

# **Pension Income Splitting and Other Tax Measures**

**Charles Rotenberg, B.A. (Hons.) L.L.B.**

In addition to the new rules destined to kill the income trust as a tax-efficient investment vehicle, Finance Minister Flaherty introduced other tax measures which will provide some benefit to certain taxpayers.

In one of the most significant provisions that we have seen in a long time, the Finance Minister has introduced the ability to split pension income between spouses.

## **Pension Income Splitting**

In the United States, married couples often file a “joint tax return”. Canada’s income tax system generally requires each individual taxpayer to report and pay tax on all of the income they earn, and there are many pages of rules designed to stop Canadians from splitting income with other family members. This is the case even if the individual, like many Canadians, actually uses much of their income to support other family members.

Today, the Finance Minister has introduced a new mechanism for pension income splitting. The measure will allow any Canadian resident who receives income that qualifies for the existing pension income tax credit to allocate to their resident spouse (or common-law partner) up to one-half of that income. This measure will significantly increase the incentive to save and invest for family retirement security.

For individuals aged 65 years and over, eligible pension income includes lifetime annuity payments under a registered pension plan, a registered retirement savings plan or a deferred profit-sharing plan and payments out of or under a registered retirement income fund. For individuals under 65 years of age, eligible pension income includes lifetime annuity payments under a registered pension plan and certain other payments received as a result of the death of the individual’s spouse or common-law partner.

For income tax purposes, the amount allocated will be deducted in computing the income of the transferor (the person who actually received the pension income) and included in computing the income of the transferee (the person to whom some or all of the pension income is allocated). Since it will in many cases, increase the transferee’s tax payable, both persons must agree to the allocation in their tax returns for the year in question.

The pension income splitting allocation will be available for the 2007 and subsequent taxation years, and must be made one year at a time.

Government figures suggest that this plan will provide over \$1 billion of new tax relief annually for Canadians. Whether or not those figures are accurate, this is clearly a provision with huge impact in the estate planning and retirement planning for many Canadians.

## **Age Credit Enhancement**

The age credit, a special federal income tax credit for Canadians 65 years of age and older, will be enhanced, with the increase taking effect retroactively to January 1, 2006.

The age credit is calculated by multiplying the lowest personal income tax rate by an amount that is indexed to inflation; for 2006, this amount is \$4,066. The credit is subject to an income test that targets the assistance to seniors who need it most. The unused portion of the credit may be transferred to a spouse or common-law partner.

- For 2006, the age credit amount begins to be phased out when net income reaches \$30,270. The phase-out rate is 15%, which means that the credit is fully phased out when net income reaches \$57,377.

The amount on which the age credit is computed will be increased by \$1,000 to \$5,066, effective January 1, 2006. This increase will help low- and middle-income seniors by providing up to \$155 (\$152.50 for 2006) of federal income tax relief each year for those eligible to receive the credit.

- With this enhancement, the age credit will be fully phased out when net income reaches \$64,043.

## **Corporate Income Tax Reduction**

The 2006 Budget announced that the general corporate income tax rate would be reduced from 21% to 19% by 2010. The Government will reduce the rate by a further one-half percentage point, to 18.5%, beginning in 2011.