2014 Federal Budget Special Report

February 11, 2014

In This Report:

Knowledge Bureau Reporters:

Evelyn Jacks, President

Walter Harder, DFA – Tax Services Specialist, DFA – Bookkeeping Services Specialist

Al Rowell, MFA, DFA – Tax Services Specialist

Editorial Team:

Evelyn Jacks

Jaime Kyle

Virginia Pastway

Olympic Victory – Flaherty on Track to Eliminate the Deficit

The stellar performances of our young Canadians at the Sochi Olympics seem to have inspired the Federal Finance Minister as he released his 10th budget today. He proudly announced that the $55 billion deficit we inherited with the financial crisis will be within $3 billion of elimination by 2015. In addition, a $6.4 billion surplus is anticipated by 2016; which includes a $3.0 billion annual adjustment for risk.

The path to reaching these goals is certainly a significant career achievement by this Finance Minister. According to the budget, the federal debt-to-GDP ratio is expected to fall below its low, pre-recession level in 2017–18. This will help the Federal Government achieve its target of 25 per cent of GDP by 2021, announced at the September 2013 G-20 Leaders' Summit in St. Petersburg, Russia.

In fact, if the mastery over the debt and deficit is achieved as planned in this budget, Canada will be in a very advantageous position against the fiscal performance of other nations. According to the budget, Canada's total government net debt (which includes that of the federal, provincial/territorial and local governments as well as the net assets of the Canada Pension Plan and the Québec Pension Plan) will remain the lowest of any G-7 country and among the lowest of the advanced G-20 countries.

What does this mean for average Canadians? In a nutshell, three key advantages says the Budget: a strong investment climate that will support economic and job growth, lower debt-servicing costs and, as a result of both those factors, lower taxes over the long run. Following are the details of the specific economic and tax provisions in this budget.

Knowledge Bureau
Excellence in Financial Education

Economic News: Taxes Grow Faster Than Economy, But Debt, Deficit Down

Revenues are expected to increase by 2.9 per cent in 2013–14 and then by an annual growth rate of 4.7 per cent over the forecast period ending in 2019. Some highlights appear below; followed by detailed tables in the Appendix on page 7.

- **Personal income tax revenues** are the largest component of those revenues, and they are expected to increase by 3.5 per cent to $130 billion in 2013-2014 and then are projected to average 5.2 per cent in annual growth, faster than the projected growth in the economy, expected to range from 1.7 per cent in 2013 to 2.4 per cent by 2019.

- **Corporate income tax revenues** will be $35.0 billion in 2013–14 and then grow at an annual rate of 5.9 per cent largely due to recent tax changes and increased audit activities.

- **Non-resident income tax revenues** are made up most significantly of the reporting of dividends and interest payments, expected to increase by 7.6 per cent in 2013–14 and then at an average annual rate of 5.9 per cent.

- **Goods and Services Tax (GST) revenues** are projected to grow by 3.9 per cent in 2013–14 and by 5.1 per cent per year on average in the forecast period.

- **Other excise taxes and duties** will decline slightly in 2013–14, and then increase by 6.3 per cent, to $11.3 billion in 2014–15 as a result of the new excise duty rate for tobacco announced in this budget.

- **Employment Insurance (EI) premium revenues** will increase by 5.4 per cent in 2013–14. For 2015 and 2016, EI premium rates are assumed to be 1.88% and so from 2013–14 to 2015–16, the cumulative deficit in the EI Operating Account will be eliminated. By 2017, EI premium rates are expected to fall to 1.47%. EI premium revenues are expected to grow again in 2018–19 as a result of a projected growth in wages and salaries.

Personal Tax News: Check Out Changes for Medical Expenses, Donations and Taxation of Trusts

Several interesting provisions were tabled in this budget, described below:

Applying for the Goods and Services Tax Credit (GSTC)

Beginning in 2014, taxpayers will no longer be required to apply to receive the GSTC. The government will issue notices of determination to those qualify for the credit. Those who do not qualify will not receive a notice, but may request one. For couples, the spouse whose return is assessed first will be awarded the credit if the couple qualifies. In order to qualify, CRA must know the individual's net income for the year so this will not eliminate the need to file a return to get the GSTC.

Adoption Tax Credit

The Adoption Tax Credit maximum will increase in 2014 from $11,774 to $15,000 for each eligible child starting in 2014.

Medical Expenses

Beginning in 2014, the following new expenses will qualify for the Medical Expenses Tax Credit:

- The cost of designing an individual therapy plan for disabled taxpayers if the therapy would be eligible and the plan is prescribed by a medical practitioner or the plan is required to access public funding.

- The cost of service animals to help an individual manage severe diabetes, including the cost of care and maintenance of the animal and the cost of travel for the individual to attend a facility that trains such animals.

Donations at Death

For donations made in the deceased's will after 2015, the donation will no longer be deemed to have been made by the individual immediately prior to their death but will be deemed to have been made by the estate at the time the donation is transferred to the qualified donee. The trustee may allocate the donation to

- The estate for the year in which the donation was made,
- An earlier taxation year of the estate, or
- The last two taxation years of the deceased.

Donations of Ecologically Sensitive Land

Credits for the donation of ecologically sensitive land made after February 11, 2014 may be carried forward up to ten years (five years for donations prior to that date).

Donations of Cultural Property

The current exemption to the rule that the value of a gift may not be greater than the cost of the gift to the donor will no longer apply to gifts of cultural property after February 11, 2014 if the gift is acquired as part of a tax shelter gifting arrangement.

Search and Rescue Volunteer Tax Credit

A new tax credit for search and rescue volunteers will be available beginning in 2014. The rules are substantially the same as the current tax credit for volunteer firefighters. Like the volunteer firefighters tax credit, at least 200 hours of service is required and if the credit is claimed, any currently-exempted remuneration must be included in income

In order to claim the credit, volunteers must have written certification from a team president, or other individual who fulfills a similar role, of an eligible search and rescue organization confirming the number of hours of eligible volunteer search and rescue services performed. Eligible search and rescue organizations will include search and rescue organizations that are members of:

- The Search and Rescue Volunteer Association of Canada,
- The Civil Air Search and Rescue Association,
- The Canadian Coast Guard Auxiliary,
- Other organizations whose status as a search and rescue organization is recognized by a provincial, municipal or public authority.

Mineral Exploration Tax Credit for Flow-Through Investors

The tax credit will be extended another year so that investments until the end of March 2015 will be eligible for the flow-through credit for exploration expenses to the end of 2016.

Farming and Fishing Business Rollovers

The current rollover provisions that allow for the transfer of a family farm or family fishing business to a family member will be extended to apply to a business that is a combination of farming and fishing. This change is effective for transfers that occur in 2014 or subsequent years.

Tax Deferral for Farmers

The current provision for the deferral of the taxation on the proceeds from the disposition of breeding livestock due to flood or drought conditions will be extended to bees and horses that are over 12 months of age if these animals are kept for breeding purposes.

RRSP Contributions by Amateur Athletes

Amateur athletes who contribute to an amateur athlete trust and exclude the contribution from their income in the year of contribution will be able to have that income treated as earned income for RRSP purposes for contributions beginning in 2014. In addition, amateur athletes who contributed in 2011, 2012, or 2013 may file an election (before March 2, 2015) to have those contributions treated as earned income for RRSP purposes.

Pension Transfer Limits

Effective for 2012 and subsequent years, the existing rule that allowed the maximum amount for RPP transfers from an insolvent employer to ignore the effects of underfunding will be extended to allow for transfers from an RPP (other than an IPP). This new treatment will be available where the reduction in the estimated pension benefit that results in the reduced commutation payment is approved, pursuant to the applicable pension benefits standards legislation; or if the payment is from an IPP, where the plan is being wound up and the commutation payment is the last payment made to the plan.

Tax on Split Income

The definition of "split income" is modified for 2014 and subsequent years to include any income that is paid or allocated directly or indirectly to a minor from a trust or partnership if that income is derived from rental or business income and a person related to the minor:

- Is actively engaged on a regular basis in the activities of the trust or partnership to earn income from any business or rental property, or
- Has, in the case of a partnership, an interest in the partnership (whether held directly or indirectly).

Taxation of Trusts

Beginning in 2016, the graduated tax rates currently available to testamentary trusts will only apply for the first three years of the trust. For testamentary trusts that continue beyond three years, the rate applied to income taxed in the trust will be the highest tax rate (currently 29% federally).

Inter vivos trusts will be taxed at the flat 29% rate with no three-year delay. An exception to this rule will occur in the case of trusts set up for people qualifying for the federal Disability Tax Credit.

Taxation of Non-Resident Trusts

For taxation years that end after budget day (February 11, 2014), if any contributions are made to a non-resident trust by a Canadian resident, that trust will be deemed to be resident in Canada. The 60-month exemption previously available to trusts where the contributors are new Canadian residents will continue but only if no new contributions are made to the trust after budget day.

Business News: Changes to Source Deductions and ECP Interesting

Farming and Fishing Businesses

Farming and Fishing Businesses received some special treatment in the February 11 Budget. The Income Tax Act (ITA) currently allows for a tax deferral on the intergenerational transfer of farming and/or fishing properties, as well as an $800,000 Lifetime Capital Gains Exemption (LCGE) on qualifying farming and fishing properties, including farming or fishing corporations.

However, these properties will qualify for the LCGE only if used principally (interpreted as 50% or more) in farming or fishing operations. A family involved in farming, fishing and a third business activity may not meet the 50% or more requirements. In addition, qualification for the LCGE requires that 90% or more of the fair market value of the assets *(the all or substantially all test)* of the operation be used within the operation.

Effective with the 2014 tax year, the eligibility for the intergenerational rollover and the LCGE will be extended to property that is used principally in a combination of farming ***and*** fishing.

Remittance Thresholds for Employer Source Deductions

Currently employers where employee source deductions (Income Tax, CPP and EI) exceed $15,000, but less than $50,000 on a monthly basis are required to remit to CRA twice monthly. Employers where monthly source deductions exceed $50,000 are required to remit to CRA four times a month. Effective January 1, 2015, the remittance thresholds will increase to $25,000 and $100,000 respectively effective January 1, 2015.

Capital Cost Allowance Changes: Clean Energy Generation

Capital Cost Allowance classes 43.1 and 43.2 are used for cogeneration systems and waste-fuelled electricity generation systems – depending on the systems' level of efficiency. Class 43.2 will be expanded to include Water-Current Energy Equipment and gasification equipment used to gasify eligible waste fuel for use in a broader range of applications acquired on or after February 11, 2014.

Eligible Capital Property

Eligible Capital Property (ECP) is a capital expenditure incurred to acquire rights or benefits of an intangible nature, such as Goodwill. Currently Eligible Capital Expenses (ECE) does not fall under Capital Cost Allowance rules and has an amortization calculation of its own. Public consultation will be held on a proposal to eliminate the current ECP calculation and create a new CCA class. Under the proposal, the current balance of the Cumulative Eligible Capital account would transfer to the new proposed CCA class which would feature a 100% inclusion rate and a 5% annual depreciation rate. Existing rules for recapture, capital gains and depreciation would also apply. As part of the consultation process, special rules are anticipated to simplify the transition for small businesses.

GST/HST News: Focus on Health Care and Registration Compliance

Health Care Sector. The health care sector currently has two classifications for GST/HST.

- **Exempt.** Basic health care services are exempt from GST/HST and do not charge GST/HST to their patients. In addition, they are also not eligible to claim ITC's on their expenditures.

- **Zero-rated**. Prescription drugs and medical and assistive devices designed to assist an individual in coping with a chronic disease, illness or disability are zero-rated supplies meaning that GST/HST are charges at 0%. This allows the supplier to claim ITC's on their expenditures.

Effective February 11, 2014, three changes to certain health-related services and medical and assistive devices are implemented.

- **Training Exemption.** Training services that is designed to assist individuals with a disorder or disability or to alleviate or eliminate the effects are currently exempt from GST/HST. The budget expands the exemption to include the designing and development of training programs subject to certain qualifications.

- **Acupuncturist and Naturopathic Doctors' Services.** Services covered under a provincial health care plan are exempt from GST/HST in that province. Exemptions are also provided for services by certain health care practitioners. Effective February 11, 2014, Acupuncturists and Naturopathic Doctors are added to the list of health care practitioners exempt from GST/HST.

- **Electronically Enhanced Eyewear.** Eyewear specifically designed to electronically enhance the vision of individuals with vision impairment has been added to the list of medical and assistive devices that qualify as a zero-rated supply effective February 11, 2014.

Closely Related Persons – Nil Consideration Election

Some changes have been made to provide a nil consideration election in certain circumstances for members of a closely related group, effective January 1, 2015, in cases where new members have not yet acquired any property and continue as going concerns engaged exclusively in commercial activities. A new election form will be introduced. Simplification procedures around joint venture elections have also been introduced.

GST/HST Registration Compliance

In general, a business with gross revenues in excess of $30,000 annually must register to collect and remit GST/HST on the total taxable supplies provided. After Royal Assent, the Minister of National Revenue will be given the discretionary authority to register and assign an GST/HST registration number where an individual or business has failed to comply with the requirement to register.

Previously Announced Changes to be Implemented in 2014

- **Auto Expense Deductions:** Proposed changes to automobile expense deduction limits and the prescribed rates for the automobile operating expense benefit for 2012 announced on December 29, 2011, and for 2013 announced on December 28, 2012.

- **Life Insurance Policyholder Exemption Tests:** Legislative proposals released on August 23, 2013.

- **Labour-Sponsored Venture Capital Corporations:** Legislative proposals released on November 27, 2013.

- **Requirement that international electronic funds transfers of $10,000 or more be reported to the Canada Revenue Agency:** Legislative proposals released on January 9, 2014.

- **GST/HST rules to prevent input tax credit claims that exceed tax actually paid:** Legislative proposals released on January 17, 2014.

- **GST/HST exemption for hospital parking for patients and visitors:** Legislative proposals released on January 24, 2014.

Appendix - Projected Revenue Outlook (billions of dollars)
Source: Table 4.2.5 February 11, 2014 Budget

	2012–2013	2013–2014	2014–2015	2015–2016	2016–2017	2017–2018	2018–2019
Income taxes							
Personal income tax	125.7	130.1	137.8	145.8	153.2	160.5	167.7
Corporate income tax	35.0	35.0	37.0	39.5	42.2	44.5	46.5
Non-resident income tax	5.1	5.5	5.7	6.0	6.5	6.9	7.3
Total income tax	165.8	170.6	180.4	191.2	201.9	211.9	221.5
Excise taxes/duties							
Goods and Services Tax	28.8	29.9	31.3	33.2	35.1	36.7	38.3
Customs import duties	4.0	4.2	4.4	5.0	4.7	4.9	5.1
Other excise taxes/duties	10.8	10.6	11.3	11.3	11.3	11.4	11.4
Total excise taxes/duties	43.6	44.8	47.0	49.5	51.1	53.0	54.8
Total tax revenues	**209.3**	**215.3**	**227.5**	**240.7**	**253.0**	**264.9**	**276.3**
Employment Insurance premium revenues	20.4	21.5	22.7	23.6	23.0	19.4	20.2
Other revenues	26.9	27.1	26.2	29.0	30.8	33.4	35.8
Total budgetary revenues	**256.6**	**264.0**	**276.3**	**293.3**	**306.8**	**317.7**	**332.4**

.

Summary Statement of Transactions in Billions of dollars - Projected

	2012–2013	2013–2014	2014–2015	2015–2016	2016–2017	2017–2018	2018–2019
Program expenses	246.4	251.2	250.2	256.9	266.5	275.2	286.3
Public debt charges	29.2	29.3	29.0	30.0	32.1	34.4	35.8
Total expenses	**275.6**	**280.5**	**279.2**	**286.9**	**298.7**	**309.7**	**322.1**
Budgetary balance	**-18.9**	**-16.6**	**-2.9**	**6.4**	**8.1**	**8.1**	**10.3**
Federal debt[1]	602.4	616.0	618.9	612.4	604.3	596.2	586.0

[1] The projected level of federal debt for 2013–14 includes an estimate of other comprehensive income. Note: Totals may not add due to rounding.

Knowledge Bureau®
Excellence in Financial Education

About The Knowledge Bureau

The Knowledge Bureau is Canada's leading financial educator and publisher whose mission is to raise standards for excellent services in the tax and financial industries.

Founded by award-winning financial educator Evelyn Jacks, it provides relevant and practical knowledge and skills through continuing professional development in the area of tax, investment, retirement, estate and business planning services. Over 100,000 courses have been taken by thousands of students across Canada since inception in 2003.

A national post-secondary educational institution, Knowledge Bureau offers comprehensive, certificate courses leading to the prestigious MFA™ (Master Financial Advisor) and Distinguished Financial Advisor™ designations. These courses are available online, through instructor-led workshops and the Distinguished Advisor Conference (DAC), or a combination of blended learning options. These programs are also recognized broadly for CE/CPD accreditation by most regulators and professional associations in the tax, bookkeeping, accounting and financial services industries.

For more information visit our website at www.knowledgebureau.com or call us toll-free in North America at 1-866-953-4769.