

Tax Tip

Week of March 23, 2009

Prescribed Rate of Interest

CRA has announced the prescribed rate of interest used to calculate taxable benefits for employees and shareholders from interest-free and low-interest loans will be 1% for the period April 1 to June 30, 2009. If you believe certain stocks that pay high dividends have either bottomed out or will be trading at a higher level in three to five years, this represents a potential tax planning opportunity.

Assume one is considering the purchase of a Canadian bank stock that currently has a dividend yield of 6%. An employee could borrow an amount, say \$100,000 from his employer and purchase the bank stock. Although the employee would receive a taxable benefit of 1% on the amount of the loan, the return on the loan would be 6%, without taking into consideration the benefits of the dividend tax credit.

The downside of such a strategy is that if the stocks drop significantly in value and do not recover in the near term.