RBC WEALTH MANAGEMENT SERVICES

Federal Budget 2019

Key tax measures that have a direct impact on you

Wealth Management

2019 Federal Budget Analysis

The Liberal government tabled its pre-election budget on March 19, 2019. The budget announced spending initiatives with a special focus on housing, skills for a changing job market, targeted measures for seniors, new support for zero-emission vehicles, steps toward implementing national pharmacare, and a commitment to bring high-speed internet to every Canadian home and business. The budget also aims to reduce inequity in our tax system, for example, by announcing the government's intention to limit the stock option deduction available to employees of large, established corporations. There were no changes to personal or corporate income tax rates. The spending measures and updated economic forecast results in an updated annual budgetary deficit for the 2018-19 fiscal year of $14.9 billion, compared to the $18.1 billion annual budgetary deficit forecast by the government in its Fall Economic Statement (November 21, 2018).

Housing measures

The Government continues to monitor the effects of its mortgage finance policies, including the stress test for insured mortgages, but has not adjusted them in this budget. Instead, the budget introduces a plan to support housing affordability through a number of measures to boost supply in Canada's housing and rental markets, as well as targeted measures for first-time home buyers and separated or divorced individuals.

The First-Time Home Buyer Incentive

The budget proposes to introduce the First-Time Home Buyer Incentive. This incentive utilizes a unique financing model that enables first-time home buyers to reduce the money required from an insured mortgage without increasing the amount they must save for a down payment. The incentive is a shared equity mortgage that will give eligible first-time home buyers the ability to lower their borrowing costs by sharing the cost of buying a home with Canada Mortgage and Housing Corporation (CMHC).

Eligible first-time home buyers who have the minimum down payment for an insured mortgage[1] may apply to finance a portion of their home purchase through a shared equity mortgage with CMHC. The Incentive will reduce the monthly payments required to buy a home. This will give first-time home buyers greater flexibility both in purchasing a home and managing its ongoing costs.

CMHC will offer qualified first-time home buyers a 10 percent shared equity mortgage for a newly constructed home or a 5 percent shared equity mortgage for an existing home.

As a means-tested program, the Incentive will be available to first-time home buyers with household incomes under $120,000 per year. At the same time, participants' insured mortgage and the Incentive amount cannot be greater than four times the participants' annual household incomes.

The following example is adapted from the 2019 budget plan and illustrates how the First-Time Home Buyer Incentive will work.

1. If your down payment is less than 20% of the purchase price of your home, you will require a mortgage that's insured against default. This insurance protects the lender in case you default on your mortgage payments and is required by law.

Anita is seeking to buy a new condo for $400,000. Under the First-Time Home Buyer Incentive, Anita can apply to receive $40,000 in a shared equity mortgage (10% of the cost of a new home) from CMHC, lowering the total amount she needs to borrow.

Compared with an insured mortgage, the CMHC First-Time Home Buyer Incentive would enable Anita to pay $228 less in mortgage payments every month. Anita can use these savings to invest in her future, such as buying a home better suited to her needs, paying down her insured mortgage sooner, or having more monthly disposable income. When Anita sells her condo in the future, CMHC is repaid.

SAVINGS IN MORTGAGE PAYMENTS WITH THE CMHC FIRST-TIME HOME BUYER INCENTIVE

$228 per month / $2,736 per year

Insured Mortgage Model (No Incentive)		CMHC First-Time Home Buyer Incentive Model	
House Price	$400,000	House Price	$400,000
Down Payment	$20,000 (5%)	Down Payment	$20,000 (5%)
		CMHC First-Time Home Buyer Incentive	$40,000 (10%)
Insured Mortgage	$380,000 (95%)	Insured Mortgage	$340,000 (85%)
Monthly Carrying Cost*	$1,973	Monthly Carrying Cost*	$1,745

* Assumes an amortization period of 25 years and a mortgage rate of 3.5%.

Home Buyers' Plan

The home buyers' plan (HBP) helps first-time home buyers save for a down payment by allowing them to withdraw from their registered retirement savings plan (RRSP) to purchase or build a home without having to pay tax on the withdrawal. You are considered a first-time home buyer if you or your spouse or common-law partner have not owned a home that you occupied as your principal residence at any time during the relevant calendar year or in any of the four preceding calendar years.

To provide first-time home buyers with greater access to their RRSPs the budget proposes to increase the HBP withdrawal limit to $35,000 from $25,000. As a result, a couple will potentially be able to withdraw $70,000 from their RRSPs to purchase a first home. This will be available for withdrawals made after March 19, 2019.

To help those who have experienced a breakdown in their marriage or common-law partnership, the budget also proposes that these individuals may be permitted to participate in the HBP, even if they do not meet the first-time home buyer requirement. This is provided that they live separate and apart from their spouse or common-law partner for a period of at least 90 days as a result of a breakdown in their marriage or common-law partnership. Certain other conditions also need to be met. This measure will be available for HBP withdrawals made after 2019.

Change in Use Rules for Multi-Unit Residential Properties

When a property is converted from income-producing use (e.g., a rental property) to personal use (e.g., a residential property), or vice versa, you are deemed to dispose of and reacquire the property for income tax purposes. This deemed disposition also occurs when the use of only part of a property is changed and you cannot elect out of the deemed disposition. For example, this can occur where you own a multi-unit residential property, such as a duplex, and either start renting it or move into one of the units. The budget proposes to allow a taxpayer to elect that the deemed disposition that normally arises on a change in use of part of a property not apply. This measure will apply to changes in use of property that occur on or after March 19, 2019.

Skills and job measures

Canada Training Credit

The budget proposes to introduce a new Canada Training Credit, a refundable tax credit aimed at providing financial support to help cover up to half of eligible tuition and fees associated with training. Eligible individuals must be at least 25 years old and less than 65 years old and will be able to accumulate $250 each year in a notional account up to a maximum amount of $5,000 over a lifetime. There will be earning and income thresholds that will be subject to annual indexation. An individual's net income must not exceed $147,667 in 2019 to accumulate the $250 in respect of that year. This measure will apply to the 2019 and subsequent taxation years. Consequently, the annual accumulation to the notional account will start based on eligibility in respect of the 2019 taxation year and the credit will be available to be claimed for expenses in respect of the 2020 taxation year.

EI Training Support Benefit and Leave Provisions

The budget proposes to introduce a new EI training benefit through the EI program that is expected to be launched in late 2020. The benefit is expected to provide up to four weeks of income support every four years - paid at 55 percent of a worker's average weekly earnings. This benefit will provide support to workers while on training who are without a regular paycheque. To make this new benefit work for both workers and employers, the government proposes to consult with provinces and territories on changes under the leave provisions to labour legislation and to introduce an EI small business premium rebate for employers.

Senior measures

Permitting additional types of annuities in registered plans

An RRSP must mature by December 31 of the year in which you turn 71. On maturity, the funds must be withdrawn, transferred to a registered retirement income fund (RRIF) or used to purchase an annuity. In exchange for a lump-sum amount of funds, an annuity provides you a stream of periodic payments, generally for a fixed term, for your life or for the joint lives of you and your spouse or common-law partner.

To provide Canadians with greater flexibility in managing their retirement savings, the budget proposes to permit two new types of annuities for certain registered plans:

- "advanced life deferred annuities" will be permitted under an RRSP, 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.

These measures will apply to the 2020 and subsequent taxation years.

Advanced Life Deferred Annuities (ALDA)

An ALDA will be a life annuity the commencement of which may be deferred until the end of the year in which the annuitant attains 85 years of age. There are other requirements to be considered an ALDA, limits on how much of your registered plan can be invested in an ALDA and penalties related to non-compliance which are not discussed here.

Variable Payment Life Annuities (VPLA)

The current tax rules generally require that retirement benefits from a PRPP or defined contribution RPP be provided to you by means of a transfer of funds from your account to an RRSP or RRIF, variable benefits paid from your account or an annuity purchased from a licensed annuities provider. However, in-plan annuities (annuities provided to members directly from a PRPP or defined contribution RPP) are generally not permitted under the current tax rules.

The budget proposes to amend the tax rules to permit PRPPs and defined contribution RPPs to provide a VPLA to members directly from the plan. A VPLA will provide payments that vary based on the investment performance of the underlying annuities fund and on the mortality experience of VPLA annuitants. There are other requirements under these proposed rules which are not discussed here.

Contributions to a specified multi-employer plan for older members

In general, the pension tax rules effectively ensure that contributions to a defined benefit registered pension plan (RPP) in respect of a member are not made after the member can no longer accrue further pension benefits. This is usually after the end of the year in which the member turns 71 years old or if the member has returned to work for the same or a related employer and is receiving a pension from the plan (except under a qualifying phased retirement program).

However, in the case of a specified multi-employer plan (SMEP), a specific type of union-sponsored, defined benefit pension plan, this is not the case. Such contributions do not benefit the member because they can no longer accrue any corresponding pension benefits under the plan.

To bring the SMEP rules in line with the pension tax provisions that apply to other defined benefit RPPs, the budget proposes to amend the tax rules to prohibit contributions to a SMEP in respect of a member after the end of the year the member attains 71 years of age and to a defined benefit provision of a SMEP if the member is receiving a pension from the plan (except under a qualifying phased retirement program).

This measure will apply in respect of SMEP contributions made pursuant to collective bargaining agreements entered into after 2019, in relation to contributions made after the date the agreement is entered into.

Applying for the Canada Pension Plan benefit

To ensure that all Canadian workers receive the full value of the benefits to which they contributed, the budget proposes to introduce legislative amendments to proactively enroll Canada Pension Plan (CPP) contributors who are age 70 or older in 2020 but have not yet applied to receive their retirement benefit.

Guaranteed income supplement earnings exemption

To allow low-income older Canadians to effectively take home more money while they work, the budget proposes to introduce legislation that will enhance the guaranteed income supplement (GIS) earnings exemption beginning with the July 2020 to July 2021 benefit year.

Personal tax measures

Carrying on a business in a Tax-Free Savings Account (TFSA)

The TFSA is a registered account that allows you to earn tax-free investment income on a wide range of investments. However, a TFSA is liable to pay tax on income earned from a business carried on by the TFSA. Currently, the trustee of a TFSA is jointly and severally liable with the TFSA for any tax payable on income earned from carrying on a business in the TFSA. The budget proposes to extend this joint and several liability to the TFSA holder.

This measure will apply to the 2019 and subsequent taxation years.

Employee stock options

Employee stock options, which provide employees with the right to acquire shares of their employer at a designated price, are an alternative compensation method used by incorporated businesses. The difference between the fair market value of the shares on the day the options are exercised and the amount that is paid for the shares is considered a taxable benefit. The tax rules provide employee stock options with preferential personal income tax treatment in the form of a stock option deduction which effectively results in the benefit being taxed at 50% of the normal rate of personal taxation, the same rate as capital gains.

The budget proposes to apply a $200,000 annual cap on the employee stock option grants (based on the fair market value of the underlying shares) that may receive tax-preferred treatment for employees of large, long-established, mature firms. For start-ups and rapidly growing Canadian businesses, employee stock option benefits will remain uncapped.

Further details of this measure will be released before the summer of 2019. Any changes will apply on a go-forward basis only and will not apply to employee stock options granted prior to the announcement of new legislative proposals.

Support for Canadian journalism

The budget proposes the following tax measures to support Canadian journalism:

- Individuals will be entitled to a 15% non-refundable tax credit on amounts paid for eligible digital news subscriptions. This credit will allow individuals to claim up to $500 in eligible costs, for a maximum credit of $75 annually. This credit will be available for amounts paid after 2019 and before 2025.
- Qualifying journalism organizations will be able to register as qualified donees as of January 1, 2020.
- A refundable labour tax credit will be provided to qualifying journalism organizations for salary expenses incurred in respect of a period on or after January 1, 2019.

Donations of cultural property

The current tax rules provide certain enhanced tax incentives to encourage donations of cultural property to certain designated institutions and public authorities in Canada, in order to ensure that such property remains in Canada for the benefit of Canadians.

To qualify for the incentives, one of the requirements is that the donated property must be of “national importance” to such a degree that its loss to Canada would significantly diminish the national heritage.

In response to a recent court case, the budget proposes to remove the requirement that property be of “national importance" in order to qualify for the enhanced tax incentives for donations of cultural property.

This measure will apply in respect of donations made on or after March 19, 2019.

Registered disability savings plan (RDSP)

The RDSP is a tax-assisted savings vehicle intended to help an individual with a disability save for their long-term. An RDSP may be established only for a beneficiary who is eligible for the Disability Tax Credit (DTC). Currently, if the beneficiary of the RDSP ceases to be eligible for the DTC, the RDSP will generally need to be closed by the end of the year following the first full year throughout which the beneficiary is not eligible for the DTC. If a medical practitioner certifies in writing that the nature of the beneficiary's condition makes it likely that the beneficiary will be eligible for the DTC in the foreseeable future due to the condition, the RDSP may remain open.

The budget proposes to remove the time limitation on the period that an RDSP may remain open after the beneficiary becomes ineligible for the DTC and to eliminate the requirement for medical certification.

In light of the changes, a rollover of proceeds from a deceased individual's RRSP or RRIF to the RDSP of a financially dependent infirm child or grandchild will be permitted only if the rollover occurs by the end of the fourth calendar year following the first full calendar year throughout which the beneficiary is ineligible for the DTC.

These measures will apply after 2020. Additionally, an RDSP will not have to be closed on or after March 19, 2019 solely because the RDSP beneficiary is no longer eligible for the DTC.

The budget also proposes to exempt RDSPs from seizure in bankruptcy, with the exception of RDSP contributions made in the 12 months before filing for bankruptcy.

Tax measures for kinship care providers

A number of provinces and territories offer kinship and close-relationship care programs as alternatives to foster care for children in need of protection who require out-of-home care on a temporary basis. As part of their kinship care programs, some of these jurisdictions provide financial assistance to care providers to help defray the costs of caring for the child.

The budget proposes to ensure that kinship care providers will be eligible for the Canada Workers Benefit amount and that financial assistance payments received by care providers under a kinship care program are neither taxable, nor included in income for the purposes of determining entitlement to income-tested benefits and credits. These measures will apply for the 2009 and subsequent taxation years.

Zero-emission vehicle measures

The budget proposes the following measures that will make it easier and more affordable for Canadians to choose zero-emission vehicles:

- The Government will provide Natural Resources Canada with funds to deploy new recharging and refuelling stations in workplaces, public parking spots, commercial and multi-unit residential buildings, and remote locations.
- A new federal purchase incentive of up to $5,000 for electric battery or hydrogen fuel cell vehicles will be provided where the vehicle's manufacturer's suggested retail price is less than $45,000. More details of this program will be provided at a later date.
- Businesses will be able to fully write-off, for tax purposes, the cost of qualifying vehicles in the year they are put in use. Qualifying vehicles will include electric battery, plug-in hybrid or hydrogen fuel cell vehicles purchased by a business.

Business tax measures

Small Business Deduction – Farming and Fishing

Currently, certain relief is given to Canadian-controlled private corporations carrying on a farming or fishing business from the tax rules designed to prevent the multiplication of the small business deduction. The budget proposes to extend that relief to sales of farming products and fishing catches to any arm's length corporation. This measure applies to taxation years that begin after March 21, 2016.

Strengthening Beneficial Ownership Transparency

The budget proposes further amendments to the Canada Business Corporations Act to make the beneficial ownership information maintained by federally incorporated corporations more readily available to tax authorities and law enforcement.

The 2018 budget had proposed the introduction of enhanced tax reporting requirements for trusts, effective for the 2021 and later taxation years, in order to improve the collection of beneficial ownership information for income tax purposes.

Beneficial ownership refers to the identity of individuals who own, control or profit from a corporation or trust.

Scientific Research and Experimental Development (SR&ED) Tax Incentive Program

The SR&ED Tax Incentive Program encourages business innovation by providing at 15% tax credit for businesses that conduct scientific research and experimental development in Canada. An enhanced 35% refundable tax credit is provided to eligible small and medium-sized businesses. The budget proposes to eliminate the income threshold for accessing the enhanced credit.

This measure will apply to taxation years that end on or after March 19, 2019.

Closing tax loopholes

The budget proposes to close the following tax loopholes they perceive may result in some taxpayers paying less than their fair share.

- Prevent the use by mutual fund trusts of a method of allocating capital gains or income to their redeeming unitholders where the use of that method inappropriately defers tax or converts fully taxable ordinary income into capital gains taxed at a lower rate.
- Improve existing rules meant to prevent taxpayers from using derivative transactions to convert fully taxable ordinary income into capital gains taxed at a lower rate.
- Stop the use of Individual Pension Plans to avoid the prescribed transfer limits. These limits are meant to prevent inappropriate tax deferrals when individuals transfer assets out of certain types of pension plans. When an individual terminates members in a defined benefit plan, a tax-deferred transfer of all or a portion of the commuted value of accrued pension benefits can be made to another defined benefit plan sponsored by another employer or to a locked-in plan (subject to prescribed limits). As such, it may be possible to transfer 100% of the commuted value of the pension plan to an IPP that is sponsored by a newly incorporated private corporation that is controlled by the individual who has terminated employment with their former employer. To prevent this type of planning, the budget proposes to prohibit IPPs from providing retirement benefits in respect of 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). This measure applies to pensionable service credited under an IPP on or after March 19, 2019.

Previously announced measures

The budget confirms the Government's intention to proceed with a number of previously announced tax and related measures, as modified to take into account consultations since their release:

- Income tax measures announced on November 21, 2018 in the Fall Economic Statement to:
  - Provide for the Accelerated Investment Incentive
  - Allow the full cost of machinery and equipment used in the manufacturing and processing of goods, and the full cost of specified clean energy equipment to be written off immediately
  - Extend the 15% mineral exploration tax credit for an additional five years
  - Ensure that the business income of communal organizations retain its character when allocated to members of the organization for tax purposes
- Enhancing reporting requirements for certain trusts to provide additional information on an annual basis that were announced in the 2018 budget
- Income tax measures to facilitate the conversion of Health and Welfare Trusts to Employee Life and Health Trusts announced in the 2018 budget
- Information reporting requirements for certain dispositions of an interest in a life insurance policy announced in the 2016 budget

Prior to implementing any strategies, individuals should consult with a qualified tax advisor, legal professional or other applicable professional.

While it has been the long-standing practice of Canada Revenue Agency (CRA) to allow taxpayers to file their tax returns based on proposed legislation, a taxpayer remains potentially liable for taxes under current law in the event that a budget proposal is not ultimately passed. Therefore, if proposed legislation does not become law, it is possible that CRA may assess or re-assess your tax return based on existing legislation. It is recommended that you consult a qualified tax advisor to assist you in assessing the costs and benefits of proceeding with specific budget proposals as they relate to you.

Please contact us for more information about the topics discussed in this article.