December, 2004

The purpose of this letter is to highlight those items which can affect your 2004 income tax position. We do so by listing the details under each of the various headings. If you would feel more comfortable calling us rather than delving into the details, please do so. Otherwise, please read on.

TAX PLANNING

The object of this review is to increase your after-tax funds by making tax related decisions on a timely basis. In order to have a tax effect on your 2004 taxation year, certain decisions should be made **prior to December 15th.** These include selection and payment of:

1) Deductible Amounts
2) Registered Retirement Savings Plans (RRSP)
3) Registered Retirement Income Funds (RRIF)
4) Pension Income
5) Income Splitting
6) Tax Shelter Investments
7) Alternative Minimum Tax (AMT)
8) Capital Gains
9) Charitable Donations and Gifts of Cultural Property
10) Medical Expenses
11) Compound Debt Instruments
12) Tax Instalments
13) E-filing

We strongly advise that you address yourself to the required tax planning considerations **now** in order to make informed decisions as early as possible. We do recognize that the Income Tax Act creates complexities which are beyond the knowledge of the average taxpayer. As such, we would be pleased to assist you in considering the various strategies which would be appropriate to your particular circumstances.

Chartered Accountants

1) **<u>Deductible Amounts</u>**

Any deductible amounts which apply to your 2004 taxation year **must be paid** prior to December 31, 2004. Items of this nature which are commonly overlooked are safekeeping charges, investment counsellor fees, donations, and medical and dental expenses where the work was performed prior to December 31, 2004.

2) **<u>Registered Retirement Savings Plans (RRSP)</u>**

In order to qualify as a deduction on your 2004 income tax return, your contribution must be made on or before March 1, 2005.

The rules allow for a basic limitation of 18% of **prior year's earned income** with a maximum of $15,500.

You require $86,111 of earned income in 2003 in order to claim an RRSP deduction of $15,500 in 2004.

If you are an employee and a member of a registered pension plan, the annual limit will be reduced by your pension adjustment (**pa**). This is calculated by your employer and represents the value of pension benefits or deferred profit sharing plan benefits paid by that employer on your behalf.

The Canada Revenue Agency (CRA) issues a contribution limit statement as part of your Notice of Assessment which indicates their calculation of the amount which you could contribute to your 2004 RRSP.

A reminder that the maximum age at which an individual can contribute to a Registered Retirement Savings Plan was reduced from 71 to 69 effective 1996.

There are rules which should be considered:

i) You are permitted to defer the deduction of your RRSP contribution to a later year subject to the contribution limits in that year.

ii) Any amount which you are entitled to deduct in a particular year, less the amount which you actually deduct, may be carried forward indefinitely.

Interest costs on money borrowed to make a 2004 RRSP contribution are not deductible unless you are still paying interest on a **pre-1982** contribution.

3) **<u>Registered Retirement Income Funds (RRIF)</u>**

If you have an RRSP and if you turn 69 at anytime in 2004, you must roll your RRSP into an RRIF prior to December 31st. Failure to do so will result in the inclusion of the entire RRSP in your income for 2004. You can transfer funds to an RRIF anytime after you reach the age of 65. If you have no other source of pension income subject to the $1,000 pension income deduction, you should **consider drawing down $1,000** from your RRIF.

iv) RRSP spousal contributions for individuals over 69, as long as they have earned income and their **spouse is under 69.**

v) Withdrawal of RRSP funds if income in a certain year is unexpectedly low. This will result in tax being paid at a lower rate.

vi) RRSP contributions for individuals who have no earned income in the current year, but who did have **earned income in the prior year** (e.g. retirees).

5) **Income Splitting**

In order to avoid clawbacks of your old age exemption of your Old Age Security payments, you should be aware that there are several strategies which you can follow to transfer income to your spouse and thus reduce the incidence of income tax. Please call us if you believe that this situation could apply to you.

6) **Tax Shelter Investments**

The most important factor involving the acquisition of tax shelters should still be whether or not they make good business sense as investments.

Since the availability of tax deferral schemes has been severely restricted by the CRA, we would suggest a consultation with a member of our firm before proceeding with tax shelter investments.

7) **Alternative Minimum Tax (AMT)**

Alternative Minimum Tax is designed to target higher income individuals with significant investments in tax shelters and can have the effect of increasing income taxes.

We would suggest a consultation with a member of our firm if you are concerned that AMT may be applicable to you.

8) **Capital Gains**

The inclusion rate for capital gains is 50% for 2004.

There is a $500,000 exemption which applies to gains on sales of shares of qualifying active small business corporations and bona fide farm property. Any gain in excess of the exemption is taxable at the applicable 2004 rate.

Warning: If you have a Cumulative Net Investment Loss (CNIL), i.e., claims for investment expenses and losses that exceed investment income and gains, they may be applied to reduce any available tax-free capital gains and thus render part of your gain taxable. Other capital transactions from as early as 1984 may also affect your claim.

Tax Planning Considerations:

9) **Charitable Donations and Gifts of Cultural Property**

There are ways of giving to charity in a tax efficient way, but donations are limited to 75% of net income. Should donations exceed the limit, they may be carried forward for 5 years. **There are special rules with respect to gifts of cultural property and marketable securities.** We would be pleased to discuss them with you should you wish to make such a donation.

Tax Planning Considerations:

Accelerate planned donations in order to qualify for 2004 deduction.

Charitable donations qualify for a tax credit. The first $200 of donations is credited at the low rate while any excess amounts are credited at the high rate you may receive. As a result, you may receive a tax benefit by making donations as the tax credit may exceed your effective tax rate.

If donations are converted to tax credits prematurely they will be lost. Therefore, care must be taken when claims are made.

10) **Medical Expenses**

Should your medical expenses and those of your spouse and dependants exceed the lesser of 3% of your net income or $1,814, you will be entitled to a tax credit. Medical expenses include a multiplicity of items including doctor's bills, dentist's bills, purchases of eye glasses, purchases of hearing aids, premiums paid to private health plans, etc.

Tax Planning Considerations:

Should you require new eye glasses, for example, it might be advisable to purchase them in December rather than in January so as to have an amount which will qualify as a 2004 medical expense.

11) **Compound Debt Instruments**

Interest on debt instruments purchased after December 31, 1989 must be reported on an annual basis.

12) **Tax Instalments**

If more than 25% of your total income arises from sources from which there is no requirement for withholding tax (i.e., investment income, etc.), or if you have to pay at least $2,000 in instalments, you are required to make quarterly income tax instalments on the 15th day of March, June, September and December. If these instalments are deficient or late, non-deductible interest will be charged by CRA. This interest is calculated on a daily basis. In addition, CRA assesses a penalty of 50% of interest levied for late or deficient instalments where the total amount of the interest exceeds $1,000.

Organize your finances so that you may incur tax deductible interest expenses and have funds available to pay your quarterly tax instalments.