Year End Tax Planning 2023-2024

Crowe BGK LLP

YEAR END TAX PLANNING

November 2023

Fall is an appropriate time to review various income tax and financial planning techniques that are available to individual and corporate taxpayers. Most tax planning transactions require analysis before being implemented, so that they can be applied appropriately and consistently with the tax law. We encourage you to consult your Crowe BGK advisor before initiating any of the strategies outlined in this issue.

WHAT'S NEW FOR 2023

New Trust Filing Requirements

Trusts having taxation years ending on or after December 31, 2023 are subject to new filing and information reporting requirements. These new reporting rules will apply to most trusts resident in Canada and non-resident trusts that are currently required to file a trust return. They also create a filing obligation for certain trusts that would not otherwise have to file a trust return. Failure to comply with these new requirements will result in significant additional penalties which could amount to 5% of the maximum fair market value of the trusts' assets during the year.

First Home Savings Account

A first home savings account (FHSA) is a registered plan allowing prospective first-time home buyers to save for their first home tax-free (up to certain limits). Canadian residents aged 18 years or over may open a FHSA, and this since April 1, 2023, provided they meet the eligibility requirements. The annual contribution limit is $8,000 and the lifetime contribution limit is $40,000. Contributions will generally be tax-deductible and qualifying withdrawals will not be taxable.

Changes to Alternative Minimum Tax (AMT)

The Alternative Minimum Tax (AMT) is a parallel tax calculation that allows fewer deductions, exemptions, and tax credits than under the ordinary income tax rules, and that currently applies a flat 15% tax rate with a standard $40,000 exemption amount instead of the usual progressive rate structure. The taxpayer pays the AMT or regular tax, whichever is highest. Additional tax paid as a result of the AMT can generally be carried forward for seven years and can be credited against regular tax to the extent regular tax exceeds AMT in those years. The AMT does not apply in the year of death.

A number of changes are proposed to broaden the AMT base by further limiting deductions, exemptions, and tax credits, increasing the standard exemption amount to $173,000 (for the 2024 taxation year) and increasing the AMT rate to 20.5%. These changes will apply to taxpayers as of January 1, 2024. If you are considering realizing significant capital gains and/or disposing of shares for which the capital gains exemption may be claimed, consult with your Crowe BGK advisor to determine if it is more advantageous to conclude such transactions before or after December 31, 2023.

Updates to the Intergenerational Share Transfer Rules

Because capital gains are generally subject to a lower tax rate than dividends, individuals may seek to obtain significant tax benefits by entering into a series of transactions aimed at converting corporate distributions of after-tax business income from their corporations (ordinarily taxed as dividends) into lower-taxed capital gains. Section 84.1 of the Income Tax Act is designed to address this type of tax planning by re-characterizing the capital gain as a dividend. However, this anti-avoidance provision limits an individual in transitioning their business to the subsequent generations in a tax efficient manner.

A private member's bill from the 43rd Parliament (Bill C-208) introduced an exception to section 84.1, effective June 29, 2021, for certain share transfers from parents to corporations owned by their children or grandchildren. The rules introduced by Bill C-208 were amended to ensure that they apply only where a genuine intergenerational business transfer takes place. These new measures will apply to transactions that occur on or after January 1, 2024.

If you are contemplating an intergenerational business transfer, consult with your Crowe BGK advisor to determine whether it is more advantageous to do so before or after December 31, 2023.

PLANNING FOR OWNER-MANAGERS

Salary/Dividend Planning

Many factors must be considered in determining the most beneficial method of remunerating the owner-manager of a closely held corporation. Each case must be examined separately and there is no one "rule of thumb" that applies to all situations.

Here are a few factors that should be taken into consideration:

- The tax rate of the corporation;
- The marginal tax rate of the individual;
- Exposure to “Alternative Minimum Tax”;
- The ability to benefit from childcare expenses, paternity/maternity benefits and RRSP & CPP/QPP contributions, which are all based on salary and not dividend income;
- Wage levies applicable to salaries, such as the Ontario Employer Health Tax, Quebec's Health Services Fund and 1% Training Tax;
- Quebec restrictions on the deductibility of investment expenses by individuals where expenses exceed investment income;
- Whether eligible or tax-free dividends can be paid to shareholders;
- Receiving dividend income will result in a higher net income compared to receiving an equivalent salary, since dividend income is grossed up by 38% for eligible dividends or 15% for non-eligible dividends. This can have an impact on certain credits and benefits of an individual (e.g. old age security benefits);
- Receiving salary income (max $175,333 for 2023) will result in a higher RRSP contribution room in 2024; and
- Remuneration that is accrued and expensed (e.g. bonuses) by a corporation must be paid to the employee within 180 days of the corporation's year-end.

Income Splitting

<u>Prescribed Rate Loans</u>

The prescribed interest rate for the fourth quarter of 2023 is 5%.

Generally, investment income earned by an individual who invested money borrowed at low or no interest from a related person will attribute back to the lender. Subject to a purpose test, this rule does not apply where the loan is to a related person other than a spouse or minor child. Nor will it apply where the loan is to a spouse or minor child if interest is charged at the prescribed rate in effect at the time the loan is made. When relying on this exception, interest must be paid no later than 30 days after the end of the year to avoid the attribution of income.

Since the attribution rules are complex and given the current prescribed interest rate, caution is advised when contemplating a transfer of property or a loan to a spouse or a minor child (including transfers indirectly through a corporation or a trust). Prior to entering into or altering such an arrangement, we suggest you consult with your Crowe BGK advisor.

Tax on Split Income (TOSI)

TOSI may cause certain types of income from private corporations, partnerships or trusts to be taxed at the highest marginal rate. These rules apply to many Canadian resident taxpayers.

These income splitting rules are very broad and complex. Prior to distributing any amounts (other than salary) from a private corporation, partnership or trust we suggest you consult with your Crowe BGK advisor.

Other Basic Tax Planning Ideas

- Depositing Canada Child Benefit (CCB) and Quebec Family Allowance payments directly into accounts opened in the children's names;
- Using the income of the spouse with the higher income to pay the family's household expenses so that the spouse with the lower income can accelerate the growth of his or her capital; or
- Paying reasonable salaries to your spouse and/or children based on actual work performed.

PLANNING FOR INVESTORS

Capital Gains and Losses

Capital losses realized in 2023 (net of any capital gains realized) can be carried back up to three years and carried forward indefinitely to offset future capital gains. It may be worthwhile to conduct an investment portfolio analysis in order to dispose of assets with unrealized losses prior to the end of the calendar year for individuals and taxation year for corporations. Using losses against gains realized in previous years will result in additional tax refunds. Capital losses will not be recognized at the time of disposition where, during the period that begins 30 days before and ends 30 days after the disposition of the investment, the taxpayer or a person affiliated with the taxpayer acquires an identical property (a "superficial loss").

Deductibility of Interest and Investment Expenses

Individuals who have debt should generally make it a priority to first repay debt having non-deductible interest. In general, interest on loans contracted for personal purposes will not be deductible. However, interest on loans contracted to earn income will be. The Courts have confirmed that a taxpayer can sell an income-producing asset to repay a debt with non-deductible interest and then contract a new debt for the purpose of repurchasing the same asset or a different income-producing asset.

In Quebec, investment expenses incurred in the year by individuals are deductible up to the amount of investment income for that year. The excess amount may be carried back to the three preceding years or carried forward indefinitely. There exists no similar restriction for corporations.

Donations

Charitable donations are generally limited to 75% of net income (no limit for Québec). Unclaimed amounts can be carried forward for 5 years.

It is generally advantageous to donate publicly traded securities rather than cash to a registered charity. The amount of the donation receipt will be equivalent to the fair market value of the securities at the time of the donation. However, any increase in value of the securities above the donor's original cost will not be subject to capital gains taxation. In addition, for private corporations, 100% of the gain is credited to the capital dividend account.

Strategies concerning donations of marketable securities can be complex. Potential donors should consult their Crowe BGK advisor prior to donating marketable securities.

Political Contributions

If you've made a personal contribution to a recognized federal party, you are eligible to receive a federal tax credit. The maximum amount of the credit is $650 for 2023. If you've made a personal contribution to a recognized provincial party and you reside in that province at the end of the year, you may be eligible to receive a provincial tax credit. The maximum amount of the credit is $1,552 for Ontario. In Quebec, only contributions made to municipal political parties are eligible and the maximum credit is $155 for 2023.

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RETIREMENT PLANNING

Registered Retirement Savings Plan (RRSP)

The maximum amount individuals are allowed to contribute to an RRSP for 2023 is the lesser of 18% of their earned income for 2022 (essentially employment income net of any expenses, business income and rental income) and $30,780 plus unused RRSP contribution room from previous years. RRSP contribution room available for 2023 is reported on an individual's 2022 Federal Notice of Assessment. Membership in a Registered Pension Plan (RPP) or a Deferred Profit-Sharing Plan (DPSP) may reduce the amount of eligible RRSP contributions.

All or part of an RRSP contribution may be paid to a spousal plan without affecting the contribution room available to the spouse. This tax planning strategy effectively allows income splitting between spouses. Individuals may contribute to their own RRSPs up to and including the year in which they turn 71. If additional contribution room is generated subsequently, RRSP contributions may be made to a spousal plan up to the end of the year in which the spouse turns 71.

If you turn 71 in the current year, you are required to collapse your RRSP no later than December 31, 2023. In order to avoid paying tax on the value of the RRSP, it is recommended that you purchase an annuity or transfer the RRSP to a Registered Retirement Income Fund (RRIF) no later than December 31, 2023.

For individuals who anticipate their income being taxed in a higher tax bracket in a subsequent year, it may be worthwhile to delay the RRSP deduction to that subsequent year.

The amount of RRSP over-contributions must not exceed the RRSP contribution limit by more than $2,000 at any time, otherwise a penalty will be imposed on the excess amount.

RRSP contributions should, when possible, be made early in the year to benefit from the longer period that income is earned on a tax-sheltered basis within the RRSP.

Interest paid on a loan contracted to contribute to an RRSP is not tax deductible. RRSP management fees are also not deductible.

Tax-Free Savings Account (TFSA)

A TFSA allows investment income, including capital gains, to accumulate on a tax-free basis, rather than only defer taxation as is the case with an RRSP. Canadian residents aged 18 or older are able to contribute $6,500 in 2023 to a TFSA. Unused contribution room is carried forward to a subsequent year. The cumulative contribution limit in 2023 is $88,000. Unlike an RRSP, no deduction is available for contributions made to a TFSA.

Individual Pension Plan (IPP)

An IPP is an option for owners of incorporated businesses who wish to enhance the amount of their retirement savings. Contributions are made by reference to the owner's salary and the pension benefit desired. This can significantly exceed RRSP contribution limits, including a potentially large past-service contribution (and deduction) by the corporate employer. Minimum annual withdrawals are required once a plan member reaches age 72, similar to the rules for RRIFs.

Government Pensions

Individuals who have turned or are about to turn 65 should file their Old Age Security (OAS) and Canada Pension Plan (CPP)/Quebec Pension Plan (QPP) retirement applications. Old age spousal or widow(er)'s allowances may also be available. **Reduced** CPP/QPP retirement benefits may be available to persons between ages 60 to 65. **Enhanced** CPP/QPP benefits and OAS pensions are available if the application is delayed until after age 65 (up to age 70).

Taxpayers must repay their OAS at the rate of 15% of 2023 net income in excess of $86,912 The entire OAS amount must be repaid if a taxpayer has net income in excess of $142,609 and is between ages 65 to 74 or if a taxpayer has net income in excess of $148,179 and is age 75 or older.

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PLANNING FOR HIGHER EDUCATION

Registered Education Savings Plan (RESP)

An RESP can assist individual contributors achieve tax-free growth on the funds they will use to pay for the post-secondary education of designated beneficiaries, usually their children or grandchildren. The lifetime contribution limit that may be contributed to all RESPs of a beneficiary is $50,000, with no annual limit. No deduction is available for contributions made to an RESP.

An RESP is also entitled to government assistance. The federal government awards the Canada Education Savings Grant (CESG). The current annual maximum CESG per beneficiary is $500 (i.e. 20% of the first $2,500 of contributions paid annually). Each child is entitled to a cumulative limit of $7,200. A family that has not contributed to their child’s RESP for one or more years can receive a grant of not more than $1,000 as a CESG in a year (i.e. on a maximum contribution of $5,000).

Quebec also provides assistance in the form of the Québec Education Savings Incentive (QESI), under which it grants an annual maximum of 10% of RESP contributions up to a maximum annual incentive amount of $250.

The beneficiaries of an RESP will not be taxed on the withdrawal of the contributions but will be taxed on the withdrawal of accumulated income, including government assistance, which they will receive in the form of Educational Assistance Payments (EAP). Initial contributions may either be paid to the beneficiary or returned to the subscriber.

To learn more about how to optimize tax-efficient withdrawals from your RESP, contact your Crowe BGK advisor.

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INTERNATIONAL PLANNING

Form T1135 Foreign Income Verification Statement

Taxpayers who hold foreign property with a total cost greater than CAD $100,000 at any point in the year are required to provide detailed information regarding each specified foreign property owned during the taxation year.

Significant penalties may apply to a taxpayer that fails to report or inaccurately reports the information respecting any specified foreign property.

US Citizens in Canada

A US citizen resident in Canada must file Canadian and US income tax returns, reporting worldwide income. We recommend that the US tax returns be prepared by a US tax advisor due to the complex interplay of foreign tax credits.

US citizens who may not be compliant with US filing requirements should be aware that the U.S. Internal Revenue Service (IRS) has an amnesty program for Americans living in Canada and abroad. The IRS may waive significant penalties for certain “low compliance risk” taxpayers who opt to be compliant.

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DATES TO REMEMBER – December 2023 to June 2024

**Deadlines falling on holidays or Sundays may be extended to the next business day.*

December 15, 2023	Fourth personal income tax instalment for 2023 is due.
December 27, 2023	Anticipated final day of trading on Canadian stock exchanges for the transaction to be recognized in 2023.
January 30, 2024	Final day for paying interest for 2023 on loans to a spouse or minor child in order to avoid attribution.
February 29, 2024	Deadline for distributing 2023 remuneration slips to employees (T4/RL-1) and independent sales representatives (T4A/RL-1), slips for payments of dividends and interest (T5/RL-3), and for filing the related summaries.

February 29, 2024	Deadline to submit your 2023 RL-31 slip to Revenu Québec and to distribute the slip to your tenants.
February 29, 2024	Deadline for 2023 RRSP contributions.
March 15, 2024	First personal income tax instalment for 2024 is due.
March 30, 2023	Deadline for filing T3 returns for trusts with a December 31, 2023 year-end. T3/RL-16 slips must be sent to beneficiaries no later than 90 days after the end of the trust's tax year.
April 30, 2024	Deadline to submit T1 returns for individuals (other than individuals or their spouse who have business income).
June 15, 2024	Deadline to submit T1 returns for individuals (or spouse) with business income.

US Filings

April 15, 2024	Deadline to submit 1040 returns or extensions as well as remit the 2023 balance of tax owing for individuals (residing in the United States at the date of filing).
June 17, 2024	Deadline to submit 1040 returns or extensions for individuals (residing outside the United States at the date of filing). Note: the balance of tax must be paid by the April 15, 2024 due date to be considered timely.

TO OBTAIN CURRENT DEDUCTIONS AND TAX CREDITS, THE FOLLOWING EXPENDITURES MUST BE PAID BY DECEMBER 31, 2023

- Investment counsel fees
- Certain legal and accounting fees
- Charitable donations
- Political contributions
- Tuition fees
- Deductible support payments
- Childcare expenses
- Professional membership fees and union dues
- Eligible medical expenses
- Deductible moving expenses
- Expenses associated with an objection or appeal related to a tax assessment
- Deductible interest expenses, including interest on student loans

The matters described herein, as well as other techniques used in tax planning, should be subject to ongoing review and analysis. It may be more appropriate to implement some decisions earlier, rather than later, in the year.

If you have any questions or you believe any of the abovementioned strategies apply to you, please contact your Crowe BGK advisor today.

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