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"EQUALITY & GROWTH – A Strong Middle Class"
Federal Budget 2018 Summary and Review
Tabled: February 27, 2018

Summary

The 2018 Federal budget continues to build on the Government's plan to build equality and growth to build a strong middle class through the development of the following areas:

a) Growth - The Government has a plan to invest in the middle class and people working hard to join it. This includes more support for those who need it most, to ensure that the benefits of growth are widely shared.

b) Skills for Tomorrow's Economy – The Government recognizes that Our economy is evolving rapidly, with new opportunities and technologies driving growth and reshaping the world of work. To make the most of these emerging opportunities, governments, employers and workers must work together to ensure Canadian workers have the skills they need to succeed in an evolving economy.

c) Strengthening and Diversifying Trade - To ensure that trade benefits Canadians, and to ensure that those benefits are felt by everyone, the Government is:

- Actively deepening trade relationships, through modern, progressive free trade agreements in North America, Europe and new, fast-growing markets in Asia. As a result of the recently concluded Canada-European Union Comprehensive Economic and Trade Agreement (CETA) and Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), preferential market access for Canadian goods and services abroad has more than doubled, from 31 per cent to 63 per cent of world gross domestic product (GDP).
- Making new, transformative enhancements to Canada's export programs to help Canadian businesses find customers around the world.
- Ensuring that trade is done responsibly, in a rules-based way.

d) A Fair Tax System for All Canadians
When middle class Canadians have more money to invest, save and grow the economy, all Canadians benefit. That's why our first substantial piece of legislation was to restore fairness to Canada's tax system, by raising taxes on the wealthiest one per cent, so that we could cut taxes for the middle class.

Forecasted Deficits

As anticipated, the budget projects significant deficits over the next several years.

Projection	Deficit (billions)
2017 – 2018	19.4 (previously forecasted 28.5)
2018 – 2019	18.1 (previously forecasted 27.4)
2019 – 2020	17.5 (previously forecasted 23.4)
2020 – 2021	16.9 (previously forecasted 21.7)
2021 - 2022	13.8 (previously forecasted 18.8)

NOTICEABLY ABSENT MESURES

Noticeable measures **not** included in Budget 2018 include:

a) Additional revisions to the draft income sprinkling rules released on December 13, 2017 to reflect or address stakeholder feedback;
b) A legislative response to the recently enacted US tax reforms;
c) A rumoured increase to the capital gains inclusion rate or the elimination of employee stock option deductions;
d) Comments of a new patent-box regime or enhancements to the refundable SR&ED credits;
e) Amendments to address the issues and anomalies regarding the application of amended ITA 55

BUSINESS INCOME TAX MEASURES

Passive Investment Income Earned by Private Corporations

As expected, Budget 2018 proposes new rules pertaining to the taxation of passive investment income earned by private corporations. Where fuds invested passively within a private corporation have been financed with retained earnings that have been taxed at preferential corporate tax rates, owners of the corporation can benefit from a tax deferral advantage relative to a situation where the corporation distributes the retained earnings and the owners invest personally in passive investments.

Budget 2018 proposes two measures, applicable to taxation years that begin after 2018:

f) Business limit reduction

The budget will limit access to the small business tax rate for SME's that have over $50,000 of passive income in a year; The government backtracked on its earlier pledge to grandfather passive assets and the income from those investment made before this year – as of now there is no such protection in legislation relative to the reduction in the availability of the small business tax rate;

The most important practical effect of the change is the new cap on passive investments within your corporation of $50,000 per year. Exceed the cap, and you will progressively and rapidly lose access to the small business tax rate on active income. Exceed $150,000 and the small business tax rate is eliminated.

Capital gains realized from the sale of active investments or investment income incidental to the business (i.e., interest on short-term deposits held for operational purposes) will not be taken into account in the measurement of passive investment income for purposes of this measure

g) Refund ability of taxes on investment income

Corporations will have new limits on recovering refundable taxes.

Current system - Investment income earned by private corporations is generally paid as non-eligible dividends. However, a corporation may obtain a refund of taxes from its RDTOH account regardless of whether the dividends paid are eligible or non-eligible.

The budget proposes that CCPCs will no longer be able to obtain refunds of taxes paid on investment income while distributing dividends from income taxed at the general corporate rate. Refunds of RDTOH will be available only in cases where a private corporation pays non-eligible dividends.

An exception to this rule applies where an eligible dividend is paid to generate a refund of refundable tax assessed in relation to the receipt of an eligible dividend. To accommodate this exception, the RDTOH of a company will now be divided into two separate classes: an eligible RDTOH pool, which arises from refundable tax assessable on eligible dividends received; and a non-eligible RDTOH pool, which arises from refundable Part I and Part IV tax on everything else.

Restrictions on Income Splitting

The budget legislation did not contain any modifications or improvements beyond those released in October 2017 and it failed to address a number of issues and further clarification on this issue. The key elements of these changes are:

- There are new limits on how business income can be distributed to those who do not have a substantial ownership (10% or more) or who have not contributed substantially to the business
- The most restrictive rules apply to professional business, as well as those businesses that derive income from "services" – which is still undefined.

Small business rate to be lowered over two years

Small business rates to be lowered over a two-year period as follows:

2018 10.0%

2019 9.0% - effective January 1, 2019

Tax Support for Clean Energy

Budget 2018 proposes to extend eligibility for class 43.2 by five years so that it is available in respect of property acquired before 2025

Stop-Loss Rules on Share Repurchase Transactions

Stop-loss rule on share repurchase transactions Budget 2018 proposes to tighten the stop loss rules first introduced in Budget 2011 with respect to share repurchases where shares are held as "mark-to-market" property.

Specifically, the proposed measures expand the existing stop-loss rules to include a denial of the portion of the loss associated with the marked-to-market incremental share value, as that mark-to-market income in most cases is fully offset under a hedging relationship and therefore not taxed. This measure will apply in respect of share repurchases that occur on or after Budget Day.

Health and Welfare Trusts

The current tax system contains two sets of rules for certain trusts established to provide health and welfare benefits to employees. Health and Welfare Trusts, have no legislated rules, but instead have been governed by Canada Revenue Agency (CRA) administrative policies since the 1960s.

More recently, rules have been added in 2010 to the Income Tax Act, governing Employee Life and Health Trusts, which are similar in nature to Health and Welfare Trusts.

Budget 2018 proposes that only one set of rules apply to these types of trust arrangements, and proposes that the CRA no longer apply their administrative policies with respect to Health and Welfare Trusts after the end of 2020.

The government has commenced a stakeholder consultation on these proposed changes and transitional issues, after which the government will propose draft legislation for these changes.

Stakeholders are invited to provide comments to the government by June 29, 2018.

Reassessment Period

Requirements for Information and Compliance Orders Under our current tax system, a taxpayer may normally be reassessed by the CRA within a finite period of time, after which, the tax year becomes statute-barred.

Where the CRA issues a requirement for information to a taxpayer, the taxpayer may choose to contest the requirement in court which can cause delays in the reassessment process, essentially shortening the window in which the CRA has the ability to reassess.

Budget 2018 proposes to introduce a "stop-the-clock" rule for requirements for all information and compliance orders. This rule will extend the reassessment period by the period of time during which the requirement or compliance order is contested.

PERSONAL MEASURES

Canada Workers Benefit

Previously known as the "Working Income Tax Benefit," Budget 2018 has reintroduced this benefit as the "Canada Workers Benefit."

The new Canada Workers Benefit will provide working, low-income Canadians with a benefit equal to 26% of each dollar of earned income that is in excess of $3,000, to a maximum of $1,355 for single individuals without dependents and $2,335 for couples and single parents.

Individuals eligible for the Disability Tax Credit

Further changes have been made with regards to individuals receiving the Canada Workers Benefit who are also eligible for the Disability Tax Credit. Beginning in 2019, the maximum benefit provided to such individuals will be increased to $700.

Medical Expense Tax Credit

Budget 2018 has expanded the application of the Medical Expense Tax Credit (METC), allowing for certain eligible expenses incurred for an animal that is specially trained to assist patients with certain mental impairments.

Currently, eligible expenses related to animals supporting patients who are affected with: blindness, profound deafness, severe autism, severe diabetes, severe epilepsy, or a severe and prolonged impairment that markedly restricts the use of the patient's arms and legs are allowed under the METC.

This eligibility has now been expanded in respect of eligible expenses incurred after 2017 to include such eligible expenses for animals supporting patients with severe mental impairments.

Registered Disability Savings Plan

Budget 2018 has extended the current temporary measures in place that allow for qualifying family members (parents, spouses, or common-law partners) of disabled adult individuals who do not have a legal representative in place to be the plan holder of the disabled individual's Registered Disability Savings Plan (RDSP).

Foreign-born status Indigenous peoples

Currently, foreign-born status Indigenous peoples are eligible for the new Canada Child Benefit, which was introduced in July 2016. Despite their eligibility under this program, such individuals were not eligible for the predecessor programs to the Canada Child Benefit (i.e., the Canada Child Tax Benefit, the National Child Benefit supplement, and the Universal Child Care Benefit).

Budget 2018 therefore proposes that foreign-born status Indigenous peoples be made retroactively eligible for these predecessor programs in the case that all other eligibility requirements have been met. The retroactive effect will apply from the 2005 taxation year to June 30, 2016. Access to taxpayer information.

Access to taxpayer information

As a result of Budget 2018, the Income Tax Act (ITA) will be amended to allow provincial and territorial access to taxpayer information gathered as part of the Canada Child Benefit program, to assist the provinces and territories in their administration of their social assistance payment programs as of July 1, 2018.

Mineral exploration tax credit for flow-through share investors

Budget 2018 has proposed to extend the existing mineral exploration tax credit for an additional year, and flow-through share agreements entered into on or before March 31, 2019 will now qualify. This credit allows resource companies to "flow-through" the tax expenses associated with their Canadian exploration activities to their investors, who are then able to deduct those expenses in the calculation of their own taxable income. In order to provide an additional benefit, a 15% tax credit is then provided on such expenses.

New Reporting Requirements for Trust

Budget 2018 has proposed to require that certain trust be obligated to file a T3 return on an annual basis as of 2021 and subsequent years.

Should the new reporting requirements apply, the trust will now be required to report the following information on their T3 return:

- The identity of all trustees;
- The beneficiaries of the trust;
- The settlors of the trust; and
- The identity of all persons who have the ability (through the trust terms or a related agreement) to exert control over trustee decisions regarding the appointment of income or capital of the trust.

Budget 2018 has also introduced new penalties. Should a trust fail to file a T3 return, in the case that a beneficial ownership schedule is required, a penalty of $25 per day of delinquency will be incurred—with a minimum penalty of $100 and a maximum penalty of $2,500.

SALES AND EXCISE TAX

GST/HST and investment limited partnerships

GST/HST will be payable on the fair market value of management and administrative services provided to an investment limited partnership rendered by the general partner on or after September 2017.

Tobacco taxation

Inflationary adjustments will take effect on April 1 of every year, starting in 2019. Also increases to the excise duty rates by a additional $1.00 per carton of 200 cigarettes. Inventory tax of $0.011468 per cigarette will be charged on inventory held by manufacturers, importers, wholesalers and retailers.

Cannabis taxation

A new federal excise duty framework for cannabis products to be introduced. Generally the duty will apply to all products available for legal purchase, which at the onset of legalization will include all products.

INTERNATIONAL MEASURES NOT SUMMARIZED