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Assante® WEALTH MANAGEMENT

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MONEY *matters*

IMPACT OF BUDGET 2016 ON YOUR FINANCIAL PLANNING

Finance Minister, Bill Morneau, presented the first federal budget of prime minister, Justin Trudeau's Liberal government on March 22, 2016.

Budget 2016 included a big emphasis on infrastructure spending, eliminated certain tax credits and advantages and tried to eliminate tax structures that abused the system. Other significant changes introduced in this budget included the introduction of a new method of depreciation of eligible capital property and reduction of the eligibility age for Old Age Security and Guaranteed Income Supplement from 69 to 65.

According to the new budget, a deficit of $5.4 billion is expected for Canada in 2015-2016, which will grow to $29.4 billion in 2016-2017 and will gradually decrease after that with no indication of when Canada will have a balanced budget again.

A detailed explanation of the significant tax measures proposed in Budget 2016 that would have an impact on your personal financial planning follows below.

PERSONAL TAX MEASURES

New Canada Child Benefit

In an effort to provide more benefits to lower-and-middle income families, Budget 2016 proposed to replace the current Canada Child Tax Benefit (CCTB) and the Universal Child Care Benefit (UCCB) with a new Canada Child Benefit (CCB).

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"According to the government the new Canada Child Benefit will help nine out of ten families save an estimated $2,300 a year."

The Canada Child Benefit provides greater benefits for families at lower income levels and is tax-free. It will start on July 1, 2016 and will provide a non-taxable maximum benefit of $6,400 per child under the age of six and $5,400 per child for children who are age six through 17. If a child is eligible for the disability tax credit, the CCB maximum is increased by an additional $2,730. The CCB maximum benefit levels will be reduced based on family income and the number of children in the family.

According to the government the new Canada Child Benefit will help nine out of ten families save an estimated $2,300 a year. It would therefore be prudent for families with children who are 17 and under to funnel their tax savings into a Registered Education Savings Plan (RESP) to save for their children's higher education and take advantage of the 20% Canada Education Savings Grant (CESG) that the government will pay on up to $2500 of annual savings in an RESP.

Elimination of Family Tax Cut

The Conservative government of Stephen Harper had enacted the family tax cut that allowed income splitting between spouses. This would allow a higher-income spouse with at least one child under 18 to notionally transfer up to $50,000 of taxable income to his/her spouse or common-law partner, in order to reduce the couple's total income tax liability by up to $2,000.

Budget 2016 proposed to eliminate the family tax cut effective for 2016 and future taxation years.

Elimination of Education and Textbook Tax Credits

According to Budget 2016, starting in 2017, the education and textbook tax credits will be eliminated. However, any unused education and textbook tax credits carried forward from years before 2017 will remain available to be claimed in 2017 and subsequent years.

Taxation of Fund Switches in Corporate Class Mutual Funds

Currently, switching funds in a mutual fund corporation (commonly referred to as Corporate Class Mutual Funds) will not trigger any taxes and the Income Tax Act does not deem the exchanges to be dispositions for income tax purposes.

Budget 2016 surprised the investment community by proposing to amend the Income Tax Act so that starting September 2016 an exchange between different classes of funds in mutual fund corporations will be deemed to be a disposition at fair market value.

If the shares that are exchanged only differ in respect of management fees or expenses borne by the investor, and otherwise drive their value from the same fund or portfolio within the mutual fund corporation, then the proposed changes will not apply.

Taxation of Linked Notes

An equity linked note is a debt instrument whose return is determined by the performance of a single equity security or stock, a basket of stocks, or an equity index.

It has been a common practice for investors in linked notes to sell the notes prior to maturity. By doing so they were able to convert the tax treatment of the return from interest income to capital gains. Based on Budget 2016, for linked notes offered after September 2016, the return on a linked note will be treated as interest income whether it is earned at maturity or through a sale on a secondary market before maturity.

Return of the Labour-Sponsored Venture Capital Corporations (LSVCC) Tax Credit

The federal Labour-Sponsored Venture Capital Corporations (LSVCC) tax credit was introduced in the 1980s when access to venture capital for small and medium-sized businesses was limited. However, the economic environment and the structure of the venture capital market have changed significantly since that time.

While the federal tax credit for federally registered LSVCCs will remain at five percent for the 2016 taxation year and will be eliminated for the 2017 and subsequent tax years, Budget 2016 proposed to restore this tax credit to 15 per cent for share purchases of provincially registered LSVCCs for 2016 and subsequent taxation years.

Ontario Electricity Support Program

The Ontario Electricity Support Program (OESP) will provide assistance to low-income households in Ontario for the cost of electricity effective January 1, 2016. The OESP, which is based on household income and the number of people living in the household, will provide a non-taxable monthly credit on a tax payer's electricity bill.

Mineral Exploration Tax Credit for Flow-Through Shares Investors

According to Budget 2016, the eligibility for the mineral exploration tax credit will be extended for one year, to flow-through share agreements entered into, on or before March 31, 2017.

This tax credit provides investors in mining flow-through shares with a credit equal to 15 per cent of specified mineral exploration expenses incurred in Canada.

Retirement Income Improvements

Budget 2016 included a number of welcome improvements to retirement income provisions for Canadians including the following:

1- Guaranteed Income Supplement (GIS) for low-income single seniors will be increased.
2- The Canada Pension Plan (CPP) will be enhanced and the government's goal is to make a collective decision in this regard with the provinces and territories before the end of 2016.
3- Old Age Security benefit will start at 65 years old instead of at 67.
4- Benefits will be increased for senior couples who live apart for health or other reasons in recognition of the fact that they face higher expenses.

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Increase in Canada Student Grant

Budget 2016 proposed to increase Canada Student Grant amounts by 50 per cent, from $2,000 to $3,000 a year for low-income families; from $800 to $1200 per year for middle-income families; and from $1,200 to $1,800 for part-time students.

Setback for Charitable Donations

While the measure announced in Budget 2015 that provided an exemption from capital gains for certain dispositions of private corporation shares or real estate where the cash proceeds from the disposition are donated to a registered charity within 30 days drew cheers from the charitable sector, Budget 2016 announced the government's intention not to proceed with this measure.

Therefore, if you had done any estate planning based on this tax measure you would need to revise your planning based on the new changes proposed in Budget 2016.

Increase in Top Tax Rate on Personal Service Business Income

As a result of the new top marginal personal income tax rate being increased to 33% effective January 1, 2016, a federal tax rate increase form 28% to 33% on personal service business income earned by a corporation is proposed to be introduced to the Income Tax Act. Therefore, the combined corporate income tax rate in Ontario will increase to 44.5% on personal service business income.

BUSINESS TAX MEASURES

Small Business Tax Rate

Based on previous budgets the federal small business tax rate applicable on the first $500,000 of business income earned by a Canadian-controlled private corporation (CCPC) had been legislated to reduce to 9%. However, despite an election promise to reduce the small business tax rate over the next three years, Budget 2016 not only did not include any reductions to the small business tax rate but instead proposed to cancel these previously legislated reductions and to keep the small business tax rate at 10.5 per cent after 2016.

Multiplication of Small Business Deduction

For years, skilled and experienced accountants had helped their small business owner clients multiply their $500,000 small business deduction through creative and complicated tax planning. Budget 2016 put an end to this type of planning and proposed to prevent business owners from multiplying access to the $500,000 small business deduction through the use of complex partnerships and corporate structures effective March 22, 2016.

Life Insurance Policies

Going forward, the government is planning to close loopholes that allow private corporations to use a life insurance policy to distribute amounts tax-free that would otherwise be taxable.

Transfer of an interest in a life insurance policy to a corporation will be affected by this change in rules. Budget 2016 proposed to amend the Income Tax Act to ensure that when a disposition of an interest in a life insurance policy happens, the amounts are not received tax-free by a policyholder. While in the past proceeds of disposition of the policy were equal to the policy's cash surrender value, after March 22, 2016 the fair market value of any consideration received in exchange for an interest in a life insurance policy will be included in the policyholder's proceeds of disposition.

CONSIDER PRESCRIBED ANNUITIES BEFORE TAX CHANGES IN 2017

Income Tax regulation 304 prescribes that certain annuity contracts be exempted from accrual rules (where all growth has to be taxed annually) when it comes to their income reporting requirement, hence the term prescribed annuities. Therefore, non-registered prescribed annuities have served as a very tax effective source of guaranteed retirement income for Canadian retirees.

Annuity payments are based on life expectancy. The longer the life expectancy of the annuitant, the smaller the annuity payments would be and vice versa, the shorter the life expectancy, the bigger the payments.

Currently, the life expectancy rates used for non-registered prescribed annuities are based on life expectancy rates included in 1971 Individual Annuity Mortality Tables (IAM). Based on new changes to the Income Tax Act, starting in January 1, 2017, life expectancy for prescribed annuities will be updated and will be based on the Annuity 2000 Basic Mortality Tables. Since longevity has increased in the past few decades, the new tables include longer life expectancies. Since annuity payments are a blend of return of capital and interest, this will reduce the portion of each payment that will be treated as a return of capital, as the principal portion has to be spread over a longer period. As a result, each prescribed annuity payment on contracts purchased after January 1, 2017 will have a higher taxable portion.

Therefore, if you are contemplating the use of prescribed annuities in your financial and retirement planning you should discuss the impact of these changes with your financial advisor and try to make a decision before the end of 2016 to be able to take advantage of the existing preferential tax rates applicable to prescribed annuities.

2016 BRINGS NEW FLEXIBILITY FOR CHARITABLE DONATIONS ON DEATH

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You may have heard about recent changes to the tax rules that apply to charitable giving on death, which was mentioned in our December 2015 newsletter. Generally speaking, these changes are positive for donors (and, it follows, charities) in providing new flexibility for donors and their estates when it comes to the tax treatment of their donations.

Previously, the old tax rules distinguished between donations made through a donor's will on the one hand, and the donor's estate, on the other. Donation tax credits for donations made through a donor's will could only be used to lower the deceased donor's tax

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liability in the year of death or the year preceding death. Donation tax credits for donations made by the donor's estate could only be used in the year the donation was made (which could be several years after the year of death) or the five years after the year of donation. In many cases, it was more tax-efficient for a donation to be considered to have been made through the donor's will since: (a) a deceased donor's tax bill can often be significant in the year of death; and (b) the donation tax credit rate is increased from 75% of annual net income to 100% for donations made in the year of death or the year before that. However, whether a donation was made through a donor's will or by the donor's estate was not always straightforward and certain requirements had to be met in order for a donation to be considered to have been made through a donor's will for tax purposes.

Under the new rules that came into effect on January 1, 2016, for all deaths occurring after December31, 2015, all donations made by a deceased donor – whether through his or her will, by beneficiary designation or by his or her estate – will be considered for tax purposes to have been made by his or her estate. If the donor's estate is a qualifying estate* (or, where certain conditions are met, a former qualifying estate), the donor's executor will have the flexibility to allocate any donations made by the deceased donor to any of the following tax years:

- The year the donation is made
- Any year of the donor's estate before the gift is made (under recent federal government proposals, an executor will not be able to allocate donations to these years if the donor's estate is a former qualifying estate)
- The year of death
- The year before the year of death
- Any five years after the donation is made

Under the new rules, executors will generally have much more flexibility to allocate donation tax credits to the tax years where they are needed the most as long as the donor's estate is a qualifying estate. In many cases, this will result in less overall tax paid by the donor's estate and more funds available for distribution to the deceased donor's loved ones.

**Very generally, a qualifying estate is a deceased individual's estate where no more than 36 months have passed since the individual's death and the executor has designated the estate as the individual's "graduated rate estate" in the estate's first tax return.*

NOT TO BE FRAMED - ART NIGHT ON MARCH 10, 2016

On March 10, 2016, we held our third Art Night event on the occasion of International Women's Day on March 8th. This event featured the works of four talented young women artists of Iranian origin who are all members of the Matrix Art Collective. Works by Samira Alborzkouh, LelylaFathizadeh, YaldaKhajehzadeh and Sara Niroobakhsh were displayed and two of the artists, Leyla and Sara were present at the event to greet over 80 guests. You can view the works and see pictures of the event at http://www.art.maison/not-to-be-framed/

From left to right: Leila Fathizadeh, Tina Tehranchian, and Sara Niroobakhsh

ABOUT THE EDITOR

Tina Tehranchian MA, CFP, CLU, CHFC, is a Branch Manager and Senior Financial Planner with Assante Capital Management Ltd., one of Canada's largest wealth management firms, offering integrated financial solutions to create wealth and prosperity for you and your family. The 750 advisors serve over 300,000 Canadian families across the country and take pride in the exceptional service they offer to clients through trusted face-to-face relationships and a level of service excellence second to none. Money Matters is published as a special service for clients of Tina Tehranchian.

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- Camille Jordann