

# Federal Budget Brief 2017



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## Federal budget missing key target for future planning

Today's federal fiscal blueprint charts a course for economic renewal but fails to identify an important destination by not outlining when the government plans to return to balanced budgets.

The budget deficit is expected hit a high of \$28.5 billion in fiscal 2017-2018 and eventually decline to \$18.8 billion in fiscal 2021-2022.

Budget 2017 raises concerns because there is no timeline to address these persistent deficits. Establishing a target date to bring the budget back into balance would create a goalpost to guide the government in its financial planning. This would greatly assist in fostering business confidence, supporting essential programs and minimizing the burden on future generations.

CPA Canada recognizes that for the economy and Canadians to truly prosper, strong fiscal management is only part of the equation. It must come in conjunction with measures aimed at helping individuals, families and businesses succeed, achieve and prosper. The new budget outlines extensive long-term investments in skills training, innovation and infrastructure funding, including a focus on lifelong learning, youth employment, and measures to support innovation.

We support the federal government's focus to address how Canadians are being affected by broad economic forces, including technological change and automation. Canada's future prosperity will be directly linked to the competitiveness of its workforce.

In addition, the budget builds on earlier announced efforts to combat tax evasion and to improve compliance. The government also is reiterating its commitment to work with international partners to ensure a coherent and consistent response to fight tax evasion.

CPA Canada is dedicated to supporting the government in implementing measures for a globally equitable, consistent and modern international tax system. The government's commitment to strengthening compliance reinforces Canada's determination to protect the public interest.

The budget notes that the federal government will work with the provinces to implement strong standards for corporate and beneficial ownership transparency to provide safeguards against money laundering, terrorist financing, tax evasion and tax avoidance.

Budget 2017 announces several measures resulting from its review of federal tax expenditure announced in 2016. This budget includes measures described below to streamline and eliminate certain personal tax credits, and to conduct further review on the tax treatment of private corporations. The scientific research and experimental development (SR&ED) tax incentive program is being studied as part of a broader review of government support for innovation.

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CPA Canada firmly believes a more comprehensive review of the entire system is required.

We have consistently called for a broad-based approach to be applied when looking at making changes to the tax system. An extensive review can identify areas that will assist in recalibrating the tax system so that it not only enhances efficiencies and fairness for Canadians and the business community but also plays a role in cultivating long-term, sustainable economic and social growth.

Successful Canadian businesses must always navigate change. With the current economic uncertainty south of the border, CPA Canada is encouraging the Canadian government not to become paralyzed in its decision making and to continue to focus on strategies and measures that ensure Canada remains competitive and is able to attract and retain top talent.

One final note, it is the end of an era. The Canada Savings Bonds Program, created in 1946, is being phased out as it is no longer a cost-effective source of funds for the federal government.

Below we summarize some of the key measures in Budget 2016 and their impact on Canadians and Canadian businesses.

## Business Tax Measures

### **Business income of professionals**

Budget 2017 eliminates the tax deferral available to certain designated professionals through the use of billed-basis accounting for income tax purposes. For tax years starting after March 22, 2017, accountants, lawyers, medical doctors and other designated professionals may not longer elect to exclude the value of work-in-progress when computing their taxable income. A transitional measure is provided for the first taxation year in which this measure applies.

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## Taxation of private corporations

The government announced it is reviewing the use of tax planning strategies involving private corporations that inappropriately reduce personal taxes of high-income earners. A paper will be released in the coming months. Examples in the budget plan of strategies that may create unfair tax advantages include:

- “sprinkling income” using private corporations by using dividends or capital gains to cause income to be taxable to family members at a lower personal tax rates (or not taxed at all)
- holding passive investments inside private corporations
- converting a private corporation’s regular income into capital gains.

The government also says it will consider whether there are features of the current income tax system that have an inappropriate adverse impact on genuine business transactions involving family members (e.g., presumably, intergenerational transfers).

## Investment fund mergers

Budget 2017 proposes to extend the mutual fund merger rules to facilitate the reorganization of a mutual fund corporation that is structured as a switch corporation (corporations with multiple share classes) into multiple mutual fund trusts on a tax-deferred basis, for qualifying reorganizations that occur on or after March 22, 2017.

To provide consistent treatment between mutual fund trusts and segregated funds, Budget 2017 proposes to allow insurers to effect tax-deferred mergers of segregated funds under rules generally parallel those for mutual fund mergers. The budget also proposes to allow segregated funds to carry forward non-capital losses that arise in taxation years that begin after 2017, subject to the normal limitations for non-capital loss carryovers.

To give the life insurance industry an opportunity to comment on these proposals, these measures will apply to mergers of segregated funds carried out after 2017 and to losses arising in taxation years that begin after 2017.

## Other business tax measures

Additional tax measures affecting business in Budget 2017 include:

- eliminating the immediate deduction for expenses associated with oil and gas discovery wells and treating these expenses as depreciable Canadian development expenses, unless and until these expenses become unrecoverable
- eliminating the tax preference that allows small oil and gas companies to reclassify Canadian development expenses as immediately deductible Canadian exploration expenses when they are renounced to flow-through share investors
- expanding the accelerated capital cost allowance treatment of eligible geothermal energy equipment to additional heat- and electricity generating

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equipment and expanding geothermal equipment-related expenses that qualify as Canadian renewable and conservation expenses

- eliminating the tax exemption for insurers of farming and fishing property.

## Personal Taxes and Benefits

### Canada Caregiver Credit

Following the federal tax expenditure review, Budget 2017 proposes to simplify the tax system by replacing the Caregiver Credit, Infirm Dependant Credit and Family Caregiver Tax Credit with a single credit: the Canada Caregiver Credit. This non-refundable credit will apply to caregivers whether or not they live with their family member, and aims to help families with caregiving responsibilities.

### Cancelled personal tax supports

Following the government's tax expenditure review, the following personal tax measures are being eliminated due to their limited impact, low take-up or duplication with other support:

- the deduction for employee home relocation loans
- the public transit tax credit, eliminated for transit use occurring after June 30, 2017
- the GST/HST rebate for non-resident tourists and non-resident tour operators for the accommodation portion of tour packages
- the 25-per-cent investment tax credit for child care spaces
- the first-time donor's super credit (already set to expire in 2017).

### Adjustments to existing credits

Among changes to existing tax credits, Budget 2017 proposes to:

- add nurse practitioners to the list of medical practitioners that can certify the impacts of impairments for disability tax credit applicants
- expand the range of courses eligible for the tuition tax credit to include occupational skills courses that are undertaken at post-secondary institutions and to allow the full amount of bursaries received for such courses to qualify for the scholarship exemption
- extend eligibility for the medical expense tax credit to expenses of individuals who require medical intervention in order to conceive a child (including single people and same-sex couples).

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## Mineral exploration credit

As previously announced, to encourage investment through tax incentives, Budget 2017 proposes to extend eligibility for the mineral exploration tax credit for one year, to flow-through share agreements entered into on or before March 31, 2018.

# Protecting the Tax Base

## Improving tax compliance

### More funds to prevent tax evasion and tax avoidance

CPA Canada supports government efforts to maintain the integrity of the tax system and welcomes this budget's commitment of an additional \$523.9 million over five years to prevent tax evasion and improve tax compliance. The investment will be used to support the Canada Revenue Agency in its continued efforts to crack down on tax evasion and combat tax avoidance by:

- increasing verification activities.
- hiring more auditors and specialists with a focus on the underground economy
- developing business intelligence infrastructure and risk assessment systems to target high-risk international tax and abusive tax avoidance cases
- improving the quality of investigative work that targets criminal tax evaders

These funds are expected to raise an additional \$2.5 billion in tax revenues over five years.

## Improving domestic tax integrity

### Closing loopholes

Budget 2017 proposes a number of actions to strengthen the integrity of the tax system that would:

- prevent the avoidance or deferral of income tax through the use of offsetting derivative positions in straddle transactions
- extend to Registered Education Savings Plans and Registered Disability Savings Plans anti-avoidance rules similar to the ones applicable in connection with Tax-Free Savings Accounts and Registered Retirement Savings Plans
- clarify the Income Tax Act's definition of "factual control" for determining who has control of a corporation to prevent inappropriate access to supports such as the small business tax rate and the enhanced SR&ED tax credit for small businesses

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## Improving international tax integrity

### Base erosion and profit shifting

Budget 2017 renews the federal government's commitment to work with other G20 and OECD members to ensure a coherent and consistent response to international tax avoidance through base erosion and profit shifting, although only one specific new measure was announced (see below).

### Extending BEPS rules for foreign branches of Canadian life insurers

The one new measure announced in this budget to improve the integrity of the tax system is a proposal to prevent the avoidance of tax on income from the insurance of Canadian risks. This would be achieved by extending the foreign-affiliate base erosion rules to foreign branches of Canadian life insurers for tax years of Canadian taxpayers starting on or after March 22, 2017.

# Indirect Tax Measures

## Sales and excise tax changes

Budget 2017 announces a series of targeted sales and excise tax measures that include:

- extending the definition of a taxi business for GST/HST purposes to include ride-sharing businesses, making them subject to the same GST/HST rules as taxis
- eliminating the surtax on domestic tobacco manufacturers, and adjusting tobacco excise duties accordingly to continue discouraging tobacco consumption
- increasing excise duty rates on alcohol products by 2 per cent on March 22, 2017, and adjusting these rates for inflation on April 1 of 2018 and later years
- adding the opioid treatment drug naloxone to the list of GST/HST-free non-prescription drugs that are used to treat life-threatening conditions.



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# Improving Tax Administration

## Electronic distribution of T4 slips

Budget 2017 proposes to allow employers to distribute T4 (Statement of Remuneration Paid) information slips electronically to current active employees without having to obtain their advance consent, provided the employer has sufficient privacy safeguards in place.

CPA Canada welcomes this measure as it will reduce compliance costs and increase efficiencies for employers, increase convenience for many employees, and streamline administration for the Canada Revenue Agency. CPA Canada call for this change in its pre-budget representations in support of a recommendation made by the Canadian Payroll Association.

# Outstanding Tax Measures

Budget 2017 confirms the government's plans to move ahead with several proposals that are not yet enacted, as modified to reflect consultations and review:

- changes to the principal residence exemption announced on October 3, 2016
- information reporting requirements announced in Budget 2016
- for certain dispositions of an interest in a life insurance policy
- proposed income tax technical amendments released on September 16, 2016
- proposed GST/HST amendments released on July 22, 2016
- measures confirmed in Budget 2016 relating to the GST/HST joint venture election.



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# Promoting Economic Growth

## Infrastructure

Building on the 2016 Fall Economic Update, Budget 2017 contains some further detail on proposed infrastructure spending, although in broad strokes. Similarly, new information about the proposed Canada Infrastructure Bank is brief.

The government will begin a process to identify the bank's Chief Executive Officer and Chairperson of the Board of Directors. It aims to have the bank operational in late 2017. While Budget 2017 mentions the importance of high-quality data and performance measurement, details about the governance structure of the bank and how it will evaluate infrastructure proposals will depend on forthcoming legislation.

## Innovation

After the government devoted much of the past year to consultations on its Innovation Agenda, Budget 2017 had initially been billed as the "Innovation" budget. While it does establish the framework of the agenda and includes a number of positive new initiatives, it also announces more reviews and consultations.

### Innovation and skills plan

The Innovation and Skills Plan is described in the budget document as "an ambitious effort to make Canada a world leader in innovation, with a focus on expanding growth and creating good, well-paying jobs." Six sectors are identified, with three – clean technology, digital industries and agri-food – receiving priority for funding.

### Innovation "superclusters"

Budget 2017 proposes to invest up to \$950 million over five years, starting in 2017-18 to support a small number of business innovation "superclusters". Most of that money (\$800 million) was allocated in Budget 2016, with the other \$150 million to be drawn from the public transit and green infrastructure allocations announced in the 2016 Fall Economic Statement. Importantly, funding will be provided on a competitive basis, focusing on highly innovative industries such as advanced manufacturing, agri-food, clean technology, digital technology, health/bio-sciences and clean resources, as well as infrastructure and transportation. Another key feature is that these superclusters are to be business-led.

### Innovation Canada

Budget 2017 announces proposals to review dozens of existing innovation programs across various departments and agencies with the goal of consolidating and simplifying them. The budget also proposes to establish Innovation Canada. Led by Innovation, Science and Economic Development Canada, the new platform will coordinate and simplify the support available to Canadian businesses. These moves

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are in line with recommendations made by CPA Canada during consultations on the Innovation Agenda.

### Strategic Innovation Fund

One such consolidation effort is the new Strategic Innovation Fund, which proposes to consolidate and simplify the existing Strategic Aerospace and Defence Initiative, Technology Demonstration Program, Automotive Innovation Fund and Automotive Supplier Innovation Program. While the fund will continue to be available to automotive and aerospace firms, it will be expanded to other sectors such as agri-food and clean technology. A further \$200 million over three years is proposed to supplement existing funding.

### Scientific Research & Experimental Development (SR&ED) program

Perhaps the most important innovation program for business, and the most expensive for government, is the SR&ED tax credit program. In addition to the above-mentioned review of innovation programs, SR&ED will undergo its own parallel review to ensure its continued effectiveness and efficiency. CPA Canada is pleased that changes were not made to this program without a proper review, and we encourage the government to provide an opportunity for stakeholder input to the review.

### Innovative Solutions Canada

Budget 2017 proposes a new government procurement program, Innovative Solutions Canada, which will allocate a portion of funding from federal departments and agencies to purchase goods and services from Canadian entrepreneurs. Modelled on the successful U.S. Small Business Innovation Research program, it fills a gap that had been identified by CPA Canada and several other groups during Innovation Agenda consultations.

### Venture Capital Catalyst

To support the financing challenges faced by growing innovative companies, Budget 2017 proposes to make \$400 million available through a new initiative called the Venture Capital Catalyst. Administered by the Business Development Bank of Canada, the initiative will increase late-stage venture capital available to Canadian entrepreneurs.

## Skills and Immigration

As foreshadowed by the minister, Budget 2017 contains a number of measures related to developing and attracting a skilled workforce. Many of the measures are administrative in nature and do not involve significant spending. But taken in total, they may help Canadians develop skills that are in demand and find employment in sectors of future growth.

### Investing in skills innovation

Budget 2017 proposes a new organization to support skills development and measurement in Canada, following on recommendations of the Advisory Council on Economic Growth. The new organization will work in partnership with willing

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provinces and territories, the private sector, educational institutions and not-for-profit organizations to identify the skills sought by employers and explore new approaches to developing those skills. More details will be forthcoming.

### Training

The government plans to collaborate with provinces and territories to reform Labour Market Transfer Agreements and to provide an additional \$1.8 billion over six years to expand the Labour Market Development Agreements. An additional \$900 million over six years is proposed for new Workforce Development Agreements to provide job training support to unemployed Canadians who are not eligible for Employment Insurance-funded training. Adults and part-time students will have better access to Canada Student Loans and Grants and there is an initiative to create work-integrated learning opportunities through partnerships between employers and post-secondary institutions.

### Global Skills Strategy

Budget 2017 also provides funds to implement a new Global Talent Stream under the Temporary Foreign Worker Program, as part of the Global Skills Strategy. As outlined in the 2016 Fall Economic Update, a new short-duration work permit exemption will be introduced to be used for short-term, inter-company work exchanges, study exchanges or the entrance of temporary expertise. Further refinements of the Express Entry system, which manages Canada's economic permanent residence programs, are promised.

### Recognizing foreign credentials

Budget 2017 contains a new initiative to help integrate internationally trained professionals into the Canadian workforce. The Targeted Employment Strategy for Newcomers will be funded by the reallocation of existing resources from Employment and Social Development Canada and will have three components:

- improved pre-arrival supports to assist newcomers to begin the foreign credential recognition process in their home countries
- a loan program that will assist newcomers with the cost of the credential recognition process
- targeted measures to assist newcomers to gain Canadian work experience.

The loan component appears to be based on the Foreign Credential Recognition Loans program, a successful pilot project introduced by the previous government.

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# Confronting Climate Change

## **Addressing climate change adaptation**

Following on the Pan-Canadian Framework on Climate Change, Budget 2017 includes a number of measures addressing climate change adaptation. Initiatives address climate science, health risks caused by climate change, resources for First Nations and Inuit communities, and risk assessments on federal transportation infrastructure assets, among other initiatives. One new initiative, to be delivered through its infrastructure plan, is \$2 billion for a Disaster Mitigation and Adaptation Fund, which will support infrastructure required to deal with the effects of a changing climate.

What is missing, however, is a National Adaptation Plan that would coordinate these and other public and private sector initiatives to address the impacts of climate change. CPA Canada has called for such a plan and urged the government to consult the business community in its development.

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## ABOUT CPA CANADA

The new Canadian designation, Chartered Professional Accountant (CPA), is now used by Canada's accounting profession across the country. The profession's national body, Chartered Professional Accountants of Canada (CPA Canada), is one of the largest in the world with more than 200,000 members, both at home and abroad. The Canadian CPA was created with the unification of three legacy accounting designations (CA, CGA and CMA). CPAs are valued for their financial and tax expertise, strategic thinking, business insight, management skills and leadership. 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. CPA Canada also issues guidance and thought leadership on a variety of technical matters, publishes professional literature and develops education and professional certification programs. [cpacanada.ca](http://cpacanada.ca)

