

# Separation & Divorce

FOR LAWYERS



TAX MATTERS TOOLKIT



THE CANADIAN  
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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.

# Tax Matters Toolkit: Separation and Divorce (for lawyers)

## Table of Contents

<b>Proof of Separation .....</b>	<b>1</b>
Ways to prove “living separate and apart” .....	1
How to notify CRA of a change in marital status.....	3
Same house/separate living quarters.....	3
Couch surfing/no new fixed address .....	3
When are you considered separated? .....	4
<b>Deduction for Legal Fees.....</b>	<b>4</b>
Legal basis for deduction of legal fees .....	4
CRA approach .....	5
<b>“Principal Residence” Rules .....</b>	<b>6</b>
“Principal residence” criteria.....	6
Issues at time of separation or divorce .....	7
<b>Spousal Support .....</b>	<b>8</b>
Characteristics of spousal support .....	8
Payments to a third party.....	8
How to notify CRA of spousal support payments.....	9
Spousal support payers – Deductions for spousal support payments.....	9
Spousal support payers – reducing taxes withheld at source .....	10
Spousal support recipients – increasing taxes withheld at source .....	11
Spousal support paid before there is a written agreement or court order in place.....	11
Deductions for the payer – year of relationship breakdown .....	12
<b>Arrears and Lump-sum Payments .....</b>	<b>13</b>
Tax impact of a lump-sum payment on the payer .....	13
Qualifying Retroactive Lump-sum Payments (QRLSP).....	13
Tax impact of a QRLSP on the recipient .....	13
<b>Child Support .....</b>	<b>14</b>
Tax treatment: written agreements and court orders from before May 1997.....	14
Federal Child Support Guidelines .....	15
<b>Child Benefits .....</b>	<b>15</b>
Canada Child Tax Benefit.....	15
Child Disability Benefit.....	16

<b>Deductions and Credits for Children.....</b>	<b>16</b>
Eligible dependent credit .....	16
Child Care Expense Deduction.....	18
Tuition, Education, and Textbook Credit.....	18
<b>Pensions.....</b>	<b>19</b>
Canada Pension Plan .....	19
CPP: credit splitting .....	19
CPP: end of pension sharing.....	21
Payment of taxes at source when pension plan benefits paid.....	21
<b>Registered Retirement Savings Plans (RRSPs) and Registered Retirement Income Funds (RRIFs).....</b>	<b>22</b>
Transfer of RRSP or RRIF funds to a former spouse or common-law partner.....	22

## Proof of Separation

Basic tax rule: It is up to the taxpayer to provide CRA with proof relating to a claim on a T1 Return.

Proving the date and fact of separation 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 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 proving separation to CRA.

### Ways to prove “living separate and apart”

- 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/lease agreement or a letter from the landlord
  - insurance policies
  - utility bills (gas, electricity, cable television)
  - employer medical or dental plan
  - registered retirement savings or employment pension plan naming the beneficiary for the period under review

- driver's license and vehicle registration (front and back)
- other bills (telephone, cell phone) or letters (with letterhead) that show the residential addresses
- letters from **two** different [third parties](http://www.cra-arc.gc.ca/bnfts/vldtn/dcmnts-eng.html#thrd) (http://www.cra-arc.gc.ca/bnfts/vldtn/dcmnts-eng.html#thrd) with:
  - the name and signature of the writer
  - the profession of the writer
  - the writer's contact information, including address and telephone number
  - an attestation that the writer has personal knowledge that the person did not reside with the other person during the period of separation
  - the dates of the period(s) of separation.

Examples of third parties who can write the letter:

- employer
- social worker
- school authorities
- band council
- insurance company
- bank manager or officer with financial signing authority
- clergy
- medical doctor
- lawyer
- notary (in the province of Quebec)
- post master.

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

#### Resources

- [Documents required to support your benefits and credits](http://www.cra-arc.gc.ca/bnfts/vldtn/dcmnts-eng.html)  
(http://www.cra-arc.gc.ca/bnfts/vldtn/dcmnts-eng.html)

## How to notify CRA of a change in marital status

A taxpayer must notify the CRA of a change in marital status by the end of the month following the month in which marital status changed. However, when a couple separates, they must wait 90 days before getting in touch with CRA.

- File forms:
  - [Form R65, Marital Status Change](http://www.cra-arc.gc.ca/E/pbg/tf/rc65/README.html)  
(<http://www.cra-arc.gc.ca/E/pbg/tf/rc65/README.html>)
  - [Form T1158, Registration of Family Support Payments](http://www.cra-arc.gc.ca/E/pbg/tf/t1158/README.html)  
(<http://www.cra-arc.gc.ca/E/pbg/tf/t1158/README.html>)
- Notify CRA of a change in marital status by writing or phoning, or by updating MyAccount. This must be done by the taxpayer or an authorized representative, [Form T1013](http://www.cra-arc.gc.ca/E/pbg/tf/t1013/README.html) (<http://www.cra-arc.gc.ca/E/pbg/tf/t1013/README.html>).

## Same house/separate living quarters

When a separated couple live under the same roof after a relationship breakdown, CRA generally will not consider them to be “living separate and apart”. However, there may be sufficient evidence of the impossibility of reconciliation and an end to the marital or common-law relationship to convince CRA of the fact of separation. Evidence could 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; not presenting themselves in public as a couple
- absence of sexual relations
- each individual runs a separate household and makes independent financial decisions.

## Couch surfing/no new fixed address

When, after 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 can be more difficult to prove “living separate and apart”. Without documents to show a new address, proving separation will depend on having letters from third parties.

## When are you considered separated?

Lawyers with a client in this situation may wish to alert the client to the benefit of speaking to people who would be considered “third parties” by CRA, about the separation. Then, if required, there would be the two necessary third parties in a position to write a letter based on their knowledge. For example, talking to a doctor or the school principal about the separation, having mail forwarded to a family member or friend’s address, or filing [Form T1213](#) or [TD1](#) (<http://www.cra-arc.gc.ca/E/pbg/tf/t1213/README.html> or <http://www.cra-arc.gc.ca/formspubs/frms/td1-eng.html>) to change deductions at source may help to prove “living separate and apart” to CRA.

### Resources

- [Marital Status Questions and Answers](#)  
(<http://www.cra-arc.gc.ca/bnfts/mrtl/menu-eng.html>)

## 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 recipient in the year they are incurred. Legal fees paid by the payer 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

In cases of divorce or breakdown of a relationship, a child’s or a spouse or common-law partner’s right to support constitutes property for purposes of the *Income Tax Act*. 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 producing business or property income.

## 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 221.

When there is a written agreement or court order for child support made before May 1997, a recipient may deduct, on line 232 of his/her return, legal fees incurred to try to make child support payments non-taxable.

### Resources

- [Support Payments](http://www.cra-arc.gc.ca/E/pub/tg/p102/p102-13e.pdf), PC102, page 14  
(<http://www.cra-arc.gc.ca/E/pub/tg/p102/p102-13e.pdf>)
- [IT Technical News](http://www.cra-arc.gc.ca/E/pub/tp/itnews-24/itnews-24-e.pdf), No. 24, October 10, 2002  
(<http://www.cra-arc.gc.ca/E/pub/tp/itnews-24/itnews-24-e.pdf>)

### 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.

Payers 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.

## **“Principal Residence” Rules**

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

The following housing units could qualify as a principal residence:

- a house
- an apartment or unit in a duplex, apartment building, or condominium
- a cottage
- a mobile home
- a trailer
- a houseboat
- a leasehold interest in a housing unit
- 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 they 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 their principal residence.

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 neighbourhood. 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.

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.

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](http://www.cra-arc.gc.ca/E/pbg/tf/t2091_ind/) (other than a Personal Trust) ([http://www.cra-arc.gc.ca/E/pbg/tf/t2091\\_ind/](http://www.cra-arc.gc.ca/E/pbg/tf/t2091_ind/))
- Section 54, Income Tax Act, defines “principal residence”
- [Sale of your principal residence](http://www.cra-arc.gc.ca/tx/ndvdl/tpcs/ncm-tx/rtrn/cmpltng/rprtng-ncm/lns101-170/127/rsdnc/dspsng/menu-eng.html) (<http://www.cra-arc.gc.ca/tx/ndvdl/tpcs/ncm-tx/rtrn/cmpltng/rprtng-ncm/lns101-170/127/rsdnc/dspsng/menu-eng.html>)
- [Income Tax Folio, S1-F3-C2, Principal Residence](http://www.cra-arc.gc.ca/tx/tchncl/ncmtx/fls/s1/f3/s1-f3-c2-eng.html) (<http://www.cra-arc.gc.ca/tx/tchncl/ncmtx/fls/s1/f3/s1-f3-c2-eng.html>)

It is important for a client to consider the tax consequences of the designation of a property as a principal residence. The tax impact may be a factor in determining a fair distribution of the assets of the marriage or common-law relationship.

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. Until then, the principal residence designation will only apply to one property.

## **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
- the recipient can decide how the money will be spent.

### **Payments to a third party**

Payments made to a third-party for the benefit of the spouse or child (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.

The third-party payments are considered a support payment when the recipient has discretion about how the payments may be spent, for instance, by having the discretion to change maintenance or insurance companies, or move to a new rental property. 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 support payments.

Form T1158 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, any adjustments to be made to the support amount (e.g. changes to reflect the cost of living), and any end date for support payments.

Along with Form T1158, taxpayers must send CRA a copy of their written agreement or court order.

Submitting Form T1158 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.

### **Resources**

- [Form T1158, Registration of Family Support Payments](http://www.cra-arc.gc.ca/E/pbg/tf/t1158/README.html)  
(<http://www.cra-arc.gc.ca/E/pbg/tf/t1158/README.html>)

## **Spousal support payers – Deductions for spousal support payments**

On line 220 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. CRA treats child support payments as the priority.

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 for any reason, such as to assist with a home repair or for a gift for a child.

CRA does not require the payer to provide 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:

- cancelled 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
- 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.

## **Spousal support payers – reducing taxes withheld at source**

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

1. Have taxes withheld at source as usual from his/her salary and enjoy an income tax refund after filing the T1 Return, or
2. 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**

- [T1213, Request to Reduce Tax Deductions at Source for Year\(s\)](http://www.cra-arc.gc.ca/E/pbg/tf/t1213/README.html)  
(<http://www.cra-arc.gc.ca/E/pbg/tf/t1213/README.html>)

## Spousal support recipients – increasing taxes withheld at source

On line 128 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:

1. Have taxes withheld at source as usual from his/her salary and pay an additional amount of tax when filing the T1 Return, or
2. 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](http://www.cra-arc.gc.ca/E/pbg/tf/td1/td1-14e.pdf) (<http://www.cra-arc.gc.ca/E/pbg/tf/td1/td1-14e.pdf>)

## 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 **and**
- The support payments have all the [required characteristics of support payments](#).

The payer may claim the tax deduction for the support payments paid in the year when the written agreement was signed or court order made *and* support payments paid in the previous calendar year. The payer may ask CRA to re-assess the previous year's tax return in light of the written agreement or court order.

## 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.

1. the payer may claim a deduction for the spousal support paid during the year at line 220 of his/her T1 Return, or
2. the payer may claim a non-refundable tax credit for the spouse or common-law partner amount at line 303 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 303 of the *General Income Tax and Benefit Guide* provides the indexed amount for the tax year.

With either option, the payer should report the amount of spousal support paid at line 230. The support recipient must report the spousal support payments received as income at line 128 of his/her Annual Income Tax and Benefit Return.

- [Line 303](http://www.cra-arc.gc.ca/tx/ndvdl/tpcs/ncm-tx/rtrn/cmpltng/ddctns/lns300-350/303/menu-eng.html) (<http://www.cra-arc.gc.ca/tx/ndvdl/tpcs/ncm-tx/rtrn/cmpltng/ddctns/lns300-350/303/menu-eng.html>)
- [Support Payments Q & A](http://www.cra-arc.gc.ca/tx/ndvdl/tpcs/ncm-tx/spprt pymnts/clm-eng.html) (<http://www.cra-arc.gc.ca/tx/ndvdl/tpcs/ncm-tx/spprt pymnts/clm-eng.html>)
- [P102, Support Payments](http://www.cra-arc.gc.ca/E/pub/tg/p102/p102-13e.pdf) (<http://www.cra-arc.gc.ca/E/pub/tg/p102/p102-13e.pdf>)
- [IT530R, Support Payments](http://www.cra-arc.gc.ca/E/pub/tp/it530r/it530r-e.pdf) (<http://www.cra-arc.gc.ca/E/pub/tp/it530r/it530r-e.pdf>)

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.

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 more than \$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](http://www.cra-arc.gc.ca/E/pbg/tf/t1198/)  
(<http://www.cra-arc.gc.ca/E/pbg/tf/t1198/>)

### 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 four situations described in the CRA publication P102 applies:

The payer of child support should report all deductible child support payments made on line 220 of his/her T1 Return and both deductible and non-deductible child support payments made at line 230.

The recipient of child support should report the taxable amount of child support payments received on line 128 of his/her T1 Return and both taxable and non-taxable child support payments on line 156.

#### **Resources**

- [Form T1157, Election for Child Support Payments](http://www.cra-arc.gc.ca/E/pbg/tf/t1157/) (http://www.cra-arc.gc.ca/E/pbg/tf/t1157/)
- [P102, Support Payments](http://www.cra-arc.gc.ca/E/pbg/tf/t1157/), page 9 (http://www.cra-arc.gc.ca/E/pbg/tf/t1157/)

## 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](http://www.justice.gc.ca/eng/rp-pr/fl-lf/child-enfant/guide/index.html),  
(<http://www.justice.gc.ca/eng/rp-pr/fl-lf/child-enfant/guide/index.html>)
- [Child Support Table Look-Up, Department of Justice Canada](http://www.justice.gc.ca/eng/fl-df/child-enfant/look-rech.asp)  
(<http://www.justice.gc.ca/eng/fl-df/child-enfant/look-rech.asp>)

## 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 has custody of 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 the parents have shared custody of 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](http://www.cra-arc.gc.ca/E/pbg/tf/rc65/README.html)  
(<http://www.cra-arc.gc.ca/E/pbg/tf/rc65/README.html>)
- [Form RC66 Canada Child Benefits Application](http://www.cra-arc.gc.ca/E/pbg/tf/rc66/README.html)  
(<http://www.cra-arc.gc.ca/E/pbg/tf/rc66/README.html>)
- [Canada Child Tax Benefit calculator](http://www.cra-arc.gc.ca/bnfts/clcltr/cctb_clcltr-eng.html)  
([http://www.cra-arc.gc.ca/bnfts/clcltr/cctb\\_clcltr-eng.html](http://www.cra-arc.gc.ca/bnfts/clcltr/cctb_clcltr-eng.html))
- [Information Booklet T4114](http://www.cra-arc.gc.ca/E/pub/tg/t4114/t4114-e.html) (<http://www.cra-arc.gc.ca/E/pub/tg/t4114/t4114-e.html>)
- [Information on GST/HST credit](http://www.cra-arc.gc.ca/E/pub/tg/rc4210/rc4210-e.html)  
(<http://www.cra-arc.gc.ca/E/pub/tg/rc4210/rc4210-e.html>)

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 custody of the child, the Child Disability Benefit may be split 50/50.

### Resources

- [Child Disability Benefit](http://www.cra-arc.gc.ca/cdb/) (<http://www.cra-arc.gc.ca/cdb/>)

## 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 will have to agree on who may claim a tax credit.

### 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).

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 and that the payer has an obligation to pay support, even if it works out that only one person makes 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.

#### Resources

- Section 118(5.1), *Income Tax Act*
- [Shared custody and the amount for an eligible dependant](http://www.cra-arc.gc.ca/tx/ndvdl/tpcs/ncm-tx/spprtymnts/shrdcstdy-eng.html) (http://www.cra-arc.gc.ca/tx/ndvdl/tpcs/ncm-tx/spprtymnts/shrdcstdy-eng.html)
- [Line 305](http://www.cra-arc.gc.ca/tx/ndvdl/tpcs/ncm-tx/rtrn/cmpltng/ddctns/lns300-350/305/menu-eng.html) (http://www.cra-arc.gc.ca/tx/ndvdl/tpcs/ncm-tx/rtrn/cmpltng/ddctns/lns300-350/305/menu-eng.html)

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 and when they were incurred, i.e. 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](http://www.cra-arc.gc.ca/E/pbg/tf/t778/t778-13e.pdf)  
(<http://www.cra-arc.gc.ca/E/pbg/tf/t778/t778-13e.pdf>)
- [S1-F3-C1: Child Care Expense Deduction](http://www.cra-arc.gc.ca/tx/tchncl/ncmtx/fls/s1/f3/s1-f3-c1-eng.html#N104E6)  
(<http://www.cra-arc.gc.ca/tx/tchncl/ncmtx/fls/s1/f3/s1-f3-c1-eng.html#N104E6>)

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 did 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 T2202A, Tuition, Education, and Textbook Amounts Certificate](http://www.cra-arc.gc.ca/E/pbg/tf/t2202a/README.html)  
(<http://www.cra-arc.gc.ca/E/pbg/tf/t2202a/README.html>)

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.

[These tables](http://www.hrsdc.gc.ca/eng/retirement/cpp/credit_splitting.shtml) ([http://www.hrsdc.gc.ca/eng/retirement/cpp/credit\\_splitting.shtml](http://www.hrsdc.gc.ca/eng/retirement/cpp/credit_splitting.shtml)) provide 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

- [Canada Pension Plan Credit Splitting Guide for the Legal Profession](http://www.hrsdc.gc.ca/eng/retirement/cpp/credit_splitting.shtml), ([http://www.hrsdc.gc.ca/eng/retirement/cpp/credit\\_splitting.shtml](http://www.hrsdc.gc.ca/eng/retirement/cpp/credit_splitting.shtml))
- 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 this 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

- [IT-499R, Superannuation or Pension Benefits](http://www.cra-arc.gc.ca/E/pub/tp/it499r/README.html)  
(<http://www.cra-arc.gc.ca/E/pub/tp/it499r/README.html>)

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 or RRIF to Another RRSP or RRIF on Breakdown of Marriage or Common-law Partnership](http://www.cra-arc.gc.ca/E/pbg/tf/t2220/t2220-12e.pdf)  
(<http://www.cra-arc.gc.ca/E/pbg/tf/t2220/t2220-12e.pdf>)

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](http://www.taxinterpretations.com/)  
(<http://www.taxinterpretations.com/>)