Tax Tips for Investors 2015 Edition

Knowing how the tax rules affect your investments is essential to maximize your after-tax return. Keeping up to date on changes to the tax rules may open up new opportunities that could affect how your financial affairs should be structured.

This edition of Tax Tips for Investors (updated to include proposals originating from the 2015 Federal Budget and all 2015 provincial budgets, except the new Alberta government's budget expected in fall 2015, and Alberta's Bill 2) provides you with ideas that you may want to incorporate into your wealth management strategy. As always, we recommend that you consult an independent tax professional to determine whether any of these tips would be appropriate for your particular situation and to ensure the proper implementation of any tax strategies.

Tax Tip 1: Reduce Tax With Income Splitting

Under our tax system, the more you earn, the more you pay in income taxes on incremental dollars earned over threshold levels. With this in mind, it makes sense to spread income among family members who are taxed at lower marginal rates, in order to lower your family's overall tax burden. However, the income attribution rules can prevent most income-splitting strategies where there has been a transfer to a spouse or minor child for the purpose of earning investment income. The attribution rules re-allocate the taxation of investment income (and capital gains in the case of a gift to a spouse) to the person who made the gift regardless of the name on the account in which the investment is registered. While there are significant restrictions, there are a number of legitimate income splitting strategies available to you.

Loan at the Prescribed Rate

An interest-bearing loan made from the person in the higher marginal tax bracket to a family member in a lower tax bracket for the purpose of investing provides an income-splitting opportunity. However, it is important to note that there are a number of requirements that must be met. For example, interest must be charged at the Canada Revenue Agency's (CRA) prescribed rate in effect at the time the loan is made, and interest must be paid by January 30 of each year. The CRA sets the

Table of Contents

Tip 1 Reduce Tax With Income Splitting....1

Tip 2 Make Your Portfolio Tax-Efficient.... 3

Tip 3 Maximize Your Tax-Deferred Savings With an RRSP or TFSA.................... 5

Tip 4 Donate Appreciated Securities 7

Tip 5 Use Registered Plans To Save For Children's Educational or Other Needs.................................. 8

Tip 6 Use Borrowed Funds to Invest 9

Tip 7 Manage Income Tax Withholding/ Instalments 9

Tip 8 Reduce Tax For Your Estate 10

Tip 9 Consider US Estate Tax Implications If You Own US Investments 12

Tip 10 Year-End Tax Planning 14

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Continued

prescribed interest rates quarterly, based on prevailing market rates. Periods of low prescribed interest rates are generally the best time to establish a loan since the low rate can be locked for the duration of the loan. In order for there to be a net benefit, the annual realized rate of return on the borrowed funds should exceed the annual interest rate charged on the loan, which is included in the income of the transferor and deductible to the transferee family member if used for investment purposes. Any potential impacts of increased income to the transferee family member (e.g. loss of spousal tax credit) should also be considered before employing this strategy. Finally, it is important to consider the possible recognition of capital gains or capital losses (which may be denied) when assets other than cash are transferred or loaned to a family member.

Income Splitting With a Spouse or Common-law Partner

Income splitting with a spouse or common-law partner (hereinafter referred to as 'spouse') can be achieved with a prescribed rate loan, or in a number of other ways. For example, the individual earning the higher income (who pays tax at a higher marginal rate), should pay as much of the family's living expenses as possible. This allows the lower-income spouse to save and invest his or her income. The earnings on those invested funds will be taxed at a lower marginal rate and the overall family tax burden will be reduced. Income splitting in retirement can be achieved by making spousal Registered Retirement Savings Plan (RRSP) contributions while working (see page 5), through pension income splitting (see next section) and by sharing Canada Pension Plan (CPP)/ Quebec Pension Plan (QPP) benefits.

In addition, with the introduction of the Tax-Free Savings Account (TFSA) in 2009 (see page 6), money can be provided to a spouse (or adult child) to allow them to contribute to their own TFSA, subject to their personal TFSA contribution limit. Since the income earned within a TFSA is tax exempt and is not subject to the attribution rules, a TFSA provides a simple and effective income-splitting tool. However, care must be taken if assets other than cash are gifted to a family member to fund their TFSA contribution.

Pension Income Splitting

The introduction of pension income splitting legislation in 2007 allows a transfer of up to 50 percent of **eligible pension income** to a spouse, which provides a significant opportunity to split income where retirement incomes are disproportionate. The allocation of this income is done by each spouse making a joint election annually in their respective tax returns. For income tax purposes, the amount allocated will be deducted from the income of the person who actually received the **eligible pension income** and this amount will be reported by the other (lower income) spouse. The definition of **eligible pension income** (see below) is similar to the definition used for determining eligibility for the $2,000 pension income tax credit, such that individuals currently eligible for this credit will generally be eligible to split pension income with their spouse. **NOTE**: It is the age of the spouse entitled to the pension income that is relevant in determining the eligibility for pension income-splitting, such that it is possible to allocate eligible pension income to a spouse under age 65.

Definition of Eligible Pension Income

From the perspective of the recipient spouse, eligible pension income will include:

Canadians who are 65 and over and receive:*

1. Registered pension plan payments;
2. Registered Retirement Income Fund (RRIF) payments (includes Life Income Fund (LIF) and Locked-in Retirement Income Fund (LRIF) payments);
3. Lifetime annuities from registered plans; or
4. Prescribed and non-prescribed annuities (interest component only)

Canadians who are under 65 and receive: **

1. Registered pension plan payments; or
2. Items (2) to (4) above; only if received as a result of the death of a spouse.

* effective for 2013 and subsequent taxation years, certain RCA payments may also qualify for individuals aged 65 or over.

** Quebec residents should note that changes originating from the 2014 Quebec budget will no longer allow individuals under the age of 65 (at the end of the year) to split pension income in their Quebec provincial tax return, effective for the 2014 taxation year.

Income Splitting With Adult Family Members

In making a gift to adult children or other adult family members, you will not likely have any control over how the money will be used. However, a gift may allow them to make an RRSP or TFSA contribution or give them an opportunity to earn investment income at their lower marginal tax rate. In addition to adult children or adult grandchildren, you may want to consider this strategy for parents whom you otherwise support in after-tax dollars. The attribution rules do not generally apply to an adult relative (other than a spouse) if a **gift** is made. However, these rules may apply in a situation where a **loan** is made to a related adult where no interest (or interest below the prescribed rates) is charged on the loan, if one of the main reasons for making the loan is to split income. As previously mentioned, it will be necessary to consider the possible recognition of capital gains, or capital losses (which may be denied), when assets other than cash are transferred or loaned to a spouse or other family member.

Income Splitting With Family Members Under Age 18

If structured properly, income splitting can be achieved by making a gift to a minor child – directly or through a trust structure – to acquire investments which generate only capital gains. In most cases, capital gains earned after the transfer on a gift can be taxed in the minor's hands. However, interest or dividend income will attribute back to the transferor parent unless fair market consideration (such as a prescribed rate loan) is received. Also, second generation income (i.e., income earned on income from the original gift) does not attribute back to the giftor. Any income earned on Registered Education Savings Plan (RESP) contributions made for a child is taxable to the child when withdrawn for education purposes (see Tip 5 on page 8). Income splitting with minor children where the income is derived from dividends from a private corporation or from a business carried on or owned by related persons is no longer an effective strategy. The 'kiddie tax' rules can apply to automatically tax the minor on such income at the top marginal tax rate and not at the graduated rates.

Tip 2: Make Your Portfolio Tax-Efficient

There are literally thousands of investment options available today, each with its own investment merits and many with unique characteristics. As an investor trying to determine the most appropriate investment strategy for your portfolio, it's important to consider the level of risk associated with the investment and its expected return. When evaluating returns, you should consider the impact of income taxes, since not all investment income is taxed in the same manner.

Despite the wide range of investments available, there are three basic types of investment income: interest, capital gains and dividends. Each of these is subject to different tax treatment.

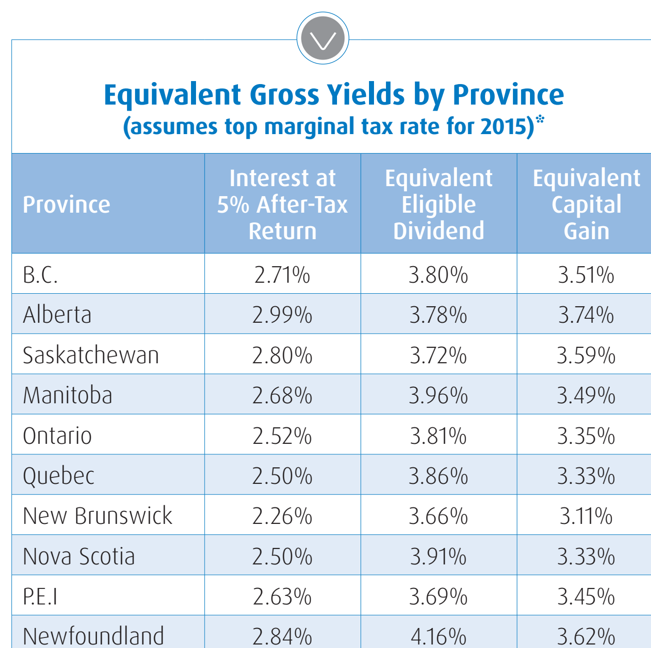
Interest income is taxed at your marginal tax rate. However, if you realize a capital gain, you only pay tax on 50 per cent of the gain. By including only 50 per cent of the capital gain, the actual tax you pay is lower than if you had earned the same amount in interest income.

Some investments distribute a return of capital (ROC) which is not taxable upon receipt. Instead, the ROC reduces the adjusted cost base of your investment which will impact your gain or loss on the ultimate sale of the investment.

Canadian dividends also receive special tax treatment through the federal and provincial dividend gross-up and tax credit mechanisms. A new dividend tax regime exists for dividends paid by a Canadian corporation to a Canadian individual investor after 2005. Specifically, the concept of an "eligible" dividend was introduced to encompass distributions to Canadian resident investors from income that has been subject to the general corporate tax rate, i.e., generally, most dividends paid by public Canadian corporations. Dividends received which are not "eligible" dividends are subject to higher effective tax rates.

The table on page 15 provides the combined top tax rates by province on the various types of investment income.

The table below illustrates the approximate pre-tax rate of return, by province, for eligible dividends and capital gains that will result in the same after-tax return as earning interest at five per cent.



Equivalent Gross Yields by Province
(assumes top marginal tax rate for 2015)*

Province	Interest at 5% After-Tax Return	Equivalent Eligible Dividend	Equivalent Capital Gain
B.C.	2.71%	3.80%	3.51%
Alberta	2.99%	3.78%	3.74%
Saskatchewan	2.80%	3.72%	3.59%
Manitoba	2.68%	3.96%	3.49%
Ontario	2.52%	3.81%	3.35%
Quebec	2.50%	3.86%	3.33%
New Brunswick	2.26%	3.66%	3.11%
Nova Scotia	2.50%	3.91%	3.33%
P.E.I	2.63%	3.69%	3.45%
Newfoundland	2.84%	4.16%	3.62%

* See page 15 for top marginal rates.

The 2008 federal budget introduced reductions to the gross-up and credit mechanism for eligible dividends, which effectively increased the tax rate on eligible dividends beginning in 2010. Changes originating from the 2013 Federal Budget have further increased the effective tax rate on "ineligible" dividends beginning in 2014 as noted in the chart on page 15 which reflects the current top marginal tax rates for individuals. In addition, the 2015 Federal Budget introduced further changes to the dividend gross-up and tax credit factors on ineligible dividends to be phased in over four years, beginning in 2016 in tandem with related decreases to corporate tax rates on qualifying active business income. Ask your financial professional for a copy of our publication entitled **Eligible Dividends** for more information on the taxation of dividend income.

If a regular income stream is your primary investment objective, rather than fixed income interest-bearing securities, you may want to consider investing in preferred shares of Canadian corporations – which pay dividends that will be taxed at lower rates. However, keep in mind the potential impact that the gross-up on dividends can have on your taxable income and any income-based benefits (such as Old Age Security). When deciding how to invest your RRSP and non-RRSP portfolios, consider holding interest-bearing securities in your RRSP, and investments that generate Canadian dividends and long-term capital gains (or losses) outside your RRSP. All sources of investment income earned in an RRSP are tax-sheltered until withdrawn, but all withdrawals are taxed at your marginal rate for ordinary investment income (such as interest). Many fixed income investments pay regular interest at set dates throughout the term of the investment. However, compound-interest investments pay interest only upon maturity. These investments include Strip Bonds, Guaranteed Investment Certificates (GICs) and compound-interest Canada Savings Bonds. For tax purposes, the difference between the purchase price and the maturity value is considered interest income.

With compound-interest investments, even though you do not receive regular interest payments, you must include the amount of interest "earned" each year on your annual tax return. This can result in a negative cash flow if the compound investment is held in a non-registered plan. If your investment strategy includes compound-interest investments, it may be more appropriate to hold these investments in your RRSP since you will not be responsible for paying tax on the income until it is withdrawn from the plan.

The introduction of the Tax-Free Savings Account (TFSA) in 2009 provides investors with another tax-advantaged savings vehicle. Because of the significant flexibility of the TFSA, the purpose of investments held within a TFSA will vary for each investor – from short-term savings to saving for retirement. Planning opportunities for the TFSA are discussed in the next section.

Tip 3: Maximize Your Tax-Deferred Savings With an RRSP or TFSA

Your RRSP is likely the cornerstone of your overall retirement strategy. Allowable contributions to your RRSP are tax-deductible and thereby reduce your taxable income. In addition, the income earned in an RRSP is not taxed until it is withdrawn, which means that your savings will grow faster than they would if held outside an RRSP.

Maximize Contributions

The maximum RRSP contribution that can be deducted in a particular year can be found on your prior year's Notice of Assessment. Otherwise, to estimate your contribution limit start with any unused RRSP contribution room from prior years (accumulated since 1991) and add 18 per cent of your prior year's qualifying "earned income" up to the current year's maximum deduction limit: $24,930 for 2015, and $25,370 for 2016. If you are a member of a Deferred Profit Sharing Plan (DPSP) or Registered Pension Plan (RPP), you must deduct your pension adjustment (and net past service pension adjustment, if any) when calculating your RRSP contribution room.

If you leave your employer before retirement and lose the value of benefits under an employer-sponsored DPSP or RPP, a pension adjustment reversal may be available which restores contribution room lost because of previously reported pension adjustments. Contributions to an RRSP in excess of your maximum contribution room will result in a penalty tax of one per cent per month, if these cumulative 'over-contributions' exceed $2,000.

A previous federal budget extended the deadline for collapsing an RRSP until the year in which you reach age 71 (previously 69). This change recognized that many individuals are deferring their retirement and allows further contributions – where available contribution room exists – and further deferred growth within the RRSP. Notably, the 2015 Federal Budget implemented reductions to the RRIF minimum factors that apply for ages 71 to 94 to be more consistent with long-term historical rates of return and expected inflation. Please see our publication entitled **Registered Retirement Income Funds** for more information on these changes which take effect in 2015.

Contribute Securities

If you do not have enough cash to maximize your RRSP contribution, consider transferring securities you already own to a Self-Directed RRSP. This is called an "in-kind" contribution because property, not cash, is contributed. Securities include stocks and bonds of publicly-traded Canadian corporations as well as Canada Savings Bonds and other bonds issued by the federal and provincial governments. The amount of the deductible contribution will be the fair market value of the property on the date of transfer. You will be required to report any capital gains accrued to the date of transfer on your tax return. Avoid transferring assets with accrued capital losses since a capital loss realized on this transfer is denied for tax purposes.

Use a Spousal RRSP

A Spousal RRSP is the same as a regular RRSP except that it is registered in your spouse's name, allowing you as the contributor to take a tax deduction for your contributions made to the plan. When your spouse withdraws the funds at retirement, your spouse will be taxed at his or her marginal tax rate. The most advantageous scenario for a Spousal RRSP occurs when the plan holder would otherwise have little retirement income, while the contributing spouse would have a significant amount of retirement income. Contributions you make to a Spousal RRSP reduce your contribution room, not your spouse's.

The use of Spousal RRSPs as an income-splitting tool may still be recommended despite the opportunities created by pension income-splitting (discussed on page 2), since Spousal RRSPs will allow for income splitting prior to age 65. In addition, a Spousal RRSP provides a further opportunity to increase the amount of income-splitting beyond the 50% limitation provided by the new pension income-splitting rules.

If you are over age 71 and have "earned income" that has created new RRSP contribution room, you can still contribute to a Spousal RRSP as long as your spouse is 71 or younger – even though you can no longer contribute to an RRSP for yourself.

Tax-Free Savings Account

Introduced in 2009, the Tax-Free Savings Account (TFSA) is a general-purpose, tax-efficient savings vehicle that has been hailed as the most important individual savings vehicle since the introduction of the RRSP. Because of its flexibility, it complements other existing registered savings plans for retirement and education.

In 2013, the annual TFSA contribution limit was raised to $5,500, an increase of $500 from previous years; and remained at this limit for 2014. However, the 2015 Federal Budget increased the TFSA contribution limit to $10,000 from $5,500, effective for 2015 and subsequent years. Any unused contribution room can be carried forward for use in future years. If you do not already have a TFSA, you may be eligible to contribute up to $41,000 ($5,000 for 2009 to 2012 plus $5,500 for 2013 and 2014 and $10,000 for 2015). Contributions are not deductible for tax purposes, however, all income and capital gains earned in the account grow tax-free.

All withdrawals from the TFSA (including income and capital gains) are received tax-free. In addition, the amount of the withdrawal will increase your TFSA carry-forward contribution room in the following year.

A TFSA is beneficial for many investors and for many different reasons, including saving for short-term purchases such as an automobile or saving longer term for retirement. TFSAs can also be an effective income-splitting tool. A higher-income spouse can give funds to the lower-income spouse or an adult child so that they can contribute to their own TFSA (subject to their personal TFSA contribution limits). As well, the attribution rules will not apply to income earned within the spouse's (or adult child's) TFSA.

For older investors, TFSAs provide a tax-efficient means of investing – particularly beyond the age of 71 when they are no longer eligible to contribute to their own RRSP. In addition, if retirees are required to take more income than they need from a RRIF, they can contribute the excess amounts to a TFSA to continue to shelter future investment earnings from tax. Furthermore, any withdrawals from a TFSA will not affect the eligibility for federal income-tested benefits and credits (such as Old Age Security clawback or Guaranteed Income Supplements).

Where possible, the TFSA should be used in conjunction with an RRSP and other tax-deferred savings plans, such as an RESP. However, where funds are limited, a TFSA may be an appropriate savings vehicle for individuals who have forgone RRSP contributions because of the limited benefit of a tax deduction at low marginal tax rates. For others in a higher marginal tax bracket, a tax refund resulting from an RRSP contribution could be used to fund a contribution to a TFSA. Otherwise, the benefit of contributing to an RRSP versus a TFSA will depend largely on your tax rate at the time of contribution and at the time of withdrawal upon retirement. Generally, an RRSP contribution will be more beneficial where the individual is in a higher tax bracket when contributing than they are expected to be when drawing upon the RRSP funds at retirement (including the possible clawback of any government benefits). However, there is no "one-size fits all" rule and each situation should be considered individually.

The types of investments eligible for a TFSA are very similar to those investments eligible to be held within an RRSP. Similar to an RRSP, because of the tax-free nature of a TFSA, income that would otherwise be taxed at high rates outside a registered account, such as interest income, would be appropriate for a TFSA. Investments that may generate capital losses may not be appropriate for a TFSA since capital losses realized within a TFSA will have no tax benefit. However, ultimately the choice of specific investments in a TFSA will be unique to the investor, depending on such factors as their income needs, the investment time frame and their investment goals, tolerance for risk and overall investment strategy.

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Tip 4: Donate Appreciated Securities

The benefits of making a charitable donation are countless – from helping those in need to the personal satisfaction we feel when giving something back to a cause we feel passionate about. With proper planning, you can also reduce your income tax liability and maximize the value of your donation. To optimize the tax benefit of making a charitable gift, a donation of qualifying publicly-traded securities may be preferred over a cash donation of equal value, particularly in cases where you have already decided to dispose of the securities during the year.

The fair market value of securities donated to charity will reduce your taxes through a charitable donation tax credit. On donations over $200 this will result in a tax savings of approximately 46 per cent of the value of the donation (depending on your province of residence).

Tax Benefit Example

Province	Sell Shares & Donate Cash Proceeds	Donate Shares
Capital gain	$100.00	$100.00
Taxable portion	50%	nil
Taxable capital gain	$50.00	nil
Income tax (46% rate)	$23.00 (A)	nil
Charitable donation amount	$100.00	$100.00
Potential tax savings (46% rate)	$46.00 (B)	$46.00 (B)
Net Tax Savings (B)-(A)	$23.00	$46.00

A donation of securities is considered a disposition for tax purposes. If the security donated has appreciated in value since its purchase, you may incur a tax liability on the accrued capital gain. However, because of a special tax incentive to benefit those who donate appreciated qualified securities to charity, the capital gain inclusion rate on the donated securities is nil instead of the normal 50 per cent that would otherwise apply. The tax benefit realized as a result of this incentive can be significant.

Qualified securities include shares, mutual funds and a debt obligation or right listed on designated Canadian and international stock exchanges.

The example above illustrates how this special incentive increases the value of a charitable donation when the property donated is a qualified security, instead of the cash proceeds from a sale of the security. The example assumes the fair market value of the security is $100 and the adjusted cost base is nil (such as shares received from an insurance demutualization). It also assumes that sufficient other income is realized to avoid the annual limit on donation claims of 75% of net income and that other donations of at least $200 have been made in the year.

It should be noted that a 2011 federal budget amendment may limit the tax benefits associated with this strategy when flow-through securities are donated to charity. For more information on this development, please ask your financial professional for a copy of our publication entitled **Donating Appreciated Securities** and/or consult with your tax advisor.

It is also worthwhile to mention that the 2013 Federal Budget introduced a temporary "First-Time Donor's Super Credit" which will supplement the existing tax credits on up to $1,000 of donations in qualifying circumstances. Notably, however, this enhanced tax credit only applies to cash donations and will not apply to the donations in-kind described above.

Finally, on a related note, the 2015 Federal Budget has proposed a similar incentive in specific situations after 2016 where cash proceeds following the arm's length disposition of private corporation shares or real estate are donated within 30 days of the sale. Please see our **2015 Federal Budget Review** for further details regarding this proposal.

Tip 5: Use Registered Plans To Save For Children's Educational or Other Needs

The increasing cost of post-secondary education is causing many parents to be concerned about funding. To assist parents in saving for their children's education, the government introduced the Canada Education Savings Grant (CESG), which applies to certain contributions made to Registered Education Savings Plans (RESPs). These grants, combined with previous changes that allow the contributor access to the accumulated income if not used by the beneficiary for education expenses, make RESPs a very attractive vehicle to fund your children's or grandchildren's education.

Contributions to an RESP are not tax deductible. However, the income from investments in an RESP (including the income from investments purchased with the CESG) is tax-sheltered as long as it remains in the plan. Withdrawals to pay education expenses from accumulated income and the CESG will be taxable in the beneficiary's hands at his/her marginal tax rate.

There have been several recent enhancements to RESPs. In particular, the annual contribution limit to an RESP has been eliminated (which was previously $4,000 per beneficiary) and the lifetime contribution limit for each beneficiary has increased to $50,000 (from $42,000). More recently, greater flexibility for RESPs was provided by effectively extending the potential lifetime of RESPs by an additional 10 years. In addition, changes originating from the 2011 federal budget provide further flexibility for individual RESP plans by allowing certain transfers amongst RESP plans for siblings, without triggering penalties or the repayment of CESGs.

The CESG applies only to RESP contributions made after 1997. On the first $2,000 of annual RESP contributions made prior to 2007, for children up to the year they turn age 17, the government contributed an additional 20 per cent directly to the RESP, for a maximum CESG available per year of $400 (i.e., 20 per cent of $2,000). The 2007 federal budget increased the maximum annual CESG to $500 per year (i.e. 20 per cent of $2,500), although the maximum lifetime CESG remains at $7,200. If no contribution is made during the year, the CESG contribution room is carried forward. However, despite the elimination of the annual RESP contribution limits, the maximum CESG that can be received in a year from current and prior years' unused grants is restricted to $1,000.

The introduction of the TFSA (discussed previously) provides another source of funding for a child's educational or other needs. Although a TFSA can not be established for a child under 18, due to the flexibility of the TFSA it is possible for a parent to direct their TFSA savings towards the funding of their child's education. However, parents should first consider using RESPs to save for their child's education to maximize the available CESGs and other government incentives that may be available for each child, particularly where it is expected that their child(ren) will pursue post-secondary education. Thereafter, if additional educational savings are required, the TFSA could be used as a supplement. It is also worth noting that once a child turns 18, they will be able to make contributions to their own TFSA, which can be funded by parents without attribution. Thereafter, the TFSA assets can be used by the child for education or any other purpose.

Registered Disability Savings Plans

For disabled individuals, a tax-deferred investment savings vehicle similar to the RESP was introduced several years ago. The Registered Disability Savings Plan (RDSP) is a registered savings plan intended to help parents and others save for the long-term financial security of persons with severe or prolonged disabilities who are eligible for the Disability Tax Credit. Contributions up to a lifetime maximum of $200,000 per beneficiary can be made to

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an RDSP until the end of the year in which the disabled beneficiary turns 59, with no annual limit. Contributions are not tax deductible; however, any investment earnings that accrue within the plan grow on a tax-deferred basis. When earnings are withdrawn as part of a disability assistance payment, they are taxable in the hands of the beneficiary. Canada Disability Savings Bonds (CDSB) and Canada Disability Savings Grants (CDSG), up to annual and lifetime limits, can be received in an RDSP from the federal government depending on family income. Recent federal budgets have provided further enhancements to RDSPs, including the 10-year carryforward of CDSB and CDSG entitlements, the possible roll-over of RESP investment income to RDSPs, increased flexibility on withdrawals for beneficiaries with a shortened life expectancy and the extension of the existing RRSP/RRIF roll-over rules to allow the roll-over of a deceased's RRSP/RRIF proceeds to the RDSP of a financially dependant child. Speak to your financial professional if you or a family member are disabled to understand more about these plans.

Tip 6: Use Borrowed Funds To Invest

Generally, interest expenses are deductible for tax purposes if the funds are borrowed for the purpose of earning income from a business or an investment vehicle, both initially and on an ongoing basis. Interest on borrowed funds that are used only to generate a capital gain is generally not deductible. Consider paying down non-deductible personal debts (such as RRSP loans, mortgages on home purchases and credit card balances) before paying down investment-related debt. Speak to your tax advisor about the appropriate structuring of your particular investment strategy to achieve interest deductibility in light of the relevant tax legislation and case law.

Tip 7: Manage Income Tax Withholding / Instalments

If you are one of many Canadians that receives an income tax refund each year, ask yourself "why am I giving the government an interest-free loan"? If you are getting a refund, it's usually because the income taxes that are withheld by your employer exceed your actual tax liability. Income tax withholding rates are an estimate of the taxes you will owe for the year if your only income source is the one upon which the taxes are being calculated. Withholding rates do not take into consideration all income tax deductions and credits such as RRSP contributions, deductible alimony payments or charitable donations. This can result in an overpayment of tax during the year and a refund when you file your tax return.

If you would like your employer to reduce the amount of withholding taxes from your earnings, you must make your request in writing to your local CRA District Taxation Office (or Revenue Quebec). Include documentation to support your request such as RRSP contribution receipts or a written court order for support payments. If you qualify, your employer will receive a letter of authorization to reduce the withholding taxes on your employment income.

The reduced withholding means you will improve your cash flow by increasing your net take home pay throughout the year, instead of receiving a lump-sum tax refund the following year.

Similarly, many investors are required to remit quarterly personal income tax instalments on significant investment income which is not subject to withholding tax at source. Many investors do not adequately review the appropriate amount of tax instalments to remit, which can lead to an 'interest free loan' to the government for over-remittances or non-deductible interest and penalties for late or deficient remittances. Accordingly, investors with larger portfolios should consider reviewing and planning for potential instalment requirements with their tax advisor – with assistance from your BMO financial professional.

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Tip 8: Reduce Tax For Your Estate

Your estate plan can accommodate a number of tax-saving strategies to reduce or defer the amount of tax payable by your estate and maximize the amount available to your heirs.

Use a Trust to Split Investment Income

If your spouse or other beneficiaries are likely to invest their inheritance, it may be possible to reduce tax on investment income by using trusts created in your Will – called "testamentary" trusts. Unlike trusts created during your lifetime ("inter-vivos" trusts), currently these testamentary trusts are taxed at the graduated marginal tax rates, allowing tax savings to be achieved on income that is retained in the testamentary trust.

However, because the government has become concerned with the growth in the tax-motivated use of testamentary trusts, it announced its intention in the 2013 Federal Budget to review and consult on possible measures aimed at eliminating the special tax benefits that arise from taxing the income of testamentary trusts (and certain grandfathered inter-vivos trusts) at the marginal tax rates. Following a consultation period, the 2014 Federal Budget reaffirmed the government's intention to proceed with these measures, which include the application of the flat top tax rate to income taxed within a testamentary trust effective for 2016 and subsequent taxation years.

Two exceptions to the imposition of the flat top tax rate will apply as follows:

- During the first 36 months following death, a deceased individual's unadministered estate may be eligible for the graduated tax rates, provided the executor does not distribute the estate assets during this period (if so permitted under the terms of the Will).
- Graduated marginal tax rates will continue to apply for certain testamentary trusts (defined as "Qualified Disability Trusts") whose beneficiaries are eligible for the federal Disability Tax Credit.

The forthcoming changes in 2016 will eliminate some of the other special tax treatments accorded to testamentary trusts such as the exemption from income tax instalments and the exemption from the general requirement for trusts to have a December 31 taxation year-end. In addition, another important related legislative change introduced with these measures will deem capital gains arising in spousal trusts (or alter-ego and joint-partner trusts) on the death of the beneficiary individual after 2015 to be payable (and taxable) to that individual, which can dramatically impact an existing estate plan.

Although these forthcoming changes in 2016 will eliminate access to the graduated tax rates on income taxed within all existing and future testamentary trusts, trusts created in your Will, such as a trust for each child's family, may still provide income splitting opportunities since they can be used to "sprinkle" income on a discretionary basis to family members in the lower tax brackets. In addition, testamentary trusts offer many other benefits (including control and protection), such that they will continue to be an important consideration in tax and estate planning. Please see our publication entitled **New Tax Rules May Affect Your Estate Plan** for more information.

Because of the significance of these forthcoming changes, it will be important to consult with your external tax and legal advisors to determine any impact to your existing Wills and estate plan, as well as any existing testamentary, spousal, alter-ego or joint-partner trusts established by you or your family members.

Name a Beneficiary For Your RRSP/RRIF or TFSA

The value of an RRSP or RRIF is included in the tax return of the annuitant in the year of death. If the beneficiary is your surviving spouse or a financially dependent child or grandchild, your estate will generally not be taxable on the proceeds from the plan. Instead, the beneficiary will include the proceeds in his or her income. Your surviving

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spouse can defer the tax on the proceeds if the funds are rolled into your spouse's own RRSP or RRIF. Taxes can also be deferred if the beneficiary is a financially dependent child or grandchild who is a minor or is disabled (if under age 18, an annuity payable to age 18 is available; if disabled and financially dependent, a roll-over to the beneficiary's own plan is available).

If any of these roll-overs are not available, the fair market value of the investments in the RRSP/RRIF at the time of death is generally included in the final tax return of the deceased. If the RRSP/RRIF investments have increased in value from the time between the annuitant's death and the distribution to the beneficiary, the amount of the increase is generally included in the beneficiary's income. On the other hand, the amount of any post-death decrease in the value of the RRSP/RRIF to be carried back and deducted against the deceased annuitant's year of death income inclusion, where the distribution of the deceased's RRSP/RRIF occurs after 2008. Please speak to your tax professional for more information.

Subsequent to the introduction of the TFSA, most provinces introduced legislation also allowing beneficiary designations for TFSAs. (**NOTE**: Quebec does not allow the ability to name a beneficiary for an RRSP, RRIF or TFSA.) Where the TFSA holder designates a beneficiary (or beneficiaries), upon the death of the account holder the proceeds of the TFSA will be paid out to the beneficiary (or beneficiaries), and the TFSA will be closed. The fair market value of the TFSA at death would be received by the deceased tax-free and this amount is also received tax-free by the beneficiaries; however, any income or growth post-death is taxable to the beneficiary. A surviving spouse beneficiary has the ability to transfer the TFSA value at date of death to their TFSA ("exempt contribution"), but to the extent that there has been any appreciation post-death, they would need sufficient contribution room to transfer this increase to their own TFSA. Many of these complexities are not applicable where a spouse is named as the 'successor holder' and as such, it is usually recommended that spouses are named as 'successor holders' of TFSAs instead of beneficiaries, although generally probate fees (where applicable) will not apply in either case where a TFSA successor holder or beneficiary has been named.

Where the TFSA is not transferred to a surviving spouse, as previously stated, the fair market value of the TFSA at death would be received by the deceased tax-free and this value is also received tax-free by the beneficiaries but any income or growth post-death is taxable to the beneficiary. To the extent that the beneficiary has sufficient contribution room in their own TFSA, they would be able to transfer some or all of the inherited TFSA assets to their own TFSA, once the beneficiary has actually received the distribution from the deceased's TFSA. Assets not transferred to the beneficiary's TFSA will remain in the beneficiary's non-registered account and any income thereon will be subject to future taxation.

For TFSA holders without spouses, naming someone as a beneficiary can provide a means of avoiding probate (where applicable) but in some situations it may be desirable to have the assets pass through the Will to facilitate estate planning, notwithstanding the cost of obtaining probate. Ultimately, you should consult with your estate professional for confirmation of the appropriate designation on all of your registered plans in the context of your overall estate plan.

Defer Capital Gains

For non-registered accounts, upon death capital gains that have not been realized during your lifetime are taxable to your estate. However, if your investments are inherited by your surviving spouse (or a qualifying spousal trust), the tax on accrued capital gains can be deferred until the investment is actually sold, or until the death of your surviving spouse.

Continued

In some circumstances, subject to the terms of your Will, your executor may elect to realize a capital gain or loss on some of the property left to your spouse. For example, it may be beneficial to realize a capital gain sufficient enough to offset any unused losses carried forward in the year of death, and the spouse will inherit the higher cost base. Alternatively, a realized capital loss may be available to offset any income, not just capital gains, in the year of death or the immediately preceding year.

Charitable Bequests

The charitable donation tax credit is generally subject to an annual limit of 75% of net income. However, for donations made in the year of death the credit limitation is increased to 100% of the deceased's net income and any donations that cannot be claimed in the year of death can be claimed in the deceased's prior year tax return, also up to 100% of net income in that year. There is also a special provision within the current tax legislation that allows specific donations made pursuant to a Will to be deemed to have been made by the individual immediately prior to his or her death, even though the actual transfer may occur during the estate administration. This treatment can be beneficial in allowing a donation tax credit to reduce taxes otherwise payable at death in the individual's terminal tax return (or in the year preceding death). Similar provisions apply where an individual designates a qualified donee as a beneficiary under an RRSP, RRIF, TFSA or life insurance policy.

Conversely, under the current legislation, donations made by an individual's estate (which were not pursuant to the terms of the Will or beneficiary designation) do not qualify for this treatment and can only be applied against the estate's income tax otherwise payable, which in some cases, may not be sufficient to allow the full benefit of the donation tax credit to be realized. However, new legislation originating from the 2014 Federal Budget will allow more flexibility in the tax treatment of charitable donations in the context of a death occurring after 2015.

Specifically, a donation made by Will (and designated donations) will no longer be deemed to have been made immediately before death. Instead, these donations will be deemed to have been made by the estate at the time the specific property is donated to the qualifying donee. As a result, further planning opportunities will exist starting in 2016 for certain qualifying estates. Where applicable, estate trustees will have additional flexibility to apply the donation tax credit, resulting from donations made during the first 36 months of an unadministered estate, to:

i. the taxation year of the estate in which the donation is made;

ii. an earlier taxation year of the estate; or

iii. the last two taxation years of the deceased individual.

In light of these changes forthcoming in 2016, you should consult with your tax and estate professionals to fully review the possible tax implications and benefits of any charitable bequest strategy within your existing estate plan.

Tip 9: Consider US Estate Tax Implications If You Own US Investments

Investing in foreign assets, such as US securities, provides an opportunity for diversification. However, US estate tax could be a concern if you are a Canadian who owns US property at death.

The estate of a Canadian is potentially subject to US estate tax if the value of US property owned personally at death exceeds US$60,000 and the value of world wide assets exceeds US$5.43 million for deaths in 2015.

US estate tax generally escalates as the value of the estate increases. US estate tax rates start at 18% and increase to a maximum of 40% (see chart on page 13). US taxable property includes US real estate, shares of US corporations, many US bonds and debts of a US issuer, even if the investment is held in an RRSP, RRIF or TFSA. Canadian

mutual funds that invest in US securities or American Depository Receipts (ADRs) are generally not subject to US estate tax. In Canada, estates are subject to Canadian income tax on accrued gains on all capital property owned on death, including any US taxable property (unless the property is left to a spouse or qualifying spousal trust). This means that not only may your US taxable property attract US estate tax, but it may also be taxed by the imposition of Canadian capital gains tax.

However, relief is available to reduce the adverse effects of US estate tax imposed on Canadians in certain circumstances. The tax treaty between Canada and the US (the 'Treaty'), together with Canadian tax rules, may:

- Eliminate US estate tax for "small" estates with a worldwide value below the amount covered by the unified credit (US$5.43 million for 2015 and indexed for inflation in future years);
- Provide Canadians with access – but only on a pro-rated basis – to the same unified credit and marital credit available to US citizens to reduce US estate tax and;
- Allow US estate tax paid as a foreign tax credit but generally only against Canadian federal capital gains tax payable on the US property. Previous changes to the treaty extended the possible credit of US estate tax against Canadian income tax payable at death on RRSPs, RRIFs and stock options.

These provisions may not apply to all Canadians owning US taxable property. In particular, Canadians who are US Citizens are subject to different regulations. Investors should be aware that tax planning opportunities are available in order to minimize the exposure to US estate tax.

For more information, please your financial professional for a copy of our publication **US Estate Tax for Canadians** and **Tax and Estate Consequences of Investing in US Securities**. Cross-border planning is very complex and requires professional advice.

U.S. Estate Tax Rates (in $U.S.)

If the taxable amount is:			
Over (1)	But not over (2)	Tax on (1)	Tax rate on excess over (1)
$0	$10,000	$0	18%
$10,000	$20,000	$1,800	20%
$20,000	$40,000	$3,800	22%
$40,000	$60,000	$8,200	24%
$60,000	$80,000	$13,000	26%
$80,000	$100,000	$18,200	28%
$100,000	$150,000	$23,800	30%
$150,000	$250,000	$38,800	32%
$250,000	$500,000	$70,800	34%
$500,000	$750,000	$155,800	37%
$750,000	$1,000,000	$248,800	39%
$1,000,000		$345,800	40%

Source: Wolters Kluwer Limited, CCH

Finally, investors are reminded of the CRA requirement to disclose their foreign investments annually on Form T1135 (Foreign Income Verification Statement) if the aggregate cost of the non-registered foreign property exceeds CDN $100,000 at any time during the year. For more information on this CRA reporting requirement, please ask for our publication entitled **The CRA's Foreign Reporting Requirements**.

Tip 10: Year-End Tax Planning

Tax planning should be a year-long event, however, here are some last-minute tips and reminders to help reduce income tax costs for you and your family.

Important Dates to Remember

December 15

Due date for final income tax instalment for individuals. Consider the impact of investment income on quarterly tax instalments to avoid non-deductible arrears interest and penalties.

December 24

Possible last buy/sell date for Canadian securities to settle in the calendar year (based on trade date plus three days). Review investment portfolios to consider the sale of securities with accrued losses before the end of the year to offset capital gains realized in the year or in the three previous taxation years (if net capital loss created in current year). Watch the superficial loss rules that will deny the capital loss on the sale of an investment if repurchased within 30 days by you, your spouse or other affiliated entity. Ask your financial professional for a copy of our publication **Understanding Capital Losses** for more information on this strategy.

January 30

Last day to pay annual interest on family loans to avoid income attribution. (see page 1)

March 1

Last day to make an RRSP contribution. (see page 5) Note however that the deadline to make a 2015 RRSP contribution will be **February 29, 2016**.

RRSP/RRIF

Did you turn 71 this year?

- You must wind-up your RRSP by the end of the year in which you turn 71, so consider making a final RRSP contribution to the extent you have any unused RRSP contribution room.

Children

- File a tax return for children with “earned income” to start accumulating RRSP room.
- Start saving for your child’s education – contribute to an RESP and you may be eligible for a government grant. (see page 8)
- Keep receipts for fees paid for your children under the age of 16 (at the beginning of the year) for enrolment in an eligible physical or artistic program to support a claim for a fitness or arts tax credit. Note that the fitness credit is now $1,000 for 2014 (from $500) and will be refundable for the 2015 and subsequent tax years.
- Be aware that a new federal non-refundable tax credit of up to $2,000 was recently introduced effective for 2014 for couples with children under 18. This credit reflects the federal tax reduction, to a maximum of $2,000, that would result if up to $50,000 of taxable income were notionally transferred from one spouse to the other.
- Keep in mind that the maximum dollar amounts that can be claimed under the Child Care Expense deduction will increase by $1,000 effective in 2015 [generally $8,000 (from $7,000) per child under age 7 and $5,000 (from $4,000) per child aged 7 to 16].

Donations

- Donate appreciated securities instead of cash for enhanced tax savings. (see page 7)
- Make all charitable donations by December 31 (including donations planned for early next year).
- Combine all charitable donations for you and your spouse and claim on one income tax return for maximum tax savings.
- If the total donated is less than $200, consider carrying forward donation receipts for up to 5 years.

Medical Expenses

- Combine medical expenses for you and your family on one income tax return and choose the 12-month period ending in the year that contains the most expenses.

2015 Combined Federal and Provincial Top Marginal Tax Rates for Individuals [1]

Province	Salary and Interest	Capital Gains	Non-Eligible Dividends	Eligible Dividends
B.C.	45.80%	22.90%	37.98%	28.68%
Alberta	40.25%	20.13%	30.84%	21.02%
Saskatchewan	44.00%	22.00%	34.91%	24.81%
Manitoba	46.40%	23.20%	40.77%	32.26%
Ontario	49.53%	24.76%	40.13%	33.82%
Quebec	49.97%	24.98%	39.79%	35.22%
New Brunswick	54.75%	27.38%	46.89%	38.27%
Nova Scotia	50.00%	25.00%	41.87%	36.06%
P.E.I	47.37%	23.69%	38.74%	28.70%
Newfoundland	43.30%	21.65%	33.26%	31.57%
Yukon	44.00%	22.00%	35.18%	19.29%
NWT	43.05%	21.53%	30.72%	22.81%
Nunavut	40.50%	20.25%	31.19%	27.56%

[1] The above table reflects the 2015 top marginal tax rates by province which apply to taxable incomes over $138,586 ($150,000 in Nova Scotia, $151,050 in British Columbia, $175,000 in Newfoundland/ Labrador, $220,000 in Ontario, $250,000 in New Brunswick, $300,000 in Alberta and $500,000 in Yukon).

Conclusion

Tax Tips for Investors is neither a comprehensive review of the subject matter covered nor a substitute for specific professional tax advice. The tax strategies contained in this publication may or may not be appropriate for you. As such, we encourage you to consult with an independent tax professional to confirm the anticipated implications to your particular situation of the current tax legislation in developing and implementing any tax strategies.

We're here to help.™

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