered accounts) between now and **December 31st,** you may be in for a shock when you file your 2014 income tax return. Mutual funds must distribute all interest, dividends and realized capital gains to unit holders in the fiscal year in which they receive them. Many Canadian funds use the calendar year as their fiscal year. A year-end distribution results in you paying tax on the distribution allocated to you, even though it is effectively a return of capital from your investment. You may be best advised to defer the purchase of a mutual fund investment until January.

- **The deadline to contribute to a Registered Education Savings Plan (RESP) for 2014 is December 31st, 2014. You DO NOT have 60 days after the end of the year to contribute,** as with an RRSP. You may also contribute amounts for past years where you have not received the maximum government grant. However, there are limits to the amount of retroactive grants you can receive in one year, so it might not be advantageous to catch up all unused contributions at one time. Generally speaking, each year you are limited to claiming one year's worth of retroactive grant (i.e. a $500 grant, based on a $2,500 contribution). If you are several years behind in making RESP contributions, it will take several years for you to catch up on missed grants.

- **Tax Free Savings Account (TFSA)** – Since 2009, Canadian residents aged 18 and older have been eligible to contribute to a TFSA. While there are no tax deductions for contributions, investment income in the account grows tax-free. Any amount can be withdrawn from a TFSA at any time, for any reason, tax-free. Withdrawals will not affect income-tested benefits and credits. Any withdrawals made in the current year will be added to the contribution room for the following year, and unused contribution room can be carried forward indefinitely. If you are planning a withdrawal, consider doing so before the end of 2014 instead of early 2015.

## Capital Gains and Losses

Generally, the tax strategy discussed the most in the month of December is 'tax loss/gain selling'. As the factors surrounding this issue are based on individual circumstances, please contact your E.E.S. consultant to determine how any tax benefits may apply to you.

- **The disposition of securities** is deemed to take place not on the day that the order is placed, but rather on the 'settlement date'. For most securities, settlement occurs three business days after placing a sell order. As such, to be considered on your 2014 tax return, Canadian transactions should be placed by **December 24th, 2014** and U.S. transactions should be made by **December 26th, 2014.**

- **Capital Gains and Losses** – 50% of your **capital gains** are included in your income. **Capital losses** may be carried back and claimed against any net capital gains reported in the previous three years (2011, 2012 or 2013) or carried forward indefinitely. *However, your current year losses must be used **first** to offset your current year gains (if any).*

- **Currency** may, in certain circumstances, be considered a capital property, and holdings of currency other than Canadian currency can result in a capital gain or capital loss from fluctuations in foreign exchange rates.

- **Employer stock options** are taxed as employment income, ***not*** capital gains; hence, capital losses cannot be applied to reduce the tax payable due to the exercise of stock options.

- **Deemed Disposition** – Be aware that you may trigger a deemed disposition on acquisition of assets even though no transaction occurs. Examples include death, a marriage break-up, entering or leaving Canada, RRSP or TFSA contributions 'in kind', corporate reorganizations and 'change of use' of assets.

- **The Superficial Loss Rule** can negate the tax benefit of selling at a loss if you, your spouse or common-law partner, or another related entity acquires the same investment in the 30 days preceding *or* following the sale of the security on which you are claiming the loss. Note that an **RRSP or TFSA** is considered to be a related entity [see related item on page 2: *Transferring assets into an RRSP or TFSA*].

  However, **you can use the Superficial Loss rule to your advantage** – Assume you are holding a stock with a book loss and you do not have any gains against which you can use the loss, but your spouse does. If you sell your stock on the open market and within 30 days your spouse acquires the same stock, you trigger the Superficial Loss Rule. You have forfeited the use of your loss as your sale price is assumed to be your (higher) cost base. The extension is that your spouse is deemed to have acquired the stock at your (higher) cost. Your spouse then retains the stock for at least 30 days, sells and now has the loss in his/her hands.

## Borrowing for Tax Purposes

- **Carrying Charges** – As a general rule, interest is deductible for tax purposes as long as the proceeds of the loan are used for the purpose of earning income from a business or property. This is often referred to as 'carrying charges'. Several tax cases exist regarding the application of this rule. Québec has rules in place which limit the amount of deductible interest charges to the investment income earned in the taxation year.

- **Spousal Loans –** For any such loan done at CRA's prescribed interest rate (done to achieve income splitting between spouses/partners), interest accrued to December 31st, 2014 must be paid by **January 30th, 2015.** The current prescribed rate is 1%, effective until December 31st, 2014. The prescribed rate changes on a quarterly basis, however this only applies to new loans. As an example, a loan done at today's 1% rate will continue to be onside with CRA's rules for the duration of the loan—even if CRA increases the prescribed rate in the future.

## Charitable Donations

- **Share Security and Option Donation –** Consider making a charitable donation of a security with an accrued capital gain instead of using cash. As a result of donating the security instead of cash, none of the gain will be included as taxable income instead of the standard 50% inclusion. A tax receipt will be issued for the entire fair market value of the donated security.

  This special tax treatment is also available for proceeds received through the exercise of employee stock options if the proceeds are donated directly by the exercising broker within 30 days of acquisition.

- **Donation of Air Miles or other loyalty program points –** Companies often make it difficult to redeem air miles and loyalty program points, which results in an accumulation of miles and points with little or no value. Donating these miles or points to charity is a great way to redeem them and make a difference at the same time. Depending on the organization, these donations may yield a tax receipt.

## Employment - Related Expenses

- **Stock options** give employees the right to purchase shares of their employer's company at a set price, known as the exercise price. The difference between the fair market value and this exercise price is taxed as employment income (*we emphasize: this is **not** a capital gain*). Most employees can claim a deduction of 50% of the taxable benefit on qualified options, resulting in only 50% of the stock option benefit being taxed.

- **If you received a loan from your employer**, and you did not use the proceeds for the purpose of generating investment income; you can reduce the amount of the taxable benefit by making an interest payment before **January 30th, 2015**.

- **If you have a company car,** there is a taxable benefit attributable to your use of the vehicle that is reported on your T4 and Relevé 1. Keep a log of your personal and business-use kilometers for your company vehicle to ensure easy reconciliation for your tax return. You may qualify for a reduced *standby charge* and *operating cost benefit* based on usage.

- **Employees who use their own car for business purposes** can receive a tax-exempt allowance from their employer if the allowance is based on the kilometers driven for business purposes, as opposed to a lump-sum allowance. The 2014 limit is 54 cents for the first 5,000 kilometers and 48 cents thereafter.

- **If you have eligible employment expenses or work from home more than half of the time**, your employer may be required to provide a form T2200, *Declaration of Employment Conditions*. Be sure you obtain a T2200 if it is applicable.

## Source Deductions

- **If you have tax-deductible expenses** such as RRSP contributions, support payments, childcare expenses, investment carrying charges, rental losses, etc., application can be made to the CRA or Revenu Québec to reduce your tax deductions at source for 2014. If approved, your employer may reduce the tax withheld at source, resulting in increased cash flow for the employee. The approval process generally takes six weeks.

## Alternative Minimum Tax

- Certain tax-deductible items may expose you to **Alternative Minimum Tax (AMT)**. While this tax may be carried forward and applied in future years, it can be lost if you leave Canada and have no further taxable Canadian income. Residents of Québec can lose the provincial AMT simply by leaving the province.

## Income Tax Instalments

- If the difference between your federal tax payable and your income tax withheld at source is greater than $3,000 ($1,800 if you are a resident of Québec), you are generally asked to make income tax instalment payments. The reporting notices provided by the CRA can be confusing. If you expect that your liability will be more or less than previously calculated, you may want to adjust your final payment accordingly. While you do not want to overpay your tax, the CRA will charge you interest, and possibly penalties, if you underestimate the amount owing. The final federal income tax instalment for 2014 is due December 15th, 2014, payable to the Receiver General for Canada.

- If you were reassessed for 2013 for additional income, this may affect your 2014 tax instalment payments.

- If the difference between your **Québec tax payable** and your Québec tax withheld at source is greater than $1,800, you are generally asked to make instalments. The final Québec income tax instalment for 2014 is due **December 15th, 2014**, payable to le Ministère du Revenu. The penalty for late or insufficient Québec instalment payments is an extra 10% in addition to the normal interest rate.

- If you think your December payment should be adjusted, contact your E.E.S. consultant for assistance with the calculation as you do not want to find yourself 'off-side' with the tax department.

## Business Owners

- **For business owners** who employ family members, pay salaries by **December 31st, 2014** to add to their reported earned income for RRSP and CPP/QPP contributions.

- **Owner managers** with control over their income may want to ensure that they have enough employment income to maximize their **RRSP contributions**. In order to reach the maximum contribution level for 2015 ($24,930), you must have had $138,500 of *earned income* in 2014.

- **If purchasing capital assets** (such as computers, furniture or equipment) in the near future, consider making the purchase(s) before the calendar year end, or fiscal year end for businesses, as applicable. This will allow for a depreciation claim on your 2014 return.

- If you took a **shareholder loan** from your corporation in 2013, repay it, if possible, before the end of 2014. If not repaid, it will be taxable as income for 2013.

## Québec Differences

- The **stock option deduction** for Québec provincial tax purposes is 25%, compared to 50% for federal tax purposes.

- **Québec Strategic Economic Investments** – Québec has identified a number of "Strategic Economic Investments" for the Québec economy which continues to be supported by income tax incentives available to the Québec taxpayer. The tax credit rate was reduced in the 2014 budget.

- **Medical Expenses** – The non-refundable tax credit for medical expenses is reduced by 3% of Québec family income which is the combined net income for both spouses. Unlike the 3% federal reduction, the Québec reduction is not capped.

- For **investors in Québec**, the amount of **deductible interest and carrying charges** is **limited** to the amount of investment income, including capital gains, realized in the taxation year. Rental losses and active business losses are exempt from this limitation. These expenses can be carried back three years or carried forward indefinitely to apply against investment income and capital gains. Be aware that many tax shelter write-offs are included in the limitations and may not be deductible, depending on your circumstances.

- **Eligible childcare expenses –** Unlike the federal treatment of childcare expenses as a deduction, eligible expenses for Quebecers are claimed as a refundable tax credit.

## U. S. Citizens, Residents and Green Card Holders

- If you are a U.S. citizen, resident or green card holder, you are obliged to file a tax return with the IRS and possibly state tax returns. Several other information returns may also be required. Failure to provide the necessary filings can result in serious interest and penalties. You should discuss your situation with your E.E.S. consultant as soon as possible to ensure your affairs are in order before year-end.

- As income earned within a Tax-Free Savings Account (TFSA) is not sheltered from tax for U.S. income tax purposes, it is advisable for those subject to U.S. income tax reporting ***NOT*** to own a TFSA.

- Similarly, income earned within a Registered Education Savings Plan (RESP) is not sheltered for U.S. purposes. Therefore, those subject to U.S. income tax reporting are advised ***NOT*** to set up an RESP to save for children's education unless there is someone else not subject to U.S. income tax reporting who can be designated as the trustee.

- If you are not a U.S. citizen, resident or green card holder, **but hold U.S. assets**, you should contact your E.E.S. consultant to confirm all requisite filings are in order.

- As a client of E.E.S. we have been counseling you to review your status as it relates to U.S. holdings and the onerous, penalty riddled filing requirements. ***If you believe the I.R.S. touches you in any way, please ensure you have brought these issues to the attention of your E.E.S. consultant.***

- For those who are using Individual Taxpayer Identification Numbers (ITINs), the IRS announced in June 2014 that they will start deactivating ITINs that have not been used on at least one tax return in the past five years. The deactivation process will start in 2016. Individuals with deactivated ITINs will need to reapply for ITINs.

## Changes to the Canada Pension Plan (CPP)

- ***Adjustments for Early and Late Take-Up*** – The phase in of the early take-up rate began in 2012. For 2014 it was 0.56% per month and will reach 0.6% by 2016. The late take-up rate is 0.7% per month.

- ***Participation of Working Beneficiaries*** – If you are age 65 to 70 and receiving your CPP and working, you can choose to make CPP contributions to increase your benefits. Continuing to participate will be optional after reaching age 65 and **you will have to file a CPT30 election if you do not want your employer to withhold contributions.**

## New in 2015

**Universal Child Care Tax Benefit (UCCB)** – Beginning in January 2015, the monthly UCCB benefit for children under the age of 6 will be increased from $100 to $160.

Effective January 2015, a $60 monthly benefit will be paid for each eligible child who is at least the age of 6 until the child reaches the age of 18. The first payment will be in July 2015 which includes up to 6 months of benefit.

**Child Care Expense Deduction** – Effective for the 2015 taxation year, the maximum amount of deductible child care expenses will be increased to $8,000 for each child under age of 7, to $5,000 for each child age 7 through age 16, and to $11,000 for any child eligible for the disability tax credit.

**Children's Fitness Tax Credit** – Effective for the 2015 taxation year, the annual limit for the children's fitness tax credit is increased from $500 to $1,000. The credit will also become refundable; if the total amount of credit exceeds the taxes owed, CRA will refund the difference.

**Children's Tax Credit** – Effective for the 2015 taxation year, the non-refundable credit of $2,234 for each child under 18 will be eliminated.

**Tax Free Savings Account (TFSA)** – The annual contribution limit for TFSA remains at $5,500 for 2015.

**Please contact your E.E.S. Consultant for further details concerning any of these tax topics.**