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**Written Submission for the Pre-Budget
Consultations in Advance of the 2019 Budget**

By: Blair Corkum Financial Planning Inc.

Recommendation 1: That the government amend the Income Tax Act subsection 118(5.1) to allow it to operate regardless of whether parents exchange individual payments to each other or make only set-off payments for child support in shared custody situations.

Recommendation 2: That the CPP pension be amended so a survivor (or estate) of a CPP pensioner is entitled to minimum payments based on the same terms as the Public Service Pension Plan, instead of the current limitation based on the survivor's retirement pension (or only a \$2,500 death benefit to an estate).

The Committee wishes to focus on Economic Growth: Ensuring Canada's Competitiveness. I submit that Canada cannot be fully competitive until its tax and pension system is fair, and all Canadians are treated equally if in the same circumstances.

1. Section 118(5.1) of the Income Tax Act

The government acknowledges that "Children come first" in legislation dealing with divorce. This dictum inherently promotes shared custody of children (except in a minority of cases, such as abusive situations). While income tax legislation purports to support shared custody with ITA 118(5.1), it actually has created a multitude of income tax reassessments, tax court cases, parental disputes, mental stress, dysfunctional employees at work, and increased legal and tax advisory costs.

ITA 118 (5.1) states that the parents may choose who claims the Amount for an Eligible Dependant if both parties have a legal obligation to pay support for the same child(ren). However, if both parties have an obligation to each other (based on the way support is calculated in accordance with the Federal Child Support Guidelines) but agree to make one payment as a set-off amount instead of two payments, then this subsection no longer applies.

I recommend an amendment to Income Tax Act (ITA) subsection 118(5.1) to allow it to function whether or not a set-off amount of child support for shared custody situations is stated in the child support agreement. If both parents have equal custody of their children, the tax credits should also be equal.

Except in abusive and volatile situations, shared custody allows children to spend equal time with their father and mother, and this will help children to become better adults. Shared custody, as defined by Section 9 of the Federal Child Support Guidelines, is where both parents have physical custody of their children between 40% and 60% of the time.

The relevant references to this discussion include:

- Income Tax Act, particularly Subsections 118(5) and 118(5.1)
- Canada Revenue Agency Interpretation 2013-0502091E5 – Eligible Dependent Credit
- Court case: Verones v. Canada (2013 FCA 69 (CanLII))
- CRA Guide P102, Support Payments and CRA Folio S1-F3-C3

I will describe the problem by use of examples. In all my examples, parents will have shared custody of their two children. Both parents remain single. Dad will earn \$100,000 per year and Mom will earn \$50,000 per year. The earnings of the parents are not important as long as the higher income person is taxable; I could use other amounts. Using these figures, Dad will have a child support obligation of \$1,358 per month owing to Mom, and Mom would have an obligation of \$703 per month owing to Dad. These amounts are based on the Federal Child Support Guidelines tables effective in 2016.

For a shared custody scenario, the calculation of the support payments is governed by the Federal Child Support Guidelines, subsection 9 (a), which states that child support for shared custody should take into account the amounts set out in the applicable tables for each of the spouses. It is

typical that a judge will take these amounts and offset them to determine the final payment. A judge also has discretion to take other factors into consideration. Section 9 allows a judge to adjust the table amount for increased costs of shared custody arrangements and for consideration of the conditions, means, needs and other circumstances of each spouse.

Assuming no other factors are taken into consideration, in this scenario, Mom will receive a net amount of \$655 (\$1,358 minus \$703) for child support. In all of the scenarios I review, this will be the result – i.e. all circumstances are the same. *The difference will solely be in how this money is paid and how the related court order or agreement is worded.* My question is **“Why should the payment of individual cheques or one cheque for the net amount make any difference?”**

In Table 1, I show three couples, Tom and Betty; Dick and Jane; and Allison and Leslie.

- a) Tom and Betty write individual cheques to each other.
- b) Dick and Jane agree that it is simpler for Dick to write one cheque for a set-off amount, instead of each person writing a cheque, and their court order/ agreement is worded accordingly.
- c) Allison and Leslie, also agree to write a cheque for a set-off amount, but they make this agreement separate from the court order/ agreement (a “side agreement”).

In all cases, Betty, Jane and Leslie each received the net amount of \$655. They can also claim the Eligible Dependent Amount for one child, which saves them \$2,341 in taxes (using Prince Edward Island Tax Rates for 2015). Tom, Dick and Allison are each out-of-pocket by \$655. *Tom and Allison are entitled to claim the Eligible Dependent Amount for the other child, but Dick can claim nothing.* Dick has less money to raise his child than the other parents. This is because his court order/maintenance agreement stated that while both parties had child support obligations, only Dick was required to make a set-off payment. Because only Dick is making this payment, the courts have determined that there is only one payer of support, and subsection 118(5.1) of the Income Tax Act does not apply. Although Allison has an agreement that says the same thing, it was a side agreement, not the court order/maintenance agreement, so it is okay based on Canada Revenue Agency Interpretation 2013-0502091E5. These same scenarios would arise if both spouses had similar incomes, and the child support payments were only marginally different, say a set-off amount of \$100 per month.

Logically, writing two cheques, or using side agreements, may provide the cash flow benefits. However, CRA does not provide certainty on use of side agreements, and another problem is created related to enforcement.

Not everyone makes their child support payments. What if the higher payer defaults on his payment? Exchanging two cheques can create serious financial hardship in raising children. Consider these scenarios for another three couples with the same circumstances as in Table 1, but with non-payment by the father:

- a) Jack and Jill write individual cheques to each other. Jack’s cheque is returned “Not Sufficient Funds”.

- b) Bob and Sally agree that it is simpler for Bob to write one cheque for a set-off amount, instead of two cheques, and their court order/maintenance agreement is worded accordingly. Bob does not pay.
- c) John and Mary also agree to write a cheque for a set-off amount, but they make this agreement separate from the court order/maintenance agreement. John does not pay.

Jill is out-of-pocket by \$1,358, and the provincial maintenance enforcement department takes action to collect from Jack. Sally does not receive her payment of \$655, and similar enforcement action can be taken to collect from Bob. Having a set-off agreement was better for Sally compared to Jill because she is only out-of-pocket by \$655, not \$1,358. John does not pay Mary for \$655 as stated in the side agreement. Because it is a side agreement, not a court order or maintenance agreement, can the provincial maintenance enforcement department take action? How will they need to approach this scenario when there are two agreements dealing with the maintenance payment? Enforcement action is difficult at best of times, and now an added level of complexity has been added. Each province will likely have their own approach, and their own legislative capabilities and limits.

Conclusion

Common sense says the Income Tax Act should be corrected to treat all separated families equally.

Table 1

| | Scenario 1 | | Scenario 2 | | Scenario 3 | |
|--|--|-------------|--|-------------|---|-------------|
| | Child Support Agreement Requires Separate Payments | | Child Support Agreement Allows Set-off Payment | | Child Support Agreement Requires Separate Payments But Side Agreement Allows Set-Off | |
| | Tom | Betty | Dick | Jane | Allison | Leslie |
| Guideline income | \$100,000.00 | \$50,000.00 | \$100,000.00 | \$50,000.00 | \$100,000.00 | \$50,000.00 |
| Wording of agreement | Tom has an obligation to pay Betty \$1,358/mo. Betty has an obligation to pay Tom \$703/mo. | | Dick has an obligation to pay Jane \$1,358/mo. Jane has an obligation to pay Dick \$703/mo. Dick will pay Jane a set-off amount of \$655 | | Allison has an obligation to pay Leslie \$1,358/mo. Leslie has an obligation to pay Allison \$703/mo. | |
| Side agreement | None | | None | | Allison will pay Leslie a set-off amount of \$655 | |
| Payments | Tom pays Betty \$1,358 Betty pays Tom \$703 | | Dick pays Jane \$655 per month Jane not required to pay because of set-off | | Allison pays Leslie \$655 per month Leslie not required to pay because of set-off | |
| Cash flow (all the same) | Betty receives a net amount of \$655 | | Jane receives a net amount of \$655 | | Leslie receives a net amount of \$655 | |
| Eligible Dependant Amount for income tax purposes (2015 PEI) | Tom and Betty both eligible to claim one child - they each save \$2,341 of taxes - Total "family" savings of \$4,682 | | Only Jane is eligible to claim a child - she saves \$2,341 of taxes - Dick saves nothing. Total of \$2,341 | | Allison and Leslie both eligible to claim one child - they each save \$2,341 of taxes - Total "family" savings of \$4,682 | |
| Results | Scenario 2 is unfair to Dick - although the shared custody and the net child support payment are the same as Tom and Allison. Dick will have \$2,341 less for raising his children than the other two families, although all living circumstances are the same. | | | | | |

2. Canada Pension Plan Survivor Benefit

Current CPP legislation states that a surviving spouse or common-law partner (“survivor”) of a CPP pensioner cannot receive more than one maximum retirement pension when eligible. If that survivor is entitled to a maximum retirement pension in their own right, they will receive no survivor’s pension on the death of their spouse/partner because this maximum would be exceeded. Combined employer and employee pension contributions to the CPP in today’s dollars over 40 years would approximate \$200,000 at maximum pensionable earnings levels. Upon death at retirement age before collecting any retirement pension, the only return to the pensioner would be a taxable death benefit of \$2,500.

In contrast, for all private pension plans that are registered under the *Pension Benefits Standards Act, 1985*, if you die before retirement, your survivor or your estate, if no survivor, is entitled to the value of your benefits that you would have been entitled to on that day as though you had not died. If you have a spouse or common-law partner and you die after you retire, your surviving spouse or common-law partner is entitled to receive a lifetime pension of at least 60% of your pension after your death. There is no maximum imposed on the survivor.

Similarly, for the Public Service Pension Plan, if you have at least two years of pensionable service, your eligible survivor will be entitled to a survivor benefit. If you have no eligible survivor, your estate will receive an amount equal to the greater of the return of your contributions with interest, or 5 years of basic pension payments, less any payments already received.

Most other private pension plan function similarly to the Public Service Pension Plan, with at least a guaranteed refund of premiums plus interest or a minimum payment based on pension payments.

A survivor (or the estate) of a CPP pensioner should be entitled to the same entitlements as the Public Service Pension Plan.