Estate planners singing federal budget blues

MERRICK WEALTH

By Peter Merrick

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Peter Merrick, The ICE Solution

The federal budget will surely be a hot topic at the 18th national conference of the Society of Trust and Estate Practitioners (STEP) in Toronto on June 9-10.

"The new federal budget … continued to make good on the government's election promise to collect more taxes." And so began my recent conversation with Mark Halpern, CEO of WEALTHinsurance.com.

Halpern and I were discussing how much we both look forward to attending the STEP conference. More than 650 of the top legal, tax, trust, accounting and insurance experts from Canada and abroad will gather to address the recent and pending changes to planning and taxation in this country.

"Wealthy in Canada was recently redefined to include people earning more than $200,000 annually. With provincial taxes taken into account, the highest earners now lose more than half of their earnings to income tax. In its budget, the federal government ensured some legal "loopholes" don't accidentally pay out too much in tax benefits and this is a reality that we professional advisers must address" said Halpern.

In this month's column I want to share some of the topics we anticipate will be addressed at the STEP gathering.

The budget eliminated a version of income splitting, previously known as the "family tax cut credit." Introduced by the previous government in 2014, it would have allowed an individual to notionally transfer up to $50,000 of his or her income to the lower-income spouse or common-law partner, if they had a child under age 18. It would have meant a savings of up to $2,000 a year in taxes.

Recognizing the additional costs of caring for a child with a severe disability, the government increased the maximum child disability credit from $2,695 to $2,730.

It's important to note both the Canada child benefit and the child disability benefit are income based. The Canada child benefit will replace several current benefits, some of which (such as the universal child care benefit) were not income based. Unfortunately, as a result of the new budget, previous guidelines to qualify for the child disability benefit will probably be changed, and any family with income over $150,000 will have benefit reductions and no benefits will be available to families with income above $180,000.

Charities and taxpayers were dealt a nasty blow. The government announced it will not proceed with the implementation of a charity friendly plan (introduced by the previous government) to eliminate the capital gains tax on the sale of appreciated real estate and private company shares if the proceeds were donated to charity within 30 days.

A Canadian business that qualifies as a Canadian-controlled private corporation (CCPC) qualifies for a number of tax benefits, including access to the small business tax rate on the first $500,000 of active business income. The government announced it would freeze the small business tax rate at 10.5% for an indeterminate period.

The budget slammed the door shut on life insurance policy transfers. Your life insurance policy can still be transferred to a private corporation or partnership, but you can no longer take anything more than the fair market value of a policy over its cash surrender value as a tax-free benefit.

A similar measure will apply to cut the amount added to a capital dividend account, paid-up capital and/or adjusted cost base when a policy is transferred to a corporation of a partnership.

Upcoming tax rule changes effective Jan. 1, 2017 concerning tax-exempt life insurance will have an even greater impact on wealthy Canadians than this new budget. Halpern and I are keenly interested to see how this topic will be addressed by the experts during roundtable discussions at the STEP conference.

The new insurance rules will change the exempt test of certain life insurance policies, sharply reducing the maximum cash value accumulations allowed to build up tax-free. Currently, if the policy is deemed exempt from tax, anything over the basic amount can grow without tax within government limits. Starting next year, the tax-free amount will be reduced. Insurance policies issued before 2017 will be grandfathered. As a practical matter, this opportunity is only available until October because it usually takes about 90 days to get a new policy through the process of application, medical underwriting and issuance.

Shareholders of private corporations should consider an insured annuity because it provides higher cash flow during your lifetime than most fixed-income guaranteed instruments with lower tax rates that allow you to leave funds to your beneficiaries through a life insurance policy. The combination of an annuity plus life insurance is ideal for shareholders of private corporations with surplus capital that is not required to operate the business.

Business owners and incorporated professionals may want to look at the idea of a personal pension plan, often a better alternative to traditional RRSPs, approved by Canada Revenue Agency and available for one or more employees. All contributions made by the employer are fully tax deductible and a non-taxable benefit to the employee.

Personal pension plans (PPP) can be used by an operating company (Opco) or holding company (Holdco). The PPP test is met if the corporation pays T4 income to the employee for services rendered. A Holdco can act as plan sponsor, with an Opco as participating employer, and both can contribute to the PPP.

Under these plans, you can enjoy higher contribution limits, better returns, improved creditor protection and the ability to transfer wealth to family members on a tax-free basis. An additional benefit of setting up a PPP is that it is considered a "comparable plan" under the Ontario Retirement Pension Plan (ORPP) that is slated to impact every business in Ontario starting in 2018. The federal government may obtain the support of enough provincial governments to expand the Canada Pension Plan along the lines of the ORPP. Budget 2016 reaffirmed Ottawa's desire to implement a Canada-wide agreement on an expanded CPP.

Expect more changes and higher taxes. The government promised to undertake a comprehensive examination of the entire tax system with a view to eliminating the ability of high net worth individuals to use private corporations to inappropriately reduce or defer tax.

Halpern summed it up best by saying: "The federal government eliminated or reduced a number of benefits available to high net worth Canadians. Aside from lottery winnings, your primary residence and Tax-Free Savings Accounts (TFSAs), life insurance is still one of the few tax-free vehicles still available to everyone for effective tax planning."

The STEP conference will be only days away when this column is published. I plan to report any useful and helpful planning information gleaned from attending the CRA Roundtable and workshops. Stay tuned.

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Act mandates climate change action plan

Drewes

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Torben Drewes, Trent University

"A top concern of Ontario's business community regarding cap and trade is competitiveness. Moving into a climate leadership position in North America brings both opportunities and risks, including moving out of step with our competitor jurisdictions," he warned.

"We are therefore very supportive of the government's decision to provide transitional allowances, something that has been done and continues to be done in other jurisdictions. To be clear, large emitters will still be required to reduce their emissions. However, this design decision gives them more time to adjust to operating in an environment with a carbon price," O'Dette said.

The act also requires the Ontario government to prepare and implement a plan for achieving its targets. It must include detailed content, such as a timetable for implementing each specified action, the estimated greenhouse gas reductions that each action will achieve, and the cost per tonne of reductions, among other details.

Progress reports, as well as a review of this plan, will be required at least every five years.

The Ontario cap-and-trade will be facilitated to link with existing programs in Quebec and California.

"It makes a larger pool for trading the permits, which I think is good," said Forman.

Drewes not only believes there is an advantage associated with Ontario linking its fledgling cap-and-trade to Quebec and California, he would like to see more North American jurisdictions involved.

"If California reduces its emissions by one tonne, it has the same effect on us as if the local polluter reduces emissions by one tonne. The whole idea of cap and trade — allowing that permits be tradable efforts, is to achieve a global reduction in emissions at the least possible resource cost. We don't want to devote any more labour and capital to reducing those emissions than we have to.

"And so … the bigger that market, the deeper that market, the more efficiencies you gain," Drewes said.