2015 FEDERAL BUDGET

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Table of Contents

1 Personal Tax Measures
4 Business Tax Measures
5 International Tax Measures
Other Indirect Tax Changes

The 2014 Federal Budget was delivered on February 11, 2014. The Department of Finance is continuing its drive towards a balanced budget in 2015. The federal deficit is expected to be $16.6B in 2014 and $2.9B in 2015. The government expects a surplus of $6.4B in fiscal 2016.

Key Highlights

Connecting Canadians with available jobs, by helping them to acquire the skills that employers need.

Fostering job creation, innovation and trade, by keeping taxes low, reducing the burden of tax compliance, and providing Canadian businesses and investors with the market access they need to succeed in the global economy.

Developing resources responsibly and conserving Canada's natural heritage, by supporting mining, forestry and agriculture sectors, investing in national parks and conservation initiatives and expanding support for clean energy.

Investing in infrastructure and transportation, by focusing on specific infrastructure project funding and transportation services.

Supporting families and communities, by protecting Canadian consumers, keeping taxes low for families, and improving the safety of Canadians.

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Personal Tax Measures

The following are the key personal tax measures proposed in Budget 2014:

Taxation of Trusts and Estates

If you recall back in Budget 2013, the Government announced its intention to consult on possible measures to eliminate the tax benefits arising from taxing certain trusts at graduated tax rates. The types of trusts targeted include testamentary trusts and grandfathered inter vivos trusts (created during a settlor's lifetime before June 18, 1971). The current tax treatment of these trusts and estates effectively allowed their beneficiaries access to more than one set of graduated rates and for an indefinite amount of time.

A consultation paper was released in 2013 that contained possible measures to change these rules. Budget 2014

- the first 36 months of an estate will still give rise to tax at graduated tax rates (the top rate will apply after 36 months), and
- the graduated rates will continue to apply where a trust has beneficiaries who are eligible for the federal Disability Tax Credit.

In addition, further measures will cause such trusts to no longer benefit from special treatment under certain rules including:

- the requirement to remit instalments;
- the requirement to have a calendar year-end;
- alternative minimum tax requirements; and
- classification as a personal trust.

Testamentary trusts that do not already have a calendar year-end will be deemed to have a year that ends on December 31, 2015 (or, for an estate, the end of its 36-month period, if later).

Adoption Expense Tax Credit

Budget 2014 proposes to increase the maximum amount of eligible expenses to $15,000 per child for 2014 (up from the previous maximum of $11,774 for 2013) and indexed to inflation thereafter.

The 15 percent non-refundable tax credit allows adoptive parents to claim eligible adoption expenses relating to the completed adoption of a child under the age of 18. These expenses include, for example, fees paid to a licensed adoption agency and mandatory immigration expenses in respect of the child. This credit may only be claimed for the taxation year in which the adoption is completed.

Medical Expense Tax Credit

The 15 percent non-refundable tax credit for medical expenses is based on eligible medical and disability-related expenses in excess of a threshold that is the lesser of 3 percent of the taxpayer's net income and the indexed dollar amount of $2,171 for 2014.

The list of expenses eligible for the credit are enhanced by Budget 2014 to now include amounts paid for the design of an individualized therapy plan (for individuals with a severe and prolonged mental or physical impairment) if the cost of the therapy itself would be eligible for the credit and so long as specific conditions are met.

In addition, expenses for service animals specially trained to assist an individual in managing their severe diabetes are now eligible to be claimed. Eligible expenses include the cost of the service animal and its care and maintenance as well as reasonable travel expenses incurred for the individual to attend a facility that trains individuals in the handling of these service animals.

Mineral Exploration Tax Credit

Budget 2014 proposes to extend eligibility for the Mineral Exploration Tax Credit for one year, to flow-through share agreements entered into on or before March 31, 2015.

Flow-through shares allow companies to “flow through” tax expenses associated with their Canadian exploration activities to investors, who can deduct the expenses in calculating their own taxable income. The Mineral Exploration Tax Credit is an additional benefit, available to individuals who invest in flow-through shares, equal to 15 per cent of specified mineral exploration expenses incurred in Canada.

Farming and Fishing Businesses

Budget 2014 proposes to simplify the rules relating to the intergenerational transfers of farming and or fishing property from an individual to the individual’s child along with the application of the Lifetime Capital Gains Exemption available to the individual on certain shares or interests in farming or fishing businesses.

Modifications of these rules include extending eligibility for both the intergenerational rollover and the Lifetime Capital Gains Exemption to allow a combination of farming and fishing. Previously the property had to be 50 percent or more in either farming or fishing as rules did not allow a combination of the two in order to qualify. Budget 2014 changes this and allows a combination of farming and fishing.

Pension Transfer Limits

Budget 2014 proposes to extend changes to the pension transfer limits to help individuals who are leaving an underfunded pension plan. Specifically, individuals leaving a defined benefit Registered Pension Plan may receive a cash-out payment from the plan reflecting the lump-sum value of their pension benefits. The income tax rules limit the amount of these payments that may be transferred tax-free to a Registered Retirement Savings Plan, Registered Retirement Income Fund or other defined contribution retirement savings vehicle.

In 2011, the Government introduced relieving changes to these limits for individuals leaving an underfunded plan that is being wound up due to an employer’s insolvency. Budget 2014 proposes to extend these changes to additional situations to ensure the appropriate application of these rules to individuals leaving an underfunded plan. This measure will apply in respect of cash-out payments made after 2012. As a general rule, an individual will be able to transfer a higher percentage of your commuted value to a registered plan, which will defer tax.

GST/HST Credit Administration

The Goods and Services Tax/Harmonized Sales Tax (GST/HST) Credit is a non-taxable benefit that is paid to individuals based on their adjusted family net income. In the past, an individual (whether eligible or not) could apply for the GST/HST Credit by checking the GST/HST Credit application box on their annual income tax return. The Minister would respond in writing, sending the individual a notice of determination as to their eligibility for the GST/HST Credit.

Budget 2014 proposes to eliminate the need for an individual to manually apply for the GST/HST Credit and allow the Canada Revenue Agency to automatically determine if an individual is eligible to receive the GST/HST Credit. A notice of determination will be sent to each individual who is eligible for the GST/HST Credit. No action will be required for eligible taxpayers. The credit will apply automatically assuming the tax return for the eligible individual has been filed. It’s worth noting that, in the case of eligible couples, the credit will be paid to the spouse whose tax return is assessed first. Individuals ineligible for the credit won’t be notified, but can request a notice of determination if seeking an objection.

Tax on Split Income

The Income Tax Act currently has rules in place to reduce the ability of a higher-income taxpayer to split taxable income inappropriately with lower-income individuals. The “tax on split income” limits income-splitting techniques that seek to shift certain types of income from a higher-income individual to a lower-income minor.

The tax on split income does not currently apply to situations where a minor is allocated income from a partnership or trust that is derived from business or rental activities conducted with third parties. Budget 2014 proposes to change this by modifying the definition of "split income" to include business or rental income that is, directly or indirectly, paid or allocated to a minor from a trust or partnership where certain conditions are met.

Non-Resident Trusts

The Income Tax Act contains rules to prevent the use of non-resident trusts by taxpayers to avoid Canadian tax. If a person resident in Canada contributes property to a non-resident trust, rules (the deemed residence rules) may apply to treat the non-resident trust as resident in Canada. An exemption (the 60-month exemption) from the deemed residence rules applies if the contributors to the trust are individuals each of whom is resident in Canada for a total period of not more than 60 months.

In the past, this worked to the benefit of immigrants to Canada who, for the first 60 months of residency in Canada, could avoid tax on income earned on assets they may have placed in an offshore trust – called an immigration trust. Budget 2014 proposes to eliminate the 60-month exemption from the deemed residence rules, including related rules that apply to non-resident trusts.

Amateur Athlete Trusts

It is possible for an amateur athlete who is currently a member of a registered Canadian amateur athletic association, and is eligible to compete in international sporting events as a Canadian national team member, to place certain income in an arrangement known as an "amateur athletic trust" (AAT).

Income received in connection with the athlete's participation in international sporting events including endorsement income, prize money, or public appearances may be contributed to an AAT. When this is done, the income will not be taxed in the year it's received, but will be taxed later when withdrawals are made from the AAT. In addition, the income earned in the AAT (investment income, for example) is not taxable until it is withdrawn (or eight years after the last year in which the athlete competes as a Canadian national team member, at the latest).

Budget 2014 proposes to allow income that is contributed to an amateur athlete to qualify as earned income for the purpose of determining the RRSP contribution limit of the athlete. Contributions made in prior years may also qualify to increase RRSP contribution room.

Search and Rescue Volunteers Tax Credit

New this year, and in recognition of the important role played by search and rescue volunteers in contributing to the security and safety of Canadians, Budget 2014 proposes a 15 percent non-refundable tax credit based on an amount of $3,000 to be claimed by eligible ground, air and marine search and rescue volunteers.

To be considered eligible, the individual must perform at least 200 hours of volunteer services in a taxation year consisting primarily of responding to and being on call for search and rescue and related emergencies, attending the required meetings and participating in the required training. Written certification confirming the number of hours may be required.

Charitable Donations

a. Ecologically Sensitive Land

Donations of ecologically sensitive land, or easements, covenants and servitudes on this type of land, are eligible for special tax assistance similar to regular donations for individual and corporate donors. As with other charitable donations, amounts not claimed for a year can be carried forward for up to five years. Budget 2014 proposes to extend to 10 years the carry-forward period for donations of ecologically sensitive land, or easements, covenants and servitudes on this type of land.

b. Estate Donations

Currently, where an individual makes a donation by will, the donation is treated for income tax purposes as having been made by the individual immediately before the individual's death. Similar provisions apply where an individual designates, under a RRSP, RRIF, TFSA or life insurance policy, a qualified charity as the recipient upon the individual's death of the proceeds of the plan or policy. Under these circumstances, the Charitable Donations Tax Credit (CDTC) available may be applied against only the individual's income tax otherwise payable. On the other hand, a CDTC available in respect of a donation made by an individual's estate may be applied against only the estate's income tax otherwise payable.

Budget 2014 proposes to provide more flexibility in the tax treatment of charitable donations made in the context of a death that occurs after 2015. Donations made by will and designation donations will no longer be deemed to be made by an individual immediately before the individual's death. Instead, these donations will be deemed to have been made by the estate, at the time at which the property that is the subject of the donation is transferred to the qualified donee.

The trustee of the individual's estate will then be able to allocate the available donation among any of: the taxation year of the estate in which the donation is made; an earlier taxation year of the estate; or the last two taxation years of the individual. The carry-forward period for any unused donations will remain at five years.

c. Other Issues Regarding Charities and Non-Profit Organizations

Budget 2014 proposes to remove, for certified cultural property acquired as part of a tax shelter gifting arrangement, the exemption from the rule that deems the value of the gift to be no greater than its cost to the donor. Other donations of certified cultural property will not be affected by this measure.

Budget 2014 proposes that where a charity accepts a donation from a foreign state listed as a supporter of terrorism, the Minister will refuse to register the charity or may revoke its registration, taking into consideration the specific facts of each case.

Finally, the budget announces the Government's intention to review whether the income tax exemption for Non-Profit Organizations remains properly targeted and whether sufficient transparency and accountability provisions are in place. A consultation paper for comment will be released.

Business Tax Measures

The following is a brief update regarding some of the proposed changes that will impact those who are business owners:

Employer Source Deductions

Budget 2014 reduces the tax compliance burden by proposing to reduce the frequency of remittance of source deductions for employers by increasing the threshold level of average monthly withholdings for employers required to remit bi-monthly to $25,000 from $15,000; and increase this level to $100,000 from $50,000 for employers required to remit weekly.[7]

Clean Energy Generation

In order to encourage investment in technologies that can contribute to a reduction in emissions of greenhouse gases and air pollutants, Budget 2014 proposes to expand Class 43.2 (50 percent per year on a declining-balance basis) to include water-current energy equipment and equipment used to gasify eligible waste fuel for use in a broader range of applications.

Eligible Capital Property

The government recognizes that over the years, the Eligible Capital Property (ECP) regime has become increasingly complicated and the complexity could be significantly reduced if the ECP regime were replaced with a new class of depreciable property to which CCA rules would apply.

As such, Budget 2014 announces a public consultation on a proposal to repeal the ECP regime, replacing it with a new CCA class available to businesses and transfer taxpayers' existing CEC pools to the new CCA class. Further updates are to be provided at a later time.

International Tax Measures

Budget 2014 proposes the following changes on an international tax level:

- Amendments to the existing anti-avoidance rule in the FAPI regime relating to "captive insurance" – a strategy that has allowed individuals to earn certain income offshore that would escape the Canadian tax net.
- Adding new conditions for qualifying under the regulated foreign financial institution exception.
- Adding a specific anti-avoidance rule in respect of withholding tax on interest payments, and amending the existing anti-avoidance provision in the thin capitalization rules.
- Consultation papers announced surrounding Tax Planning by Multinational Enterprises and Treaty Shopping.

Other Indirect Tax Changes

- The GST/HST will no longer apply on professional services provided by acupuncturists and naturopathic doctors.
- Eyewear specially designed to treat or correct a defect of vision by electronic means, if supplied on the written order of a physician or optometrist will be added to the zero rated GST/HST list.

Prior to implementing any tax strategies contained in this article, it is recommended that you consult a tax professional to assist you in assessing the costs and benefits of proceeding with specific budget proposals as they relate to you.