Canada | Tax | December 8, 2015

Canadian tax alert

New government's proposed tax changes

On Monday, December 7, the new government of Canada followed up on the Speech from the Throne with Finance Minister Bill Morneau releasing a Notice of Ways and Means Motion ("NWMM") that will implement a number of the tax campaign promises made in the recent election.

This alert provides a summary of the changes included in this NWMM and important related considerations.

Personal tax rate changes

As expected, the government introduced a new, reduced tax rate applicable on income between $45,282 and $90,563. The rate will drop from 22% to 20.5% effective for the 2016 and subsequent taxation years.

A new tax rate of 33%, up from the previous top marginal tax rate of 29% and applicable to income in excess of $200,000, has also been introduced. This increase is also effective for the 2016 and subsequent taxation years. This new rate will be referred to as the "highest individual percentage".

There are two consequential changes to apply the highest individual percentage to the tax rate for trusts other than graduated rate estates and the tax on split income.

Donation credit changes

Given the new highest individual percentage, modifications to the computation of donation credits have also been proposed. Rather than increase the donation credit rate for donations in excess of $200 from 29% to 33%, a more complex formula was introduced which allows donations to receive a 33% credit rate, but only to the extent that the individual's taxable income exceeds $200,000. For any donations made in excess of $200 where the individual's taxable income is less than $200,000, a 29% credit will continue to apply. Three examples are provided below, assuming that $7,200 in donations are made:

	Taxable income of $195,000	Taxable income of $205,000	Taxable income of $250,000
Donation eligible for 15% credit	$200	$200	$200
Lesser of:			
Amount by which total gifts exceeds $200	$7,000	$7,000	$7,000
Amount by which taxable income exceeds $200,000	$0	$5,000	$50,000
Amount of donation eligible for 33% credit rate	$0	$5,000	$7,000
Amount of donation eligible for 29% credit rate	$7,000	$2,000	$0
Total donation credit	$2,060[1]	$2,260[2]	$2,340[3]

The 33% tax credit rate will only be available for donations made after 2015 so any donations carried forward from 2015 or prior years will have a maximum credit rate of 29%.

TFSA changes

As outlined during the Federal election campaign, the Tax Free Savings Account (TFSA) contribution limit for 2015 will remain at $10,000; however, the limit will be reduced to $5,500 for 2016.

Refundable tax on CCPC investment income and dividend refunds

Currently, where a Canadian-controlled private corporation ("CCPC") earns investment income, a refundable tax, equal to 6 2/3% of the lesser of "aggregate investment income" or taxable income, is payable by the corporation. The NWMM amends this rate to 10 2/3%, with the intention being to "reduce personal income tax deferral possibilities that individuals earning investment income directly might otherwise obtain by earning such income through a CCPC"[4].This increase in refundable tax rate will be prorated based on the number of days in the corporation's taxation year that are after 2015.

In addition, where a private corporation receives a taxable dividend from another corporation resident in Canada and is not "connected" with the payer corporation, previous legislation provided that a tax equal to 33 1/3% of the dividend received would be required to be paid under Part IV of the *Income Tax Act*. The NWMM proposes that this rate be increased from 33 1/3% to 38 1/3% of the dividend received. This amendment also applies to taxation years that end after 2015. For taxation years that started before 2016, dividends will be taxed at 33 1/3% if they are received before 2016 and at 38 1/3% if they are received after 2015.

This increase in refundable tax obligations for CCPCs means that modifications to strategies and structures to manage investment income may need to be revisited. Further, the payment of dividends between corporations that are not connected may warrant acceleration in order to reduce the cash flow cost of the increase in Part IV tax.

With the higher refundable tax rate and increased Part IV tax, a corresponding increase in the dividend refund rate, from 33 1/3% to 38 1/3% of taxable dividends paid, is also introduced. This refund rate will also be prorated based on the number of days in the corporation's taxation year that are after 2015. Amendments to related provisions, including the definition of refundable dividend tax on hand, are also proposed to fully reflect the impact of the desired change.

[1] $200 X 15%, plus $7,000 X 29%
[2] $200 X 15%, plus $5,000 X 33%, plus $2,000 X 29%
[3] $200 X 15%, plus $7,000 X 33%
[4] Explanatory Notes relating to proposed amendments to the *Income Tax Act*, Clause 6

Stock option deduction

As has been noted in earlier Deloitte tax alerts, the election platform of the governing Liberal party did call for significant changes to the taxation of stock options to be made. These changes are currently under review and submissions are being made by parties related to the impact of the possible changes.

Dividend tax credit

The NWMM does not propose any changes to the gross up or credit for either eligible or ineligible dividends.

Next steps

Members of Parliament will sit this week before the holiday break, during which time it is expected that this NWMM will pass, moving on to the Senate for consideration thereafter. The Senate is scheduled to sit both this week and next, resulting in a reasonable likelihood of this legislation receiving Royal Assent before the end of the calendar year.

To fully understand the impact on your business and family, it will be important to consider these changes in rates and other anticipated modifications to the tax policy. Your Deloitte team will continue to keep you apprised of the impact of changes.

Updated top marginal tax rates

The table below has been updated for rate changes effective January 1, 2016.

	Ordinary income	Capital gains	Eligible dividends	Non-eligible dividends
British Columbia	47.70%	23.85%	31.30%	40.61%
Alberta	48.00%	24.00%	31.71%	40.25%
Saskatchewan	48.00%	24.00%	30.33%	40.06%
Manitoba	50.40%	25.20%	37.78%	45.69%
Ontario	53.53%	26.76%	39.34%	45.30%
Quebec	53.31%	26.65%	39.83%	43.84%
New Brunswick	58.75%	29.38%	43.79%	51.75%
Nova Scotia	54.00%	27.00%	41.58%	46.97%
Prince Edward Island	51.37%	25.69%	34.22%	43.87%
Newfoundland and Labrador	48.30%	24.15%	38.47%	39.40%
Yukon	48.00%	24.00%	24.81%	40.17%
Northwest Territories	47.05%	23.53%	28.33%	35.72%
Nunavut	44.50%	22.25%	33.08%	36.35%

If you have any questions regarding these changes, please do not hesitate to contact your Deloitte advisor.

For further details on the measures contained in the federal budget, we refer you to the **Department of Finance website**.

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