

Year end strategies for 2007

As the final weeks of 2007 draw to a close, most of us are focused on Christmas shopping, holiday parties and New Year's festivities. However, this is also the time to implement any final tax strategies that could help put more tax dollars back in your pocket. Here is a laundry list of strategies that may go a long way to helping reduce your taxes for 2007.

By: Mackenzie's Tax & Estate Planning Group

Investors should consider the following strategies for their portfolios:

Initiate trades before investment deadline

If you are planning to sell an investment at a loss in order to offset it against capital gains this year or in the past three years, the settlement date must fall in 2007. For most securities and mutual fund trades, you will need three business days for the transaction to settle. Therefore, you will need to place your stock or mutual fund trade by December 24th, 2007 in order to ensure the trade settles in 2007, and your capital loss applies to 2007.

Trigger accrued losses before year-end

Capital losses are used to offset capital gains in the current year first, then any excess can be applied against capital gains in any of the three prior calendar years. If you have paid tax on capital gains this year or in the previous three years and have losing investments, consider triggering the capital loss before year-end. It is preferable to carry back losses to the earliest year possible since the oldest years will expire first. This strategy will help you recover taxes paid on previously reported capital gains.

Treat capital gains appropriately

Capital gains are triggered when an asset is sold for more than what you paid for it. While capital gains are a tax efficient form of income, there are opportunities to treat capital gains in a manner that will minimize the tax bill even further. Here are some ideas to consider:

- 1) If you have unused losses, you can use those losses against your capital gains
- 2) Crystallize In-trust for (ITF) accounts where the beneficiary has little or no income. With the use of the basic personal amount (\$9,600 for 2007), you may trigger up to \$19,200 in capital gains without paying any tax.
- 3) Delay any sale until after December 31st, 2007. Doing so allows you to push your tax bill to April 2009, the time you have to file your 2008 personal tax return
- 4) Structure the sale of an asset such that the proceeds are collected over more than one year. The capital gains reserve allows you to spread the tax liability over a maximum period of five years if you receive payment over five years. See a tax professional who can assist you with this strategy.

- 5) Claim the \$750,000 capital gains exemption if you're selling qualifying small business shares (QSBC) or qualified farm/fishing property. Even if you do not plan on selling your QSBC shares, farming / fishing property, consider crystallizing the shares / property in order to bump up the ACB of your shares / property. This is a highly complex area of tax law. It is advisable to speak to a tax professional about this strategy.

Transfer investments to child

Consider transferring investments that have dropped in value to a minor child before year-end. You will trigger a capital loss that can be offset against capital gains this year or in the previous three years. In addition, you can pass the tax liability for any future growth of the investment to the minor child, since the attribution rules do not apply to capital gains triggered by minor children.

Donate securities to charity

A donation to a registered charity by year-end provides valuable tax credits. If you are planning to make a donation to charity, consider directly donating publicly traded securities or mutual funds that have appreciated in value, instead of cash. You will receive a donation receipt equal to the value of the investment at the time of the donation and any resulting capital gain is exempt from tax.

Better yet, if you own mutual fund units that were the result of matured flow-through shares, consider donating these investments to charity. In addition to the tax savings that resulted from the CDE & CEE deductions at the time you owned the flow-through limited partnership units and the tax deferral of the capital gain when the rollover to the mutual funds occurred, this strategy allows you to avoid the tax on capital gain at the time of the donation, plus benefit from the donation tax credit. A triple benefit!

Establish a private foundation

Consider donating cash, securities or insurance to the Mackenzie Charitable Giving Fund by December 31st to obtain tax savings. This cost effective private foundation allows you the flexibility of establishing grants to any number of charities or other institutions of your choice, providing you tax savings and simplifying your philanthropic objectives.

Adjust your installment payments

Some investors are subject to tax instalments, due March 15, June 15, September 15 and December 15. Instalment payments are based on previous years income. Therefore, if your income for 2007 is lower than in previous years, consider reducing your final instalment payment on December 15th.

Investors should consider the following strategies for their RRSP:

Make your RRSP contribution on time

RRSP contributions must be made by the end of the first 60 days of 2008. As 2008 is a leap year, the RRSP contribution deadline is February 29, 2008. Make your contribution as soon as possible as you will have more money working for you sooner. Refer to your latest Notice of Assessment, which will inform you of your available RRSP contribution limit. Any excess contributions exceeding \$2,000 are subject to a 1% per month penalty tax. Also, if you have a pre-authorized chequing plan (PAC) running into an RRSP on the 1st of each month, consider making an advance contribution to your RRSP in replacement of your March 1st, 2008 contribution, since March 1, 2008 is not within the first 60 day period as it normally is in non leap years.

Make the most of your unused RRSP contribution room

If you have contributed less than the maximum permitted in prior years to your RRSP, you should have unused RRSP contribution room carried forward to 2007. Consider topping up your RRSP to the maximum possible in order to take advantage of the benefits RRSPs have to offer. If you're short on cash to maximize your RRSP room, consider borrowing to make your RRSP contribution or transferring mutual funds or securities in-kind to your RRSP. Speak to your financial advisor about ways you can maximize your RRSP contribution room.

Contribute to a spousal RRSP

If you have a spousal RRSP established, make your spousal RRSP contribution before year-end to minimize the possibility of having the attribution rules apply on any future withdrawals. For example, if you make a spousal RRSP contribution this year, your spouse can safely withdraw funds from the spousal plan and pay tax on the income as early as January 1st, 2010. A spousal RRSP contribution made in January 2008 will mean that your spouse will have to wait until January 2011 before he/she can safely withdraw funds without the attribution rules applying.

Contribute to spousal RRSP if your spouse / CLP passed away in 2007

Where your spouse or common law partner passed away with unused RRSP contribution room this year, the executor of the estate (which may be you) should consider making a final contribution to a spousal RRSP by February 29th, 2008. This will provide tax savings as the RRSP contribution can be deducted against income on the deceased's final tax return.

Base withdrawals on age of younger spouse or common law partner

If you will be 71 by the end of 2007, you must convert your RRSP to a RRIF and begin drawing an income from your RRIF. Consider basing the minimum RRIF withdrawal on the age of the younger spouse. This will keep your required annual RRIF income as low as possible each year and allow you to keep more in your RRIF, thus deferring tax longer.

Delay HBP withdrawals until after year-end

The Home Buyer's Plan (HBP) is a great way to help fund a down payment for a home. However, there are some tricky rules that can be handled more easily if you delay your withdrawal until after year-end. Specifically, you must purchase a qualifying home by October 1st of the year following the withdrawal, all withdrawals must be made in the same calendar year and repayments begin two years following the year of withdrawal. Delaying your withdrawal until after year-end allows you more time to purchase a home, make more withdrawals under the plan and extend the time before which you must begin repaying funds to your RRSP.

Make your required HBP repayment

You are required to begin your HBP repayments in 2007 if you participated in the program prior to 2006. To avoid any unnecessary income inclusion, be sure to make your required repayment and designate the contribution as a repayment on Schedule 7 of your personal tax return. Check your latest Notice of Assessment from the CRA for more information if you're unsure of your repayment requirement.

Consider missing your HBP repayment

As discussed above, failure to meet your minimum HBP repayment creates an income inclusion. However, in some instances it may work to your advantage to intentionally miss your HBP repayment. Consider missing your HBP repayment if you are in an unusually low-income year, or where the funds were borrowed from a spousal RRSP and your spouse / CLP is in a lower tax bracket. HBP withdrawals are not subject to the spousal RRSP attribution rules and therefore the income inclusion will fall in the hands of the annuitant spouse – another great way to income split!

File appropriate elections for your RRSP

If you are a US citizen, resident or green-card holder and own a Canadian RRSP, you are required to disclose certain information to the IRS about your RRSP. Even worse, you may also be liable for US income taxes on any investment income earned inside your RRSP, since the IRS does not recognize the tax-deferred status of an RRSP. Be sure to file Form 8891 to the IRS for 2007. This allows you to meet the IRS disclosure requirements and ensures that you continue to defer tax in the US to a future point in time when it becomes taxable in Canada (i.e. upon withdrawal).

Taxpayers with pensions, income plans and government benefits also have opportunities to minimize tax by implementing the following strategies:

Make an advanced RRSP contribution

If you are 71 by the end of this year and have earned income in 2007, consider making an RRSP over contribution in December 2007. Earned income in 2007 creates RRSP contribution room for 2008. However, you will not be permitted to contribute to an RRSP in 2008, since you are required to convert your RRSP to a RRIF before year-end. This strategy does mean that you will be over-contributed for one month and hence subject to a 1% per month penalty tax. However, you will also be entitled to an RRSP deduction in 2008 that will provide tax savings that will far outweigh the penalty tax cost. Speak to your financial advisor about the specifics in your situation.

Convert your RRIF back to an RRSP

If you are age 70 or 71 this year, you can take advantage of the 2007 Federal Budget measure to increase the maturity age of an RRSP from 69 to 71. This means that if you do not need the income from your RRIF, you can waive the requirement to receive income from your RRIF this year and/or next year and convert your plan back to an RRSP. In addition, if you choose to keep your RRIF intact, consider reducing the minimum payment, as there is no longer a minimum payment requirement if you are 70 and 71 this year.

Repay RRIF withdrawals back to RRIF or RRSP

The 2007 Federal Budget announced measures to increase the maturity age of an RRSP from 69 to 71. If you are between 70 or 71 and do not need the RRIF payments you have received from your plan thus far, consider repaying those funds back to your RRIF / RRSP before year-end to avoid paying tax on the RRIF income. Keep in mind that any repayments to the RRIF / RRSP are not tax deductible.

Unlock locked-in funds where possible

Some provinces have begun taking steps to increase financial flexibility in retirement planning by relaxing some rules relating to locked-in plans. Specifically, Alberta introduced rules that will allow you to unlock up to 50% of your locked in plans at the time you convert to a LIF. However, if you owned a LIF prior to November 1st, 2006 governed under Alberta jurisdiction, you must take advantage of this unlocking opportunity by December 31st, 2007. After year-end, you will no longer be able to unlock the funds to a regular RRSP or RRIF. Therefore, ensure you unlock your locked-in funds before year-end.

Apply for government benefits (OAS & CPP)

If you have reached age 60 in 2007, consider applying for your CPP retirement pension benefit. When you apply for CPP before the age of 65, your pension will begin the month after you stop working or when you earn less than the allowable maximum pension payment (\$863.75 in 2007) for two consecutive months.

If you have reached age 65 in 2007, you should also apply for Old Age Security (OAS) benefits as soon as possible. Do not delay your application after turning 65, since retroactive payments are only available for up to 11 months plus the month in which you apply for OAS.

Create eligible pension income

New rules have been introduced this year to allow for spouses & common law partners (CLP) to allocate up to 50% of pension income that qualifies for the existing pension income tax credit to their spouse / CLP, as a means of income splitting. If you are over 65 in 2007 and have no other eligible pension income, consider drawing on your RRIF in order to take advantage of the income splitting opportunity presented with these new rules. Additionally, if your spouse / CLP is over the age of 65 as well, you and your spouse will qualify for the pension income tax credit. Therefore, in addition to the tax savings from income splitting, you will receive tax savings from the pension income tax credit – a double benefit! Speak to your financial advisor about applying this strategy in your specific situation.

Employees receive a number of taxable benefits that can be dealt with tax efficiently by following some of these strategies:

Pay interest on loans

If you have received an employee loan, a taxable benefit may exist if you pay anything less than the prescribed interest rate set by the CRA. To avoid the taxable benefit, ensure any interest owing on the loan is paid by January 30, 2008

Defer your bonus

This is the time of year in which many employees receive bonuses for exceptional work. Consider speaking with the employer about delaying payment of the bonus until after year-end. Delaying your bonus by one month allows you to defer the resulting tax bill to April 2009, a full 16 months to when you have to file your 2008 tax return.

Reduce the stand-by charge & operating benefit

Employer provided vehicles are a great perk, but can have nasty taxable benefits in the form of a standby charge and operating benefit if you're not careful about tax planning. To reduce the possible stand-by charge, reduce the number of days between today and year-end that the car is available to you. Also, consider reimbursing your employer for any operating costs by February 14th, 2008.

Reduce source withholdings

If you expect a refund when you file your tax return, due to RRSP contributions, interest deductions on investment loans, charitable donations, alimony or maintenance payments, your employer has withheld too much income tax during the year. Consider speaking to your employer about reducing source deductions from your pay, or file form T1213 with the CRA so that you reduce your tax bill now, as opposed to waiting until April to get your refund!

Defer tax on stock options

Consider deferring tax on stock options you exercised in 2007. You are eligible to defer up to \$100,000 of stock options per year, however you must notify your employer by January 15, 2008 of your intention so that they may prepare your federal T4 tax slip accordingly.

Families have a number of last minute ideas that can help reduce total taxes on a family basis. Here are a few ideas:

Identify income-splitting opportunities

Families have the ability to creatively split income so that their tax bill can be reduced. Here are some popular ways families can income split to reduce taxes for 2007 and beyond:

- a) Setting up a loan with your spouse / CLP
- b) Create second generation income
- c) Swap assets with family member
- d) Transfer assets to adult or minor children
- e) Contribute to a spousal RRSP
- f) Apply for CPP retirement pension sharing
- g) Consider RESPs for a child's education

Please see Mackenzie's "Income Splitting Brochure" for more information on these and other great income splitting strategies.

Contribute to an RESP

In addition to the income splitting opportunities available with the use of RESPs, there are other important benefits of RESPs that you should take advantage of before year-end. Contributions to an RESP entitle you to a grant, known as the Canada Education Savings Grant (CESG) of up to \$500 per year, or \$1000 if there is unused grant room because of contributions of less than the maximum CESG-eligible contributions from previous years.

Consider contributing at least \$2,500 to an RESP by year-end to receive the maximum CESG for 2007, or possibly more if you have unused grant room from previous years.

If you haven't started an RESP for your growing children it may not be too late to maximize the CESG. In fact, if your child is age 10 or younger, you still have the opportunity to maximize the CESG. Also, if your child is age 15 and you have never started an RESP for that child, consider contributing at least \$2,000 by year-end. Otherwise, your child is not eligible to receive any CESG at age 16 or 17, regardless of whether RESP contributions are made in those years. Speak to your financial advisor about obtaining as much grant as possible for your RESP.

Take advantage of the new tax credits

A variety of new non-refundable tax credits have been introduced recently, including the Child Fitness Tax Credit and the Public Transit Tax Credit. The Child Fitness Tax Credit is available to parents of children under the age of 16 who are registered in an eligible program of physical activity, to a limit of \$500 per child. The Public Transit Tax Credit is a credit for the cost of buying a monthly (or longer duration) pass for commuting on buses, streetcars, subways, commuter trains and local ferries. Unlike other non-refundable tax credits, you will need to provide original copies of receipts to claim either of these tax credits, therefore be sure to obtain all receipts for eligible expenses in 2007.

Pay child care expenses to adult children

Consider paying your adult children (over 18 in the year) for any qualifying child care services they provided to you, for your younger children (16 or younger) throughout 2007. The services must be incurred to allow you, the parent, to earn employment or business income. Qualifying child care expenses are tax deductible in the year they are paid. The income is taxable to the adult child, who is likely taxed at a very low to zero tax rate. A great way to income split with your family.

Accelerate medical expenses

Medical expenses can be claimed for any 12-month period up to the end of the year and only provide tax savings where they exceed the lesser of a) 3% of your net income or b) \$1,926. Therefore, accelerate medical expenses for you, your spouse/CLP and children before year-end in order to maximize tax savings.

Review family trust income

Trusts are established for a variety of purposes, including income splitting. Consider working with your financial advisor or tax professional to determine how much income was earned in the trust and how much income, if any, should be flowed out to the beneficiaries of the trust. Special care should be taken where Henson Trusts are established to ensure distributions from the trust do not affect any government disability benefits for the disabled beneficiary.

Incorporated business owners have great flexibility in their tax planning. The following are some last minute tax saving ideas with the use of corporations:

Defer your income

Consider delaying certain income you expect to receive during the remainder of this year until 2008. This will allow you to defer the tax bill on that income by a full year. Speak to a tax professional about this strategy.

Pay salaries to family

Income splitting among family members is a simple strategy for an incorporated business owner. Consider paying family members (i.e. spouse / children) a reasonable salary or wage for services provided to the corporation in 2007. This is an easy way to shift income into hands of family members who pay tax at lower tax rates. In addition, this provides an opportunity for children to start building RRSP contribution room.

Determine compensation mix

As a shareholder, you may be compensated from your corporation either in the form of salary, eligible or non-eligible dividends. The optimal compensation mix can only be determined after considering the financial and tax position of both yourself and your corporation. Speak with your corporate accountant about determining what optimal compensation mix is most appropriate in your situation.

Purchase a vehicle from your company

Consider purchasing the vehicle that the company has provided you if the car has depreciated in value and you continue to be stung by the taxable stand-by and operating cost benefit annually. This will allow you to avoid the annual taxable benefits and begin receiving a tax-free car allowance from the corporation for business use of your vehicle.

Claim an ABIL

A business investment loss may be available to you if you lent money to, or invested in shares of a small business corporation that has become insolvent or bankrupt. The allowable business investment loss (ABIL) is equal to 50% of the loss and does not only offset capital gains, but can be applied against any other type of income as well. The ABIL rules can be quite tricky, so be sure to speak to a tax professional about your ability to claim an ABIL this year.

Reduce taxable capital

Consider strategies to reduce taxable capital before year-end if your corporation is subject to provincial capital tax in 2007 (federal capital tax has been eliminated). Corporate class mutual funds are a great way to alleviate capital tax, as it qualifies for the investment allowance that helps to reduce capital tax.

Shareholder loans to your company

Consider reclassifying payments made to you throughout the calendar year by your corporation as a repayment of a shareholder loan owing to you. Shareholder loan payments are tax-free and a very tax efficient way of drawing money out of the corporation with excess cash.

Shareholder loans from your company

If you have borrowed money from your corporation in the year before the most recent corporate year-end, you should consider repaying the loan in full before the corporate year-end. Otherwise, you will face an income inclusion on your personal tax return for the value of the loan payment not repaid. Speak to a tax professional about certain exceptions to the rule and whether they may apply in your situation.

Make a gift or award to an employee

As an employer, you are entitled to provide up to two non-cash gifts or awards annually to employees provided the aggregate cost of the gifts, including GST and PST does not exceed \$500. If you are planning to provide gifts or awards to your employees, be sure to not exceed the \$500 threshold, since exceeding the threshold will cause the entire value of the gift (not just the excess over \$500) to be taxable to the employee.

There's only a few weeks left in 2007. Therefore, if you wish to consider any of these strategies for yourself, contact your financial advisor immediately who can assist you in implementing any strategies that benefit you.

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