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BUDGET2014

From gift giving to farming, what you need to know about the federal budget

The good, the bad

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Another year, another budget. Sometimes I feel like I should not be surprised by what the Canadian government has in mind. Other years, I feel like a truck has side-swiped me out of nowhere.

This year's budget had a bit of both. And if you have not had a chance to spend a couple of hours reading the ins and outs of the economic outlook according to the government of Prime Minister Stephen Harper, then here is a summary of some of the personal tax proposals that might affect you.

Personal Tax Measures

Split Income

Currently the Tax Act has a definition of "split income" aimed at minors so that they are taxed at the highest federal tax rate.

The Budget proposes to amend the definition of "split income" to include income that is directly or indirectly paid or allocated to a minor from a trust or partnership if the income is derived from a business or a rental property AND a person who is related to such a minor is either:

✓ Actively engaged on a regular basis in the activities of the trust or partnership to earn income from any business or rental property; or

✓ In the case of a partnership, has an interest in the partnership (whether held directly or through another partnership).

This measure will apply to the 2014 and subsequent taxation years.

Bye Bye Graduated Rates

This proposal was hinted at by the government in last year's budget, so it came as no surprise that they actually made good on their threat.

Currently, testamentary trusts created under a Will get the benefit of the graduated tax rates. The Budget proposes that beginning in 2016, testamentary trusts (other than the first 36 months of an estate) will no longer benefit from the following:

- Gradated tax rates;
- Exemption from making income tax instalments; and
- Having an off-calendar year end.

As a result, after the first 36 months of an estate that arises after death, testamentary trusts will now be subject to a flat top-tax rate. There will continue to be access to graduated rates for trusts that have individuals eligible for the federal Disability Tax Credit as beneficiaries.

Tax Credits

Medical Expense Tax Credit – This credit will be expanded to include the design of an individualized therapy plan (subject to certain conditions) as well as expenses for service animals specially trained to assist individuals in managing severe diabetes.

Adoption Expense Tax Credit – Currently the maximum credit for adoption expenses is $11,774 per child. This amount has been increased to $15,000 per child for 2014 (to be indexed to inflation for years after 2014).

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Mineral Exploration Tax Credit – The Budget has extended the eligibility for the Mineral Exploration Tax Credit for flow-through share investors for one year. This applies to flow-through share agreements entered into on or before March 31, 2015.

GST/HST Credit – You will no longer be required to apply for the GST/HST credit on your return; rather the CRA will automatically determine if an individual is eligible to receive the GST/HST Credit. A notice of determination will be sent to you rather than having to apply for the credit. This measure will apply for 2014 income tax returns and for subsequent taxation years.

Search and Rescue Volunteers Tax Credit – The budget proposes a Search and Rescue Volunteers Tax Credit to allow eligible ground, air and marine search and rescue volunteers to claim a 15 per cent non-refundable tax credit based on an amount of $3,000. This measure will apply to the 2014 and subsequent taxation years.

Pension Transfer Limits

Back in 2011, a special rule was introduced in certain situations allowing a member leaving a defined benefit registered pension plan (RPP) – one whose estimated pension benefit was reduced due to plan underfunding – to disregard that benefit reduction when calculating the portion of a lump-sum commutation payment from the RPP that may be transferred to an RRSP on a tax-free basis (i.e., the transferable amount).

If the rule applies, the maximum transferable amount for a plan member who leaves an underfunded RPP will be the same as if the RPP was fully funded.

The budget proposes to extend this rule to commutation payments made, after 2012, to a plan member who leaves an RPP if that payment has been reduced due to plan underfunding and either:

✓ If the plan is an RPP other than an individual pension plan, the reduction in the estimated pension

benefit that results in the reduced commutation payment is approved pursuant to the applicable pension benefits standards legislation; or

✓ If the plan is an individual pension plan, the commutation payment to the plan member is the last payment made from the plan (i.e., the plan is being wound up).

This application of the rule must still be approved by the CRA.

Amateur Athlete Trusts

The budget proposes to allow income contributed to an amateur athlete trust after 2013 to qualify as earned income for purposes of determining the registered retirement savings plan (RRSP) contribution limit of the trust's beneficiary.

If an individual who contributed to an amateur athlete trust before 2014 makes an election in writing and submits it to the CRA before March 3, 2015, any contributions made in 2011, 2012 and 2013 will also qualify as earned income.

The individual's RRSP limit will be re-determined for each of these years and any additional RRSP room will be added to the individual's RRSP contribution room for 2014.

Farming

The budget proposes to extend eligibility for the intergenerational rollover of farming and fishing property and the lifetime capital gains exemption to:

✓ Property of an individual used principally in a combination of farming and fishing;

✓ An individual's shares in a corporation, or interest in a partnership, if the corporation or partnership carries on both a farming business and a fishing business (in particular, if a property of the corporation or partnership is used principally in either business, or is used principally in a combination of farming and fishing, the property will count towards the existing "all or substantially all" test).

Tax Deferral for Farmer: Currently farmers who dispose of breeding livestock due to drought, flood or excess moisture conditions in certain regions are permitted to defer up to 90 per cent of their sales proceeds until the next year (or a later year in certain conditions).

This deferral is to be extended as of 2014 to disposals of bees, and horses that are over 12 months of age that are kept for breeding.

International Tax Changes

And, Bye Bye Immigration Trusts. If you were not already aware, new immigrants to Canada were eligible for a 60-month tax holiday where assets were contributed to a non-resident trust (commonly referred to as "immigration trusts").

However in a move that has still left me reeling (and calling up many of my new immigrant clients with the bad news), the government decided that this was no longer something they wanted to extend to new immigrants (without allowing for grandfathering any existing immigration trusts).

So any existing immigration trusts must essentially be shut down by the end of 2014.

Thin Capitalization – Back-to-Back Loans

The thin-capitalization rules contain a specific anti-avoidance rule for back-to-back loan arrangements. These rules will be expanded to apply where, among other things, a taxpayer is indebted to an intermediary and the latter's loss exposure on the loan has been limited by certain non-resident persons.

Interest on such loans will be subject to the thin-capitalization rules and may be treated as a non-deductible dividend payment subject to a 25 per cent withholding tax. The expansion of the thin-capitalization rules will apply to taxation years that begin after 2014 and, for withholding tax, to amounts paid or credited after 2014.

Treaty Shopping

Following recent consultations, the Government is proposing a domestic law that would impact benefits derived from treaty shopping, which would be denied if it is reasonable to conclude that one of the main purposes of the transaction (or series of transactions) was to obtain such benefit from a tax treaty (although a safe-harbour presumption will apply in certain situations where a person carries on an active business in a country with which Canada has a tax treaty).

Charities and Non-profits

Estate Donations: The budget proposes that donations made by Will (and certain designated donations) will be deemed to be donations made by the estate, and may be claimed in the taxation year of the estate in which donation is made, an earlier taxation year of the estate or the last two taxation years of the deceased individual.

(Note – the donation must be made within 36 months following the death of the individual. This will apply for 2016 and subsequent taxation years.)

Donations of Ecologically Sensitive Land: For donations of ecologically sensitive land, or easements, covenants and servitudes on such land made after February 10, 2014, the carry-forward period will be extended to ten years.

Donations of Certified Cultural Property: Gifts of certified cultural property acquired as part of a tax shelter gifting arrangement will no longer be measured at fair market value for the purpose of donation tax credits. Rather, the value of such a gift shall be limited to its cost amount to the donor. This restriction applies to gifts made after February 10, 2014.

Employer source deduction remittances

The Budget proposes to reduce the frequency of remittance of source deductions by certain employers. Currently, the frequency of remittance of source deductions depends on the employer's total average monthly withholding amount in preceding calendar years in respect of these source deductions.

Under the Budget proposals, the threshold level of average monthly withholdings for employers required to remit source deductions up to twice per month will be increased to $25,000 from $15,000, while the threshold for those employers required to remit up to four times per month will be increased to $100,000 from $50,000. This measure will apply to amounts to be withheld after 2014.

Joint ventures

The Ministry of Finance intends to propose new joint venture election measures to simplify the GST/HST accounting obligations for joint venture activities.

The new measures, as well as associated anti-avoidance measures, will allow joint venture participants to make the joint venture election as long as the joint venture's activities are exclusively commercial and the participants are engaged exclusively in commercial activities.

The Ministry of Finance notes that it will release related draft legislative proposals later in the year for comments. ❐