TAXBULLETIN
WILKINSON TAX GROUP

Finance Minister Bill Morneau delivered the Liberal Government's second budget on March 22, 2017 ("Budget Day"). The Budget anticipates a deficit of $28.5 billion for 2017-2018 and projects that by 2022 the deficit will drop to $18.8 billion.

The major spending announcements in the budget include amounts for infrastructure, indigenous communities, creation of new child care spaces and innovation.

The tax changes did not include an increase in the capital gains inclusions rate despite much speculation that it would. There are also no major tax changes that affect large groups of taxpayers although there are several targeted measures that will have significant impacts on professionals and financial institutions.

The biggest announcement from a tax perspective is the announcement to review various tax planning strategies commonly utilized by private corporations. Needless to say, we will pay close attention to developments in this area.

Details of the key tax highlights of the budget are as follows.

Personal Income Tax Measures

Disability Tax Credit - Certification

The Disability Tax Credit (or DTC) is a credit available for individuals who suffer from a severe and prolonged impairment in physical or mental functions. In order to qualify, the disability must by certified by a certain medical practitioners (typically medical doctors or specialists in the relevant field of medicine).

Budget 2017 proposes to add nurse practitioners to the list of medical practitioners that could certify eligibility for the disability tax credit. A nurse practitioner would be permitted to certify for all types of impairments that are within the scope of their practice.

This measure will apply to disability tax credit certifications made on or after Budget Day.

Medical Expense Tax Credit – Eligible Expenditures

Currently in order to claim the medical expenses for the use of reproductive technologies, the individual must have an existing illness or condition related to the infertility.

Budget 2017 proposes to clarify the application of the medical expense tax credit so that individuals who require medical intervention in order to conceive a child are eligible to claim the same expenses that would generally be eligible for individuals on account of medical infertility.

This measure will apply to the 2017 and subsequent taxation years. A taxpayer will be entitled to elect in a year for this measure to apply for any of the immediately preceding ten taxation years in their return of income in respect of the year.

Consolidation of Caregiver Credits

Currently tax relief for caregivers includes three credits, with varying eligibility conditions based on the circumstances of the caregiver and the dependant. The infirm dependant credit, the caregiver credit and the family caregiver tax credit.

Budget 2017 proposes to simplify the existing system of tax measures for caregivers by replacing the existing credits with a new Canada Caregiver Credit.

Budget 2017 proposes that the new Canada Caregiver Credit amount will be:

- $6,883 in respect of infirm dependants who are parents/grandparents, brothers/sisters, aunts/uncles, nieces/nephews, adult children of the claimant or of the claimant's spouse or common law partner.
- $2,150 in respect of
  - an infirm dependent spouse or common-law partner in respect of whom the individual claims the spouse or common-law partner amount,
  - an infirm dependant for whom the individual claims an eligible dependant credit, or
  - an infirm child who is under the age of 18 years at the end of the tax year.

These amounts are consistent with the amounts that could have been claimed in respect of these dependants under the current caregiver credit and family caregiver tax credit, respectively. The Canada Caregiver Credit will be reduced dollar-for-dollar by the dependant's net income above $16,163. The dependant will not be required to live with the caregiver in order for the caregiver to claim the new credit. The Canada Caregiver Credit will no longer be available in respect of non-infirm seniors who reside with their adult children.

The Canada Caregiver Credit will apply for the 2017 and subsequent taxation years

Mineral Exploration Tax Credit for Flow-Through Share Investors

The Government proposes to extend eligibility for the mineral exploration tax credit for an additional year, to flow-through share agreements entered into on or before March 31, 2018.

Electronic Distribution of T4 Information Slips

Budget 2017 proposes to allow employers to distribute T4 (Statement of Remuneration Paid) information slips electronically to current active employees without having to obtain express consent from those employees in advance. An employer will be required to have sufficient privacy safeguards in place before electronic T4s can be sent without express consent.

This measure will apply in respect of T4s issued for the 2017 and subsequent taxation years.

Tuition Tax Credit

Currently, a tuition tax credit is not available for occupational skills courses that are offered by a university, college or other post-secondary institution and that are not at the post-secondary level.

Budget 2017 proposes to extend the eligibility criteria for these types of courses to those institutions.

Budget 2017 also proposes to extend eligibility as a "qualifying student" to individuals in the specific circumstances described above, who otherwise meet the conditions to be a "qualifying student". Whether or not an individual is a "qualifying student" is relevant for the tax exemption for scholarship and bursary income.

This measure will apply to the 2017 and subsequent taxation years.

Ecological Gifts Program

The Ecological Gifts program provides a way for Canadians with ecologically sensitive land to benefit from special tax assistance on the donation the property.

Budget 2017 proposes the following measures in order to better protect gifts of ecologically sensitive land:

Transfers of Ecogifts
Where ecogifts are transferred between organizations for consideration a tax of 50 per cent of the fair market value of the land may be imposed upon a recipient who, without the consent of Environment and Climate Change Canada (ECCC), changes the use of the property or disposes of it.

Budget 2017 proposes that the transferee (and not the recipient) of the property in such a situation be subject to the 50-per-cent tax if the transferee changes the use of the property, or disposes of the property, without the consent of ECCC.

Program Administration
Budget 2017 proposes that the Minister of ECCC has the ability to determine whether proposed changes to the use of lands would degrade conservation protections.

Approval of Recipients
Currently the Minister of ECCC must approve a registered charity as the recipient of an ecogift on a gift-by-gift basis. Budget 2017 proposes that the requirement to approve recipients be extended, on a gift-by-gift basis, to municipalities and municipal and public bodies performing a function of government.

Private Foundations
Budget 2017 proposes that private foundations no longer be permitted to receive ecogifts.

These measures will apply in respect of transactions or events that occur on or after Budget Day.

Public Transit Tax Credit

A public transit tax credit is currently available in respect of the cost of eligible public transit passes, which include annual and monthly passes, as well as weekly passes and electronic fare cards that are used on an ongoing basis.

Budget 2017 proposes to eliminate the public transit credit, effective July 1, 2017. The cost of public transit passes and fare cards that are attributable to use after June 2017 will no longer be eligible for the credit.

Allowances for Members of Legislative Assemblies and Certain Municipal Officers

Generally allowances received by individuals that do not have to provide details or supporting receipts to justify the amount paid are required to be included in income as a taxable benefit.

Currently the following officials are not required to include these amounts, within limits, in computing their income for tax purposes:

- Elected members of provincial and territorial legislative assemblies and officers of incorporated municipalities;
- Elected officers of municipal utilities boards, commissions, corporations or similar bodies; and
- Members of public or separate school boards or of similar bodies governing a school district.

Budget 2017 proposes to require that these allowances be included in income for 2019 and subsequent years.

Home Relocation Loans Deduction

Currently when an employee receives a loan as a result of their employment, and the interest rate on the loan is lower that the prescribed rate, that individual is deemed to have received a taxable benefit calculated by reference to the difference between the two rates. However if the employee has received a loan, for up to $25,000, as a result of a requirement for them to relocate as a result of moving to a new work location and the new residence is at least 40 km closer to the new work location that the old residence, they are eligible to deduct the benefit from their taxable income.

Budget 2017 proposes to eliminate this deduction for 2018 and subsequent years.

Anti-avoidance Rules for Registered Plans

A number of anti-avoidance rules exist for Tax-Free Savings Accounts, Registered Retirement Savings Plans and Registered Retirement Income Funds to help ensure that the plans do not provide excessive tax advantages unrelated to their respective basic objectives including:

- the advantage rules, which help prevent shifting returns from a taxable investment to a registered plan; and
- the prohibited and non-qualified investment rules, which restrict the classes of investments that may be held by a registered plan.

Budget 2017 proposes to extend the above mentioned anti-avoidance rules to Registered Education Savings Plans and Registered Disability Savings Plans. Subject to the following exceptions, this measure will apply to transaction occurring, and investments acquired, after budget day.

The exceptions to the effective date include:

- The advantage rules will not apply to swap transactions undertaken before July 2017. However, swap transaction undertaken to ensure that an RESP or RDSP complies with the new rules will be permitted until the end of 2021.
- Subject to certain conditions, a plan holder may elect by April 1, 2018 to pay regular tax in lieu of the advantage tax on distributions from an investment held on Budget Day that becomes a prohibited investment as a result of this measure.

Business Income Tax Measures

Tax Planning Using Private Corporations

The government has identified a number of perceived issues regarding tax planning strategies using private corporations, which can result in certain individuals gaining tax advantages. These strategies include:

Sprinkling Income
Strategies that reduce income taxes by allocating certain corporate distributions (e.g., dividends or capital gains) to lower income family members instead of higher income family members.

Holding a Passive Investment Portfolio Inside a Private Corporation,
It is financially advantageous for owners of private corporations to keep profits in a corporation to invest rather than distributing the profits to shareholders to invest. This is mainly due to the fact that corporate income tax rates, which are generally much lower than personal rates, facilitate accumulation of earnings that can be invested in a passive portfolio.

Converting a Private Corporation's Regular Income into Capital Gains
Capital gains are taxed at a rate that is half of other forms of income. There are a number of strategies that can be utilized in specific circumstances to take advantage of this disparity by arranging distributions to be taxed as capital gains.

The Government is therefore further reviewing the use of these strategies. In doing so, the Government will also consider whether there are features of the current income tax system that have an inappropriate, adverse impact on genuine business transactions involving family members.

The Government intends to release a paper in the coming months setting out the nature of these issues in more detail as well as proposed policy responses. As we have used several of these strategies to benefit our clients, we will pay close attention to developments with respect to this consultation.

Consultation on Cash Purchase Tickets

When a farmer delivers certain grains the operator may pay with a cash purchase ticket. If the cash purchase ticket is payable in the subsequent year, the taxpayer includes the amount of the ticket in income in that following year. This treatment is a departure from the general rule for most other tax payers.

The government believes that with the deregulation of the grain marketing regime and commercialization of the Canadian Wheat Board, the delivery of the listed grains is now the responsibility of private business rather than the federal government. There is arguably no longer a policy rationale for the tax deferral.

Budget 2017 launches a consultation on the income tax deferral available in respect of deferred cash purchase tickets for deliveries of listed grains.

Billed-basis Accounting

Taxpayers are generally required to include the value of work in progress in computing their income for tax purposes. However certain professionals (i.e., accountants, dentists, lawyers, medical doctors, veterinarians and chiropractors) may exclude work in progress in computing their income. The election effectively allows income to be recognized when the work is billed (billed-basis accounting).

This enables taxpayers to defer tax by deducting the costs associated with work in progress without including the related revenues.

Budget 2017 proposes to eliminate the ability for professionals to use billed-basis accounting.

This measure will apply to taxation years that begin on or after Budget Day. A transitional period will be provided to phase in the inclusion of work in progress into income. For the first taxation year that begins on or after Budget Day, 50 per cent of the lesser of the cost and the fair market value of work in progress will be allowed as a deduction in the first year.

Investment Fund Mergers

Budget 2017 proposes various technical rules to extend certain mutual fund merger rules to facilitate the tax-deferred reorganization of mutual fund corporations and segregated funds.

Clean Energy Generation Equipment: Geothermal Energy

Budget 2017 proposes an expansion of the accelerated CCA rates for geothermal energy equipment that is used primarily for the purpose of generating heat or a combination of heat and electricity.

Meaning of Factual Control

The current small business deduction limit of $500,000 must be shared among associated corporations. Based on a recent court decision, the definition of "control in fact" for purposes of determining association has been restricted to an ability to influence the directors or shareholders and not the business on the entity. Budget 2017 serves to re-establish and potentially expand the use of de facto control in determining control for association purposes for taxation years that begin on or after Budget Day.

Insurers of Farming and Fishing Property

Insurers of farming and fishing property benefit from a tax exemption based upon the proportion of their premiums that is earned from the insurance of property used in farming or fishing (including residences of farmers or fishers).

Budget 2017 proposes to eliminate the tax exemption for insurers of farming and fishing property.
This measure will apply to taxation years that begin after 2018.

Investment Tax Credit for Child Care Spaces

The investment tax credit for child care spaces provides a 25-per-cent non-refundable tax credit on costs incurred to for child care spaces for the benefit of a taxpayer's employees' children. The maximum value of the credit is $10,000 per space created.

Budget 2017 proposes to eliminate the investment tax credit for child care spaces.

This measure will apply in respect of expenditures incurred on or after Budget Day. To provide transitional relief, the credit will be available in respect of eligible expenditures incurred before 2020 pursuant to a written agreement entered into before Budget Day.

Additional Deduction for Gifts of Medicine

Corporations that donate medicine from their inventory can claim an additional deduction in excess of the standard deduction for donations.

Budget 2017 proposes to eliminate this additional deduction for gifts of medicine made on or after Budget Day.

Straddle Transactions

A straddle is a transaction in which a person invests in two or more positions that are expected to generate equal and offsetting gains and losses. The taxpayer claims a deduction in respect of the realized loss against other income in the initial taxation year and defers the recognition of the offsetting gain until the following taxation year.

Budget 2017 proposes to defer the realization of any loss on the disposition of a position to the extent of any unrealized gain on an offsetting position.

The stop-loss rule will be subject to a number of exceptions. In particular, it will generally not apply to a position if it is held by a financial institution, certain business hedging transactions, the offsetting position is held for a period of time, or a main purpose is not to defer or avoid tax.

This measure will apply to any loss realized on a position entered into on or after Budget Day.

Elective use of the Mark-to-Market Method

The mark-to-market method allows certain taxpayers to recognize profits and losses on investments as they are accrued rather than realized.

Budget 2017 proposes to introduce an election that will allow taxpayers to mark to market all of their eligible derivatives. Once made, the election will remain effective for all subsequent years unless revoked with the consent of the Minister of National Revenue.

This election will be available for taxation years that begin on or after Budget Day.

Canadian Exploration Expenses

Eligible small oil and gas corporations will no longer be permitted to treat their first $1 million of Canadian Development Expenses (CDE) as Canadian Exploration Expenses (CEE) (which are fully deductible in the year they are incurred) when renounced to shareholders owning flow through shares.

These measures will apply to expenses incurred after 2018.

International Tax Measures

Extending the Base Erosion Rules to Foreign Branches of Life Insurers

Budget 2017 proposes to amend the Income Tax Act to ensure that Canadian life insurers are taxable in Canada with respect to their income from the insurance of Canadian risks. This rule will be modeled on the existing anti-avoidance rule in the FAPI regime.

This measure will apply to taxation years of Canadian taxpayers that begin on or after Budget Day.

Sales and Excise Tax Measures

Taxi and Ride-Sharing Services

Under the GST/HST, all taxi operators are required to register for the GST/HST and charge tax on their fares, even if the total amount of sales they make is less than the normal $30,000 exemption.

Commercial ride-sharing services facilitated by web applications (i.e. Uber) provide passenger transportation services that are similar to taxi services. However, such ride-sharing services may not be subject to the same GST/HST rules that apply to taxi services since they may not meet the GST/HST definition of a taxi business.

Budget 2017 proposes to amend the definition of a taxi business to require providers of ride-sharing services to register for the GST/HST and charge tax on their fares in the same manner as taxi operators.

The amendment will be effective as of July 1, 2017.

Other Sales and Excise Tax Measures

Other measures include:

- Tobacco Taxation
  - Proposed removal of 10.5% surtax on manufacturers; and
  - Proposed increase in excise duty rates.
- Alcohol Taxation
  - Proposed increase in excise duty rates by 2%. Rates to increase with inflation starting April 1, 2018.
- Naloxone
  - Proposed to add drug to list of GST/HST-free non-prescription drugs that are used to treat life-threatening conditions.
- GST/HST Rebate to non-residents for tour package accommodations
  - Proposed repeal of existing rebate (transitional to January 1, 2018 implementation)

Other Measures

The Government of Canada confirms its willingness to discuss and put into effect direct taxation arrangements with interested Aboriginal governments.

The Government of Canada also supports direct taxation arrangements between interested provinces or territories and Aboriginal governments and will continue to facilitate such arrangements.