Manulife

TAX TOPICS

April 2015

Budget 2015 – More splash than cash

Introduction

Finance Minister, Joe Oliver, delivered the 2015 Federal Budget which contained many measures that were leaked prior to the Budget. In some cases, the manner in which the measures were described made them sound much greater than what we actually got – more splash than cash. Some of the positive measures announced have delayed implementation to 2017 making their inclusion in the Budget feel more like election posturing.

The following represents a summary of measures of interest to investment and insurance advisors.

Personal Tax Measures

Tax-Free Savings Account

For 2015 and subsequent years, the Budget proposes to increase the annual Tax-Free Savings Account (TFSA) annual contribution limit from the current $5,500 to $10,000. The TFSA annual contribution limit will no longer be indexed to inflation.

The TFSA annual contribution limit increase is welcome news for Canadians with the means to make additional contributions. For those who can’t make use of their TFSA contribution room the good news is that at least it will accumulate so that hopefully they can make use of it in the future.

Those saving for retirement continue to face the traditional debate of a TFSA versus Registered Retirement Savings Plans (RRSP) and that analysis hasn’t changed. High income earners may look at maximizing contributions to both. Low income earners are often better served by investing in TFSAs as the RRSP deduction may not be of much value and TFSA withdrawals do not impact federal income tested benefits and tax credits like Old Age Security (OAS) and the Age Credit. The majority of Canadians are somewhere in the middle and their decision may depend on their current financial situation and income level versus their expected future financial situation and income level.

As mentioned in the 2008 Federal Budget clients will likely choose to do their TFSA investing first before turning to exempt life insurance as a tax-preferred investment.

T1135 reporting forms — Streamlined reporting requirements

Taxpayers owning specified foreign property with a cost of more than $100,000 are currently required to file Form T1135 each year. Recent revisions to Form T1135 have required increased detail for each property and therefore created significant compliance issues for taxpayers.

The Budget proposes to simplify the foreign property reporting system for taxation years that begin after 2014. Under a revised form being developed by the Canada Revenue Agency (CRA), if the total cost of the taxpayer's foreign property is less than $250,000 throughout the year, the taxpayer can report the property under a new simplified foreign asset reporting system.

The current reporting requirements will continue to apply to taxpayers owning specified foreign property that has a total cost at any time during the year of $250,000 or more.

Specified foreign property continues to include funds held outside of Canada, shares in foreign companies even if held in a Canadian brokerage or through a separately managed account (SMA) and foreign life insurance policies. Canadian domiciled mutual funds and segregated fund contracts regardless of the underlying fund assets, and property held in registered plans, such as RRSPs and TFSAs, continue to be excluded from the Form T1135 reporting requirements.

Minimum Withdrawal Factors for Registered Retirement Income Funds

If not taken into income, an RRSP must be converted to a Registered Retirement Income Fund (RRIF), or the proceeds used to purchase a qualifying annuity, by December 31st of the year in which the RRSP holder turns 71. A minimum amount needs to be withdrawn from the RRIF beginning the year after it is established (i.e. the year the RRIF holder turns 72). A percentage factor is applied to determine the minimum withdrawal amount. This factor is based on the RRIF holder's age at the beginning of the year and multiplied by the corresponding RRIF assets at that time. RRIF holders can also base the minimum withdrawal amount on the age of their spouse or common-law partner if done when establishing the RRIF (before any payments are received).

The current RRIF factors were determined in order to provide a regular payment stream from age 71 to 100. The factors are capped at 20 per cent for ages 94 and above. Many industry bodies have recommended changes to the RRIF withdrawal factors based on current interest rate and life expectancy assumptions.

In response, Budget 2015 proposes to adjust the RRIF minimum withdrawal factors that apply from age 71 to 94. As a result, the new RRIF factors will be significantly lower than the existing factors. Minimum withdrawal factors applicable to ages 70 and below will not change and continue to be determined by the formula 1/(90 – age). Table 1 shows the existing and proposed RRIF factors.

The new RRIF factors will apply to the 2015 and subsequent taxation years. RRIF holders who withdraw more than the reduced 2015 minimum amounts will be permitted to re-contribute the excess to their RRIFs. Any re-contributions will be permitted until February 29, 2016 and will be deductible for the 2015 taxation year. Similar rules are applicable to annual payments received from a defined contribution Registered Pension Plan (RPP) or a Pooled Registered Pension Plan (PRPP).

These new RRIF factors will allow holders to preserve more of their RRIF savings for income at older ages during their retirement years. Lower required RRIF minimums mean more savings remain tax deferred, as well as reduce the possible claw back of the Guaranteed Income Supplement (GIS), OAS and other income tested benefits and tax credits.

Table 1: Existing and Proposed RRIF Factors

Age (at start of year)	Existing Factor (%)	Proposed Factor (%)
71	7.38	5.28
72	7.48	5.40
73	7.59	5.53
74	7.71	5.67
75	7.85	5.82
76	7.99	5.98
77	8.15	6.17
78	8.33	6.36
79	8.53	6.58
80	8.75	6.82
81	8.99	7.08
82	9.27	7.38
83	9.58	7.71
84	9.93	8.08
85	10.33	8.51
86	10.79	8.99
87	11.33	9.55
88	11.96	10.21
89	12.71	10.99
90	13.62	11.92
91	14.73	13.06
92	16.12	14.49
93	17.92	16.34
94	20.00	18.79
95 & over	20.00	20.00

Transfer of Education Credits – Effect on the Family Tax Cut

The Family Tax Cut is a proposed federal non-refundable tax credit, capped at $2,000, for couples with children under the age of 18. The Family Tax Cut allows a higher-income spouse or common-law partner to notionally transfer up to $50,000 of taxable income to a spouse or common-law partner. The credit is intended to reduce or eliminate the difference in federal tax payable by a one-earner couple relative to a two-earner couple with a similar family income. The credit applies for the 2014 and subsequent taxation years.

The Family Tax Cut rules may in some instances reduce the value of the Family Tax Cut for couples who transfer education-related amounts (Tuition, Education and Textbook Tax Credits) between themselves. Budget 2015 proposes to revise the calculation of the Family Tax Cut for the 2014 and subsequent taxation years to ensure that couples claiming the Family Tax Cut and transferring education-related credits between themselves receive the appropriate value of the Family Tax Cut. After the enacting legislation receives Royal Assent, the CRA will automatically reassess affected taxpayers for the 2014 taxation year to ensure that they receive any additional benefits that they are entitled to under the Family Tax Cut.

New Home Accessibility Tax Credit

The Budget proposes a new, non-refundable Home Accessibility tax credit for seniors and persons with disabilities. This proposed tax credit will provide tax relief of 15 per cent on up to $10,000 of eligible expenditures per year, per qualifying individual, per eligible dwelling starting in 2016. So, a maximum benefit of $1,500 per year.

Registered Disability Savings Plan – legal representation

In the 2012 Budget, a temporary measure allowed a qualifying family member (i.e. a beneficiary's parent, spouse or common-law partner) to become the plan holder of a Registered Disability Savings Plan (RDSP) for adults lacking the capacity to enter into a plan. This measure was to apply until 2016.

In order to allow the provinces to streamline the processes and appointments of such qualified family members, Budget 2015 proposes to extend the temporary measure to apply to the end of 2018. A qualifying family member who becomes a plan holder before the end of 2018 can remain the plan holder after 2018.

Small Business Measures

Small Business Tax Rate

The federal small business tax rate applies to the first $500,000 of active business income of a Canadian-controlled private corporation. The Budget proposes to reduce this rate from 11 per cent to nine per cent as follows:

Effective January 1, 2016 – 10.5%
Effective January 1, 2017 – 10%
Effective January 1, 2018 – 9.5%
Effective January 1, 2019 – 9%

For corporations with non-calendar tax years the reduction in the small business tax rate will be pro-rated.

Non-eligible Dividends

In conjunction with the proposed changes to the small business tax rate, the Budget also proposes to adjust the gross-up factor and dividend tax credit that applies to non-eligible dividends. The Budget proposes to adjust the gross-up factor and dividend tax credits as follows:

	2015	**2016**	**2017**	**2018**	**As of 2019**
Gross-up (%)	18	17	17	16	15
Dividend tax credit (%)	11	10.5	10	9.5	9

This proposed change will increase the federal top marginal tax rate for non-eligible dividends from 21.2 per cent in 2015 to 23 per cent as of 2019.

Lifetime Capital Gains Exemption for Qualified Farm or Fishing Property

The Lifetime Capital Gains Exemption for 2015 is $813,600. For dispositions of qualified farm or fishing property the Budget proposes the Lifetime Capital Gains Exemption increase to $1 million. The increase applies to dispositions of qualified farming or fishing property that occur after April 20, 2015.

Going forward, for dispositions of qualified farm or fishing property the exemption will be the greater of $1 million and the indexed Lifetime Capital Gains Exemption applicable to capital gains realized on the disposition of qualified small business corporation shares.

Donations involving private corporation shares or real estate

A measure was announced which would provide an exemption from capital gains tax in respect of the gift of the proceeds of sale of private company shares or real estate to a charity. The donation must occur within 30 days of the sale. The sale must be to a purchaser that is dealing at arm's length with both the donor and the charity to which the proceeds are donated. If only a portion of the proceeds from the sale is donated, the exemption from capital gains tax would apply to that portion. An anti-avoidance rule would limit the exemption in certain circumstances occurring within five years of the sale.

This measure will not come into effect until 2017. These measures can put these types of gifts on an equal footing with gifts of publicly listed securities, and ecological or cultural gifts which currently enjoy exemption from capital gains tax when donated to charity.

Things to watch

The Budget announces a consultation on the circumstances in which income from a business, the principal purpose of which is to earn income from property, should qualify as active business income. Currently such businesses with more than five full time employees are able to claim the small business deduction. It is anticipated these types of businesses with fewer employees may qualify for the small business deduction.

A consultation relating to the repeal of the eligible capital property regime and replacement with a new capital cost allowance class was announced in the 2014 Federal Budget. Budget 2015 promises that detailed draft legislative proposals will be circulated for comment before inclusion in a bill. On the sale of assets of a private company, goodwill can be a significant component of the value of the business. This measure will mean an increase in tax on the sale of goodwill, certain licenses, franchises and quotas.

Conclusion

It's an election year!

The commentary in this publication is for general information only and should not be considered legal, tax or other professional advice to any party. Individuals should seek the advice of professionals to ensure that any action taken with respect to this information is appropriate to their specific situation.

Manulife, the Block Design, the Four Cube Design, and Strong Reliable Trustworthy Forward-thinking are trademarks of The Manufacturers Life Insurance Company and are used by it, and by its affiliates under licence.