FULLER LANDAU
LLP

Federal Budget
February 11, 2014

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INTRODUCTION

On February 11, 2014, Minister of Finance Jim Flaherty tabled Economic Action Plan 2014, which in his opinion, confirms that the Government is on track to return to balanced budgets in 2015, with new measures that will create jobs and opportunities in an uncertain global economy.

With no new taxes on Canadian families or businesses, Economic Action Plan 2014 projects that the deficit will decline to $2.9 billion in 2014–15, after taking into account a $3 billion annual adjustment for risk. A surplus of $6.4 billion is expected in 2015–16, again after taking into account a $3 billion annual adjustment for risk.

Here are the highlights of the 2014 budget.

PERSONAL INCOME TAX MEASURES

Adoption Expense Tax Credit

The budget proposes to increase the maximum amount of eligible expenses to $15,000 per child for 2014. This maximum amount will be indexed to inflation for taxation years after 2014.

Medical Expense Tax Credit

The budget proposes that amounts paid for the design of an individualized therapy plan be eligible for the Medical Expense Tax Credit (METC) if the cost of the therapy itself would be eligible for the METC and the following conditions are met:

> an individualized therapy plan is required to access public funding for specialized therapy, or a medical doctor or an occupational therapist (or, in the case of a mental impairment, a medical doctor or psychologist) prescribes an individualized therapy plan;
> the plan is designed for an individual with a severe and prolonged mental or physical impairment who is, because of the impairment, eligible for the Disability Tax Credit; and
> the amounts are paid to persons ordinarily engaged in the business of providing such services to unrelated individuals.

The budget also proposes to add to the list of expenditures eligible under the METC expenses for service animals specially trained to assist an individual in managing their severe diabetes.

These measures will apply to expenses incurred after 2013.

Search and Rescue Volunteers Tax Credit

The budget proposes to introduce a Search and Rescue Volunteers Tax Credit (SRVTC) to allow eligible ground, air and marine search and rescue volunteers to claim a 15-per-cent non-refundable tax credit based on an amount of $3,000.

An eligible individual will be a search and rescue volunteer who performs at least 200 hours of volunteer search and rescue services in a taxation year, for one or more ground, air or marine search and rescue organizations.

Volunteer search and rescue service hours will be ineligible if the individual also provides search and rescue services, otherwise than as a volunteer, to that organization.

An individual who claims the SRVTC will be ineligible for the existing tax exemption of up to $1,000 for honoraria paid by a government, municipality or public authority to an emergency services volunteer.

This measure will apply to the 2014 and subsequent taxation years.

Extension of the Mineral Exploration Tax Credit for Flow-Through Share Investors

The budget proposes to extend eligibility for the Mineral Exploration Tax Credit for one year, to flow-through share agreements entered into before April 1, 2015.

Farming and Fishing Businesses

The budget proposes to extend eligibility for the intergenerational rollover and the lifetime capital gains exemption to:

> property of an individual used principally in a combination of farming and fishing;
> an individual's shares in a corporation, or interest in a partnership, where the corporation or partnership carries on both a farming business and a fishing business.

This measure will apply to dispositions and transfers that occur in the 2014 and subsequent taxation years.

Tax Deferral for Farmers

The tax deferral is targeted at breeding livestock. The budget proposes to extend this tax deferral to bees, and to all types of horses that are over 12 months of age, that are kept for breeding.

This measure will apply to the 2014 and subsequent taxation years.

Amateur Athlete Trusts

The budget proposes to allow income that is contributed to an amateur athlete trust to qualify as earned income for the purpose of determining the RRSP contribution limit of the trust's beneficiary.

This measure will apply in respect of contributions made to amateur athlete trusts after 2013. In addition, individuals who contributed to an amateur athlete trust before 2014 will be permitted to make an election to have income that was contributed to the trust in 2011, 2012 and 2013 also qualify as earned income. An individual will be required to make the election in writing and submit it to the Canada Revenue Agency on or before March 2, 2015.

Pension Transfer Limits

The budget proposes that, under certain circumstances, the maximum transferable amount for a plan member who is leaving an underfunded registered pension plan (RPP) be the same as if the RPP were fully funded.

This rule will be available in respect of a commutation payment to a plan member who is leaving an RPP if that payment has been reduced due to plan underfunding and either:

> where the plan is an RPP other than an individual pension plan, 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

> where the plan is an individual pension plan, the commutation payment to the plan member is the last payment made from the plan (i.e., the plan is being wound up).

The existing requirement that the application of this rule must be approved by the Minister of National Revenue will be maintained.

This measure will apply in respect of commutation payments made after 2012.

GST/HST Credit Administration

The budget proposes to eliminate the need for an individual to apply for the GST/HST Credit and to allow the Canada Revenue Agency to automatically determine if an individual is eligible to receive the GST/HST Credit. A notice of determination will be sent to each individual who is eligible for the GST/HST Credit. In the case of eligible couples, the GST/HST Credit will be paid to the spouse or common-law partner whose tax return is assessed first.

An ineligible individual, however, will be able to obtain a notice of determination upon request, which will preserve their right to object to the determination.

This measure will apply in respect of income tax returns for the 2014 and subsequent taxation years.

Tax on Split Income

The budget proposes that the definition “split income” be modified to include income that is, directly or indirectly, paid or allocated to a minor from a trust or partnership, if:

> the income is derived from a source that is a business or a rental property; 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 through another partnership).

This measure will apply to the 2014 and subsequent taxation years.

Graduated Rate Taxation of Trusts and Estates

The budget proposes to proceed with the measures described in the consultation paper of June 3, 2013.

Specifically, the budget proposes to apply flat top-rate taxation to grandfathered *inter vivos* trusts, trusts created by will and certain estates (including a number of consequential changes). Two exceptions to this treatment are proposed.

First, graduated rates will apply for the first 36 months of an estate that arises on and as a consequence of an individual’s death and that is a testamentary trust. If the estate remains in existence more than 36 months after the death, it will become subject to flat top-rate taxation at the end of that 36-month period.

Second, graduated rates will continue to be provided in respect of trusts having as their beneficiaries individuals who are eligible for the federal Disability Tax Credit.

Also under this proposal, testamentary trusts (other than estates for their first 36 months) and grandfathered *inter vivos* trusts will not benefit from special treatment under a number of related tax rules, in particular:

> an exemption from the income tax instalment rules;
> an exemption from the requirement that trusts have a calendar year taxation year and fiscal periods that end in the calendar year in which the period began;
> the basic exemption in computing alternative minimum tax;
> preferential treatment under Part XII.2 of the *Income Tax Act*;
> classification as a personal trust without regard to the circumstances in which beneficial interests in the trust have been acquired;
> the ability to make investment tax credits available to a trust's beneficiaries; and
> a number of tax administration rules that otherwise apply only to ordinary individuals.

Testamentary trusts that do not already have a calendar year taxation year will have a deemed taxation year-end on December 31, 2015 (or in the case of an estate for which that 36-month period ends after 2015, the day on which that period ends).

This measure will apply to the 2016 and subsequent taxation years.

Non-Resident Trusts

The budget proposes to eliminate the 60-month exemption from the deemed residence rules, including related rules that apply to non-resident trusts. Where the 60-month exemption applies the trust is not subject to Canadian taxation on its foreign-source income.

This measure will apply in respect of trusts for taxation years:

> that end after 2014 if, at any time that is after 2013 and before February 11, 2014, the 60-month exemption applies in respect of the trust, and no contributions are made to the trust on or after February 11, 2014 and before 2015; or
> as of February 11, 2014 in any other case.

BUSINESS INCOME TAX MEASURES

Remittance Thresholds for Employer Source Deductions

The budget will:

> increase the threshold level of average monthly withholdings at which employers are required to remit up to two times per month to $25,000 from $15,000; and
> increase the threshold level of average monthly withholdings at which employers are required to remit up to four times per month to $100,000 from $50,000.

This measure will apply in respect of amounts to be withheld after 2014.

Tax Incentives for Clean Energy Generation

The budget proposes to expand Class 43.2 to include water-current energy equipment and equipment used to gasify eligible waste fuel for use in a broader range of applications.

Consultation on Eligible Capital Property

The budget announces a public consultation on a proposal to repeal the eligible capital property regime, replace it with a new capital cost allowance (CCA) class available to businesses and transfer taxpayers' existing cumulative eligible capital pools to the new CCA class.

Proposed Rules

New CCA class

Expenditures would be included in the new CCA class at a 100-per-cent inclusion rate. The new class would have a 5-per-cent annual depreciation rate.

Special rules

Special rules would apply in respect of goodwill and in respect of expenditures and receipts that do not relate to a specific property of the business.

Transitional rules

For the first ten years, the depreciation rate for the new CCA class would be 7 per cent in respect of expenditures incurred before the implementation of the new rules.

CHARITIES AND NON-PROFIT ORGANIZATIONS

Donations of Ecologically Sensitive Land

The budget proposes to extend from five to ten years the carry-forward period for donations of ecologically sensitive land, or easements, covenants and servitudes on such land.

This measure will apply to donations made on or after February 11, 2014.

Estate Donations

The budget proposes to provide more flexibility in the tax treatment of charitable donations made in the context of a death that occurs after 2015. Donations made by will and designation donations will no longer be deemed to be made by an individual immediately before the individual's death. Instead, these donations will be deemed to have been made by the estate, at the time at which the property that is the subject of the donation is transferred to a qualified donee.

In addition, the trustee of the individual's estate will have the flexibility to allocate the available donation among any of: the taxation year of the estate in which the donation is made; an earlier taxation year of the estate; or the last two taxation years of the individual.

A qualifying donation will be a donation effected by a transfer, within the first 36 months after the individual's death, of property to a qualified donee.

This measure will apply to the 2016 and subsequent taxation years.

Donations of Certified Cultural Property

The value of a gift of property is deemed to be no greater than its cost to the donor if, generally, the donor acquired the property as part of a tax shelter gifting arrangement or held the property for a short period. Gifts of certified cultural property are exempt from this rule and also benefit from a capital gains exemption.

The budget proposes to remove the exemption for certified cultural property acquired as part of a tax shelter gifting arrangement.

This measure will apply to donations made on or after February 11, 2014.

State Supporters of Terrorism

The budget proposes that where a charity (or a Canadian amateur athletic association) accepts a donation from a foreign state listed as a supporter of terrorism for purposes of the *State Immunity Act*, or from an agency of such a state, the Minister of National Revenue may refuse to register the charity (or amateur athletic association) or may revoke its registration.

This measure will apply to donations accepted on or after February 11, 2014.

Consultation on Non-Profit Organizations

The budget announces the Government's intention to review whether the income tax exemption for NPOs remains properly targeted and whether sufficient transparency and accountability provisions are in place. This review will not extend to registered charities or registered Canadian amateur athletic associations.

INTERNATIONAL TAXATION

Captive Insurance

The budget proposes to amend the existing anti-avoidance rule in the foreign accrual property income (FAPI) regime relating to the insurance of Canadian risks.

Where the anti-avoidance rule applies, the affiliate's income from the insurance of the foreign risks and any income from a connected agreement or arrangement will be included in computing its FAPI.

This measure will apply to taxation years of taxpayers that begin on or after February 11, 2014.

Offshore Regulated Banks

The budget proposes to add new conditions for qualifying under the regulated foreign financial institution exception.

Back-to-Back Loans

The budget proposes to address back-to-back loan arrangements by adding a specific anti-avoidance rule in respect of withholding tax on interest payments, and by amending the existing anti-avoidance provision in the thin capitalization rules.

This measure will apply, in respect of the thin capitalization rules, to taxation years that begin after 2014, and in respect of Part XIII withholding tax, to amounts paid or credited after 2014.

Consultation on Tax Planning by Multinational Enterprises

The Government is interested in obtaining views on how to ensure fairness among different categories of taxpayers (e.g., multinational enterprises, small businesses and individuals) and how to better protect the Canadian tax base, while maintaining an internationally competitive tax system that is attractive for investment.

The Government is seeking the views of stakeholders.

Consultation on Treaty Shopping

The Government invites comments from interested parties on a proposed rule to prevent treaty shopping.

The rule would use a general approach focussed on avoidance transactions and, in order to provide more certainty and predictability for taxpayers, the rule would contain specific provisions setting out the ambit of its application.

The rule would apply to taxation years that commence after the enactment of the rule into Canadian law.

Update on the Automatic Exchange of Information for Tax Purposes

The Government of Canada successfully negotiated an intergovernmental agreement with the U.S. Under the approach in the Canada-U.S. agreement, which was signed on February 5, 2014, Canadian financial institutions will report to the Canada Revenue Agency (CRA) information in respect of U.S. persons that will be transmitted by the CRA to the Internal Revenue Service (IRS) under the Canada-U.S. tax treaty and be subject to its confidentiality safeguards.

Meanwhile, the CRA will receive information from the U.S. in respect of Canadian resident taxpayers that hold accounts at U.S. financial institutions.

SALES AND EXCISE TAX MEASURES

Improving the Application of the GST/HST to the Health Care Sector

Designing Training for Individuals with a Disorder or Disability

The budget proposes to expand the exemption for training that is specially designed to assist individuals with a disorder or disability to also exempt the services of designing an individualized training plan that sets the specific needs and training objectives for the individual. The exemption will apply to the initial development and design of the plan and any subsequent adjustments.

This measure will apply to supplies made after February 11, 2014.

Acupuncturists' and Naturopathic Doctors' Services

The budget proposes that acupuncturists and naturopathic doctors be added to the list of health care practitioners whose professional services rendered to individuals are exempt from the GST/HST.

This measure will apply to supplies made after February 11, 2014.

Eyewear Specially Designed to Electronically Enhance the Vision of Individuals with Vision Impairment

The budget proposes to add eyewear specially designed to treat or correct a defect of vision by electronic means, if supplied on the written order of a physician or optometrist for use by a consumer named in the order, to the list of GST/HST zero-rated medical and assistive devices.

This measure will apply to supplies made after February 11, 2014.

GST/HST Election for Closely Related Persons

The budget proposes to extend, effective January 1, 2015, the availability of the group relief to new members that have not yet acquired any property, provided that the new members continue as going concerns engaged exclusively in commercial activities.

It is also proposed that a filing requirement in relation to the group relief election be introduced. Effective January 1, 2015, parties to a new election will be required to file that election in a prescribed manner with the Canada Revenue Agency. Generally, the election will have to be filed by the first date on which any of the parties to the election is required to file a return for the period in which the election becomes effective. Parties to an election made before January 1, 2015 that is in effect on January 1, 2015 will also be required to comply with this filing requirement, but will have until January 1, 2016 to do so.

In addition, the budget proposes that parties to an existing or new group relief election be subject to a joint and several (or solidary) liability provision with respect to the GST/HST liability that may arise in relation to supplies made between them on or after January 1, 2015.

Joint Ventures

In order to allow more commercial joint venture activities and participants access to the GST/HST simplification benefits available under the joint venture election, the Government intends to propose new joint venture election measures, as well as complementary anti-avoidance measures, that will allow the participants in a joint venture to make the joint venture election as long as the activities of the joint venture are exclusively commercial and the participants are engaged exclusively in commercial activities.

Strengthening Compliance with GST/HST Registration

The budget proposes that the Minister of National Revenue be given the discretionary authority to register and assign a GST/HST registration number where a person fails to comply with the requirement to register, even after having been notified of the requirement to register by the CRA.

This measure will apply on Royal Assent to the enacting legislation.

Standardizing Sanctions Related to False Statements in Excise Tax Returns

The budget proposes to add a new administrative monetary penalty, and to amend the existing criminal offence, for the making of false statements or omissions in an excise tax return and related offences under the non-GST/HST portion of the *Excise Tax Act*. These provisions will be consistent with the GST/HST portion of the *Excise Tax Act*.

These measures will apply to excise tax returns filed after the day of Royal Assent to the enacting legislation.

OTHER MEASURES

Canada Job Grant

The Canada Job Grant will be launched in 2014.

Businesses with a plan to train unemployed and underemployed Canadians for a new or a better job will be eligible to apply for a Canada Job Grant. All Canadians seeking training can, in partnership with an employer, benefit from the Canada Job Grant.

The Canada Job Grant could provide up to $15,000 per person for training costs, including tuition and training materials, which includes up to $10,000 in federal contributions. Employers would be required to contribute on average one-third of the total costs of training. Small businesses will benefit from flexible arrange-ments under the Canada Job Grant, such as the potential to count wages as part of the employer contribution.

The Grant will be for short-duration training provided by an eligible third-party trainer, such as community colleges, career colleges, trade union centres and private trainers. Training can be provided in a classroom, on site at a workplace or online.

Canada Apprentice Loan

Economic Action Plan 2014 proposes to create the Canada Apprentice Loan, which will offer interest-free loans to help registered apprentices with the cost of their training.

Apprentices registered in their first Red Seal trade apprenticeship will be able to apply for interest-free loans of up to $4,000 per period of technical training.

CUSTOMS TARIFF MEASURES

Supporting Offshore Oil and Gas Development

The budget proposes to eliminate the 20-per-cent Most-Favoured-Nation rate of duty on imported mobile offshore drilling units.

This tariff elimination will be given effect by amendments to the Customs Tariff and will be effective in respect of goods imported into Canada on or after May 5, 2014.