Separation & Divorce

FOR LAWYERS

TAX MATTERS TOOLKIT

THE CANADIAN BAR ASSOCIATION
L'ASSOCIATION DU BARREAU CANADIEN

Tax Matters Toolkit: Separation and Divorce (for lawyers)

March 2014 (revised May 2022) © Canadian Bar Association
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Produced by the National Family Law Section of the Canadian Bar Association with funding from the Department of Justice Canada.

The information in the Toolkit covers federal tax rules under the *Income Tax Act* and other federal legislation. The information in the Toolkit needs to be considered in context with provincial tax rules as well.

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Separation and the Canada Revenue Agency

A taxpayer's marital status can affect the amount of benefits and credits they receive as well as how they file their annual tax return.

Filing the T1 Annual Income Tax Return

Taxpayers tick the box on their T1 Income Tax Return that applies to their marital status on December 31 of the year for which the taxes are being filed.

- **Separated** means that the taxpayer has been living apart from their spouse or common-law partner because of a breakdown in the relationship for at least 90 days.
- Once they have been separated for 90 days because of a breakdown in the relationship, the effective date of the separated status is the day they started living apart.
- If the taxpayer files the return before the 90-day separation period is over and that period includes December 31, they enter the marital status as married or living common-law, as applicable.
- If, after filing the return, the taxpayer continues to live separate and apart from their spouse or common-law partner and have lived this way for at least 90 days, they must complete Form RC65, Marital Status Change. The date of the start of the 90-day period is the date of separation.
- They must also file an amended return to adjust their entitlement for any credits claimed or to apply for credits that they may not have been entitled to when they were married or living common-law.
- **Divorced** means that the taxpayer is legally divorced from the former spouse.

Did you know...

Taxpayers are still considered to have a spouse or common-law partner if they separated involuntarily and not because of a breakdown in their relationship. An involuntary separation could happen when one spouse or common-law partner is living away for work, school or health reasons, or is incarcerated.

Resources

- Completing the Income Tax Return when separated or divorced

Notifying CRA of a change in marital status

Aside from notifying CRA in the T1 Income Tax Return each year, a taxpayer must notify CRA of new marital status **by the end of the month following the month in which marital status changed**, as it may impact the amount of child tax benefit, GST/HST credits or other benefits. If a taxpayer's status changed in March, for example, they must tell CRA by the end of April.

Taxpayers (or their authorized representative) must notify CRA if:

- The taxpayer marries
- The taxpayer enters a common-law relationship
- The taxpayer separates for more than 90 days due to a breakdown in the relationship
- The taxpayer divorces
- The taxpayer's spouse or common-law partner dies

CRA will recalculate benefits based on the new marital status and adjusted family net income. The adjustment will start the month after the marital status changed.

Taxpayers (or an authorized representative on their behalf) can notify CRA of the marital status change by

- filing Form RC65, Marital Status Change
- signing into MyAccount, MyBenefits CRA web app or MyCRA web app
- phone
- mail

Taxpayers may also wish to file Form T1213 Request to Reduce Tax Deductions at Source or TD1 Personal Tax Credit Return when there has been a change in marital status.

Resources

- Form RC65, Marital Status Change
- Representative Authorization
- Form T1158 Registration of Family Support Payments
- Form T 1213 Request to reduce tax deductions at source
- Form TD1 Personal Tax Credit Returns

Documents supporting Change in Marital Status

Basic tax rule: It is up to the taxpayer to provide CRA with documents supporting a change in marital status

The supporting documents help CRA to determine the date and fact of separation which is relevant to deductions, non-refundable tax credits, tax credits, and benefits including:

- child care expenses
- eligible dependent credit
- Canada Child Tax Benefit
- Working Income Tax Benefit
- GST/HST credits.

CRA considers the date of separation as a question of fact to be determined on a case-by-case basis and will require more information or supporting documentation from a taxpayer when it has contradictory information on file.

A separation agreement or a court order is not always sufficient proof of the date or fact of separation, especially when it does not show separate addresses for the separated parties.

The taxpayer has the responsibility of giving adequate information and documentation to CRA.

The documents should show that there has been a change to the taxpayer's situation. For example, a rental agreement showing names of both the taxpayer and the spouse or common-law partner, and another dated after the separation in the taxpayer's name only is an example. Documents that may assist are:

- A separation agreement/divorce decree with different addresses for the former spouses/common-law partners for the period under review
- Documents with a current address, such as:

  – property tax bills

  – mortgage papers

  – rental or lease agreement

  – insurance policies

  – household bills (gas, electricity, cable television, telephone)

  – medical or dental plan

  – registered retirement savings plan or employment pension plan

  – driver's license or vehicle registration (front and back)

– car insurance

– credit card statements

– any other document or information that shows a change to the taxpayer's marital status

If the taxpayer cannot provide any of these documents, CRA will accept a letter from **two different third parties who have personal knowledge of the taxpayer's situation during the period being reviewed**. The letter must include:

- name and signature of the writer
- profession of the writer
- writer's contact information, including address and telephone number
- dates of the period(s) of separation.

Examples of third parties who can write the letter:

- employer
- landlord
- social worker
- school authority
- band council
- shelter or community support organization
- resettlement worker/sponsor
- insurance company
- clergy
- medical doctor or nurse
- lawyer or Quebec notary.

Note: Lawyers may have only indirect information about the separation of a couple and may not be able to provide all the information required by CRA.

Resources

- Supporting Documents

When are you Living apart?

Same house/separate living quarters
CRA generally does not consider taxpayers separated until separate residences are being maintained by both parties, but sometimes parties remain in the same residence and, when that is the case, CRA will generally not consider a separation to have occurred.

However, there are exceptions: CRA may consider a taxpayer separated and living apart even while living in the same residence if that residence has personal self-contained quarters and if they don't share parenting and financial responsibilities.

Also, even when sharing parenting and financial responsibility, CRA may consider the taxpay separated. These exceptions are granted following a fact based analysis and on a case-by-case basis, as was addressed in *R v Aukstinaitis* 2008 TCC 104.

Facts that could be considered include:

- the individuals have two distinct households within the home with separate entrances and separate kitchens, bathrooms, bedrooms, etc.
- meals are not taken together
- absence of joint social activities or only those done jointly involve coparenting;
- not presenting themselves in public as a couple
- absence of sexual relations
- each individual runs a separate household and makes independent financial decisions
- why the parties are in the same residence (i.e., nowhere else to go, coparenting reasons).

Couch surfing/no new fixed address
When, after a relationship breakdown, one of the parties does not move into a permanent new home and instead stays with friends or family or moves around, it becomes more difficult to obtain the supporting documents outlined by CRA to determine the change in marital status. This is where the Letters from Third Parties may be of assistance, especially if there is a social worker, shelter, community support organization, or resettlement worker/sponsor involved.

Deduction for Legal Fees

Basic tax rule: Legal fees relating to establishing the amount of support, increasing support, or defending against a reduction in support are tax deductible for the support recipient in the year they are incurred. Legal fees paid by the support payor are not tax deductible.

CRA finds that, for the payer, legal fees are a personal or living expense. They have not been incurred to produce income from a business or property and do not meet the necessary test for a deduction in the *Income Tax Act*. Paragraphs 18(1)(b) and (h) of the Act state that amounts are not deductible to the extent that they are "on account of capital" or are "personal living expenses".

Legal basis for deduction of legal fees

Although the *Income Tax Act* does not specifically mention the deductibility of legal fees, the Federal Court of Appeal has held that the "right to support, once established by a court, is 'property' within the meaning of subsection 248(1) of the [*Income Tax*] *Act*, and that income from such support constitutes, in the hands of the person receiving it, income from property" (*Nadeau v M.N.R.,* 2003 FCC 400, at para 14). Support payments are a pre-existing right of a spouse or child. The right to support exists as a function of common and civil law. Legal fees incurred do not establish the *right* to support. Rather, legal fees are incurred to establish or enforce the *amount* of support a recipient is entitled to.

So, legal fees incurred to obtain or increase support are considered incurred to produce income from property and may be deducted from income. This is the case even when the support amount is exempt from taxation, as is child support in most situations.

Specifically, paragraph 18(1)(a) of the *Income Tax Act* allows a taxpayer to deduct from business or property income expenses incurred for the purpose of "gaining or producing" business or property income. This also means only the support recipient is entitled to deduct a portion of their legal fees against their own income. A person paying legal fees on behalf of a support recipient is **not** entitled to deduct legal fees paid on behalf of someone else against their own income.

Because paragraph 18(1)(a) requires that the expenses be incurred to "gain or produce" income, or to enforce a pre-existing right to income, the support payor has no legal basis to deduct legal fees. Only a party receiving income (in this case, support payments) may claim deductions for expenses incurred to establish or enforce their right to income. Because the deductibility is based on receiving income, independent of gender or other enumerated grounds, it does not offend s. 15(1) of the *Charter*.

CRA approach

CRA interprets paragraph 18(1)(a) to mean that legal fees are NOT deductible when they are incurred to **establish a right** to:

- obtain a separation or divorce
- establish child custody or visitation.

Legal fees incurred to **exercise a pre-existing right** ARE deductible. This includes legal fees incurred by the support recipient to:

- collect late spousal or child support payments
- establish the amount of spousal or child support payments from a current or former spouse/partner or the legal parent of his/her child
- increase the amount of spousal or child support
- defend against the reduction of spousal or child support.

These legal fees may be claimed on Line 22100.

When there is a written agreement or court order for child support made before May 1997, a recipient may deduct, on Line 23200 of his/her return, legal fees incurred to try to make child support payments non-taxable.

Resources

- Support Payments, Income Tax Folio S1-F3-C3 at 3.78 to 3.84 effective May 16, 2019
- *Grenon v Canada*, 2016 FCA 4 (leave to Supreme Court denied in 2016 CanLII 41074
- *Nadeau v M.N.R.*, 2003 FCC 400

Notes:

- The deduction for legal fees relating to child support are permitted even though tax rules do not require child support payments to be included in the recipient's income.
- Legal fees to obtain a lump-sum payment may only be claimed as a deduction when the lump-sum payment covers arrears for periodic payments of support.
- Court-awarded costs must be subtracted from a recipient's deduction claim for legal fees paid to a lawyer.

Recipient clients need a billing statement from their lawyer which separates out the fees for legal services which are eligible for the deduction from the fees for other legal services which are not. Lawyers may also provide a letter outlining the total legal fees paid in

the year with an estimate of what portion/percentage of legal fees related to deductible categories.

Deductibility of legal fees is not tied to the recipient's success in a claim for child or spousal support. For example, where a recipient unsuccessfully defends against a reduction in support and the support is reduced, the recipient is still entitled to deduct his or her legal fees.

Payors may be upset when they learn that their legal fees are not deductible on their T1 Return when the recipients' are. This may affect negotiations.

In shared parenting arrangements using s. 9 set-off child support calculations, the Agreement or Order may be worded so that both parents have a child support obligation to the other. The Eligible Dependent Tax Credit can then be shared between parents. A "payor" is ineligible to claim the credit; however, this ineligibility does not apply if both parents have an established obligation to pay support to the other. The corollary of this is: if both parents are "payors", both parents must also be "recipients". As such, both parties **may** be entitled to claim a deduction for legal fees. However, as of the date this Toolkit was prepared, there are no reported decisions on deducting legal fees when both parties are payors and recipients.

"Principal Residence" Rules

Basic tax rule: A property that was a principal residence for every year that it was owned may be sold at a profit without any capital gain needing to be report on a T1 Return.

"Principal residence" criteria

A property must be owned by one or both of the spouses/common-law partners to be considered their principal residence for tax purposes.

The following types of property could qualify as a principal residence:

- a housing unit, which CRA has accepted could include:

  – a house;

  – an apartment or unit in a duplex, apartment building or condominium;

  – a cottage;

  – a mobile home;

  – a trailer; or

  – a houseboat;

- a leasehold interest in a housing unit; or

- a share of the capital stock of a co-operative housing corporation, if such share is acquired for the sole purpose of obtaining the right to inhabit a housing unit owned by that corporation.

According to the *Income Tax Act*, a couple may have only one principal residence in a given year. So long as the taxpayer or by his or her spouse or common-law partner, former spouse or common-law partner, or child have "ordinarily inhabited" the property at some point during the year and it is not owned to gain or produce income, it can be designated as the principal residence by including the appropriate forms on the taxpayers Income Tax Return.

For example, Robin and Claire own a home in the city and a cottage. They usually spend a month at the cottage every summer and go there on weekends throughout the year. They do not rent out either property. For any tax year, they can designate either their city home or their country cottage as their principal residence as they are considered to "ordinarily inhabit" both properties.

Robin and Claire decide to sell their cottage property. It has increased in value by $200,000. On the other hand, their city home's value has remained constant since they bought it and they believe this is unlikely to change because of the neighborhood. It would probably be beneficial for Robin and Claire to designate their cottage property as their principal residence. No capital gains tax would be owing on the profit made when they sell it.

Issues at time of separation or divorce

Tax issues relating to the designation of a principal residence most often arise for separating or divorcing spouses/common law partners when:

- they own more than one property;
- the time between the breakdown of the relationship and a court order or the signing of a written separation agreement is lengthy and property values have risen significantly;
- one party remained in the principal residence and the other party bought a new home after marriage breakdown but before a court order or written separation agreement was in place.

Until there is a written separation agreement or a court order, CRA requires the spouses/common-law partners to designate the same property as their principal residence for the year.

When the spouses/common-law partners have been living separate and apart throughout the year and there is a written separation agreement or court order, each party may claim a different principal residence. After separation, CRA recognizes two households instead

of one, and therefore it is possible for each ex-spouse to own one tax- exempt principal residence.

It's important to note that, with the exception of the matrimonial home, property brought into the marriage by one of the spouses will be considered owned by that individual and assigned to that person during the negotiation of the separation agreement. Rules can differ by province.

Since no capital gains tax results from the sale or deemed disposition of a principal residence, the decision as to which property to designate as a principal residence can have significant tax consequences. The tax impact may be a factor in determining a fair distribution of the assets of the marriage or common-law relationship.

Note: A principal residence is considered a "personal-use property" and there can be no capital loss claimed should it sell for less than its original purchase price.

Resources

- Form T2091, Designation of a Property as a Principal Residence by an Individual (other than a Personal Trust)
- Form T2091(IND)-WS, Principal Residence Worksheet
- Section 54, *Income Tax Act*, defines "principal residence"
- Disposing of your principal residence
- Income Tax Folio, S1-F3-C2, Principal Residence

Spousal Support

Basic tax rule: The person who makes spousal support payments may deduct the amounts paid from income, generally reducing taxes owing. The person who receives spousal support payments must include the amounts as income and may have to pay taxes on that income. This must be done even if the person making the payments does not take advantage of the deduction.

Note that when there is a child (children) and a written agreement or court order provides a global amount for support – without specifying the part of the amount that is for spousal support – the full amount is considered child support. Generally, child support payments made under a written agreement or court order after April 1997 are not deductible from income by the payer and do not have to be included in income by the recipient.

Characteristics of spousal support

To qualify as "spousal support" payments, the payer and the recipient must be living separate and apart due to relationship breakdown at the time the payment was made.

Spousal support payments have four other characteristics:

- the terms and schedule of payments are set out in a written agreement or court order;
- payments are made on a periodic basis (e.g. weekly, monthly, quarterly);
- payments are for the maintenance of the recipient; and
- payments are made to the recipient or an agent enforcing collection of the amount.

Even if these characteristics are not met, the following three types of payments may (in limited circumstances) be considered support payments taxable in the hands of the recipient and deductible in the hands of the payer:

1. Payments made before the date of the court order or written agreement;
2. "Specific purpose" or third-party payments; and
3. Lump-sum payments for retroactive support.

Payments before a court order and "specific purpose"/third party payments are considered below. Lump sum payments are considered later in this Toolkit.

Resources

- P102, Support Payments Guide, Support Payments

Spousal support paid before there is a written agreement or court order in place

Spousal support payments made *before* a written agreement or court order may be deducted by the payer and will be taxable for the recipient when:

- The written agreement or court order states that any amount previously paid is considered to have been paid under the written agreement or court order;
- The support payments have all the required characteristics of support payments; and
- The support payments were made the same or prior year as the order or agreement.

The payer may ask CRA to re-assess the previous year's tax return in light of the written agreement or court order.

"Specific Purpose" and Third-Party Payments

Payments made to a third-party for the benefit of the spouse or child (children), or for a specific purpose that **benefits** the spouse and children, may also qualify as support payments.

The payment may be, for example, to a landlord for rent, to a maintenance company for property upkeep, or to cover insurance. The third-party payment must be set out in the written agreement or court order, and must be to support the recipient's expenses for a specific purpose. Where the amounts are payable directly to the recipient to cover specific expenses, they are "specific purpose" expenses. Where the amounts are payable to a third party to cover such expenses, then they are third-party payments.

These payments are considered a support payment when the recipient has discretion about how the payments may be spent. For instance, a reimbursement for an expense a recipient has already paid may be used as the recipient sees fit. If the recipient has the discretion to change maintenance or insurance companies, or move to a new rental property, these may be classified as support payments. The recipient may choose a less expensive option and retain the rest. When the recipient does not have discretion about how the payments may be spent, they may not be considered a support payment **unless** the written agreement or court order specifically states that the recipient will include the third-party payments in income and the payer may deduct them.

How to notify CRA of spousal support payments

Taxpayers should register the amount of support payments with CRA as soon as they have signed a written agreement or have received a court order setting out spousal support payments. Agreements or orders setting out **both** child support and spousal support payments must be registered. Agreements or orders setting out **only** child support **but not** spousal support do not need to be registered. However, where an agreement or order is registered, subsequent agreements or orders varying either child support or spousal support must also be registered.

Form T1158E, Registration of Family Support Payments asks for the Social Insurance Numbers of both the payer and the recipient and details on the starting date for support, the amount of support for a child, the amount of support for a spouse, any adjustments to be made to the support amount (e.g. changes to reflect the cost of living), and any end date for child and spousal support payments.

Along with Form T1158E, taxpayers must send CRA a copy of their written agreement or court order.

Submitting Form T1158E and a copy of the written agreement or court order should be done as soon as possible. It is a separate process and not part of a T1Return. There is no need to wait until CRA requests a copy. Waiting may delay the receipt of a tax refund.

CRA does not require the payer to give proof of payment when filing a T1 Return but may ask for proof of payment at a later date.

Proof of payment of spousal support may be shown by:

- canceled cheques, or cheque images, showing both the front and back of the cheques;
- bank statements if they show a transfer of funds from the payer's account to the recipient's account or to a provincial maintenance enforcement program;
- employer statements if they show a transfer of funds from the employee's pay cheque to the recipient's account or to a provincial maintenance enforcement program;
- a statement from a provincial maintenance enforcement program showing the amount paid to it; or
- a signed receipt from the support recipient stating the total amount of support paid during the tax year.

The funds transferred or in a statement or receipt should match the support amounts in the written agreement or court order.

Resources

- Form T1158, Registration of Family Support Payments
- P102, Support Payments: Registering your court order or written agreement

Spousal support payers – Deductions for spousal support payments

On line 22000 of the T1 Return, payers may claim a deduction equal to the amount of spousal support they paid according to a written agreement or court order. However, if the written agreement or court order requires the payer to pay both spousal and child support, CRA will only allow deductions for spousal support when the child support payments for the year and any arrears from previous years have been paid in full. Overdue child support amounts are carried forward to the next year and may not be deducted by the payer. CRA treats child support payments as the priority. However, the priority of child support does not apply when the child support and spousal support are

1. payable under different court orders or written agreements; **and**

2. the recipients are different individuals.

In order to claim deductible support payments, the payer enters the **total amount** of support payments made under all orders and agreements, including non-deductible child support payments at line 21999. The payer then enters the deductible part of this amount on line 22000.

Note that the amounts to be claimed on the payer's T1 Return cannot be greater than the amounts set out in the written agreement or court order. The payer cannot claim other money that might have been provided to a spouse or child in excess of support for any reason, such as to assist with a home repair or for a gift for a child. The payer cannot claim any amounts carried over from previous years as unpaid child support.

If the recipient has been ordered to repay support amounts, the payer must report the reimbursed amounts on lines 12799 and 12800 in the year it was received and included as income if

- the payer deduced the reimbursed amount on that year's tax return; **or**
- the payer deducted the reimbursed amounts on previous tax years.

When a payer is a resident of Canada making payments to a non-resident of Canada, they don't need to withhold taxes that the recipient would need to pay if they were a Canadian resident. However, so long as the payment meet the characteristics of spousal support, the payer may still deduct payments.

Payments made after a recipient's death (i.e., to their estate or to the children) do not meet the conditions of a support payment, and are not deductible to the payer. Similarly, payments made by an estate after the payer's death are not deductible to the estate.

Resources

- Income Tax Folio S1-F3-C3, Support Payments
- P102, Support Payments: Tax Rules
- About Your Tax Return: Support Payments
- About Your Tax Return: Support Payments: Amount you can claim or report
- About Your Tax Return: Support Payments: Lines 21999 and 22000 – Support Payments Made
- About Your Tax Return: Support Payments: Payments to or from a non-resident

Spousal support recipients – Reporting spousal support payments

Spousal support amounts received must be included in the recipient's income. Recipients must report taxable support income in the year it is received. A recipient cannot, for example, delay cashing a support cheque in order to delay reporting support as income.

Support payments are taxable to the recipient if:

1. The order or agreement clearly states the amount to be paid for the current or former spouse or common-law partner; **and**
2. All payments for child support are fully paid for the current and previous years.

An order or agreement must specifically designate payment amounts as spousal support to the recipient. Without this designation, support payments will be considered non-taxable child support, and do not need to be reported in the recipient's income.

Child support is given priority. That is, all amounts paid to a recipient in a year will be applied first to child support for that year, then to child support outstanding in previous years. Only amounts paid over and above child support obligations are considered taxable support to a recipient. Priority of child support does not apply, however, where child support and spousal support are payable under different court orders or written agreements **and** the recipients are different people.

The recipient must enter the **total** amount of support payments received under a court order or written agreement at line 12799. Note that the total amount **does not** include amounts in excess of support payments received, such as amounts for gifts or allowances. The recipient then enters the taxable portion of total support at line 12800. The taxable portion of support is calculated as total support paid, less amounts for child support paid in that year, less amounts for child support carried forward from previous years.

The recipient must still report total and taxable support amounts even if they have assigned or transferred support payments to a provincial government to receive social assistance. In that case, however, support amounts are not included in the recipient's Form T5007 Statement of Benefits.

If the recipient has been ordered to repay support amounts, he or she may claim a deduction for previously reported support amounts if the repayment amounts were reported as income on that year's, or a previous year's income tax return, **and** the recipient has not already claimed a deduction for the repayment.

If the recipient's payments are made by a payer in another country, the recipient must still include the payments per lines 12799 and 12800 if the characteristics of spousal support are met. However, if there is a tax agreement or treaty between Canada and the payer's

resident country, the recipient may claim a foreign tax credit. A foreign tax credit may be claimed where:

1. The payer's country has already withheld tax from support payments; **and**
2. The recipient must also pay taxes on the support payments.

Payments received from the payer's estate after death are not taxable. They do not meet the conditions of a support payment.

Resources

- Income Tax Folio S1-F3-C3, Support Payments
- P102, Support Payments: Tax Rules
- About Your Tax Return: Support Payments
- About Your Tax Return: Support Payments: Amount you can claim or report
- About Your Tax Return: Support Payments: Line 12799 Total and 12800 Taxable Amount
- About Your Tax Return: Support Payments: Payments to or from a non-resident

Spousal support payers – reducing taxes withheld at source

A spousal support payer with regular employment income has two options:

- Have taxes withheld at source as usual from his/her salary and enjoy an income tax refund after filing the T1 Return, or
- Ask CRA to permit his/her employer to decrease the taxes withheld at source to reflect the deduction for spousal support payment that will be claimed when filing the T1 Return. Before this request is considered, the payer must not have outstanding amounts owing to CRA and must be up-to-date in filing returns.

Resources

- About Your Tax Return, Support Payments: Deductions from your pay
- T1213, Request to Reduce Tax Deductions at Source for Year(s)

Spousal support recipients – increasing taxes withheld at source

On line 12800 of their T1 Return, recipients must include the taxable amount of spousal support they received according to a written agreement or court order.

Note that the amounts to be reported on the recipient's T1 Return are those set out in the

written agreement or court order. Other money that might have been provided by the payer for any reason, such as to assist with a home repair or for a gift for a child, should not be included.

A spousal support recipient with regular employment income has two options:

- Have taxes withheld at source as usual from his/her salary and pay an additional amount of tax when filing the T1 Return, or
- Ask his/her employer to withhold additional taxes at source from his/her salary to spread the tax impact of the spousal support payments throughout the year. The spousal support recipient must submit Form TD1 to his/her employer.

Resources

- TD1, Personal Tax Credits Return

Deductions for the payer – year of relationship breakdown

In the year of relationship breakdown, a payer who is making spousal support payments according to a written agreement or court order may have the option of choosing between the following options, whichever is more beneficial to the taxpayer.

- the payer may claim a deduction for the spousal support paid during the year at line 22000 of his/her T1 Return, or
- the payer may claim a non-refundable tax credit for the spouse or common-law partner amount at line 30300 of his/her T1 Return. The spouse or common-law partner amount may only be claimed when the support recipient's net income for the year is less than the indexed amount set for the year. Line 30300 of the *General Income Tax and Benefit Guide* provides the indexed amount for the tax year. Additionally, all other requirements to claim personal tax credits for an eligible dependent or eligible caregiver amount must also be met.

With either option, the payer should report the amount of spousal support paid at line 21999 (total support paid), and then the deductible portion of support at line 22000. If the payer is choosing to claim personal tax credits rather than support deductions, the payer must enter $0.00 on Line 22000. The support recipient must report the spousal support payments received as income at line 128000 of his/her Annual Income Tax and Benefit Return.

Resources

- P102, Support Payments, Filling out your tax return
- Income Tax Folio S1-F3-C3, Support Payments
- Support Payments Q & A
- Line 30300, Spouse or common-law partner amount
- Line 30400, Amounts for eligible dependents
- Line 30425, Canada caregiver amount for spouse or common-law partner, or eligible dependent age 18 or older
- Line 30450, Canada caregiver amount for other infirm dependents age 18 or older
- Line 30500, Canada caregiver amount for infirm children under 18 years of age

Spousal support payments may only be deducted from a payer's income when they meet all the characteristics of a support payment, including that the payments are set out in a written agreement or court order. It is beneficial when the agreement or order also specifies the amount of the spousal support payment as distinct from any child support payment, and states that the spousal support payments will be treated as deductible for the payer and as income for the recipient. Without this distinction, spousal support amounts may be characterized as non-taxable child support.

Filing Form T1158, Registration of Family Support Payments, is an important step which ensures that CRA has the information it needs to process the tax returns of former spouses or common-law partners expeditiously after a relationship breakdown.

A payer may deduct spousal support payments beginning with the year in which the written agreement or court order was made and including the preceding year, provided that the written agreement or court order states that any amount paid before the agreement was signed or the court order made is considered paid under the agreement or order. For tax purposes, it may be important for a person who began paying spousal support at the time of relationship breakup to have a written agreement or court order in place within two years.

Arrears and Lump-sum Payments

Basic tax rule: A qualifying retroactive lump-sum payment (QRLSP) is tax deductible for the payer in the year it is paid. Other lump-sum payments are not tax deductible.

Tax impact of a lump-sum payment on the payer

A lump-sum payment from one former spouse/common-law partner to the other is not

usually tax deductible for the payer.

However, a lump-sum payment made by one former spouse/common-law partner to the other to make up for missed periodic spousal/common-law partner support payments or taxable child support payments (arrears), is tax deductible by the payer, when the support payments are set out in a written agreement or court order. The payer can claim the payment on line 220 of his/her T1 Return in the year it is paid.

Qualifying Retroactive Lump-sum Payments (QRLSP)

A lump-sum payment must have these elements to be a Qualifying Retroactive Lump-sum Payment (QRLSP):

- it is for at least $3000, not including interest
- it is paid by a former spouse/common-law partner to the other former spouse/common-law partner
- it is a payment to cover missed periodic payments (arrears) for spousal/common-law support or taxable child support
- the support payments are set out in a written agreement or court order which was in place at the time the support payments were missed
- it applies to missed support payments for one or more previous years.

When a QRLSP has been made, the payer should complete Form T1198 and give the completed and signed form to the recipient of the QRLSP.

- Form T1198, Statement of Qualifying Retroactive Lump-Sum Payment

Tax impact of a QRLSP on the recipient

When the recipient receives a QRLSP, the recipient has to report the whole payment at line 128 of his/her T1 Return in the year it is received.

At the request of the recipient, CRA will review the impact of taxing the QRLSP as if the payments had been received in the year(s) in which they were supposed to have been paid. When that is to the advantage of the recipient, CRA will recalculate taxes owing for those years. The recipient must have been resident in Canada at the time.

The recipient should have received the completed and signed Form T1198 from the payer and should include it when filing the Annual Income and Benefits Tax Return. Without the completed and signed form, CRA will ask the recipient for the breakdown of the payments – what was owing when – and for other related information.

The tax treatment of lump sum payments will depend on the reason for the payment. It is beneficial to the payer to be able to deduct the payment from income. It is advantageous

to the recipient to receive a lump-sum payment without having to include it in income. Careful attention to the tax rules and case law concerning lump sum payments is required.

Child Support

Basic tax rule: Generally, child support payments made under a written agreement or court order made after April 1997 are neither taxable as income for the recipient nor deductible from income for the payer.

Tax treatment: written agreements and court orders from before May 1997

Note: Child support payments made under a written agreement or court order made before May 1997 are usually taxable to the recipient and deductible by the payer, unless one of the these situations applies:

- The order or agreement is modified after April 1997 to change child support amounts, in whole or in part. In this case, the tax rules regarding child support in place after April 1997 apply to only the revised amount. However, automatic changes to support included stated in the order or agreement (i.e., adjustments for cost-of-living or income changes) are exempt and remain fully taxable;
- The order or agreement made prior to May 1, 1997, specifies that child support will not be taxable and deductible after a particular date; or
- The payer and recipient agree that tax rules in place after April 1997 will apply and complete Form T1157, Election for Child Support Payments.

The recipient of child support should report the taxable amount of child support payments received as part of total support on line 12799 of their T1 Return, and shall include the taxable portion of child support on line 12800.

Resources

- Form T1157, Election for Child Support Payments
- P102, Support Payments: Tax Rules
- Form T1157, Election for Child Support Payments

Federal Child Support Guidelines

The Federal Child Support Guidelines provide a way to calculate the child support that a judge would likely order should parties be unable to agree and go to court to have a judge decide. Parents can use the Guidelines to calculate how the law expects each of them to support their child financially after a relationship breakdown.

The Department of Justice Canada has extensive materials to explain the Guidelines and to help parents to calculate child support amounts.

Resources

- Step-by-Step, Federal Child Support Guidelines,
- Child Support Table Look-Up, Department of Justice Canada

Child Benefits

Basic tax rule: After the breakdown of a marriage or common-law relationship, the net income of each former spouse/partner is used to determine each of their entitlement to receive the Canada Child Tax Benefit and the GST/HST credit.

Canada Child Tax Benefit

When one parent is primarily responsible for a child (children), that parent's net income is used to determine entitlement to receive the Canada Child Tax Benefit. When entitled, that parent will receive 100% of the benefit. A parent receiving child support remains eligible for the benefit. Child support is not part of the parent's net income for the purposes of calculating entitlement to for the Canada Child Tax Benefit.

When both parents are primarily responsible for a child (children), each parent's net income will be used to determine entitlement. If entitled, each parent would receive half (50%) of the amount they would have received if the child resided with them full time. This is the rule even though one parent may not be entitled to the benefit (net income too high) and the other parent would be entitled to the maximum benefit (because of a low net income).

Taxpayers must notify CRA of the end of a marriage or common-law partnership 90 days after separating without any reconciliation having occurred.

- Form RC65, Marital Status Change
- Form RC66 Canada Child Benefits Application
- Canada Child Tax Benefit calculator
- Information Booklet T4114
- Information on GST/HST credit

For low and middle-income parents, the Canada Child Tax Benefit and the GST/HST credit provide additional income that may be a factor to consider when deciding on support payments and the financial impact of separation and divorce on the parents and child (children).

Child Disability Benefit

The Child Disability Benefit (CDB) is a tax-free benefit for families who care for a child under age 18 with a severe and prolonged impairment in physical or mental functions.

After separation or divorce, the parent with primary responsibility for the child will receive the benefit. When both parents share responsibility, the Child Disability Benefit may be split 50/50.

Resources

- Child Disability Benefit
- Child Disability Benefit Guideline Tables

Deductions and Credits for Children

Basic tax rule: After relationship breakdown, the parent with sole custody of a child (children) may claim the child-related deductions from income. When parents share custody of a child (children), i.e. a shared parenting situation, in some situations each parent may claim related child expenses and in some cases they can select who may claim a tax credit by consensus.

Eligible dependent credit

After a relationship breakdown, a parent may be able to claim the eligible dependent credit for a child.

For the parent to make the claim, all these conditions must have been met at some time during the year:

- the child is under 18 years of age, or is older and has a medical or physical disability
- the child lives with the parent for most of the year (may be away at school, camp, etc.)
- the parent is not making support payments for the child
- no one else is claiming the credit for the child or for anyone else in the household (there is only one eligible dependent credit allowed per household and only one eligible dependent credit allowed for a specific child).

In **shared custody** situations, sometimes both parents are required to pay child support and, therefore, following the eligible dependent credit rules set out above, neither parent would be able to claim the credit. However, in 2007, the *Income Tax Act* was changed to allow a parent in a shared custody situation to claim the eligible dependent credit, even

though the parent was contributing to child support. For this to be allowed, the obligation of each parent to pay support must be clearly stated in a written agreement or court order. Wording that support was calculated using the Federal Child Support Guidelines is not sufficient. The written agreement or court order must state that the recipient has an obligation to pay support (including how much) and that the payer has an obligation to pay support (including how much), even if in practice the parties are choosing to have only one person make a payment.

When the situation allows either parent to claim the eligible dependent credit, it is up to the parents to decide which one of them will make the claim. Without a decision (for example, if both parents claim the credit in their T1 Returns), then neither parent will receive the credit.

When parents have shared custody of two or more children, one parent may claim the eligible dependent credit for one child and the other parent may claim the eligible dependent credit for another child, provided that they qualify for the credit. A taxpayer is only allowed one eligible dependent credit per year, no matter how many children live with the taxpayer, and can only claim a child as their eligible dependent if they do not have a new spouse living with them.

Resources

- Section 118(5.1), *Income Tax Act*
- Shared custody and the amount for an eligible dependant
- Line 305

The wording of a written agreement or court order regarding spousal and child support will have an impact on the ability to claim the eligible dependent credit for a parent with sole custody and for parents with shared custody.

Child Care Expense Deduction

The child care expense deduction generally allows a parent to receive some tax relief for child care expenses incurred so that the parent could work, carry on a business or undertake certain educational activities.

During a marriage or common-law relationship, the spouse/partner with the lower net income may, with some exceptions, be the person who claims allowable child care expenses no matter which of the spouses/partners actually paid them.

After the breakdown of the relationship, when the spouses/partners have been living separate and apart for the full year, both former spouses/partners may claim child care expenses that each paid in respect of a child (children). The allowable amount of the

deduction will depend on the nature of the expenses, when they were incurred, and when the child (children) was living with the parent claiming the expense.

For the year of relationship breakdown, when the former spouses/partners were living separate and apart at year end and had either been separated for 90 days before the year end or had a divorce order before year end, the higher income earner may claim the child care expenses incurred in the year of the relationship breakdown.

There are limits on the total amount of child care expenses that are allowed, based on the age of the child, any mental or physical infirmity, and eligibility for the disability tax credit. As well, child care expenses may not be more than two-thirds of earned income for the year.

Receipts for the expenses paid are necessary. They do not have to be submitted to CRA at the time of filing but they must be provided when requested.

Resources

- Form T778, Child Care Expenses Deduction
- S1-F3-C1: Child Care Expense Deduction

Claiming the child care expense deduction will have some impact on taxes owing in a taxation year. Attention to the rules that apply during the year of relationship breakdown can maximize tax benefits.

Tuition, Education, and Textbook Credit

Students at a university, college, or other eligible post-secondary institution may claim a tax credit for tuition fees, education amount, and textbooks. When a student does not have sufficient income in the taxation year to fully use the credit, he or she can carry it forward to another year or transfer the unused portion to a parent (among others). The student must designate on the applicable form the parent to whom he/she wishes to transfer the credit. The student may designate only one parent. Or the student may accumulate unused credits for future years.

The parent claiming the credit must submit Form T2202A, Tuition, Education, and Textbook Amounts Certificate, to CRA, when asked to do so.

Resources

- Form T2202 Tuition and Enrollment Certificate

Claiming the credit can be financially beneficial to a parent. To avoid family disagreements and unnecessary pressures on the student, talking about who will claim the credit during separation or divorce discussions may be worthwhile.

Pensions

Basic tax rule: At the end of a marriage or common-law partnership a pension beneficiary may transfer (roll over) all or part of current or future pension benefits to the other spouse/partner as part of a settlement without this being taxed as a withdrawal of all the pension benefits.

Canada Pension Plan

Basic tax rule: After a relationship breakdown, a former spouse/partner has a right to split the other former spouse/partner's Canada Pension Plan credits provided cohabitation requirements and application deadlines are met. The split has an impact on the Record of Earnings for each former spouse/partner and therefore on the amount of CPP pension benefits that may be received on retirement.

CPP: credit splitting

A spouse/partner has a right to ask for a split of the other spouse/partner's CPP credits after a relationship breaks down. This right cannot be negotiated away except in British Columbia, Alberta, Saskatchewan, and Québec. In those four provinces, separating or divorcing spouses/partners can agree NOT to split CPP credits in a separation agreement or the right to the CPP credit split can be removed by a court order.

There are minimum cohabitation requirements for CPP credit splitting to take place. There are also time limits of one to four years for requesting a CPP credit split depending on the start of the marriage or common-law relationship. The time limit may be waived with the agreement of both former spouses/partners.

This web link shares information about the minimum cohabitation period and the time limit for applying for a CPP credit split:

It is up to the spouse/partner to make the CPP credit split request and to provide all the necessary information to Employment and Social Development Canada. This includes:

- social insurance numbers for both spouses/partners;
- proof of the date they began living together;
- proof of the date they no longer lived together;
- a written agreement or court order.

CPP credit splitting permanently changes the Record of Earnings for each spouse/partner on which CPP pension payments will be based. It is advantageous to the lower income spouse/partner or the spouse/partner who was out of the work force for a period of time (for example, went back to school, lost a job and didn't work for a while, stayed home to be with a child) to apply for a CPP credit split. The split will balance the period of non-

contributions by one spouse/partner during the time the spouses/partners were living together.

After relationship breakdown, each spouse/partner will continue to gain CPP credits, which will be reflected in their individual Record of Earnings, according to their own on-going CPP contributions.

Resources

- Service Canada, information on credit splitting, 1-800-277-9914 (English) and 1-800-277-9915 (French)

A CPP credit split is advantageous to the lower income spouse/partner or the spouse/partner who was out of the work force for a time. The credit split will not be done automatically by CPP – a timely application with complete documentation must be submitted. Service Canada offices can be of assistance.

In provinces where a waiver of the credit splitting is permitted (BC, AB, SK, QC) and the spouses/partners have agreed not to split CPP credits, the waiver of the credit-splitting right must be explicitly stated in the separation agreement or divorce decree.

CPP: end of pension sharing

Spouses/partners over 60 may be sharing a CPP pension to spread income between them and save on taxes. CPP pension benefit sharing cannot continue after a permanent breakdown of the relationship. However, a former spouse/partner may apply for CPP credit splitting as noted above.

In situations where pension sharing is in place, a copy of the separation agreement or court order should be provided to Employment and Social Development Canada as soon as possible to avoid having to return payments made to the wrong person. An application for credit splitting may be appropriate.

Payment of taxes at source when pension plan benefits paid

Ideally, when payments are made from a pension plan that has been divided between former spouses/common-law partners, the plan administrator would withhold taxes as applicable for each beneficiary before payments are made. However, this does not always happen and could result in after-tax division amounts that do not reflect the parties’ expectations.

Information from the plan administrator can identify the plan’s tax withholding approach.

Negotiations prior to signing a written agreement or making arguments in court could address issues such as:

- the plan beneficiary makes payments to a former spouse/common-law partner from pension income received before there is a written agreement or court order in place;
- the plan beneficiary will pay all the taxes on the payments from the plan and the income to the former spouse/common-law partner will not be taxable;
- a written agreement or court order is in place but it takes months for the pension plan administrator to make the adjustments;
- the plan beneficiary will pay all the taxes on the payments from the plan and the income to the former spouse/common-law partner will not be taxable;
- the plan beneficiary receives the full pension amount with taxes withheld and then distributes a portion to the former spouse/common-law partner according to a written agreement or court order;
- the plan beneficiary could not reduce taxes owing by the amount paid to the former spouse/common-law partner and the income to the former spouse/common-law partner will not be taxable.

Resources

- Superannuation and pension benefits that are included in income under subparagraph 56(1)(a)(i)

The division of pension assets may contribute to financial inequities for the plan holder depending on the plan administrator's tax withholding approach and how the division is set out in a written agreement or court order.

Registered Retirement Savings Plans (RRSPs) and Registered Retirement Income Funds (RRIFs)

Basic tax rule: Provided the requirements are met, all or part of the funds in one former spouse/partner's RRSP or RRIF may be transferred to the other former spouse /partner's RRSP or RRIF without any tax consequences.

Transfer of RRSP or RRIF funds to a former spouse or common-law partner

Generally, taxes are withheld on any amounts withdrawn from an RRSP or a RRIF as the amount is income to the recipient. However, separating spouses may transfer holdings in an RRSP or RRIF without having taxes withheld. Taxes will become payable when the receiving spouse/partner withdraws funds from the RRSP or RRIF. In other words, the funds

can be rolled over from the transferring spouse/partner to the receiving spouse/partner without tax consequences.

The rollover is allowed when:

- the parties are living separate and apart
- the transfer is made according to the terms of a separation agreement or court order which specifies that dividing the property in this way is in settlement of rights arising out of the breakdown of a marriage or common-law relationship
- the transfer is made directly by the trustee of one former spouse/partner's plan to the trustee of the other former spouse/partner's plan
- the person receiving the transfer of funds from an RRSP is 71-years-old or less at the end of the year in which the transfer is made
- the parties sign Form T2220 and file it with CRA along with a copy of the separation agreement or court order, within 30 days of the transfer.

Note: The person receiving the rollover of funds from an RRSP or RRIF should not claim a deduction for the amount transferred or report the amount as income in his/her T1 Return. Generally, the transfer will not affect RRSP contribution limits.

Part or all of an RRSP or RRIF may be transferred by a former spouse/partner to the other former spouse/partner as a lump sum payment to cover all future claims for spousal support.

Resources

- T2220 Transfer from an RRSP, RRIF, PRPP or SPP to Another RRSP, RRIF, PRPP or SPP on Breakdown of Marriage or Common-law Partnership

When a spouse/partner does not have an immediate need for income, the rollover of funds held in a RRSP or RRIF to that spouse/partner may be a way to settle rights arising from the breakdown of the marriage/common-law relationship.

Rollover rules also apply to other property owned by a spouse/partner including a cottage, stock holdings, and rental properties when the property is transferred to the former spouse/partner to settle rights arising from the breakdown of the marriage/common-law relationship.

Resources

- Judicial and CRA interpretations of Canadian tax law and transactional implications

APPENDIX – DRAFT TAX LETTER

Canada Revenue Agency

Winnipeg Tax Centre

Post Office Box 14001, Station Main

Winnipeg MB R3C 3M3

Dear Sir/Madam:

Re: Legal Fees - 2021

Mr./Ms. Client has asked me to provide you with a breakdown of the legal fees that he/she incurred in the pursuit of child/and or spousal support in 2021. This letter is not to be construed as taxation advice, and is simply a breakdown of Mr./Ms. Client's 2021 legal fees for your consideration. I have also enclosed a copy of Mr./Ms. Client's Order or agreement along with Form T1158E, Registration of Family Support Payments, where applicable and/or available.

The total legal fees accrued in 2021 were $Row 39, not including disbursements and taxes. Of this amount, Mr./Ms. Client paid $Row 41 in 2021. In reference to the categories outlined in Income Tax Folio S1-F3-C3, Support Payments, I estimate my 2021 professional fees as follows:

- Row 43A% of the total to collect overdue support payments owing, or Row43B;
- Row 44A% of the total to establish the amount of support payments from his/her current or former spouse or common-law partner, or $Row 44B;
- Row 45A% of the total to seek an increase in support payments, or $Row 45B;
- Row 46A% of the total to defend against a reduction in support payments, or $Row 46B;
- Row 47A% of the total to collect late support payments, or Row 47B; and/or
- % of the total to request that child support payments be non-taxable, or $.

In total, I estimate that $Row 48 of my legal fees were incurred in pursuit of support, **and Mr./Ms. Client paid Row 50 towards this amount in 2021**. Again, this is not taxation advice, nor is it a formal accounting. It is an estimate of legal fees Mr./Ms. Client paid in 2021 related to family support, which is within my personal knowledge.

Yours truly,