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Newsletter

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Capital Gains Re-investment

Bruce Barran, Bc, CA, CFP, Tax Partner, Davis Martindale LLP, London, Ontario, DFK Affiliate Firm

You have just sold the shares of your company and have been advised of your rather large tax bill. You have previously fully utilized your lifetime capital gains exemption. You ask your advisor, how can I reduce my taxes?

Deferral of Capital Gains Reinvested in Small Business Corporations

When an individual disposes of shares of a qualifying small business corporation (SBC) and realizes a capital gain, that gain can be deferred if some or all of the funds are reinvested in one or more qualifying SBCs.

The new investment's cost base is reduced by the deferred capital gain. Consequently, the gain is deferred until the disposition of the new investment.

Qualifying Dispositions

A qualifying disposition is defined as the sale of common shares of a corporation where each share was:

- Issued from treasury by a corporation which was an eligible SBC at the time of acquisition;
- A common share of capital stock of an "active business corporation" throughout the duration of ownership; and
- Owned by the individual throughout the 185-day period that ended immediately before the disposition.

Only an individual can obtain this capital gain deferral, and only in respect of a capital gain arising on a qualifying disposition. Trusts are not eligible.

An eligible SBC is a Canadian-controlled private corporation of which:

- Substantially all of the assets are used principally in an active business carried on primarily in Canada; or
- Are shares or debt of related eligible SBCs; or
- Any combination thereof.

The total carrying value of an eligible SBC's assets, and its related corporations, must not exceed $50 million immediately before and immediately after its shares are issued.

An eligible SBC does not include:

- Professional corporations;
- Corporations whose principal business is the leasing, rental, development or sale of real property owned by it; or
- Corporations more than 50 per cent of the fair market value of the property of which (net of debts incurred to acquire the property) is attributable to real property.

Eligible Small Business Investment Reinvestment

An eligible small business reinvestment must have the following characteristics:

- Investment in ordinary common shares issued from treasury of the new corporation to the investor;
- New corporation is, at the time the shares are issued, an eligible SBC;
- Replacement shares must be purchased in the year of the qualifying disposition or within 120 days after the end of that year; and
- Designation of the replacement shares must be made in your income tax return for the year of the disposition.

These rules are very specific which is why you should discuss your situation with your accountant. If the rules apply to you, they're a great tool to defer taxes and lower your bill.

Inside this issue:

"You miss 100 percent of the shots you never take."
- Wayne Gretzky

Special points of interest:

- *Tax filing deadline for the self-employed is June 15th*
- *Harper majority government determined to quickly table a budget and have it passed before summer recess.*
- *New T661 form for SRED filers after July 31, 2011*
- *Personal tax instalments:*
  - *June 15, 2011*
  - *September 15, 2011*
  - *December 15, 2011*

The Insured Annuity—An Often Overlooked Tax Efficient Investment Strategy for Seniors

David Wang, CA, KNV Chartered Accountants LLP, Surrey, BC, DFK Affiliate Firm

What is an insured annuity?

The insured annuity involves two separate financial products: a prescribed life annuity and a life insurance policy.

A prescribed life annuity provides annuity income for life. The cash flow includes both the principal (non-taxable) and interest component (taxable). Because the taxable portion is lower than the interest income earned by a GIC, the annuity stream is taxed at a lower effective tax rate.

A term-to-100 life insurance policy guarantees the return of the principal at death. Insurance premium payments continue until age 100 when the premiums normally cease while the insurance coverage continues.

An insured annuity is not CDIC insured, rather security is provided by a government-regulated entity called Assuris. Potential investors should understand how Assuris provides security to insurance-related investments so as to be comfortable that an insured annuity is indeed “low risk.”

Who is it for?

Not all investors are willing to take more risk for a higher yield on their investment portfolios. For investors whose portfolios include conservative investments such as GICs and bonds, moving the money into an insured annuity may be a good way to increase after-tax cash flow without increasing risk.

Because an insured annuity is a lifetime investment, it is generally more appropriate for those individuals who are age 65 or over and not averse to long-term planning strategies. To be insurable, the individual must be in good health and pass a basic physical examination.

How does it work?

A prescribed life annuity typically generates more after-tax cash flow than can be obtained from a conventional GIC due to its preferred tax treatment. See chart for an illustration:

	GIC (4%)	**Insured Annuity**
Total invested	$100,000	$100,000
Annual income	$ 4,000	$ 8,000
Taxable portion	$ 4,000	$ 2,000
Tax @ 40%	$ 1,600	$ 800
After-tax cash flow	$ 2,400	$ 7,200
Cost of life insurance	$ 0	$ 4,000
Net Cash Flow	$ 2,400	$ 3,200

What are the pros and cons of an insured annuity?

Pros:

1. The investor can receive more net cash flow with the insured annuity, particularly for those in higher tax brackets.
2. The death benefits are tax free to beneficiaries.
3. The investor can potentially avoid probate costs when death benefits from the life insurance bypass his or her estate and go directly to the beneficiaries.

Cons:

1. The annuity capital is locked in for life, so once the insured annuity is implemented it cannot be undone. For that reason, it is generally advisable to restrict one’s investment in this strategy to a maximum of 30 per cent of available capital.
2. The purchasing power of annuity income may be vulnerable to inflation. If interest rates rise, the strategy will become less attractive.

Insured annuities are not for everyone, but seniors in higher tax brackets may want to consider them as a method to increase their after-tax income on a low-risk basis. Speak to your advisor before making any definitive decisions.

Employment Insurance Special Benefits for Self-Employed People

Ron Klein, CA, Tax Manager, MRSB Chartered Accountants, Charlottetown, PEI, DFK Affiliate Firm

Under the amended Employment Insurance Act, self-employed Canadians and permanent residents will be eligible to apply for Employment Insurance (EI) special benefits.

If you operate your own business, or work for a corporation but were not eligible for EI benefits, you can now register for EI.

There are four types of EI special benefits of which you should be aware:

Maternity benefits are for mothers who give birth, and covers the period surrounding the birth up to 15 weeks.

Parental benefits are for either parent to care for their newborn or newly adopted child. Either parent can receive benefits, or they can share them for up to 35 weeks.

Sickness benefits are for people who cannot work due to injury, illness, or the need to be isolated in quarantine. These benefits can be received for up to 15 weeks.

Compassionate care benefits are for people who must be away from work to provide care for an ill family member with a significant risk of death. These benefits can be shared between EI-eligible family members for up to six weeks.

If you are a self-employed resident of Quebec, you are already covered for maternity, paternity, and parental benefits under the Quebec Parental Insurance Plan (QPIP). If you choose to participate in this new measure, you may be eligible for EI sickness and compassionate care benefits only.

Forward thinking is critical as you must be registered 12 months prior to being eligible for these benefits and must have earned a minimum specified amount of self-employment earnings during the calendar year before you submit an EI claim.

There are four types of EI special benefits of which you should be aware.

If you are applying for sickness benefits, a medical certificate is needed. If you are applying for compassionate care benefits, medical proof is required indicating that a gravely ill family member needs your care.

Should you be applying for maternity or parental benefits, you have to provide the expected date of birth and the actual birth date once it has occurred. In the case of adoption, the official placement date is obligatory.

If you are eligible for EI special benefits, you can expect to receive 55 per cent of your average weekly earnings up to a defined annual limit.

You can terminate your registration at any time – as long as you have never claimed any benefits. It should be noted that this termination will be effective at the end of the calendar year and you are required to pay into the program until then.

Once you have claimed EI, your participation in the program lasts indefinitely. You will have to pay premiums for the entire duration of your self-employment career, regardless of changes in the nature of your self-employment.

Receiving earnings while you receive EI may decrease your weekly benefit amount. How the earnings affect your EI special benefits depends on the nature and timing of the earnings and the type of EI benefits you are receiving.

For any clarification in regards to the Employment Insurance Act amendments, it is recommended you consult your advisor.

Estate Planning

Paul Morton, CA, CFP, TEP, Tax Partner, Ginsberg Guzman Fage & Levitz, LLP

Estate planning used to only consider how assets would be distributed upon death. Now a main focus of estate planning is the allocation of future growth in assets while the taxpayer is alive.

To maximize the future value of one's estate, the future growth in value of some assets can be transferred to family members. Specific criteria must be met to ensure future income and growth are transferred to your family members for income tax purposes, and do not remain part of your taxable income. However, through the establishment of a trust, spouses and minor children may participate in future growth. In some cases, family members may be able to utilize the $750,000 enhanced capital gains exemption in the future. The recent Federal Budget proposal may offset the enhanced capital gains exemption for minors. We will have to see what is in the Progressive Conservative majority government's upcoming budget.

However, in all cases taxpayers should have proper wills that provide specific reference to the disposition of assets. Even in instances where only the spouse has a claim to the estate, there should be a will to avoid the estate being subject to provincial intestacy laws, and the assets being temporarily frozen.

Multiple wills may be appropriate for reducing probate fees depending on how they are determined in your province.

The will should be reviewed and updated periodically to ensure it reflects the individual's current situation.

Some estates may require life insurance in order to:

- Provide funds to pay any resulting income tax liability.
- Provide funds for the remaining shareholders to purchase the company's shares from the estate of the deceased.
- Create an estate for heirs.
- Provide a good investment vehicle, since the proceeds from a policy are tax-free when received.

GGF&L
Chartered Accountants

Accounting For Your Future®

287 Richmond Road

Ottawa, ON K1Z 6X4

Phone: 613-728-5831 / Fax: 613-728-8085

www.ggfl.ca

Click here for Insolvency and Bankruptcy Services with our affiliate firm Ginsberg Gingras & Associates Inc.

Claude B. Gingras honoured as "Personality of the Year"

On November 27, 2010, Claude B. Gingras, President and Co-founder of Ginsberg, Gingras & Associates Inc., was honoured by the Gatineau Chamber of Commerce by being presented with the prestigious "Personality of the Year Award" at their Annual Business Gala. This award was followed by a reception in his honour at the Hilton Lac Leamy on April 14, 2011, where Claude was celebrated by the business community alongside his family, friends, GGFL Partners, trustees and co-workers.

Congratulations Claude in this amazing accomplishment.

Ginsberg Gingras & Associates Inc. is an affiliated firm of GGFL, which offers trustee and receivership services.

GGFL supports Project North

On May 9, 2011, GGFL sponsored an art auction, named "Arctic Kaleidoscope," which featured the work of renowned photo artist Michelle Valberg. $50,000 was raised for Project North, which provides sports equipment to northern Inuit communities and promotes improved literacy skills for Inuit children.

"We could not have been more pleased with the success of this event," said GGFL Managing Partner Deborah Bourchier.

GGFL reaches new heights

GGFL was also pleased to sponsor Partner Bruce Johnston's daughter, Kristi Johnston, in her quest to climb Mt. Kilimanjaro in support of CARE Canada. Kristi posed proudly at the summit with a GGFL banner, literally taking the firm to new heights.