

# Taxes After Separation or Divorce

Separations and divorces can be complex and often take a long time to be resolved. Here at Baker Tilly GWD LLP, we understand that these may be challenging times. In this document, we try to clarify what is needed for taxes and when to start updating your information with the Canada Revenue Agency (CRA). The information below has been gathered to help guide you in understanding your tax returns and credits after a separation or divorce.

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## **WHERE TO START**

The CRA does not consider you legally separated until you have been living separate and apart for at least 90 days. Once you are separated for 90 days, it's important to update your tax filing status so that your tax returns and benefits are calculated for your new family net income and marital status. You should notify the CRA after 3 months have passed from the date of separation or within 1 month after divorcing your spouse. See Appendix 1 for guidance on how to communicate this change. You will need to contact any other government organization that provides benefits to you to provide your new information. The CRA will not share your new marital status or other personal information with other government departments.

## **INFORMATION TO PROVIDE YOUR ACCOUNTANT IN THE YEAR OF SEPARATION**

When completing your tax return for the first time after the change in your marital status, you'll need to provide your accountant with a copy of your Separation or Divorce Settlement Agreement, which will outline what property and assets are being moved between partners, the custody arrangements for any children, who is allowed to claim various tax credits related to any children, the amount and type of support payments required to be made, and the separation date.

If you are required to pay support for your ex-spouse or dependents, your accountant will need the details regarding the total spousal support and child support paid during the year. Alternatively, if you received spousal or child support during the year, provide your accountant with the total spousal support and child support received during the year.

## **SUPPORT PAYMENTS**

Periodic spousal support payments made pursuant to a separation agreement, divorce agreement, or court order are tax-deductible to the payor and are included in taxable income of the recipient, so long as both spouses are living separate and apart from each other and all child support obligations have been met. Spousal support that is voluntary, i.e., not legally enforceable, is not tax deductible by the payor. The payor also cannot deduct spousal support paid during the year if their child support payments are in arrears.

In lieu of periodic payments, lump-sum spousal support payments are deductible only when they are:

- Made to pay off spousal support that is in arrears;

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- Paid pursuant to a court order in conjunction with an existing agreement as an advance of future support for the sole purpose of securing funds to the person being supported; or
- Paid pursuant to a court order that establishes a clear obligation to pay retroactive support for a specified period.

Legal fees incurred to establish a right to receive or collect support payments are deductible from the support payments received, while legal fees paid by the payor are not deductible.

## **CHILD CUSTODY AND RELATED TAX CREDITS**

### Claiming the amount for an eligible dependent

Claiming a child as an eligible dependent can provide a significant tax benefit, but there are some limitations on who can claim the credit and when it can be claimed.

- You can only claim this credit if you do not have a spouse or common-law partner for tax purposes at any time during the year. If you were to re-marry, you would no longer be able to make this claim.
- You can make this claim only for children under the age of 19. You can make a claim for children over the age of 18 only if they are dependent on you because of an impairment in physical or mental functions.
- You cannot claim this credit if you paid child support in relation to this dependent, unless you meet one of the following conditions:
  - You were separated from your spouse or common-law partner for only part of the year because of a breakdown in your relationship and you did not claim any support payments to your spouse or common-law partner on line 22000 of your return.
  - Both parents share custody of a child throughout the year, and you each have a clearly established requirement under a court order or written agreement to make child support payments for that child. Normally, neither of you would be able to claim the amount for an eligible dependant for that child. However, one of you may still be eligible to claim the amount, if you and the other person agree who will make the claim. If you cannot agree, neither of you can claim the amount for that child.

### Claiming child care expenses

In shared custody situations, each parent can claim child care expenses for the period the child resided with them, provided they paid the expenses to enable them to work, study, or carry on a business. It is important to note that the term “reside” refers to the child’s physical location. The CRA will look to your custody agreement to determine when the child physically lived with you and if the fees for child care were paid during that period. If one parent pays the child care provider for a period when the child was in the other parent’s custody and is reimbursed by the other parent, the payer can claim the expenses net of the reimbursement, and the reimbursing parent can claim the reimbursed amount.

### Canada Child Benefit (CCB)

You must meet all four of these conditions in order to qualify to receive the CCB:

- 1) You’re a Canadian resident;
- 2) You’re a Canadian citizen or permanent resident;
- 3) You live with a child who is under 18 years of age; and
- 4) You are primarily responsible for the care and upbringing of the child.

If you and your ex-spouse are separated and do not reside together, and if the child lives with each of you not less than 40% of the time over the course of the year, both of you are entitled to the CCB. In shared

custody situations, each parent may receive 50% of the CCB payment they would have received if the child lived with them full-time. The payments are based on each parent's adjusted family net income, so although you may be splitting the benefit entitlement equally, you may not receive the same amount of funds from the government if one parent earned significantly more than the other.

You should notify the CRA immediately after a change in your custody arrangement. See Appendix 1 for guidance on how to communicate this change. If one parent continues to receive 100% of the benefits after separation and the other parent later a claim for the CCB, the parent who received the full benefit would need to repay 50% of their benefit payments to the CRA.

## **SETTLEMENT OF ASSETS**

### Registered Retirement Savings Plans (RRSP), Registered Retirement Income Funds (RRIFs), and Tax-Free Savings Accounts (TFSAs)

Settling marital assets between spouses can have unintended tax consequences. Instead of cashing out your RRSP, which would lead to withholding and income taxes, consider transferring a portion of your RRSP account to your ex-spouse's RRSP account on a tax deferred basis. You can also transfer amounts between RRIF and TFSA accounts in a similar manner. Consult your investment advisor for more information.

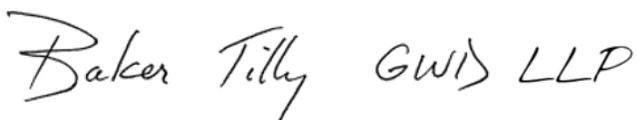
### Capital assets, investments, and property

On your separation, you may need to transfer property between spouses. This transfer of property will normally occur on a tax-deferred basis. This means that any accrued gains related to that property for the entire period of ownership will be taxed in the hands of the spouse who owns the property at the time of eventual sale. This can lead to a significant future tax burden. When preparing your separation agreement with your lawyer, consider the accrued gains on the property being transferred and adjust your division of assets to account for the future tax consequences of each asset.

If you are interested in our assistance with your tax returns or have any tax questions, please contact our office.

We look forward to serving you.

Yours very truly,



Baker Tilly GWD LLP

## **Appendix 1: Additional Resources**

### **Notifying the CRA of a change in your marital status**

You can notify the CRA of a change in your marital status by:

- Calling the CRA at 1-800-387-1193
- Updating your information on My Account on Canada.ca
- Mailing the CRA a completed Form RC65, Marital Status Change

### **Notifying the CRA of a change in your CCB benefits**

You can notify the CRA of a change in custody arrangement by:

- Using "Apply for child benefits" in My Account to update your custody information
- Mailing the CRA a completed Form RC66, Canada Child Benefits Application

### **Additional Reference Material**

- For more information related to child tax credits and support payments, see Guide P102, *Support Payments*
- For more information related to child care expense deductions see Income Tax Folio S1-F3-C1, *Child Care Expense Deduction*