



Tax Shelters

As we get closer to the end of the year, there is always an increase in the amount of questions we get from our clients concerning tax shelters. Taxpayers should be aware of the risks associated with purchasing certain tax shelters and participating in the gifting arrangements being promoted and marketed.

With such a wide spectrum of tax shelters available for purchase and their continued popularity as a means to reduce personal income taxes, it is important to understand the Canada Revenue Agency's ("CRA") position regarding tax shelters and the possible adverse consequences from being reassessed if you have recently acquired this type of investment.

Oil and gas tax shelters which offer flow-through deductions for use by taxpayers in their personal income tax returns have been condoned by the CRA as an acceptable means of reducing personal income taxes. In simple terms, if you buy an Oil & Gas Shelter for \$100, you will receive \$100 in tax deductions, saving \$46 in tax at the highest rate. Usually in two years, the shelter is rolled into a mutual fund, which will have a nil cost base. When the fund is subsequently sold, your proceeds will be your capital gain. Thus, you typically will break even, even if the tax shelter is sold for 70% of your investment.

The CRA's position is not as forgiving in respect of the more aggressive tax shelters and gifting schemes available. The more aggressive tax shelters and gifting schemes are promoted on the basis that the tax benefits and deductions arising from the arrangement will exceed the costs to purchase the shelter. Anytime the value of tax benefits received by a taxpayer exceeds the purchase costs, you can be assured that the CRA will not view the arrangement in a favorable light.

To that extent, the CRA recently published a "Tax Alert" entitled "Warning: Participating in tax shelter gifting arrangements is likely to result in a tax bill". In it, the CRA announced it is auditing all gifting arrangements, although it may take some time. The CRA also stated that it is likely that taxpayers will be reassessed as a result, thereby denying all or a portion of the tax benefits derived from the arrangement.

Please be reminded that the CRA can generally reassess an individual taxpayer up to three years after the taxpayer has received their Notice of Assessment.

In a recent tax case heard at the Federal Court of Appeal level, the Court upheld the Minister's decision to disallow deductions claimed by the taxpayer on the acquisition of a computer software license as part of an arrangement that was not promoted as a tax shelter or gifting scheme. The moral of the case is that even if not promoted as a "tax shelter", certain arrangements may still not pass the CRA's smell test.

Caveat emptor.

For more information, please contact the Tax Department at Cunningham LLP.