

Tax Advisory Bulletin

Date: March 2009

Re: Income Splitting and Tax Savings

It may now be an opportune time to implement an income splitting arrangement with family members.

The purpose of income splitting is to move income from a high-rate taxpayer to a low-rate taxpayer. Specific tax rules, known as the "attribution" rules, are designed to prevent this shift of income. So, when a parent gifts or lends property to a minor child, the income from the property is treated as income of the parent rather than the child. There is an exception for capital gains earned by minors. Similar rules apply when an individual transfers property to his or her spouse.

However, if funds are lent at an interest rate equal to the rate "prescribed" by the Canada Revenue Agency at the time of the loan, the "attribution" rules will not apply and income shifting will be allowed. For this exemption to apply, interest at the prescribed rate must be paid (for the life of the loan) no later than January 30 in the calendar year following the year in which the loan was outstanding.

The prescribed rate will be 1% per annum from April 1, 2009 to June 30, 2009. The prescribed rate of 1% provides a very good opportunity to implement this type of income-splitting strategy, as the interest rate is locked in for the life of the loan (even if prescribed rates subsequently increase). In essence, all income earned on the funds in excess of 1% per annum will be taxable to the lower income family member, rather than the high income earner. In many cases, the income earned by the lower income person will not attract any tax.

A loan can be made to a child or spouse or to a trust for their benefit.