

# Trusts, Wills, Estates and Charities Bulletin

April 2009

Fasken Martineau DuMoulin LLP

## Income-Splitting Loans

Corina S. Weigl, Toronto

The Canada Revenue Agency (the “CRA”) has announced the 2009 second quarter prescribed interest rate used to calculate taxable benefits for employees and shareholders for interest-free and low-interest loans would be 1%. With this the lowest historical prescribed rate ever, many clients may be candidates for an income-splitting structure using non-arm’s-length loans.

Under the Income Tax Act (the “Act”) many income-splitting arrangements are no longer available. There are, however, certain structures that are still open for use. For instance, it is open for one spouse to loan funds to the other spouse to make an investment. In order for attribution to be avoided, with respect to both income and capital gains earned on the lent property or property substituted therefore, interest must be charged on the loan at the prescribed rate in effect at the time the loan is made, and this rate must apply for the entire term of the loan. In addition, the interest must be paid no later than January 30th following the end of a calendar year, and there can be no defaults in the payment of interest for any year.

With the prescribed rate to be 1%, there is an opportunity here for income splitting on the assumption that the property substituted for the lent property earns income and realized

capital gains in excess of the prescribed rate of interest that must be paid to the lending spouse. It is important to note that, in order for this strategy to be effective, the requirements with respect to the payment of interest must be satisfied each year. If there is a failure to pay interest in one year, there is no means to correct this error and attribution will result in subsequent years.

Finally, other permutations of this income-splitting structure can be devised, such as a loan to a discretionary family trust, the beneficiaries of which include minor children. Where minor children are beneficiaries of a discretionary family trust, it is possible to still have significant tax savings to the extent capital gains are realized and paid to a minor beneficiary. In this situation, there is no attribution of the realized capital gains to the lending parent.

The savings from this strategy could be significant, particularly given the interest rate on the loan will remain locked in at the 1% prescribed rate.

For more information, please contact the author, or any of the other members of our Trusts, Wills, Estates and Charities group.

**Corina S. Weigl**  
416 865 4549  
[cweigl@fasken.com](mailto:cweigl@fasken.com)

Vancouver

Calgary

Toronto

Ottawa

Montréal

Québec City

London

Johannesburg

[www.fasken.com](http://www.fasken.com)

## For More Information About Our Trusts, Wills, Estates and Charities Group

### Vancouver

**Edgar A. Frechette**  
604 631 4982  
dfrechette@fasken.com

**Darrell J. Wickstrom**  
604 631 4728  
dwickstrom@fasken.com

### Toronto

**M. Elena Hoffstein**  
416 865 4388  
ehoffstein@fasken.com

**Corina S. Weigl**  
416 865 4549  
cweigl@fasken.com

**Howard M. Carr**  
416 865 4356  
hcarr@fasken.com

### Montréal

**Hugo Patenaude**  
514 397 5172  
hpatenaude@fasken.com

*The texts included in this collection are intended to provide general comments on Trusts, Wills, Estates and Charities. They reflect the point of view of their respective author and are not opinions expressed on behalf of Fasken Martineau DuMoulin LLP or other member corporations. These texts are not intended to provide legal advice. Therefore, readers should seek out advice on issues specific to them before acting on any information set out in these texts. We would be pleased to provide additional information on request.*

© 2009 Fasken Martineau DuMoulin LLP

**Vancouver**  
604 631 3131  
vancouver@fasken.com

**Montréal**  
514 397 7400  
montreal@fasken.com

**Calgary**  
403 261 5350  
calgary@fasken.com

**Québec City**  
418 640 2000  
quebec@fasken.com

**Toronto**  
416 366 8381  
toronto@fasken.com

**London**  
44 20 7929 2894  
london@fasken.co.uk

**Ottawa**  
613 236 3882  
ottawa@fasken.com

**Johannesburg**  
27 11 685 0800  
johannesburg@fasken.com