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COMMENT

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CLARITY OF INTENTIONS

A properly drafted will must be crystal clear as to the objectives of the testator. The courts are busy interpreting provisions of wills when the beneficiaries cannot agree on their legal meaning. The process of hiring lawyers to opine on the legal meaning of a provision, or hiring lawyers to object to the interpretation of a provision, can be expensive and time consuming, and can permanently damage family relationships.

A recent case before Ontario's Superior Court of Justice highlights the need to ensure clarity of the written words in a will. The facts of the case are as follows:

- The testator was Mr. Andrew Steward Cromarty.
- At the time of his death, Mr. Cromarty owned three farms (A, B and C).
- Farm B was bequeathed to Mr. Cromarty's niece.
- Farm C was bequeathed to two of Mr. Cromarty's friends, a married couple.
- Farm A fell to the residue of the estate, and the residue was left to Mr. Cromarty's nephew.
- Mr. Cromarty was entitled to the qualified farm capital gains exemption.

The following are three provisions of Mr. Cromarty's will dealing with the distribution of his property and the handling of taxes and debt. While Mr. Cromarty may have had specific intentions, the words used to articulate his intentions unfortunately resulted in conflicting interpretations.

The bequest to the niece said, in part:

"Capital gains tax with respect to this property that is the subject of this trust shall be determined as at the date of my death and the amount thereof paid from the residue of my estate. Thereafter any such tax payable with respect to the property shall be charged to or paid by the beneficiary receiving the said property."

The bequest to the friends noted as follows:

"Capital gains tax and probate fees, if any, that are attributable to this property, shall be charged to or paid by the beneficiaries of the said property."

The will included a general provision in respect of taxes:

"It is my express intention that all taxes, including capital gains tax, and probate fees, if any, shall be determined as of the date of my death and shall be paid from the residue of my estate, unless provided otherwise in this my will."

Some of the numerical information was as follows:

Capital gain on Farm A	$556,431
Capital gain on Farm B	$459,633
Capital gain on Farm C	$475,000
Capital gains exemption	$750,000
Other Income subject to tax	$50,850
Tax liability on terminal return	$194,045
Tax attributed to farm properties	$173,806

The differing interpretations of the wording of the provisions resulted in disagreement among the beneficiaries and necessitated involvement of the court.

Mr. Cromarty's nephew took the position that the residue of the estate should bear the least amount of tax and the friends the most amount of tax, and wished to apply the entire capital gains exemption to farms A and B. The nephew's position calculated the tax owing by the friends as the difference in the estate's income tax liability with and without Farm C. This approach resulted in the friends owing $111,068 in taxes in respect of Farm C.

The friends, on the other hand, took the position that the estate's tax should be allocated across the three farm properties based on the ratio of capital gains reported. This approach would allocate the total of

$173,807 across the three properties in the ratio of 37%, 31% and 32% respectively. The result was $55,357 of taxes due from the friends as per the will.

The judge presiding over the case reasoned that capital gains and taxable capital gains were taxed in the aggregate, and that the deduction for the capital gains exemption was not taken against an individual property but against the aggregate taxable capital gain reported. The judge decided that the income tax liability attributed to the three farm properties was to be allocated in ratio to the capital gains reported.

The importance of drafting a clear and understandable will cannot be overstated. When the financial interests of beneficiaries can change based on interpretation, disagreements will likely result. For this reason, a careful review should be part of every individual's process in creating a will.

I/R 2121.00

ACCOUNTING FOR AN INSURANCE POLICY

Many times, a recommendation is made for life insurance to be owned within a corporate structure. If the company names itself as the beneficiary under the contract, the premium payments generally do not give rise to any taxable benefit to the shareholder(s).

The primary advantage of corporate ownership is that it usually takes less pre-tax income to fund the required premiums. The planning rule of thumb is that, if all other things remain equal, the entity with the lowest tax rate should pay any non-deductible expenses, and life insurance premiums are generally not tax deductible.

The primary disadvantage of corporate ownership is the loss of creditor protection. Individually-owned life insurance enjoys special protection under the Bankruptcy Act of most provinces under certain specific circumstances. To the extent the beneficiary is within a prescribed class of relatives of the insured person, the policy is exempt from seizure by creditors of the owner. Since a designated corporate beneficiary cannot have a qualifying family relationship with the insured person, creditor protection is not available, thus exposing the contract to all creditors of the corporation.

When the policy is acquired by the corporation, it is important to properly record the purchase, the premium payments and any buildup of contract cash value in the books of the corporation. The International Financial Reporting Standards (IFRS) and Accounting Standards for Private Enterprises are silent as to the financial reporting of corporate owned life insurance. Guidance in respect of accounting for a life insurance policy can be taken from the United States, where the financial accounting standards board has released a statement.

Consider the following example:

$10,000	premium due annually for 10 years, after which the policy is paid up
$3,000	cash value at the end of year one
$8,000	cash value at the end of year two
$98,000	cash value at the end of year nine
$110,000	cash value at the end of year ten
$115,000	cash value at the end of year eleven

The following are the accounting entries:

DR	Cash Value	3,000		balance sheet
DR	Insurance Expense	7,000		income statement
CR	Bank		10,000	balance sheet
To record premium payment in year one and recognize year end cash value of 3,000				
DR	Cash Value	5,000		balance sheet
DR	Insurance Expense	5,000		income statement
CR	Bank		10,000	balance sheet
To record premium payment in year two and increase of 5,000 in cash value				
DR	Cash Value	12,000		balance sheet
CR	Insurance Gain		2,000	income statement
CR	Bank		10,000	balance sheet
To record premium payment in year ten and increase of 12,000 in cash value				

Debit (DR) and Credit (CR) are accounting terms and are used to ensure that the entries are always in balance — the amount(s) of debit must be equal to the amount(s) of credit.

Insurance expense and insurance gain would be reported on the Income Statement of the corporation. Even though this was reported as an accounting expense or income, it would not be tax deductible or taxable. This life insurance expense recorded on the Income Statement of the company would be added back or deducted when determining the taxable income of the company.

The accounting entries (as shown in the example above) should begin with the known facts and ensure that the entry is balanced with an expense or revenue adjustment. In year one, $10,000 was drawn from the bank and the cash value within the policy increased by $3,000; therefore, the insurance expense had to be $7,000. In year two, $10,000 was again drawn from the bank and the year-end cash value within the policy was $8,000; therefore, the cash value had to be increased by $5,000 and the offsetting insurance expense would be $5,000. In year ten, $10,000 was again drawn from the bank and the year-end cash value of the policy was $110,000. From year eleven onwards, the policy would be paid up and no amount

would be drawn on the bank. However, accounting entries could still be made based on the change in cash value over the fiscal period.

In order to enhance the value of information provided by a company's financial statements, notes are usually added to explain significant accounting policies and other information on the financial statements. The actual cash value of the corporate-owned life insurance policy as well as the death benefit and other pertinent information could be disclosed in a note to the financial statements. This will ensure that the policy has been properly accounted for and important information is available to the readers of the financial statements.

Accounting is very important because it reports the performance of the company to various interested parties. Accounting is based on conservative rules that are applied consistently over time. While not an end in itself, it is still important to be able to know how to record the purchase of corporate-owned life insurance.

I/R 300.04

MORE OPPORTUNITY TO SAVE

Federal and provincial governments encourage taxpayers to save for their retirement by granting tax relief for savings contributed to and held in a Registered Retirement Savings Plan ("RRSP"). Contributions are tax deductible and the income earned is tax deferred. And yet, as attractive as the tax incentives may be, relatively few taxpayers avail themselves fully of the opportunity.

In 2010, just under six million tax filers contributed about $34 billion to their RRSPs for an average contribution of $5,686. While the average seems fairly high, the median was only $2,790. The median is the point where half of the six million tax filers are below the amount, and half are above. These six million tax filers represented 26% of the number of tax filers who where eligible to make RRSP contributions and had available contribution room. About 93% of all tax filers are eligible to make RRSP contributions.

While $34 billion sounds like a significant amount, it represents only 5.1% of the total RRSP room available in the system across all tax filers. It is the limited use of this type of retirement savings vehicle that creates concern that Canadians are not saving sufficient amounts to truly fund their own retirements.

To be eligible to contribute to an RRSP, a taxpayer must have either new RRSP room as a result of qualifying income from the previous year, or unused room from earlier years. The limit is 18% of the previous year's earned income, to a fixed maximum, less any pension adjustments, plus any unused room carried forward.

The fixed maximum RRSP contribution limits are $22,450 for the 2011 tax year, and will be $22,970 for the 2012 tax year. Individuals can locate their unused RRSP contribution room, which is prepared and tracked by the Canada Revenue Agency, on their most recent Notice of Assessment.

Individuals can make contributions, up to their available RRSP room, into their own RRSP or into a spousal RRSP. When making a contribution into a spousal RRSP, it is the contributor who is eligible for the deduction for the contribution while the spouse or common-law partner is the actual owner/annuitant of the RRSP. It should be noted that the rollover of retirement allowances or registered pension plan amounts can only go into the individual's RRSP and not a spousal plan.

The RRSP rules can be difficult to understand, even though they have been available to Canadian taxpayers for several decades. Taxpayers need to educate themselves about RRSPs and other tax-incented savings plans (such as Tax-Free Savings Accounts and the newly-announced Pooled Retirement Pension Plans) if they hope to be able to maintain comfortable lifestyles when their income-earning years come to an end and they have to rely on accumulated savings.

I/R 5401.06

GOVERNMENT PENSION PLANS: Benefits And Contributions For 2012

Contributions and benefits under government pension plans are adjusted periodically to reflect increases in the Consumer Price Index or the average Canadian wage. The new amounts, commencing January 1, 2012, are shown in the table below. Each benefit is subject to income tax when received, with the exception of the Guaranteed Income Supplement and the Allowance. All benefits shown are paid monthly unless otherwise indicated, and are the maximum amounts.

	CPP	QPP	OAS
CPP / QPP benefits (for new beneficiaries)			
Retirement pension (at age 65)	$986.67	$986.67	
Disability pension	$1,185.50	$1,185.47	
Disabled contributor's child benefit (each child)	*$224.62	*$71.32	
Survivor's*** pension			
under age 65	**$543.82	**$815.47	
age 65 or over	$592.00	$592.00	
Surviving child's benefit (each child)	*$224.62	*$224.62	
Death benefit (lump sum)	$2,500.00	$2,500.00	
Combined benefits			
survivor's*** pension and disability (under age 65)	$1,185.50	n/a	
survivor's*** pension and retirement (age 65 and over)	$986.67	$986.67	
Annual CPP contribution			
Self-employed (9.9%)	$4,613.40		
Employee (matched by employer) (4.95%)	$2,306.70		
Annual QPP contribution			
Self-employed (10.05%) Employee (matched by employer) (5.025%)		$4,683.30 $2,341.65	
Old Age Security (OAS)			
January to March 2012			$540.12
Guaranteed Income Supplement (GIS)			
January to March 2012			
spouse/common-law partner receives OAS or Allowance			$485.61
single person (or spouse/common-law partner receives neither OAS nor Allowance)			$732.36
Allowance			
January to March 2012			
age 60 to 64, and spouse/common-law partner receives OAS and GIS			$1,025.73
age 60 to 64, survivor's*** Allowance			$1,184.35

Notes:
* flat benefit amounts
** these amounts may vary depending on whether the survivor is under age 45, disabled, or with or without children
*** a survivor is the spouse or common-law partner of a deceased individual

I/R 3201.01 and 3201.03

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