

Federal Budget 2010 summary

A leader in the timely and thorough preparation of tax information on a range of issues, Invesco Trimark has been providing a customized summary of the Federal Budget for over a decade.

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As is our practice, this Invesco Trimark summary selectively focuses on several specific budget elements that will have the biggest impact on personal finances and investments.

True to the comments from the government in the weeks leading up the release of Federal Budget 2010, there are very few broad-based tax relief measures.

There are, however, some targeted measures that will be welcome assistance in certain family situations.

Apart from individual taxpayers, there is a fairly significant proposed change that could ease how charities manage their affairs. This will obviously have direct implications for those charities, particularly for smaller charities, and in turn could affect how individuals make their gifts to those charities.

We'll begin with a summary of the federal brackets and tax rates applying in 2010.

Personal income tax measures

Rates and brackets

Federal tax brackets are indexed each year by an indexation factor defined in the Income Tax Act.

Federal Budget 2009 increased the basic personal amount credit and the two lowest bracket thresholds by 7.5%, well in excess of the calculated figure of 2.5%.

This 2010 Budget makes no comment about the indexing, and therefore the year-over-year bracket index from 2009 to 2010 will be the calculated 0.6%. For federal tax calculation, that brings the basic personal amount up to \$10,382, with the top bracket rate applicable at \$127,021.

The rates at each bracket level remain unchanged.

Applicable rate	2009	2010
15%	10,320	10,382
22%	40,726	40,970
26%	81,452	81,941
29%	126,264	127,021

Improving delivery of family support amounts

Universal Child Care Benefit (UCCB) for single parents

The Budget highlights a disparity issue between one-parent and two-parent families receiving the UCCB.

For two-parent families, the UCCB is included in the income of the lower-income spouse or common-law partner. In the case of a single-parent family, the UCCB is generally included in the single parent's income and taxed at his or her marginal tax rate.

As a result, a single parent can pay more tax on the UCCB amounts than a single-earner couple with the same income.

The Budget proposes to allow a single parent the option of including the aggregate UCCB in the parent's income or in the income of the dependant for whom an Eligible Dependant Credit (EDC) is claimed. If a single parent is unable to claim an EDC, there is an option to include the benefit in the income of one of the children for whom the UCCB is paid. This is expected to reduce and possibly eliminate the tax otherwise applying on the benefit.

Benefits entitlement - Shared custody

To improve the allocation of child benefits between parents who share custody of a child, the Budget proposes to allow an apportionment of the Canada Child Tax Benefit (CCTB), UCCB and GST/HST credit amounts between the parents.

Canada Revenue Agency's (CRA's) shared eligibility policy applies when a child lives more or less equally with two individuals who live separately. Each parent would be able to claim one-half of the annual entitlement that they would receive if they were the sole eligible individual.

The CCTB and UCCB are paid in monthly instalments over the year. The child component of the GST/HST credit is paid in quarterly instalments over the year.

This measure will apply to benefits payable commencing July 2011.

Education and disability support

Rollover of RRSP proceeds to a Registered Disability Savings Plan (RDSP)

Existing rules allow for deferral of tax otherwise applying on RRSP or RRIF amounts at death, where the funds are distributed to a surviving spouse or common-law partner, or to financially dependent children or grandchildren.

The Budget proposes to extend the existing rollover rules to allow a rollover of a deceased individual's RRSP or RRIF proceeds to the RDSP of a financially dependent infirm child or grandchild.

Generally, financial dependence is considered to apply when the child's income for the year preceding the year of death did not exceed a specified threshold (\$17,621 for 2010), but may also apply when income is above this amount, depending on the particular facts.

The amount of RRSP proceeds rolled over into an RDSP will not be permitted to exceed the beneficiary's available RDSP contribution room. The lifetime contribution limit for RDSPs is \$200,000. The rolled-over proceeds will reduce the beneficiary's RDSP contribution room, but will not attract Canada Disability Savings Grants (CDSGs). These proceeds will be considered private contributions for the purpose of determining whether an RDSP is a primarily government-assisted plan, which can in turn affect how the plan is drawn down in future.

Since the amount of RRSP proceeds rolled over to an RDSP will not have been subject to income tax, the amount will form part of the portion of a disability assistance payment that is included in the beneficiary's income when withdrawn from the RDSP.

Special transitional rules will allow the proposed measure to apply as of January 1, 2008 - the date that RDSPs were first permitted to be established under the income tax rules.

Carry forward of RDSP Grants and Bonds

Annual RDSP contributions attract CDSGs of up to \$3,500, depending on the beneficiary's family income and the amount contributed, up to a lifetime limit of \$70,000.

In addition, Canada Disability Savings Bonds (CDSBs) of up to \$1,000 annually are provided to RDSPs established by low- and modest-income families, based on a beneficiary's family income, up to a lifetime limit of \$20,000.

In recognition of the fact that families of children with disabilities may not be able to contribute regularly to their plans, Budget 2010 proposes to amend the *Canada Disability Savings Act* to allow a 10-year carry forward of CDSG and CDSB entitlements.

The carry forward will be available starting in 2011.

Provincial payments into Registered Education Savings Plans (RESPs) and RDSPs

Both the federal and provincial governments have programs in place to assist RESPs and RDSPs.

The provincial programs receive the same treatment as federal grants and bonds paid into these plans - they do not use up a beneficiary's RESP or RDSP contribution room and they do not attract federal grants. Under the current rules, provincial initiatives that are not administered by the federal government have to be prescribed in order to be treated as provincial programs, which can create uncertainty about the status of payments from these programs.

Budget 2010 proposes to clarify that all payments made to an RESP or RDSP through a program funded, directly or indirectly, by a province or administered by a province, will be treated the same way as federal grants and bonds and will therefore not themselves attract or reduce federal grants and bonds.

Charities: Disbursement quota reform

The disbursement quota was introduced in 1976 to help curtail fundraising costs and limit capital accumulation. It requires that the amount the charity spends each year on charitable activities (including gifts to qualified donees) be at least the sum of:

- 80% of the previous year's tax-receipted donations plus other amounts relating to enduring property and transfers between charities (in other words, a "charitable expenditure rule"); and
- 3.5% of all assets not currently used in charitable programs or administration, if these assets exceed \$25,000 (in other words, a "capital accumulation rule").

The impact of this rule can vary depending on the size and nature of the charity, being particularly constraining on many small and rural charities that rely mainly on tax-receipted donations.

The Budget proposes to reform the disbursement quota for fiscal years that end on or after March 4, 2010. Specifically, it proposes to:

- repeal the charitable expenditure rule;
- modify the capital accumulation rule; and
- strengthen related anti-avoidance rules for charities

Implications for charities and gift planners

Repeal of charitable expenditure rule

Provisions relating to a number of concepts will no longer be required to calculate the disbursement quota:

- Enduring property (gifts to a charity for endowments or multi-year charitable projects which are not subject to the charitable expenditure rule)
- The capital gains reduction and the capital gains pool (provisions that ensure that capital gains realized from the disposition of enduring property are not subject to the charitable expenditure rule and the capital accumulation rule)
- Specified gifts (a provision that allows charities with disbursement excesses to help charities with disbursement shortfalls to meet their disbursement quota requirements)
- Exclusions to the calculation of the base to which the 3.5% disbursement rate is applied (provisions that ensure that funds subject to the charitable expenditure rule are not also subject to the capital accumulation rule)

This will have an effect on how donors may choose to structure their charitable gifts and how any written terms are drafted, including Will provisions.

Modify the capital accumulation component

There is currently an exemption from the capital accumulation rule for charities having \$25,000 or less in assets not used in charitable programs or administration. This is proposed to increase to \$100,000 to reduce the compliance burden on small charitable organizations and provide them with greater ability to maintain reserves to deal with contingencies.

The threshold for charitable foundations will remain at \$25,000.

Strengthen anti-avoidance rules

The Budget proposes to extend existing anti-avoidance rules to situations where it can reasonably be considered that a purpose of a transaction was to delay unduly or avoid the application of the disbursement quota.

Overall, the Government will monitor the effectiveness of the CRA's guidance on "Fundraising by Registered Charities," and take action if needed to ensure its stated objectives are achieved.

Other income matters

Employee stock options

It is possible to structure employee stock option agreements so that, if employees dispose of ("cash out") their stock option rights for a cash payment from the employer (or other in-kind benefit), the employment benefit is eligible for the stock option deduction while the cash payment is fully deductible by the employer.

The Budget proposes to prevent both the stock option deduction and a deduction by the employer from being claimed for the same employment benefit. It also includes clarifications on tax-deferral elections and remittance requirements.

U.S. Social Security benefits

Changes made to the Canada-U.S. Tax Convention, effective beginning in 1996, increased the inclusion rate for U.S. Social Security benefits to 85% from 50%.

The Budget proposes to reinstate the 50% inclusion rate for Canadian residents who have been in receipt of U.S. Social Security benefits since before January 1, 1996, and for their spouses and common-law partners who are eligible to receive survivor benefits.

Mineral exploration tax credit

Flow-through shares allow companies to renounce or “flow through” tax expenses associated with their Canadian exploration activities to investors, who can deduct the expenses in calculating their own taxable income.

The Budget 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, 2011.

Non-resident trusts

There are outstanding proposals that would generally make both resident contributors and resident beneficiaries jointly and severally, or solidarily, liable for tax payable by a non-resident trust deemed resident in Canada.

It is proposed that the scope of the outstanding proposals be simplified and better targeted in several ways, including to limit attribution to resident contributors to their proportionate share of the trust's income for Canadian tax purposes.

Tax administration

Information reporting of tax avoidance transactions

Budget 2010 announces a public consultation on proposals to require the reporting of certain tax avoidance transactions. A reportable transaction would be one that has at least two of the following three characteristics:

1. A promoter or tax advisor is entitled to fees that are to any extent:
 - Attributable to the amount of the tax benefit
 - Contingent on obtaining a tax benefit, or
 - Attributable to the number of taxpayers participating
2. A promoter or tax advisor requires “confidential protection”
3. The taxpayer obtains “contractual protection”

For more information about this topic, contact your advisor, call us at 1.800.874.6275 or visit our website at www.invescotrimark.com.

Online notices

Under the *Personal Information Protection and Electronic Documents Act*, taxpayers can receive notices, such as notices of assessment under the Income Tax Act, from the CRA only through the mail system or personally.

The Budget proposes that certain Acts be amended to allow for the electronic issuance of some notices of assessment and reassessment. This will allow the CRA, if authorized by a taxpayer, to send the taxpayer an e-mail to advise that a given document has been made available on the relevant CRA secure online platforms, such as My Account and My Business Account.

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