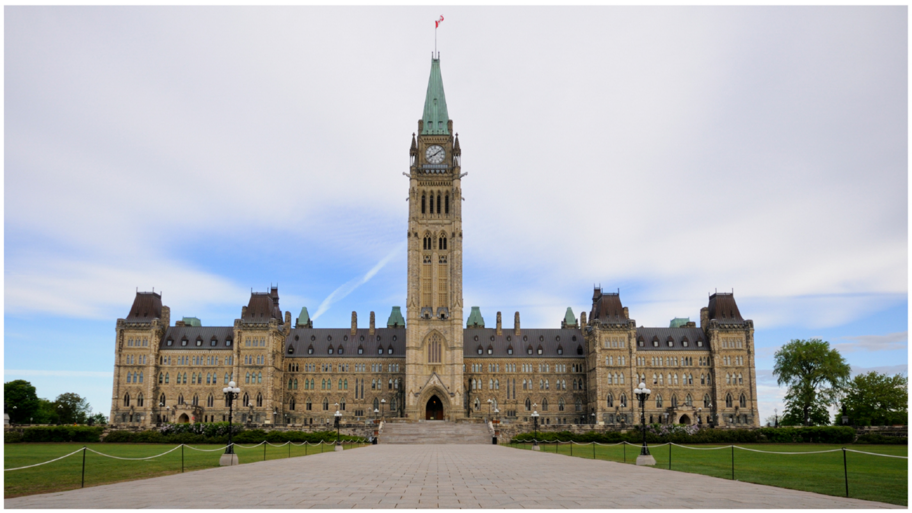
NetWorth

2017 Federal Budget Summary



On March 22, Finance Minister Bill Morneau unveiled the Liberal government's second Federal Budget entitled "Building a Strong Middle Class" which continues with many of the themes outlined in the Liberal election platform and last year's Federal Budget.

The most significant income tax measures affecting individuals and Canadian private companies are summarized below. Note that the measures introduced are only proposals at this stage and may not ultimately be enacted into law. Readers are cautioned to consult with their tax advisors for specific advice on how they may be affected by these proposals.

Summary of Personal Income Tax Proposals

In its ongoing review of tax measures viewed as ineffective and inefficient, the government proposes changes to the following tax credits:

Canada Caregiver Credit

Effective for the 2017 and subsequent taxation years, the Budget proposes to simplify the existing system of tax measures for caregivers by replacing the existing caregiver credit, infirm dependant credit and family caregiver tax credit with a new Canada Caregiver Credit. This new credit is intended to better target support to those most in need and extend tax relief to some caregivers who may not currently qualify due to the income level of their dependant.

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Tuition Tax Credit

The Budget proposes to extend the eligibility criteria for the tuition tax credit to fees for an individual's tuition paid to a university, college or other post-secondary institution in Canada for occupational skills courses that are not at the post-secondary level. The tuition tax credit would be available in these circumstances only if the course is taken for the purpose of providing the individual with skills (or improving the individual's skills) in an occupation and the individual has attained the age of 16 before the end of the year. This measure will apply in respect of eligible tuition fees for courses taken after 2016.

Medical Expense Tax Credit – Fertility-Related Expenses

In some cases, such as single individuals and same-sex couples, the use of reproductive technologies may not be directly related to a medical infertility condition. Even where such treatment is not medically indicated, the Budget proposes to clarify the application of the medical expense tax credit so that individuals who require medical intervention in order to conceive a child are eligible to claim the same expenses that would generally be eligible for individuals on account of medical infertility. This measure will apply beginning in 2017, however, the Budget will introduce the ability for individuals to elect for this measure to apply for any of the immediately preceding ten taxation years.

Public Transit Tax Credit

The Budget proposes to eliminate the existing public transit tax credit, which provides a 15-per-cent non-refundable tax credit in respect of the cost of eligible public transit passes (including annual and monthly passes, as well as weekly passes and electronic fare cards used on an ongoing basis), effective as of July 1, 2017.

Other personal tax measures identified as providing greater consistency or enhancing the integrity of the tax system include the following:

Anti-Avoidance Rules – Registered Education Savings Plans (RESPs) and Registered Disability Savings Plans (RDSPs)

A number of anti-avoidance rules currently exist for registered plans (i.e., Tax-Free Savings Accounts, Registered Retirement Savings Plans and Registered Retirement Income Funds) to help ensure that the plans do not provide excessive tax advantages unrelated to their respective basic objectives. These include the advantage rules, and the prohibited and non-qualified investment rules.

To improve the consistency of the tax rules that apply to investments held by registered plans, the Budget proposes to extend the anti-avoidance rules described above to RESPs and RDSPs. Subject to certain exceptions and transitional measures, these proposals will apply to transactions occurring, and investments acquired, after Budget Day.

Canadian Private Business Tax Measures

Billed-Basis Accounting

Taxpayers are generally required to include the value of work-in-progress (WIP) in computing their income for tax purposes. However, taxpayers in certain designated professions may elect to exclude the value of their WIP in computing their income. This election effectively allows income to be recognized when the work is billed (billed-basis accounting) while enabling taxpayers to defer tax by deducting the costs associated with WIP in advance (without the matching inclusion of the associated revenues).

The Budget proposes to eliminate the ability for designated professionals to elect to use billed-basis accounting. This measure will apply to taxation years that begin on or after Budget Day, however a transitional period is proposed to mitigate the impact to affected taxpayers.

Meaning of Factual Control

A recent court decision has restricted the scope of application of factors to consider in making a determination of factual (vs. legal) control of a corporation. Consistent with measures introduced in the 2016 federal budget, and to prevent taxpayers from inappropriately accessing certain tax benefits such as the small business deduction shared by associated companies, the Budget proposes that the tax legislation be amended to clarify that the factors considered in determining factual control are not limited to the narrower requirements of this recent decision.

Charitable Giving

Ecological Gifts

There were limited measures in the Budget impacting charitable giving, the most significant of which involves several measures intended to better protect gifts of ecologically sensitive land. Most notably, in light of the potential conflicts of interest that can arise involving a donation of ecologically sensitive land to a private foundation, the Budget proposes that private foundations no longer be permitted to receive these ecogifts, effective for transactions occurring on or after Budget Day.

Future Tax Measures

Tax Planning Using Private Companies

The government is undertaking an ongoing review of federal tax expenditures to close perceived tax loopholes and improve the integrity and administration of the tax system. Many of the above proposals from the Budget are consistent with the government's intention to improve the efficiency, certainty and fairness of the tax system.

In addition, this review of federal tax expenditures highlighted a number of issues regarding tax planning strategies involving private corporations, which can result in high income individuals gaining perceived tax advantages through a variety of tax reduction strategies available to these individuals that are not available to other Canadians. Strategies involving private corporations specifically identified by the government include:

Sprinkling income, which can reduce income taxes by causing income (such as dividends and capital gains) that would otherwise be realized by an individual facing a high personal income tax rate to instead be realized by family members who are subject to lower personal tax rates.

Holding passive investment portfolios, which may be financially advantageous for owners of private corporations compared to otherwise similar investors. This is mainly due to the fact that corporate income tax rates, which are generally much lower than personal rates, facilitate accumulation of earnings that can be invested in a passive portfolio.

Converting regular income into capital gains, which can reduce income taxes by taking advantage of the lower tax rates on capital gains relative to regular income.

A number of measures have been put in place over the years to limit the scope of some of these planning arrangements, but such measures have not always been considered fully effective. The government is therefore further reviewing the use of tax planning strategies involving private corporations that are seen as inappropriately reducing personal taxes of high-income earners. The government intends to release a paper in the coming months setting out the nature of these issues in more detail as well as proposed policy responses.

If you have any questions regarding these budget proposals, please consult with your tax advisor for further details.

Tax Filing Updates

It's that time of year again – tax filing season. April 30th marks an important date on the calendar as most Canadian individuals are required to file their personal income tax return and remit any final balances due by that date. This article seeks to summarize some important changes that may impact your personal tax return this year.

Principal Residence Exemption

It is commonly known that Canadian resident individuals who sell or dispose of their principal residence and realize a gain are exempt from any capital gains tax if that residence was their principal residence for every year they owned it, and designated as such. One of the most significant changes this year comes in the form of a change in CRA's administrative position with respect to reporting the sale of an individual's home. Previously, CRA's administrative policy did not require individuals to report the sale of a principal residence when the principal residence exemption sheltered the full amount of the gain. Beginning with the 2016 tax year, individuals who sell their principal residence are now required to report the sale and make the principal residence designation on Schedule 3 (Capital Gains (or Losses)) of their individual income tax return for the year; even when the property was solely their principal residence for every year owned. In situations where only a portion of the capital gain is sheltered from capital gains tax, an additional reporting form (Form T2091) continues to be required to be filed to determine the amount of the capital gain subject to tax. Reporting will be required for sales that occur on or after January 1, 2016 and the information required includes the address of the property, the year it was acquired, the proceeds of disposition, and a designation of the years in which the property was the individual's principal residence.

Failure to report the sale could result in the principal residence exemption being disallowed. CRA may accept late filed designations, but penalties may be applied of up to $8,000.

Note that Quebec residents who sold their principal residence in 2016 will continue to be required to file form TP-274-V in order to designate and claim the principal residence exemption, for Quebec tax purposes.

Education and Textbook Tax Credits

The education tax credit provides a 15 percent non-refundable tax credit of $400 per month of full-time enrolment in a qualifying educational program (and $120 per month of part-time enrolment) at a designated educational institution. In addition, the textbook tax credit provides a 15 percent non-refundable tax credit of $65 per month of full-time enrolment in a qualifying educational program (and $20 per month of part-time enrolment) at a designated educational institution. The 2016 tax year is the final year to claim any of these two credits, however, any unused credits from 2016 or prior years can be carried forward and be eligible to be claimed in a future tax year.

However, the tuition tax credit continues to be available after 2016 on eligible fees for tuition and examination fees paid to educational institutions.

Children's Fitness and Arts Tax Credits

The 2016 tax year is the final year to take advantage of any children's fitness and arts tax credits (for children under 16 years of age at the beginning of the year) providing tax relief for up to $500 of eligible fitness costs and $250 of eligible arts costs (excluding the supplement for children with disabilities). These two tax credits have been eliminated for the 2017 and subsequent tax years.

School Supply Tax Credit

New for the 2016 year is a tax credit aimed at assisting teachers and early childhood educators who incur eligible costs of supplies for the purposes of teaching or otherwise enhancing students' learning experience. This refundable credit allows employees who are eligible educators relief for up to $1,000 in expenses for eligible supplies (such as games, puzzles, art supplies and various stationary items) incurred in the year.

It is important to consult with a qualified tax professional for specific advice and direction on the applicability of any of these tax filing changes and reporting obligations in your particular circumstances.

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