

TAXADVISOR

Clawbacks Issue for Some

COURT REPORT

BY JAMIE GOLOMBEK



In 2005, the Old Age Security clawback, equal to 15 cents on the dollar, began at income over \$60,806. That being said, there are very few seniors in Canada that have income that even approaches this level. If you examine the data, 95% of all eligible seniors receive their full OAS, while 98% receive some OAS – i.e., only 2% of eligi-

ble recipients have their OAS fully clawed back.

Still, no one likes to lose their OAS. There are some situations where the OAS clawback seems particularly severe. Let's discuss two of them, based on two cases, one recent and one a few years back.

The first case (*Kieling Estate v The Queen*, 2006 TCC 222) was decided in Regina last month and specifically involved a challenge to the OAS clawback system.

Charles Kieling died in 2002 and named his brother Rudolf as

his executor. The executor filed his late brother's terminal tax return for the year of death. He included in that year's income a taxable capital gain of \$185,000 as a result of the automatic deemed disposition of property upon Charles' death.

As a result, Charles incurred a full "clawback" of his OAS for the year of death. The executor alleged that the "clawback" is "contrary to the Canadian *Bill of Rights*" and thus appealed the Canada Revenue Agency's assessment to the Tax Court of Canada.

The executor argued that the capital gain resulting from the deemed disposition of all capital property upon death wasn't really "income" per se and thus his late brother, Charles, "had no increase in his income while he was alive in 2002." He also argued that "Charles was entitled to '...enjoyment of property, and the right not to be deprived thereof except by due process of law...' as set forth in...the Canadian *Bill of Rights*."

The Tax Court judge did not buy this argument and rearticulated the principle set out by the Supreme Court of Canada in a 2003 decision (*Attorney General of Canada v. Joseph Patrick Authorsen*,

[2003] 2 S.C.R. 40) that "the *Bill of Rights* does not protect against the expropriation of property by the passage of unambiguous legislation...The *Bill of Rights* protects only rights that existed at the time of its passage, in 1960. At that time it was undisputed, as it continues to be today, that Parliament had the right to expropriate property if it made its intention clear."

The judge, concluding the *Income Tax Act*, was "clear and unambiguous" dismissed the estate's appeal.

Interestingly, this is not the first time that the clawback of OAS payments has been challenged in court. The second case worth looking at is one that actually made it to the Supreme Court of Canada in 1996 (*Swantje v The Queen*, (SCC) Docket: 2443).

In that case, the taxpayer had several sources of income in the years in question and among those were a German pension as well as OAS pension payments. At the time, under the Canada-Germany Tax Treaty, the German pension was exempt from Canadian tax.

The question before the court, however, was whether the amount of the German pension should be included in income for purpose of calculating the OAS clawback of the taxpayer's Canadian OAS pension received.

The court found that the German pension, while not taxable because of the treaty, must still technically be first included in the taxpayer's income and then is deducted in computing taxable income as an item exempt under the treaty. The taxpayer's net income, including the ultimately non-taxable German pension, however, must be used to calculate the OAS clawback since the purpose of the clawback legislation was to ensure the "repayment of social benefits by taxpayers who, because of their higher incomes, have a lesser need of them."

Finally, readers may wish to note that the Canada-Germany Tax Agreement was amended such that, beginning with the 2003 tax year, German pensions paid to Canadian residents under the social security legislation of Germany are now partially taxable in Canada. Canada, however, can only tax the portion of the German pension that Germany would have taxed if the pensioner was resident in Germany, which is an amount that is roughly based on the non-capital portion of the pension. **AER**

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