CHARTERED PROFESSIONAL ACCOUNTANTS CANADA
COMPTABLES PROFESSIONNELS AGRÉÉS CANADA

Budget 2015 earns a B grade

Chartered Professional Accountants of Canada (CPA Canada) gives the federal budget a B grade as the government attempts to address the challenges of today and to better prepare Canadians for the future.

Growing the economy works best from a strong fiscal base and the projected surplus is $1.4 billion for 2015-16, with a string of slightly higher surpluses for the next four years. The government will have little wiggle room in managing its finances with the contingency fund being trimmed to $1 billion from $3 billion.

Among other things, the budget reduces the small business tax rate, proposes a 10-year investment incentive that will allow a faster write-off for machinery and equipment, and almost doubles the annual contribution limit for Tax-Free Savings Plans. While support for businesses and individual Canadians is important to our prosperity, the government did not look at the broader picture and indicate its intention to address significant tax reform.

It is time for a comprehensive review of the country's tax system to reduce its complexities and inefficiencies. Tax reform and simplification would help improve Canada's international competitiveness, productivity and economic growth.

Below we summarize some of the key changes in Budget 2015 and their impact on Canadians and Canadian businesses.

Supporting small businesses

Small business tax rate

Budget 2015 proposes to reduce the small business tax rate in stages from 11% to a target rate of 9%, as of 2019. This rate applies on the first $500,000 per year of qualifying active business income of a Canadian-controlled private corporation. For dividends paid out of this income, the gross-up factor and dividend tax credit rate are also adjusted so that the benefit of this low rate is offset when the income is paid out to the shareholder.

Small business tax rate and DTC adjustment for non-eligible dividends

	2015	2016	2017	2018	2019
Small business tax rate (%)	11	10.5	10	9.5	9
Gross-up (%)	18	17	17	16	15
DTC (%)	11	10.5	10	9.5	9
Source: Department of Finance Canada, Economic Action Plan 2015					
Top marginal federal tax rate on non-eligible dividends	21.22	21.62	22.21	22.61	22.97
Source: CPA Canada					

Support for farmers and fishers

Budget 2015 increases the lifetime capital gains exemption (CGE) for individuals to up to $1 million (from $813,600) of capital gains realized on the disposition of qualified farm or fishing property. The CGE exemption amount for qualified small business corporation shares remains at $813,600.

The budget also extends the temporary tax deferral that applies to patronage dividends paid to members by an eligible agricultural cooperative to eligible shares eligible shares issued before 2021.

Business Tax Measures

CCA reform – greater commitment needed

Since 2007, manufacturing and processing equipment has been eligible for depreciation at a special rate of 50% on a straight-line basis, which was set to expire at the end of 2015. Budget 2015 proposes to provide manufacturers with an accelerated capital cost allowance (CCA) at a rate of 50 per cent on a declining-balance basis for eligible assets acquired after 2015 and before 2026.

While this investment incentive will assist Canada's manufacturing sector, we encourage the government to make a greater commitment to ongoing CCA reform. With the current pace of technological change and shortening business life cycles, CCA rates should be reviewed for all classes of equipment so that they correspond to the true economic life of the asset.

Updating CCA rates would encourage manufacturers to invest in the most modern, productivity-enhancing equipment, and thus enhance their competitiveness in the global economy. Reducing the expanding number of CCA classes would go a long way to simplifying the tax system.

Consultation – active versus investment business

Budget 2015 announces a review of the circumstances in which income from a business, the principal purpose of which is to earn income from property, should qualify as active business income. The review will cover, among other things, the current definition of "specified investment business."

Simplifying the "eligible capital property" rules

In last year's federal budget the government opened consultations in response to calls from CPA Canada and others for simplified tax depreciation for intangible property (such as goodwill, licenses and franchises) by creating a new capital cost allowance class (CCA) for such property. In Budget 2015, the government announced plans to release detailed draft legislation for further consultation.

Personal Tax Measures

Targeted tax credits versus broad-based relief

In Budget 2015, the federal government continues to opt to ease the personal tax burden through tightly targeted measures. A new 15% credit is introduced for home improvements that increase accessibility for seniors and persons with disabilities, on a maximum expenditure of $10,000, starting in 2016. Receipts will be needed to support the credit claim.

CPA Canada supports the added benefit of this credit in discouraging underground economic activity, as well as the goal of reducing the personal tax burden on Canadians. However, such specific tax measures add unneeded complexity to the tax system. The simpler alternative would be to provide broader-based tax relief (for example, through lower personal tax rates) as Canada's fiscal situation permits.

Promoting saving and retirement planning

<u>Tax-Free Savings Accounts</u>

The budget proposes to increase the annual contribution limit for Tax-Free Savings Accounts to $10,000 (from $5,500) for 2015 and later years. The limit will no longer be indexed to inflation.

The adequacy of retirement savings is a key challenge associated with our aging population. Tax-Free Savings Accounts are a welcome incentive to help Canadians save more for their eventual retirement and to manage their finances after they retire.

<u>Registered retirement income funds</u>

In another change that would give seniors more flexibility in managing their finances during retirement, Budget 2015 proposes to reduce the RRIF minimum withdrawal percentage that apply for people aged 71 to 94, starting in 2015. The withdrawal amount at age 71 has dropped to 5.28% (from 7.28%), increasing gradually each year until it reaches 20% after age 94.

Supporting charities

Donations involving private shares and real estate

To support Canadian charities, Budget 2015 proposes a capital gains exemption for the arm's length sales of private company shares and real estate when the proceeds are donated to charity within 30 days of the sale, effective for 2017 and later years.

Foreign charitable foundations

The budget proposes to extend eligibility for the charitable donation tax credit or deduction to foreign charitable foundations if they receive a gift from the federal government and if they are pursuing activities related to disaster relief or urgent humanitarian aid or are carrying on activities in the national interest of Canada.

Reducing red tape

Red tape places an undue burden on business and stifles competition and growth, especially for smaller businesses. We support the changes introduced in this budget but believe that more can and should be done.

Withholding for non-resident employees

With this budget, the government proposes to resolve persistent administrative problems with the current process for obtaining waivers from withholdings on remuneration to non-resident employees working in Canada. An exception to the withholding requirements is proposed for payments by qualifying non-resident employers to qualifying non-resident employees who are:

- exempt from Canadian income tax because of a tax treaty, and
- present in Canada for fewer than 90 days in any 12-month period that includes the time of the payment.

We encourage the government to similarly address red tape related to withholdings on payments to non-residents for services rendered in Canada under Regulation 105, as recommended by CPA Canada and others, including the Advisory Panel on Canada's System of International Taxation in its December 2008 report.

Foreign asset reporting – Form T1135

We welcome the news that the CRA is simplifying the foreign asset reporting system for 2015 and later years. Under the revised form being developed by the CRA, if the total cost of a taxpayer's specified foreign property is more than $100,000 and less than $250,000 throughout the year, the taxpayer will be able to report these assets to the CRA under a new simplified foreign asset reporting system.

The current detailed reporting requirements will continue to apply to taxpayers with specified foreign property that has a total cost at any time during the year of $250,000 or more.

We are pleased that the government has adopted this measure, which we called for in our representations to the government. However, the requirements could be further streamlined. For example, the government could adopt our other recommendations, such as extending the current filing deadline and by excluding the reporting of foreign securities held in accounts with registered Canadian securities dealers.

Penalty for repeated failure to report

We applaud the government's proposal to change the repeated failure to report income penalty. As we have pointed out in our representations to government, the penalty often applies disproportionately to nominal lapses. The amount of the penalty is reduced, and the penalty will apply only if a taxpayer fails to report at least $500 of income in the year and in any of the three preceding taxation years.

More red tape reduction measures

Other proposals to cut red tape in the tax system include:

- Reducing the frequency of remittances to the CRA by new employers to quarterly.
- Broadening the use of Business Numbers as a common identifier to simplify dealings with federal, provincial and municipal governments.
- Introducing a series of improvements to the CRA's taxpayer services, including expansion of its online services, improving the use of plain-language communications, making the pilot Liaison Officer Initiative permanent, and ensuring taxpayers can rely on written information received in a letter or on the CRA's website.

Protecting the tax base

Combatting tax avoidance and evasion

Budget 2015 commits new funds to help the Canada Revenue Agency (CRA) strengthen tax compliance in Canada and internationally:

- The budget proposes $118.2 million over five years for the CRA to expand its Underground Economy Specialist Teams.
- The budget proposes $25.3 million over five years for the CRA to expand its activities to combat international tax evasion and aggressive tax avoidance.

Curbing tax evasion by multinational companies

Budget 2015 announces that Canada will continue to participate in the OECD/G-20 project on Base Erosion and Profit Shifting, which aims to develop coordinated multilateral solutions to address international tax planning strategies used by multinational enterprises to inappropriately minimize their taxes. The government looks forward to the project's conclusion and to discussions with the international community on the implementation of the recommendations.

We support the government's view that improving business tax competitiveness fosters an environment in which businesses can thrive and compete in the global economy. Taxes are one of the main factors that drive investment decisions.

CPA Canada will continue to work closely with the Department of Finance Canada and the CRA to ensure that actions in this area are properly targeted and do not cause unintended consequences for international competitiveness of Canadian businesses and investors. We are pleased the government has indicated it will balance its efforts to reduce international tax evasion and avoidance while ensuring it does not adversely affect Canada's international competitiveness.

Specific international anti-avoidance rules

Budget 2015 proposes some new measures to combat international tax evasion and avoidance, including:

- Implementing the OECD's new common reporting standard for automatic information exchange, starting on July 1, 2017 to allow a first exchange of information in 2018.

- Ensuring that corporations do not realize unintended tax benefits on synthetic equity arrangements.
- Improving the existing anti-avoidance rule that is meant to prevent corporations from converting their taxable capital gains into tax-free dividends.
- Improving the existing anti-avoidance rule in Canada's foreign accrual property income regime regarding captive insurance to help ensure that income of foreign affiliates of Canadian taxpayers from the ceding of insured Canadian risks remains taxable in Canada.
- Clarifying that the CRA or the courts may increase or adjust an amount included in an assessment that is under objection or appeal, as long as the overall tax amount assessed does not increase.

Promoting economic growth

Strengthening financial literacy

In Budget 2015, the federal government commits to releasing a National Financial Literacy Strategy in 2015-16 for Canadians of all ages. This strategy will set out goals and priorities to strengthen the financial literacy of Canadians throughout their lives.

Given that financial capabilities vary widely among Canadians, we must ensure that people have the skills, knowledge, information and resources they need to make wise decisions regarding their long-term financial security. CPA Canada actively participates in improving financial literacy through its programs and representation on Canada's first National Steering Committee on Financial Literacy.

Supporting skilled professionals

Budget 2015 proposes to reallocate up to $35 million over five years, starting in 2015-16, to make the Foreign Credential Recognition Loans pilot project permanent to support internationally trained individuals in their pursuit of foreign credential recognition.

Skilled professionals are vital to Canada's economic future and CPA Canada welcomes the federal government's efforts to quickly integrate internationally trained professionals into the Canadian labour market.

We are pleased to work with the federal government on initiatives that speed the integration of internationally trained accountants into the Canadian workforce. Federal funding plays an important role in creating online self-assessment tools for foreign credentials and pre-arrival information for prospective immigrants.

Enhancing trade

Trade and investment are important to the continued growth of Canada's economy and contribute to the prosperity of people and businesses across Canada. CPA Canada supports efforts to negotiate trade agreements that eliminate barriers to the free movement of goods, services, capital and labour – both internationally and within our country.

Proposed actions in Budget 2015 include:

- Providing $50 million over five years for a program to share the cost of exploring new export opportunities with small and medium-sized enterprises.
- Providing $42 million over five years to expand the footprint and resources of the Trade Commissioner Service
- Creating an Internal Trade Promotion Office within Industry Canada to support efforts to renew the Agreement on Internal Trade.

Advancing innovation

Canada's ability to innovate is critical to the country's competitiveness and long-term prosperity. There is a growing consensus that Canada's relatively low levels of productivity growth in comparison to other major industrialized economies is due to an underinvestment in research and development activities by Canadian businesses.

Budget 2015 announces measures to support world-class advanced research, including investments in leading-edge research infrastructure and additional funding to the granting councils. There are also specific measures aimed at fostering business innovation.

While these measures are welcome, CPA Canada believes that enhanced tax incentives are needed to encourage businesses to conduct more R&D and commercialize innovation in Canada, as the fiscal situation permits. For example, other countries encourage the commercialization of innovation through “patent box” regimes, which reduce taxes on profits earned from such activities. Introducing a patent box regime would encourage firms to commercialize innovation in Canada, thereby spurring economic growth, creating value-added jobs, improving Canada’s productivity record, and increasing Canadians’ standard of living.

About CPA Canada

Canada’s accounting profession is uniting under a new single designation, Chartered Professional Accountant (CPA). The profession’s national body, Chartered Professional Accountants of Canada (CPA Canada), represents and supports more than 190,000 members across the country. CPAs are valued for their financial and tax expertise, strategic thinking, business insight, management skills and leadership. CPA Canada has consolidated the operations of three national accounting bodies: The Canadian Institute of Chartered Accountants, the Certified General Accountants Association of Canada and The Society of Management Accountants of Canada. CPA Canada conducts research into current and emerging business issues and supports the setting of accounting, auditing and assurance standards for business, not-for-profit organizations and government. It also issues guidance on control and governance, publishes professional literature and develops certification and continuing education programs.