CI Investments

2011 FEDERAL BUDGET

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Tax highlights from the June 2011 federal budget

Finance Minister James Flaherty tabled his second federal budget for 2011 on June 6. Readers will remember that the minister tabled his first budget of the year on March 22 – a budget that died when Parliament was dissolved and an election was called. Now that the Conservatives have been re-elected with a majority, the government has introduced essentially the same budget for parliamentary approval. This budget projects a deficit of $36.2 billion for the recently ended 2010-2011 fiscal year, which is significantly lower than last year's forecast of a $49.2 billion deficit for that period (and $4.3 billion lower than the original $40.5 billion projected in the earlier version of this budget). The budget also projects a deficit of $32.3 billion for the 2011-2012 fiscal year (a $2.7 billion increase from the original $29.6 billion projection in the earlier incarnation of the budget). The minister indicated that the government will initiate a "Strategic and Operating" review in the coming year with the goal of reducing future expenditures and returning to surplus by the 2014-2015 fiscal year, one year earlier than previously projected. Savings to be realized by the expenditure review will be included in the 2012 budget.

These projections are based on a May 31 review of various economic assumptions with respect to growth in overall gross domestic product, increasing tax revenues and spending control.

As expected, there are no substantive changes to the proposals contained in the March 22 budget, other than the introduction of two non-tax measures that were mentioned during the election campaign – the provision for $2.2 billion of compensation to Quebec with respect to the earlier implementation of a harmonized sales tax (subject to concluding an agreement), and the phase-out of the per-vote subsidy to all federal political parties.

The following pages are a summary of the provisions announced in the budget. There are no changes to the items noted in our highlights document produced in March; however, we include them again for your reference. Please note that these changes are still proposals until passed into law by the federal government.

PERSONAL TAX MATTERS

Personal income tax rates

There were no changes announced with respect to personal income tax rates in this budget. The effective rates for 2011 and corresponding tax bracket thresholds are shown in the following table.

Taxable income range	Tax rate
$10,528 - $41,544	15%
$41,545 - $83,088	22%
$83,089 - $128,800	26%
$128,801 or more	29%

Children's arts tax credit

The budget proposes a new 15% non-refundable tax credit for expenses of up to $500 incurred to enrol eligible children in a broad range of qualifying activities. In order to qualify, the expenses must be paid in respect of a child who is under 16 years of age at the beginning of the year for enrolment in an eligible program of artistic, cultural, recreational or developmental activities. An eligible program includes a weekly program that lasts for a minimum of eight consecutive weeks, or in the case of children's camps, five consecutive days. An enhanced credit is available for children under the age of 18 who qualify for the disability tax credit.

This credit is structured like the existing children's fitness tax credit, and is available for expenses incurred in 2011 and subsequent years. The tax credit may be claimed by either parent, or may be shared between them. Expenses that could otherwise be eligible for other tax credits, or that are part of a school curriculum, will not be eligible for this credit.

Volunteer firefighters tax credit

The budget proposes a new 15% non-refundable tax credit for volunteer firefighters. The credit will be based on $3,000 and will be available to individuals who perform at least 200 hours of volunteer firefighting services in a taxation year, for one or more fire departments. Volunteer hours will be ineligible to the extent that the individual also provides non-volunteer service to a particular fire department.

An individual who claims this credit will be ineligible to claim the existing tax exemption of up to $1,000 for honoraria paid in respect of firefighting duties. This new tax credit will be available in 2011 and subsequent years.

Family caregiver tax credit

The budget proposes a new 15% non-refundable tax credit for caregivers of dependants, including spouses, common-law partners, and minor children, with a mental or physical infirmity. Effective in 2012, this credit will be based on $2,000 and will enhance the existing dependency related tax credits. Only one of these new tax credits will be available for an infirm dependant, irrespective of the number of caregivers.

Medical expense tax credit

An individual can currently claim a medical expense tax credit for an unlimited amount of eligible expenses incurred in respect of themselves, a spouse or common-law partner or a minor child. However, eligible expenses in respect of other dependants, such as a child over the age of 18, a grandchild, a parent, grandparent, brother, sister, uncle, aunt, niece or nephew, who is dependent on the taxpayer for support, are limited to $10,000. The budget proposes to remove this limit, effective for 2011 and subsequent years.

Child tax credit

The budget proposes to revise eligibility for the 15% child tax credit for 2011 and subsequent years. The current rules preclude more than one individual per household from claiming the credit in respect of a dependant child. The rule will be modified to allow more than one claim per household, such that when two families share a home, each eligible parent will be allowed to claim the credit for their respective child.

Tuition tax credit

Effective for 2011, the budget proposes to extend the tuition tax credit to include examination and other ancillary fees paid to an educational institution, professional association, provincial ministry, or similar organization. These fees will qualify if they are required either to obtain professional status under a federal or provincial statute, or to be licensed or certified in order to practice a profession or trade in Canada. Ancillary fees would not include fees that are currently ineligible for the tuition tax credit, such as travel, parking, or equipment. Examination fees incurred to begin study in a profession or field are also ineligible.

Education outside of Canada

Effective for 2011, the budget proposes to reduce the minimum course duration for courses taken at foreign educational institutions from 13 consecutive weeks to three consecutive weeks, for purposes of claiming the tuition, education and textbook tax credits. This reduction in program length also applies for the purposes of claiming an educational assistance payment from a Registered Education Savings Plan (RESP). This change is in recognition of the fact that semesters at foreign universities are often shorter than 13 weeks.

Registered education savings plans

The budget proposes to provide subscribers of individual RESPs with the same flexibility to allocate assets among siblings that subscribers to family plans have. Effective for transfers after 2010, transfers from an RESP for an individual can be made to an RESP for a sibling, without tax penalties and without triggering repayment of Canada Education Savings Grants (CESGs), provided that the beneficiary of the plan receiving the assets had been under 21 years of age when the plan was opened.

Registered disability savings plans

The budget proposes to allow RDSP beneficiaries with shortened life expectancies to have greater access to their savings. This proposal allows beneficiaries with life expectancies of five years or less to make annual taxable withdrawals of up to $10,000 without triggering repayment of Canada Disability Savings Grants (CDSGs) and Canada Disability Savings Bonds (CDSBs).

This measure will apply after 2010, subject to transitional rules, to withdrawals made after the measure receives royal assent.

Registered retirement savings plans

The budget proposes to introduce a number of anti-avoidance rules to prevent the use of RRSPs in tax planning schemes that are perceived to be abusive. These new measures are similar to those introduced last year with respect to Tax Free Savings Accounts (TFSAs). The proposed measures include:

- The advantage rules – the amount of tax payable on an RRSP "advantage" will be equal to the fair market value of the benefit received.
- The prohibited investment rules – there will be a special tax equal to 50% of the fair market value of a prohibited investment.
- The non-qualified investment rules – there will be a tax equal to 50% of the fair market value of a non-qualified investment. This new tax replaces the existing income inclusion and deduction amounts as well as the 1% per month tax on non-qualified investments.

These latter two 50% taxes are refundable to the annuitant if the RRSP disposes of the investment by the end of the year following the year in which the tax applied, unless the annuitant knew or ought to have known that the investment was either prohibited or non-qualified.

These measures are proposed to apply to investments acquired after March 22, 2011, subject to certain exceptions.

Registered pension plans

The Canada Revenue Agency (CRA) will clarify the application of the rules with respect to the receipt by former employees or retirees of lump-sum amounts in respect of rights to health and dental coverage from insolvent pension plans that have been wound up. These amounts will not be treated as income for tax purposes, in relation to insolvencies arising before 2012.

Individual pension plans

The budget proposes to introduce two new rules with regard to the taxation of Individual Pension Plans (IPPs).

- Annual minimum withdrawals – similar to the Registered Retirement Income Fund (RRIF) rules, a plan member will be required to withdraw an annual minimum amount upon reaching 72 years of age. The IPP will be required to pay out an amount equal to the greater of the regular pension amount payable, and the minimum payment that would have been required if the IPP were a RRIF. This new requirement is proposed to be applicable to 2012 and subsequent years.
- Past service contributions – it will now be necessary to fund past service contributions firstly from a transfer of the plan member's RRSP assets or by reducing the individual's RRSP contribution room before new deductible past service contributions can be made. This measure will generally apply to past service contributions made after March 22, 2011.

Tax on split income

This tax, also known as the "kiddie tax," is payable at the top marginal rate (29%) and is applicable to certain types of income earned by minor children from non-arm's length private businesses. The budget proposes to extend the application of this tax to capital gains realized on the disposition of shares of a corporation to a person who does not deal at arm's length with the minor child, if taxable dividends on the shares would have been subject to the kiddie tax.

These capital gains will be treated as taxable dividends and will not benefit from the 50% capital gains inclusion rate or the lifetime capital gains exemption. This measure is proposed to apply to capital gains realized on or after March 22, 2011.

Mineral exploration tax-credit for flow-through share investors

The budget extends this credit for flow-through share arrangements that was scheduled to expire on March 31, 2011. The credit will continue to be available for flow-through share arrangements entered into on or before March 31, 2012.

Agri-Quebec

Under the AgriInvest program, farmers who contribute to an account receive matching government contributions. The government contributions and interest earned are not taxable until withdrawn from the account. This budget proposes to provide the same income tax treatment to investments made to the new Agri-Quebec program as is currently provided for investments under the AgriInvest program. These new rules will apply to 2011 and subsequent years.

Donation of publicly listed flow-through shares

Under current rules, when flow-through shares are donated to a charitable organization, the donor benefits from:

- the deduction for the expenses flowed through from the corporation
- applicable federal and provincial mineral exploration flow-through tax credits
- the charitable donations tax credit or deduction in respect of the value of the shares; and
- relief from capital gains tax, including tax on the portion of the gain attributable to the zero cost for the shares.

The net result is that the taxpayer can often acquire and donate flow-through shares at little after-tax cost.

The budget proposes allowing the exemption from capital gains tax only to the extent that the cumulative capital gains in respect of the disposition of the shares exceed the original cost of the flow-through shares. This measure applies to shares acquired pursuant to a flow-through share agreement entered into on or after March 22, 2011.

Donation of property under an option agreement

The budget proposes to clarify that the charitable donation tax credit or deduction is not available to a taxpayer in respect of granting an option to a charity to acquire property of the taxpayer until the charity actually acquires the property. The taxpayer will be allowed the tax credit or deduction at that time based on the amount by which the fair market value of the property exceeds the amount, if any, paid by the charity for the option and the property. This measure will apply to options granted on or after March 22, 2011.

Donation of non-qualifying securities

The budget proposes that the donation of a non-qualifying security (NQS) to a charity will not give rise to a charitable donation tax credit or deduction, until such time (within five years of the donation) as the charity disposes of the NQS for consideration that is not another NQS. This measure will apply to securities disposed of by charities on or after March 22, 2011.

Returned donations

The budget proposes to permit reassessments to disallow a taxpayer's claim for a tax credit or deduction, in cases where property is returned to the donor. When property for which the taxpayer received an official donation receipt is returned, the charity must issue a revised receipt. The budget proposes to require the charity to send the revised receipt to CRA when the amount of the receipt has changed by more than $50. This measure will apply in respect of gifts or property returned on or after March 22, 2011.

CORPORATE TAX MATTERS

Corporate income tax rates

There were no changes announced with respect to corporate income tax rates in this budget. The effective rates for 2011 and subsequent years are shown in the following table.

Year	Small business rate	General corporate rate
2011	11%	16.5%
2012	11%	15%

The federal government has confirmed that it still wants to achieve a maximum combined federal-provincial corporate income tax rate of 25% by 2012.

Temporary incentive for manufacturing and processing equipment

Manufacturing and processing machinery and equipment acquired after March 18, 2007, and before 2012, is currently eligible for temporarily accelerated capital cost allowance (CCA). This temporary increase, from 30% to 50% straight-line (subject to the half-year rule), results in a full write-off of qualifying new M&P equipment costs over three years.

In order to provide further stimulus to the manufacturing sector, this budget proposes to extend applicability of the 50% straight-line method to acquisitions in 2012 and 2013. The half-year rule will continue to apply, resulting in a full write-off of the cost of qualifying M&P equipment over three years. Acquisitions after 2013 will be included in Class 43, subject to a 30% declining balance rate of CCA.

Corporate tax deferral using partnerships

The budget proposes to limit deferral opportunities for certain corporations that earn income through a partnership structure. Similar changes were introduced in 1995 with respect to individuals who earned business or professional income through a partnership or proprietorship. The budget proposes to require a corporation with more than a 10% interest in a partnership to accrue the partnership's income for that period of the partnership's fiscal year that falls within the corporation's taxation year. The additional income in the first year may be brought into the corporation's income over a five-year period. This measure will apply to taxation years of a corporation that end after March 22, 2011.

Hiring credit for small business

The budget proposes a one-time credit of up to $1,000 to offset a small business's increase in 2011 Employment Insurance (EI) premiums over those paid in 2010. This new credit will be available to employers whose EI premiums were $10,000 or less in 2010.

Employee profit sharing plans

Employee Profit Sharing Plans (EPSPs) have recently been used as a means of avoiding payment of Canada Pension Plan contributions and Employment Insurance premiums on employee compensation. The budget indicates that the government intends to review the current rules with regard to EPSPs to ensure that they remain a useful vehicle for employers, and to engage in consultations with stakeholders before proceeding with any proposals to change the applicable rules.

Various other tax measures

The budget proposes various other measures that are applicable to specific industry sectors and large business enterprises. These proposed measures include:

- accelerated capital cost allowance provisions for clean energy generation
- extension of the definition of Qualifying Environmental Trust (QET) for the purposes of the Income Tax Act
- better alignment of deduction rates for intangible costs in the oilsands sector with those in the conventional oil and gas sector; and
- extending the application of the stop-loss rules to certain transactions occurring on or after March 22, 2011, in respect of the redemption of certain types of shares not previously caught under the stop-loss rules.

OTHER PROPOSALS

Guaranteed income supplement

The budget proposes to increase benefits for those seniors who rely almost exclusively on Old Age Security and Guaranteed Income Supplement. This proposed measure will provide top-up benefits of up to $600 annually for single seniors and $840 for couples.

Student loan forgiveness

The budget proposes to forgive up to $40,000 of the federal component of Canada Student Loans for new family physicians and up to $20,000 for nurse practitioners and nurses as a means of attracting more health care workers to underserved rural and remote communities. No further details on this provision were provided.

Eco-energy retrofit program

The budget proposes to provide an additional $400 million for a one-year extension of this program, which encourages home renovations that reduce electricity and heating costs.

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