TAX FLASH BULLETIN

2019 Federal Budget Highlights

On March 19, 2019, Federal Finance Minister Bill Morneau tabled the Liberal government's federal budget. The minister forecasts a $14.9 billion deficit for the current fiscal year versus the $19.4 billion deficit estimated in last year's budget. The proposed budget projects a $19.8 billion deficit for the 2019-2020 fiscal year and $19.7 billion deficit for the 2020-2021 with no forecast to return to a balanced budget by 2023-2024. We have highlighted selected income tax changes that affect Canadian individuals and businesses.

INDIVIDUALS

Personal Tax Rates

The budget did not propose any changes to individual income tax rates. The taxable income figures below reflect the indexed income brackets for 2018 and 2019.

2018 Taxable Income	2018 Tax Rates	2019 Taxable Income	2019 Tax Rates
$0 to $46,605	15%	$0 to $47,630	15%
$46,605 to $93,208	20.5%	$47,630 to $95,259	20.5%
$93,208 to $144,489	26%	$95,259 to $147,667	26%
$144,489 to $205,842	29%	$147,667,to $210,371	29%
Over $205,842	33%	Over $210,371	33%

Limitations on Stock Option Benefits

The government announced its intention to limit the preferred tax treatment of employee stock option benefits. Currently, a 50% deduction applies to exercised stock options such that the employment benefit income (fair market value less exercise price) is treated similar to capital gains for tax purposes. The government recognizes that this alternative form of compensation provides a major tax break to the highest earning employees of large, mature corporations, rather than to start-up business employees. The government intends to limit the preferred tax treatment for employees of "large, long-established, mature firms" by capping the value of employee stock option grants at $200,000 per year based on the fair market value of the underlying shares. Employees of start-ups and Canadian growth companies will not be subject to the cap.

The budget did not provide further details to define these terms, nor an effective date. More information will be provided before the summer of 2019. The budget indicated any new measures would be applied on a prospective basis and would not apply to stock options granted before any legislative proposal date. Thus, there is no need to accelerate the exercise of existing stock options grants to continue to benefit from the 50% deduction. If this measure is enacted by the current or future governments, large corporations should review the after-tax impact on key employee compensation and consider equalizing accordingly.

Introduction of Canada Training Benefit

The budget introduces a refundable tax credit called the Canada Training Benefit to financially support ongoing learning for working Canadians. Eligible individuals will accumulate a $250 tax credit each year in a notional account which helps pay for up to half the cost of eligible tuition and fees associated with training.

In order to accumulate the $250 credit each year, the individual must:

- file a tax return for the year;
- be at least age 25 and less than age 65 at the end of the year;
- be a resident of Canada throughout the year;
- have earnings of $10,000 or more in the year from employment, self-employment, parental insurance benefits, or taxable scholarship income (subject to annual indexation); and
- not have net income in the year in excess of the top of the third tax bracket ($147,667 in 2019).

Unused credits may be carried forward and accumulated up to a maximum amount of $5,000 over an individual taxpayer's lifetime. Any unused balance will expire at the end of the year in which the individual turns age 65.

Eligible tuition and other fees for the training benefit will parallel the existing rules for claiming the tuition tax credit. However, the educational institution must be located in Canada. Eligible institutions include universities, colleges, and courses at a post-secondary level, plus institutions providing occupational skills courses certified by the Minister of Employment and Social Development. The portion of tuition and fees refunded through the training credit is not claimable as a tuition tax credit. The credit is not tied to an employer which means it can be used to enhance current career skills or train for a new career.

The government proposes this measure to be effective for the 2019 and subsequent taxation years so that the first accumulation begins in respect of the 2019 taxation year and the credit may be claimed for eligible expenses for the 2020 taxation year.

Enhancement to RRSP Home Buyers' Plan

Previously, first-time homebuyers were able to withdraw up to $25,000 from their RRSPs without tax to fund the purchase of a house. This amount was then repayable into the RRSP over a number of years. The withdrawal limit has been increased to $35,000. The maximum repayment period remains at fifteen years. The increase to the HBP limit will apply to the 2019 and subsequent calendar years.

Access to the Home Buyers' Plan has also been expanded and it is now available to Canadians who have experienced marital breakdown and have lived apart from their spouse or common law partner for at least 90 days. This amendment applies for taxation years after 2019. The individual will be required to dispose of their previous principal place of residence within two years after the end of the year they withdraw the HBP to purchase a new home. The requirement to dispose of the previous principal place of residence will be waived for individuals who buy out the share of the residence owned by the individual's spouse or common-law partner.

From a long-term financial planning perspective, it is important to consider the loss of tax deferred growth opportunities when using RRSP funds to purchase a first home. The RRSP repayments in addition to regular mortgage payments will also stress the cash flow of the homeowners. Prospective homebuyers should consider deferring their home purchase for one or two years to increase their down payment savings rather than borrowing funds from their RRSP accounts.

Changes to TFSA Tax Liability

Individuals determined to be carrying on a business in their tax-free savings account (TFSA) through activities such as "day-trading" are subject to income tax. Currently, the trustee of the TFSA (financial institution) is jointly and severally liable with the TFSA for Part I tax, while the TFSA holder is not liable. The budget now extends the joint and several liability of income tax to the TFSA holder. The liability of the trustee will be limited to the assets held in the TFSA and any distributions made on or after the date the notice of assessment is sent. This measure will apply to 2019 and subsequent taxation years.

Improvements to Registered Disability Savings Plans (RDSP)

After an RDSP beneficiary ceases to qualify for the disability tax credit (DTC), the account generally has to be closed by the end of the year following the first full year throughout which the beneficiary is not eligible for the DTC. The RDSP may remain open for another four years if the plan holder elects to extend the period by obtaining certification from a medical practitioner that the beneficiary is likely to be eligible for the DTC in the future. The budget proposes to eliminate the time limitation on an RDSP after DTC ineligibility and to eliminate the requirement to obtain medical certification on probable future disability. This measure will allow the RDSP beneficiary to ultimately collect any grants and bonds earned during the DTC eligible periods provided the 10-year requirement has passed.

The general rules for DTC ineligible beneficiaries will continue to apply to the RDSP. No contributions may be made and the beneficiary is not entitled to new grants and savings bonds with respect to any year throughout which the beneficiary is not eligible for the DTC.

This measure will apply after 2020 and RDSP issuers are not required to close RDSPs after March 19, 2019 and before 2021 due to DTC ineligibility.

Addition of Annuity Types to Retirement Plans

The budget proposes to permit two new types of annuities under the tax rules for certain registered plans:

- advanced life deferred annuities will be permitted under a registered retirement savings plan (RRSP), registered retirement income fund (RRIF), deferred profit sharing plan (DPSP), pooled registered pension plan (PRPP) and defined contribution registered pension plan (RPP); and
- variable payment life annuities will be permitted under a PRPP and defined contribution RPP.

The measures will apply to the 2020 and subsequent taxation years. Draft amendments will be released for public comment.

Restrictions on Individual Pension Plan (IPP) Pensionable Service

Current tax rules allow a taxpayer to transfer 100% of the commuted value of an employer defined benefit pension plan to an Individual Pension Plan established by the taxpayer's private corporation. Without an IPP, a taxpayer generally has the option to transfer the commuted value into another employer's defined benefit plan or transfer a portion of the commuted value subject to a transfer limit (about 50%) to an RRSP and pay taxes on the balance of the value.

To prevent a taxpayer from gaining an advantage through the use of an IPP, the budget proposes to limit IPPs from providing retirement benefits for past years of employment that were pensionable service under a defined benefit plan of an employer other than the IPP's participating employer or its predecessor employer. Any transfers to an IPP regarding a prohibited service year will be considered a non-qualifying transfer subject to taxation for the individual.

This measure is effective for pensionable service credited under an IPP on or after March 19, 2019.

BUSINESSES

The budget does not propose any changes to the federal corporate income tax rates and the $500,000 small business limit.

Federal Corporate Tax Rates

Income Type	2018	2019	2020
General corporate income	15.00%	15.00%	15.00%
Small business income	10.00%	9.00%	9.00%
CCPC* investment income	38.67%	38.67%	38.67%
Non-CCPC investment income	15.00%	15.00%	15.00%
Manufacturing & processing income	15.00%	15.00%	15.00%

*Canadian Controlled Private Corporation

Extension of Small Business Limit for Farming and Fishing

Farming and fishing activities are generally entitled to the small business income tax rates for income less than $500,000. Certain income earned by a CCPC from sales to private corporations with which a specified person holds a direct or indirect interest are not eligible for small business tax rates. However, the income arising from sales to a farming or fishing cooperative corporation remains eligible for the small business rates.

The budget proposes to eliminate the requirement that sales be to a farming or fishing cooperative corporation in order to benefit from the lower tax rates. Sales of farming products or fishing catches by farming or fishing businesses to any arm's length purchaser corporation are eligible. However, consistent with the existing rules, amounts allocated to a CCPC as patronage payments from a purchaser corporation will not qualify for this exclusion. This measure will retroactively apply to taxation years that begin after March 21, 2016.

Elimination of Scientific Research and Experimental Development (SR&ED) Income Thresholds

The budget proposes to eliminate the use of taxable income as a factor in determining a CCPC's annual expenditure limit for the purpose of the enhanced SR&ED tax credit. Small CCPCs with taxable capital of up to $10 million will benefit from unrestrained access to the enhanced refundable SR&ED credit regardless of their taxable income. As a CCPC's taxable capital begins to exceed $10 million, this access will be gradually phased out. This measure will apply to taxation years that end on or after March 31, 2019.

Accelerated Capital Cost Allowance (CCA)

The government previously announced accelerated capital cost allowance measures in the November 21, 2018 economic statement. The budget confirms the government intends to proceed with these measures which are available to businesses of all sizes, across all sectors of the economy. Accelerated CCA allows the full expensing of the cost of manufacturing and processing machinery and equipment and specified clean energy equipment on a temporary basis for equipment acquired after November 20, 2018 and is available for use prior to 2024. An accelerated investment incentive provides a temporary enhanced CCA deduction of up to three times the normal first-year CCA deduction for other capital assets subject to the current half-year CCA rules (with a few exceptions) acquired after November 20, 2018 and before 2024. Then CCA is reduced to two times the normal first-year CCA in the years 2024 to 2027.

The budget also proposes a full tax-write off of up to $55,000 plus tax per vehicle for businesses that purchase zero-emission vehicles on or after March 19, 2019 and before January 1, 2024. Eligible vehicles include electric battery, plug-in hybrid (with a battery capacity of at least 15 kWh) or hydrogen fuel cell vehicles, including light-, medium- and heavy-duty vehicles.

CORPORATE HEAD OFFICES: RAYMOND JAMES LTD.
SUITE 2100 – 925 WEST GEORGIA ST. // VANCOUVER, BC V6C 3L2 // 604-659-8000
SUITE 5300 – 40 KING STREET WEST // TORONTO, ON M5H 3Y2 // 416-777-7000
LIFEWELLPLANNED.CA

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