2018 Federal Budget Highlights

The main theme of the 2018 Federal Budget—the third budget by Ottawa's ruling Liberal government—is help for working women and women in business. The government is proposing to significantly increase the size of a venture capital fund managed by the Business Development Bank of Canada for financing tech startups led by women.

Another big theme in the budget is gender equality. The Liberals are promising to enshrine gender-based analysis in the budget process and to continually track their progress on equality. There are two key budget initiatives that directly target gender equality. The first is a new paternity leave plan, costing $1.2 billion in the first five years and $344.7 million each year afterward, that supports new dads and other non-birthing parents. The second initiative involves proposed pay-equity legislation that would help bridge the gender pay gap.

And, though Budget 2018 didn't directly address the U.S. federal corporate tax cut, it promised the Department of Finance Canada will conduct a detailed analysis of the stateside tax reforms "to assess any potential impacts on Canada."

Federal income tax brackets 2018

Federal income tax brackets and rates remain unchanged, other than the usual annual indexing of brackets from 2017. The tax brackets and rates for 2018 are as follows:

Income from	**Rate**
$11,809	15.0%
$46,605	20.5%
$93,208	26.0%
$144,489	29.0%
$205,842	33.0%

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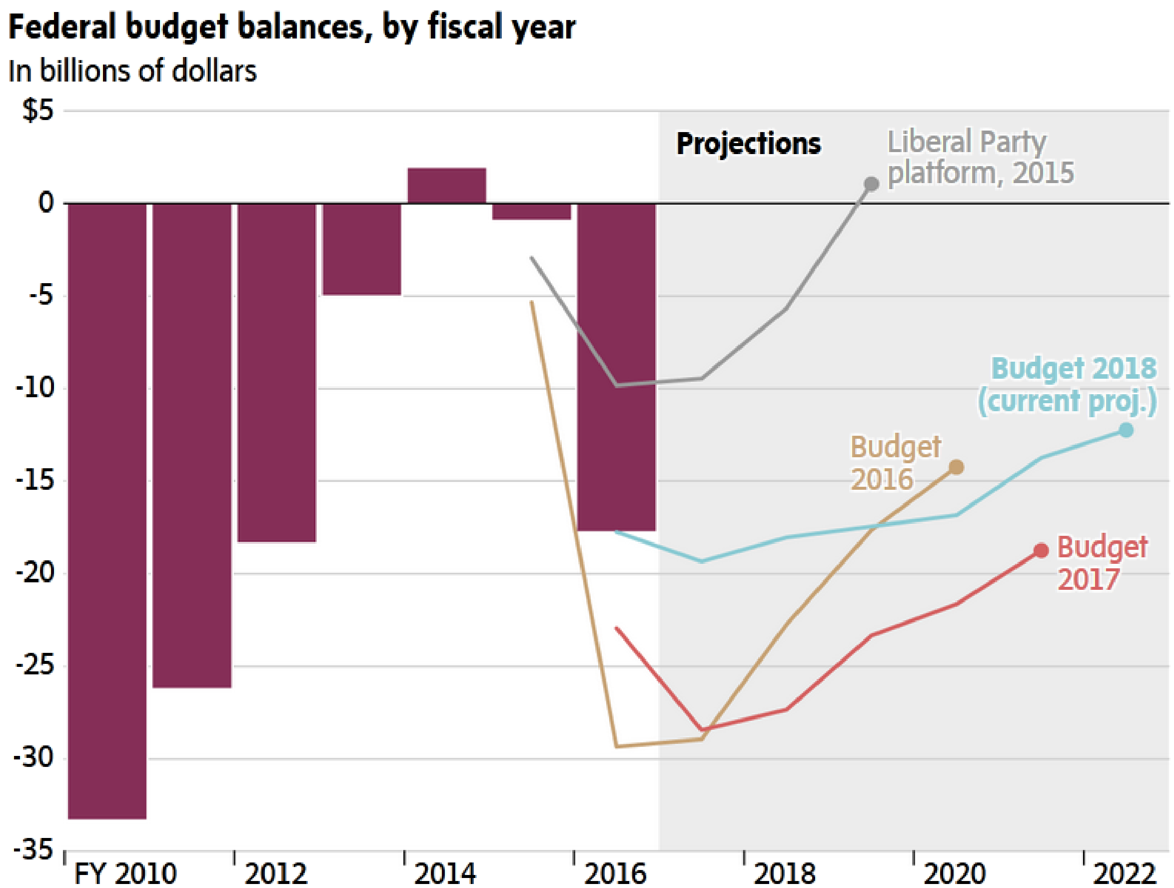
Balancing the Budget

Once again, no precise timeline was given for returning Canada to a balanced budget. The government forecasts a $18.1-billion deficit for 2018-19, with the shortfall anticipated to shrink gradually by an average of $167-million per year. According to the projections, the closest Ottawa will come to a balanced budget will be in fiscal year 2022, with a $12.3-billion deficit.



[IMAGE SOURCE: https://www.theglobeandmail.com/news/politics/2018-federal-budget-highlights/article38116231/]

Debt to GDP Ratio

The federal debt-to-GDP ratio is projected to decline gradually over the forecast horizon, reaching 28.4 per cent in 2022–23. The IMF says Canada's net debt-to-GDP ratio is by far the lowest among G7 countries and less than half the G7 average.

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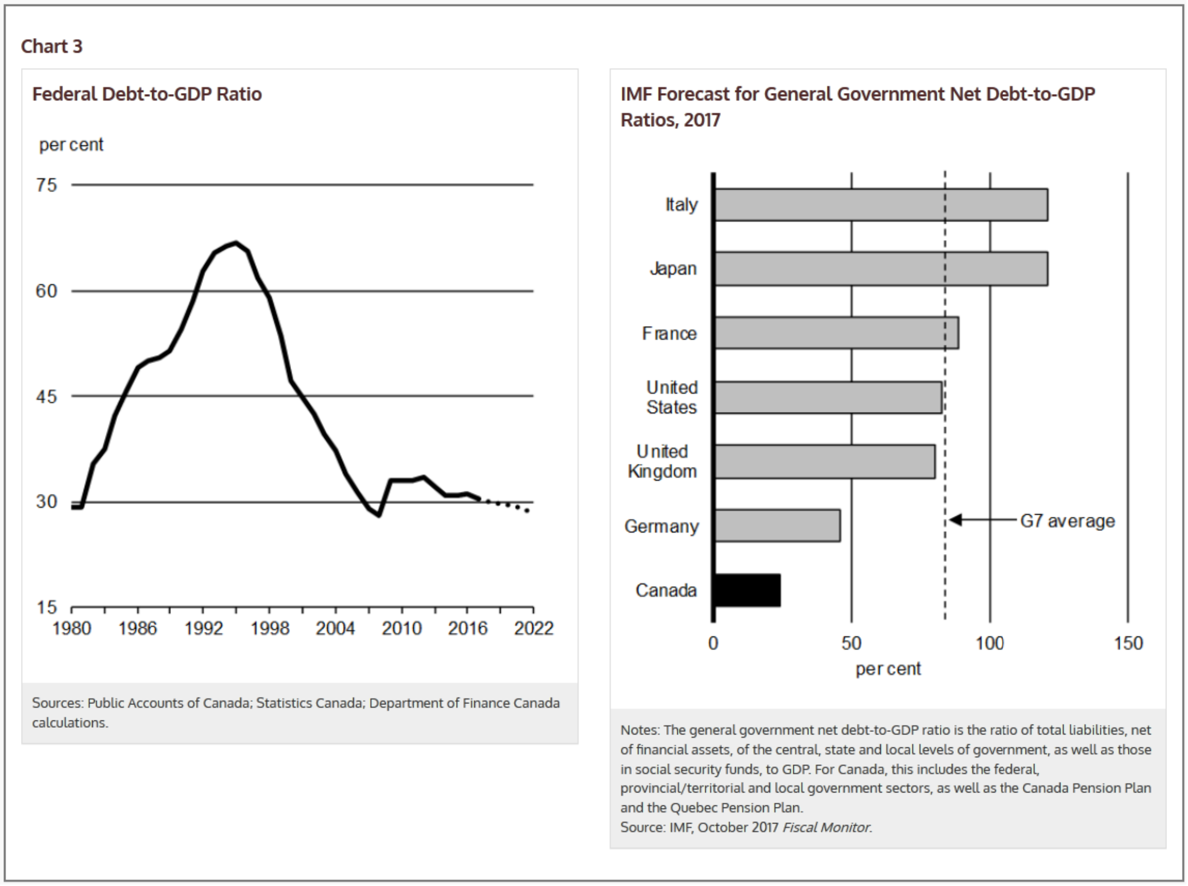

Sources: Public Accounts of Canada; Statistics Canada; Department of Finance Canada calculations.

Notes: The general government net debt-to-GDP ratio is the ratio of total liabilities, net of financial assets, of the central, state and local levels of government, as well as those in social security funds, to GDP. For Canada, this includes the federal, provincial/territorial and local government sectors, as well as the Canada Pension Plan and the Quebec Pension Plan.
Source: IMF, October 2017 *Fiscal Monitor*.

Personal Tax Measures that May Affect You

Canada Workers Benefit

The government has restructured the Working Income Tax Benefit and given it a new name—the Canada Workers Benefit (CWB). The proposals for this refundable tax credit will apply to the 2019 and subsequent taxation years.

Single individuals without dependants

- Calculated as 26% of each dollar of earned income in excess of $3,000
- Maximum benefit: $1,355
- Reduction rate: 12% of adjusted net income in excess of $12,820
- Phase-out income threshold: $24,111

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Families (couples and single parents)

- Calculated as 26% of each dollar of earned income in excess of $3,000
- Maximum benefit: $2,335
- Reduction rate: 12% of adjusted net income in excess of $17,025
- Phase-out income threshold: $36,483

Disability supplement

- Increased to $700 for 2019
- Reduction rate: 12% to match the basic benefit, and 6% if both partners in a family are eligible for the supplement
- Same phase-out income thresholds for single individuals and families as mentioned above

These amounts will be indexed for inflation after 2019. Currently, you cannot obtain the benefit unless you apply using Schedule 6. The government proposes to allow the CRA to proactively determine if individuals are eligible to receive the benefit and assess their returns as if the benefit had been claimed.

Registered Disability Savings Plan

A temporary measure in the Income Tax Act allows certain family members to be plan holders of a registered disability savings plan (RDSP) for adults with disabilities who do not have a legal representative in place. The measure is set to expire at the end of 2018, so the budget proposes to extend it by five years to the end of 2023. Separately, the government says it will continue to encourage the provinces and territories to develop streamlined processes for the establishment of a legal representative to meet the needs of RDSP beneficiaries.

Building a Secure Retirement

Starting in 2019, the Canada Pension Plan (CPP) will be gradually enhanced, following an agreement reached in 2017 by the federal, provincial and territorial governments. This means you will receive higher benefits in exchange for making

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higher contributions. Under Budget 2018, the government also intends to take the following actions for 2019:

- Increase retirement benefits under the CPP Enhancement both for parents who take time off work to care for young children and for persons with severe and prolonged disabilities.
- Raise survivor's pensions for individuals under age 45 who lose their spouse, by providing a full survivor's pension instead of the current reduced pension that is linked to the age of the widow or widower.
- Provide a top-up disability benefit to retirement pension recipients under the age of 65 who are disabled and meet eligibility requirements.
- Increase the death benefit to its maximum value of $2,500 for all eligible contributors.

Medical Expense Tax Credit

Starting this year, the Medical Expense Tax Credit will be expanded to cover more costs associated with animals that have been specially trained to assist a patient in coping with various impairments. If an animal meets the expanded definition, the METC can be applied against the following eligible expenses:

- The initial cost of the support animal
- The cost of the care and maintenance of the support animal
- The cost of training programs required for a patient to learn how to handle the support animal (including reasonable board and lodging expenses should full-time attendance be required at the training facility)

The METC is a 15-per-cent non-refundable tax credit.

Mineral Exploration Tax Credit for Flow-Through Share Investors

This credit is scheduled to expire on March 31, 2018, but Budget 2018 proposes to extend it for another year. Flow-through share agreements entered into on or before March 31, 2019 will now qualify for the credit.

Improving Access to the Canada Learning Bond

The Canada Learning Bond is a contribution that the Government of Canada makes to RESPs to help Canadians save for a child's post-secondary education. The Canada

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Learning Bond is specifically designed to assist low-income families. In last year's federal budget, the government announced a pilot project to explore new ways to increase awareness of the Canada Learning Bond and reduce barriers to access. Building on that measure, Budget 2018 announced that the government is working with the province of Ontario to integrate RESP referrals into the Ontario online birth registration service. This will enable parents to open an RESP at the same time as they apply for other services under the Ontario online birth registration service and receive the Canada Learning Bond immediately.

Business Tax Measures that May Affect You

Passive Investments in a Private Corporation

There has been controversy over the taxation of passive investments in a private corporation since the release of the July 2017 consultation paper. The Federal budget released on Tuesday, February 27, added much needed simplicity and clarity on how passive investments will treated going forward. The government was concerned that Canadian-controlled private corporations (CCPCs) could access the small business rate (currently 13% in Ontario – varies by province) and the after-tax monies could be invested in the business passively, allowing a tax deferral until the funds are distributed as a taxable dividend. In addition to accessing the small business rate, corporations could also access the RDTOH and Capital Dividend Account (CDA), lowering the overall corporate and personal income taxes paid.

The Federal Budget proposes two measures for passive investments held in a corporation, effective for taxation years beginning after 2018.

1. Business Limit Reduction

a) The 2018 Federal budget proposals for passive investments will not change how investment income is taxed, nor will it eliminate the RDTOH as previously announced. Instead, it proposes to reduce the small business limit for CCPCs (and their associated corporations) on a straight-line basis when investment income ranges between $50,000 and $150,000. The small business deduction will be eliminated for use on active income when passive investment income reaches $150,000 (reduced by $5 for every $1 of investment income above the $50,000 threshold). Earning a rate of return of 5%, passive investments of $1,000,000 can be held without a reduction in the small business limit (could vary based on your rate

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of return). For example, a CCPC with $100,000 of investment income would have a business limit reduction to $250,000. Active income up to $250,000 will still benefit from the use of the small business limit and active income in excess of the reduced business limit will be taxed at the general corporate tax rate.

b) Adjusted Aggregate Investment Income – The budget proposes to introduce a new concept of "adjusted aggregate investment income" for determining the business limit reduction. The current concept of aggregate investment income includes interest, royalties, foreign dividends and rent as well as the taxable portion of capital gains. The new concept will have some specific exclusions.

2. Refundability of Taxes on Investment Income

Currently, investment income is taxed at the corporate passive investment rate similar to the top personal income tax rate. Some of this tax paid is refundable at a rate of $38.33 for every $100 of taxable dividends paid to shareholders. Dividends may be eligible or non-eligible.

- Non-eligible dividends (taxed at higher personal tax rates) are usually paid from income subject to the small business tax rate (including non-eligible dividends received by the corporation) or from passive investment income (except non-taxable portion of capital gains and eligible portfolio dividends).
- Eligible dividends (taxed at lower personal tax rate) generally result when active income is taxed at the general rate as well as portfolio dividends from publicly traded Canadian corporations.

The current system allowed a corporation to receive an RDTOH refund when an eligible dividend was paid. This could provide a tax deferral advantage on passive investment income by allowing private corporations paying eligible dividends sourced from active business income taxed at the general corporate income tax rate to generate a refund of taxes paid on passive income.

a) New RDTOH accounts

To better align the refund of taxes paid on investment income, the Federal budget proposes that a refund of RDTOH will be available only when a private corporation pays non-eligible dividends or when RDTOH arises from eligible portfolio dividends received.

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The former RDTOH account will now be referred to as the non-eligible RDTOH account and will track refundable corporate taxes paid on investment income as well as under non-eligible portfolio dividends. In addition, different treatment proposed regarding the refund of taxes imposed on eligible portfolio dividend income will necessitate the addition of a new RDTOH account. This new account (eligible RDTOH) will track refundable taxes paid on eligible portfolio dividends. Taxable dividends paid (i.e., eligible or non-eligible) will entitle the corporation to a refund from its eligible RDTOH account but will be restricted by the new ordering rule described below.

b) RDTOH Refunds – Ordering Rule

The budget implements a new ordering rule for RDTOH refunds. Generally, a non-eligible RDTOH refund must be refunded before a refund from the eligible RDTOH account.

c) RDTOH Recapture

When a dividend is received by a connected corporation, the recipient corporation will include Part IV tax to their RDTOH account. The RDTOH account of the recipient corporation must match the RDTOH account from which the payer corporation obtained its refund.

d) Treatment of existing RDTOH Balance

The transition of the existing RDTOH account will be allocated as follows. The lesser of;

- the existing RDTOH balance, and
- 38⅓ per cent of the balance of its general rate income pool

will be allocated to its eligible RDTOH account.

Any remaining balance will be allocated to its non-eligible RDTOH account. For any other corporation, all the corporation's existing RDTOH balance will be allocated to its eligible RDTOH account.

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In summary, the budget proposals continue to reinforce the importance of tax efficient investing for passive investments in a corporation. Corporate class mutual funds remain an integral component of corporate investment portfolios.

Potpourri

Health and Welfare Trusts

A Health and Welfare Trust (HWT) is a trust established by an employer to provide health and welfare benefits to its employees. Rules have been implemented to align provisions related to the treatment of surplus income and pre-funding of benefits within a HWT, with existing rules introduced in 2010 in respect of Employee Life and Health Trusts. The CRA is expected to apply their administrative positions on Employee Life and Heath Trusts to HWTs beginning in 2021, and HWTs that do not convert or wind up will be taxed as trusts. Additionally, HWTs established after budget day will be subject to the transitional rules. The government is looking for stakeholder input on this measure, with requests for public comments to remain open until June 29, 2018.

Changes to Canada Child Benefits Affecting Foreign-born Status Indigenous Peoples

Currently, foreign-born status Indigenous peoples are eligible for the new Canada Child Benefit, which was introduced in Budget 2016. Previously, such individuals were not eligible for the predecessor programs to the Canada Child Benefit (specifically, the Canada Child Tax Benefit, the National Child Benefit supplement and the Universal Child Care Benefit). The government 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.

Tax support for clean energy

In the 2005 Budget, the government introduced beneficial accelerated capital cost allowance rates for investments in specified clean energy generation and conservation equipment acquired before 2020. Budget 2018 proposes to extend eligibility for those rates by five years so that it is available for property acquired before 2025.

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Tobacco tax

Excise duty rates on tobacco products are currently set to automatically increase every five years to account for inflation. Budget 2018 proposes to advance the inflationary adjustments for tobacco excise duty rates to occur on an annual basis rather than every five years. The inflationary adjustment is to occur each year on April 1, beginning in 2019. A Budget 2018 day inflationary adjustment was made to account for inflation that occurred since the last adjustment in 2014.

Cannabis Tax

In advance of the legalization of cannabis retail sales this summer, tax proposals have been put forward to create a framework for taxing cannabis. The federal government reached a taxation coordination deal with the provinces and territories in December 2017 for the first two years after cannabis legalization. This deal mandates that 75% of the taxation revenues from a combined $1 per gram and 10% excise duty will go to the participating provinces and territories. The remaining 25%, up to a maximum of $100 million annually, will remain with the federal government for each of the first two years. Any federal revenues in excess of $100 million annually will be distributed to the participating provinces and territories.

Previously Announced Measures

Budget 2018 confirmed the government's intention to proceed with the following previously announced tax measures:

- Income tax measures released on December 13, 2017 to address income sprinkling
- The income tax measure announced on October 16, 2017, to lower the small business tax rate from 10.5 per cent to 10 per cent, effective January 1, 2018, and to 9 per cent, effective January 1, 2019 (with related amendments to dividend tax credits for taxable dividends)
- The income tax measure announced on October 24, 2017, in the Fall Economic Statement to provide for the indexing of the Canada Child Benefit amounts as of July 1, 2018, instead of July 1, 2020
- The income tax measure announced in Budget 2016 on information reporting requirements for certain dispositions of an interest in a life insurance policy.

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Getting Advice

Reviewing your tax plan? We encourage you to talk to us. Speak to your Financial Advisor or contact investor services at 1 800 608 7707.

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