RBC Wealth Management

INVESTMENT, TAX AND LIFESTYLE PERSPECTIVES FROM RBC WEALTH MANAGEMENT SERVICES

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How tax-related campaign promises may impact you

Platform promises and the potential impacts on Canadians' tax bills

With the Liberals re-elected as a minority government, they will need to seek support from other parties in order to move forward with their agenda. This government has unique challenges ahead as a result of the COVID-19 pandemic and subsequent increase in government spending. Of particular interest will be how the current government intends to manage these expenses and support future growth in the Canadian economy.

The following information focuses on ideas and campaign promises only; it is not advanced knowledge of proposed tax legislation or policy. Prior to making any changes to your plans or implementing any planning strategies, it is important to consult with qualified tax and legal advisors.

Five main potential tax changes to boost revenue

The election brought a number of campaign promises, many of them relating to tax changes and tax credits. Some of the larger tax speculation topics as a result of the election include:

- The capital gains inclusion rate;
- Increase in tax rates or changes in tax brackets;
- New taxes;
- Nuances around the principal residence exemption; and
- Changes to tax credits and deductions.

Increase to the capital gains inclusion rate

While not specifically mentioned in the Liberal platform, increasing the capital gains inclusion rate has been widely debated over the past several years and was included in the NDP platform. This may become an interesting bargaining point between the two parties.

Currently, the capital gains inclusion rate is 50% which means that when a capital gain is realized, only 50% of the capital gain is taxable to you. While the 50% inclusion rate has been consistent for over 20 years, it has fluctuated in the past.

A change to the capital gains inclusion rate would be a relatively simple revenue booster. As an example, currently, a capital gain of $200 would result in tax of $50 (assuming a 50% tax rate) for an individual. If the inclusion rate was 75% (which is what the NDP proposed in their platform), the same $200 capital gain would result in tax of $75.

Key planning points to consider

This may be a good time to speak with your qualified tax advisor on strategies relating to a possible increase in the capital gains rate. Some planning strategies may include:

- Considering the timing for rebalancing your portfolio;
- Transferring appreciated securities to a holding company; and
- Transferring appreciate securities to a spouse or common-law partner.

For more information, ask your RBC advisor for the article on this topic, which delves into these strategies in more detail. If a change to the capital gains inclusion rate is announced, it is not known whether it would be effective immediately, be retroactive or start at a future date. Speak with your qualified tax advisor to explore any opportunities or strategies that may mitigate effects of any potentially adverse tax changes to the capital gains inclusion rate.

Increase in tax rates or changes in tax brackets

This election, like many before it, brought forward platform promises relating to current and future tax rates. There were promises made with respect to both personal tax rates and corporate tax rates.

Personal tax

With the top personal tax bracket in most provinces close to or above 50%, increasing the personal tax rate may not be a popular method to increase revenues. While specifically not in the Liberal election campaign, there's always the possibility of changes or an increase in personal tax rates. The NDP campaigned on increasing the top personal federal tax bracket from 33% to 35%.

The Liberals did campaign on creating a new minimum tax rule so that those who earn enough to qualify for the top tax bracket (earning taxable income over $216,511 for the 2021 year) will pay at least 15% each year. This new minimum tax is meant to eliminate the ability for high-income earners to use excessive deductions and credits to pay little or no tax. While there still needs to be some clarity as to what excessive use of deductions and credits means, if implemented, this could increase the overall tax paid for certain taxpayers. This may also have a significant impact on individuals with a high-income year and a legitimate offsetting deduction or credit, such as a charitable donation or the lifetime capital gains exemption, if it brought their average tax rate down to less than 15%.

Key planning points to consider

Whenever there's an increase in taxes specifically to rates, common tax planning can be an effective way to mitigate some of the impact. Regular tax planning, including RRSP contributions, maximization of all available tax credits and deductions, as well as charitable donations, can help to reduce taxes in a specific year. However, care should be taken if a minimum tax policy is implemented.

Now may also be a good time to investigate more complex tax planning strategies, which may be appropriate with the help of your qualified tax or legal advisors. Some examples may include:

- Family income splitting structures such as a prescribed rate loan to a family trust or a spousal loan, especially given the current 1% prescribed rate;
- Gifting to your adult children to contribute to their TFSA; or
- Tax-exempt life insurance, if you have surplus assets that won't be needed throughout your lifetime.

For more detail on these strategies, ask your RBC advisor for the article on tax planning strategies for high-income earners.

Corporate tax

The Liberals also had a few campaign promises relating to corporate tax changes, especially for large businesses. They intend to increase the corporate income tax rate from 15% to 18% for financial institutions and insurance companies earning over $1 billion per year, and require them to pay a temporary Canada Recovery Dividend. The NDP also promised to increase the corporate tax rate to 18% — with the Liberal and NDP aligned on this rate change, it may be more likely to be implemented.

The Liberals also proposed to limit the amount of interest that certain businesses can deduct, from 40% of their earnings to 30%, for taxation years beginning on or after January 1, 2023. This may increase taxes for highly leveraged corporations with significant interest expenses.

While these proposed changes may increase taxes for some businesses, they are unlikely to have a big impact on small businesses. The government did pass Bill C-208 just prior to the election, which made intergenerational wealth transfer and reorganizations among siblings for small businesses potentially more tax favourable.

Key planning points to consider

Should there ever be an increase in corporate tax rates, you may want to consider planning that can reduce corporate taxes paid. This would include maximizing corporate deductions, as well as considering charitable giving to the extent you are charitably inclined.

If you a have a qualified small business corporation or a family farm or fishing corporation that you intend to transfer to the next generation, or where you're contemplating a reorganization involving siblings, you should consult with your qualified tax advisor to see if you can benefit from the new rules as a result of the passing of Bill C-208.

Introduction of new taxes

Introducing new taxes is a tool governments can use to target a specific demographic or industry. The election wasn't the catalyst for this, as two new taxes were proposed in the 2021 federal budget:

- A luxury tax on the purchase of new personal-use luxury cars, aircrafts and boats. The tax will apply to luxury cars and personal aircrafts with a retail price over $100,000 and to boats with a price over $250,000. This tax change aligns with the NDP's platform where they, too, wanted to put a luxury goods tax in place on things like yachts and private jets.

- A national vacancy tax, which is proposed to be an annual 1% tax on the value of non-resident, non-Canadian owned residential real estate that's considered to be vacant or underused. This may impact those who have residences in Canada but who are not residing in Canada on a regular basis.

Both of these are set to be effective January 1, 2022.

While currently there isn't much planning that can be done to avoid these types of potential taxes, if you think they may impact you, it's important to keep an eye out for more details going forward. As well, you may want to consider the timing of such purchases with the help of your qualified tax advisor.

Speculation around a wealth tax

One of the larger speculative topics over the past year has been in relation to an annual wealth tax. While the Liberals did not touch on any type of a wealth tax throughout their campaign, the NDP campaigned loudly about this type of taxation, wanting to impose a 1% wealth tax for those with over $10 million of wealth. If a wealth tax, or the idea of it, ever gained traction in Canada, it would be an entirely new type of tax for Canadians. Implementation of a tax change of this magnitude would likely take time and due process.

And while a wealth tax would be a new concept in Canada, it has been utilized in other countries around the world. Looking at past examples, France experimented with the implementation of a wealth tax. From 1988 to 2017, France had a wealth tax rate of roughly 1.4% on fortunes larger than $13 million euro. The wealth tax didn't raise the anticipated revenues, with many of the targeted wealthy individuals instead choosing to leave France. This not only left France unable to collect the wealth tax, they also lost the existing tax generated by these ultra-wealthy individuals. It was generally considered to have failed and was repealed in 2017.

Property flipping

In the campaign, the Liberals proposed to introduce an anti-flipping tax, which would apply where a property is sold within a year of purchase. Details of this tax are unknown, but it would likely eliminate the ability to pay no tax on the appreciation of a principal residence that's purchased and sold in the same year. It's likely aimed to cool excessive price growth in the housing market by reducing the number of speculative buyers transacting, rather than a revenue-generating measure. Certain exceptions to the proposal were noted, specifically for life circumstances (death, pregnancy, employment, divorce or disability). With a minority government, it will be interesting to see if this comes to light, given that the Conservatives campaigned on pledging never to tax Canadians on the sale of their principal residence.

Changes to tax credits and deductions

Throughout the election, all parties made promises with respect to various tax credits and deductions for Canadians. Here are some of the key tax credit changes from the Liberal campaign:

- Extend the Home Expense deduction for home office expenses through the 2022 tax year and increase the deductible amount to $500 from $400.
- Double the First-Time Home Buyers' Tax Credit from $5,000 to $10,000 in eligible costs, for a maximum credit of $1,500.
- Increase the Eligible Educator School Supply Refundable Tax Credit to 25% (from 15%) and expand eligibility to include tech devices.
- Introduce a new Labour Mobility Tax Credit to allow workers in the building and construction trades to deduct up to $4,000 in eligible travel and temporary relocation expenses, giving them a tax credit of up to $600 a year.
- Develop an investment tax credit of up to 30% for a range of clean technologies.

- Expand the Canada Caregiver Credit into a refundable tax-free benefit, allowing caregivers to receive up to $1,250 per year.
- Introduce a Career Extension Tax Credit to help seniors who want to stay in the workforce. Those age 65 or over who earn a minimum of $5,000 will be able to eliminate up to $1,650 of taxes payable.
- Introduce a Multigenerational Home Renovation Tax Credit to support families looking to add a secondary unit to allow a family member to live with them. Families will be able to claim a 15% tax credit for up to $50,000 in renovation and construction costs, saving up to $7,500.
- Double the non-refundable Home Accessibility Tax Credit to provide tax relief of 15% on up to $20,000 of eligible expenditures per calendar year per eligible home for a qualifying individual.

In terms of deductions, the Liberal campaign also promised to eliminate flow-through shares for oil, gas and coal projects. This type of deduction allowed certain expenses incurred by the resource company to be "renounced" or "flowed through" to the taxpayer to be deducted on their tax return. If removed, this will curtail the ability for some individuals to invest in what many deem to be "tax-efficient investments". This could narrow the availability of tax deductions to investors in the future.

As the Liberals work with the other parties to try and put their campaign promises into action, it will be interesting to see which tax credits get approved and how this impacts Canadians.

Conclusion

With the magnitude and wide-ranging impacts of the COVID-19 pandemic, significant government spending has been necessary. As a result, there's been an increase in speculation on how the government will account for and re-capture this spending. Over the next several years, new and different tax measures and government policies may be seen and implemented as a means to raise revenues. Canada is not alone in handling the impacts and effects of the pandemic, and it is possible governments across the globe will be facing similar deficits. For Canadians, this translates into many potential planning areas that may need to be considered, now and for the future.

For a detailed list of tax-related campaign promises, please ask your RBC advisor for our "Federal Election 2021: A summary of key tax and economic platform promises" article.

This article may contain strategies, not all of which will apply to your particular financial circumstances. The information in this article is not intended to provide legal, tax or insurance advice. To ensure that your own circumstances have been properly considered and that action is taken based on the latest information available, you should obtain professional advice from a qualified tax, legal and/or insurance advisor before acting on any of the information in this article

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