

**The Eligible Dependent Tax Credit:
Turning a Bad Situation into Good Money**

Prepared for: Legal Education Society of Alberta

Family Law During Recessionary Times

Presented by:
Jonathan Garbutt
Garbutt Tax Law
Calgary, Alberta

For presentation in:
Calgary, Alberta – October 4, 2017
Edmonton, Alberta – October 11, 2017

**THE ELIGIBLE DEPENDENT TAX CREDIT:
TURNING A BAD SITUATION INTO GOOD MONEY**

REQUESTED

The Eligible Dependent Tax Credit (the “EDTC”) has long been available to provide a benefit to spouses with two or more children who make the difficult decision to separate. However, taxpayers who opt to claim the EDTC are almost always denied this credit because they have structured their affairs incorrectly. Many taxpayers appeal their denied EDTC claim to the Tax Court of Canada (the “TCC”), and the TCC generally upholds the denial on procedural grounds. The TCC is not opposed to giving the taxpayers the EDTC – indeed some justices have went so far in their written decisions to provide step-by-step instructions on how to properly claim the EDTC. The TCC justices are wanting to give taxpayers this credit! Still, taxpayers are finding themselves in situations where their claim is denied, because they (or even their non-tax lawyers) have continued to arrange their affairs improperly. The memorandum will explain how to properly order matters so the EDTC can be successfully claimed.

Dominion Tax Law has been assisting those who are eligible to claim the EDTC to do so successfully. Within this paper we provide our opinion on how to properly structure separation agreements to maximize the potential available under the EDTC found in section 118(1)(b) of the Income Tax Act (“the Act”)¹. With a little bit of tax planning the EDTC can provide a sizeable contribution to a post-secondary education for the children of the relationship. It is the aim of this memorandum to illustrate to counsel, especially those with a limited knowledge of tax law, how fully utilize the EDTC for the benefit of these children. Specifically we will set out:

- (a) A brief fact pattern, illustrating what a successfully structured EDTC would look like;
- (b) The limits of the EDTC and what the requirements are for it to succeed;
- (c) The particulars of section 118 and how the deduction functions;
- (d) A brief discussion on the family law implications of this process;
- (e) Why children can be the ultimate beneficiaries of this arrangement; and
- (f) Some recent developments in the jurisprudence.

¹ *Income Tax Act*, RSC 1985, c 1 (5th Supp).

CONCLUSIONS

Based on the facts and assumptions as set out herein, and subject to all of the qualifications, caveats, exceptions and limitations specified below, as well as our understanding of the Act and the subtleties of family law, we are of the opinion that if a separation agreement is carefully structured section 118(1)(b) of the Act could provide an extra \$3500.00 per year towards RESPs for the children of the relationship. Depending on how many RESPs are set up, the annual maximum grant available from government programmes could add an additional \$1300.00 per year on top of this. However if a separation agreement is set up in the conventional way the entire \$4800.00 is irrevocably lost.

FACTS AND ASSUMPTIONS

For the purposes of this memorandum certain facts and assumptions have been made about any spouses who are looking to take advantage of the EDTC. These are that:

1. Both recipients are Canadian residents for the purposes of the *Income Tax Act*;
2. Both recipients are earning income in Canada which is reported when filing their income tax returns;
3. There are two or more children which are the result of the relationship;
4. Both recipients are willing to work together to obtain the EDTC thereby necessitating a certain level of trust between the parties; and
5. Both recipients will avoid co-habituating with anyone in a conjugal relationship going forward.

These facts and assumptions will be further expanded upon in the pages below.

DISCUSSION

a. Fact Pattern

Often, in calculating the amount of child support payable, child support rules in a province will require that each parent calculate how much they would owe the other parent if each parent had 50% custody of the two children. Once those amounts are calculated typically the two amounts are offset. For example let's say that Pete (parent 1, or "P1") and Patricia ("P2") have two kids, Kyle (kid 1, or "K1") and Katelynn ("K2") and they agree to shared custody of the children. If P1 has to pay \$1000 in child support per month for both children, and P2 has to pay \$800 in child support each month for both children, usually the agreement would take the net amount, and say that P1 has to