

Tax Tip
Week of January 11, 2010

Strip Bonds

Strip bonds are long term bonds that have interest bearing coupons that have been separated from the bond and sold separately. As a result, the bond trades at a deep discount from its face value, but the price continues to increase as the bond approaches the maturity date. It is CRA's position that the annual increase in the bond's value is treated as interest income. However, the taxpayer must report interest income on an annual basis, but does not receive any cash to fund the tax liability.

Due to the adverse tax consequences of these bonds, individuals should normally hold them in either a Tax Free Savings Account or a Registered Retirement Savings Plan. By using a tax sheltered vehicle, the annual increase in value does not result in a tax liability.

Consider strip bonds as a possible investment vehicle for your Tax Free Savings Account.