

Divorce and Taxes

Helping Clients Put More Money in Their Pockets

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Putting More Money in Your Clients' Pockets

- ❖ Eligible Dependent Tax Credit (EDTC or AED) Update
- ❖ Canada Child Benefit Eligibility
- ❖ Spousal Support and Retroactive Arrangements
- ❖ Capital Loss
- ❖ RRSP Withdrawals
- ❖ Legal Fees - Deduction



Definition of Separated: CRA v. Family Law

When are you really separated?

- ❖ Each advises clients within scope of profession's rules
 - Family Law
 - Date of Separation is date when one or both spouses decide to no longer live together as spouses.
 - If relationship has ended but both spouses/partners are still living in the same home, they are usually still considered to be living separate and apart.
 - Clear evidence that spouses/partners are no longer sharing responsibilities, or social and family events is required if they continue to live in the same house.
 - Canada Revenue Agency
 - You are separated when you start living separate and apart from your spouse or common law partner because of a breakdown in the relationship for a period of at least 90 days and you have not reconciled.
 - If you continue to reside in the same household and continue to share parenting and financial responsibilities, CRA will *not usually* consider a separation to have occurred.
 - Should file an RC65, *Marital Status change form*

Eligible Dependent Tax Credit (EDTC or AED)

- ❖ Section 118 of the Income Tax Act allows you to claim a dependent
- ❖ Claim is worth significant money
- ❖ Must be a single parent
- ❖ Parent must not be making child support payments for child parent wants to claim (in other words, non-primary parent paying child support cannot claim a child for credit)



The Eligible Dependent Tax Credit

❖ How Agreements Are Usually Set up in *Shared Parenting*

- Couple goes through separation; one earns more than the other.
- Federal Child Support Guidelines determine how much each parent owes the other for child support.
- Higher income earning spouse writes NET cheque to lower earning parent and/or “SET-OFF” child support is referred to in agreement or court order.
(Verones v. The Queen 2012 TCC 291 disallowed)
- ONLY lower income parent can claim a child for this credit.



The Eligible Dependent Tax Credit

- ❖ 2007 ITA Revision to Subsection 118(5.1) – the exception
 - Couple goes through separation; one earns more than the other.
 - Federal Child Support Guidelines determine how much each parent owes the other for child support.
 - Each parent pays the other for both children (*Harder v. The Queen 2016 TCC 197*)
Judge Boccock as in Verones pointed out that one set-off payment is not acceptable and that each must actually pay the other.



The Eligible Dependent Tax Credit

❖ *How Shared Parenting Agreements Should Be Written To Ensure Success*

- Parent A pays Parent B the Guideline Child Support Amount based on their income for the number of children but the agreement sets out that the payment is for Child 1.
- Parent B pays Parent A the Guideline Child Support Amount based on their income for the number of children but the agreement sets out that the payment is for Child 2.
- Parent A and Parent B **ACTUALLY** each e-transfer/pay the amount of child support to the other parent.
- Each parent can claim 1 of the children (the child they are not paying in respect of) for the EDTC.



Limitations to the EDTC

- Both parents must be Canadian residents.
- Both parents must be earning income which is reported on their tax return.
- Must be 2 or more children.
- Cannot be living with new conjugal partner or spouse.



Canada Child Benefit Eligibility

❖ *Inform CRA of Your Marital Status Change*

- Affects the benefits and credits that you may be eligible for.
- Based on one parent's income if single rather than family income.
- Make sure to inform CRA of your parenting arrangement as well.
- When parents separate, they are both eligible to apply for CCB benefits; if they qualify based on their income and are a primary parent, they will receive the full benefit amount. If they qualify and are in a **SHARED PARENTING** arrangement, the full benefit amount will be **CUT IN HALF**. Rotating benefits and deferring all benefits to one parent are not available options.
- Clients should update direct deposit info on file with CRA as well.



Retroactive Spousal Support

- ❖ Work together for a net benefit
- ❖ Have amounts been paid?
- ❖ Wording and timing of agreement or court order
- ❖ Registration of T1158 form with CRA
- ❖ Example



Capital Losses

- Is cash required by the spouses?
- Are there available investments to sell?
- Will taxable capital losses be created?
- Offsetting gains on investment disposition
- Carryback or carryforward of losses



RRSP Withdrawal

- ❖ **Last resort when access to funds are required**
(usually when there is the issue of debt to be dealt with)
- ❖ **Options:**
 - Withdrawal by lower income earner
 - Process of rollover and withdrawal



Deductions in Separation and Divorce

❖ Legal Fees

- Legal fees to obtain, establish, enforce or defend a reduction of child and/or spousal support are deductible (viewed as an income source of the recipient of support).
- From the payer's standpoint, legal fees incurred in negotiating or contesting an application for support payments are not deductible since these costs are personal or living expenses in the 'eyes' of CRA.
- Legal fees in respect of filing for divorce, a separation agreement, custody, property division or other non-support issues are not deductible by the recipient.
- CRA will require a letter from legal counsel setting out the legal fees paid in respect of child and/or spousal support to support the claim at line 221.



