Mackenzie Investments

Mackenzie Tax & Estate Planning

Federal budget 2022

Bulletin

Federal budget 2022 analysis

The 2022 federal budget tabled by Finance Minister Chrystia Freeland on April 7 contained a number of proposals that will impact the financial, tax and estate plans of Canadians. The following is a summary of the most relevant budget proposals that may impact financial advisors and their clients.

Personal tax changes

Federal tax rates

There are no changes to personal federal income tax rates or income brackets.

1) Tax-Free First Home Savings Account (FHSA)

The budget proposes the creation of the Tax-Free First Home Savings Account (FHSA), a registered account that will assist individuals in saving for their first home.

a) Eligibility

- Canadian resident
- At least 18 years of age
- Not lived in a home they owned
  - In the year the account was opened, or
  - In any of the preceding four calendar years

b) Contributions

- Lifetime limit: $40,000
- Annual limit: $8,000
- Note that unused annual contribution room cannot be carried forward
- Individuals can hold multiple FHSAs, but contributions cannot exceed their annual or lifetime limits
- Full annual contribution limit will become available starting in 2023

Contributions to the FHSA will be tax-deductible and income earned within the FHSA will not be subject to tax.

c) Withdrawals

Non-taxable withdrawals may be made only for purposes of purchasing a qualifying first home. Withdrawals for any other purpose will be taxable as income in the year withdrawn.

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d) Transfers from FHSA to RRIF/RRSP

A tax-deferred transfer from an FHSA to a RRIF or RRSP will be allowed; but withdrawals will be taxed as per the existing RRIF/RRSP rules. Transfers will not reduce or be limited by the individual's available RRSP contribution room.

e) Transfers from to RRSP to FHSA

Tax-deferred fund transfers from an RRSP to an FHSA will be allowed. These allowable transfers will be subject to the $40,000 lifetime and $8,000 annual limits. Transfers of this nature will not restore the account holder's RRSP contribution room.

f) Forced account closure

If a qualifying home has not been purchased within the first 15 years of opening the FHSA, the FHSA must be closed and the savings will be paid out on a taxable basis – unless transferred to an RRSP/RRIF.

g) Home Buyers' Plan and FHSA

Important Note: An individual will not be permitted to make a Home Buyers' Plan and an FHSA withdrawal for the same qualifying home purchase.

2) Home Buyers' Tax Credit (HBTC)

Budget 2022 proposes a non-refundable Home Buyers' Tax Credit of up to $1,500 to be available to first-time home buyers who purchase a qualifying home. Under the budget, the HBTC amount will be doubled to $10,000. Spouses and common law partners can split the value of the credit if the total credit does not exceed $1,500.

a) First-time home buyer

A first-time home buyer is an individual (or their spouse or common law partner) who has not lived in another home owned in the calendar year of the home purchase, or any of the four preceding calendar years. An individual who may not be a first-time home buyer, but qualifies for the Disability Tax Credit, may be eligible for this HBTC.

b) Qualifying home

This is a home that the individual or their spouse or common law partner intends to occupy no later than one year after purchase.

3) Multigenerational Home Renovation Tax Credit (MHRTC)

Budget 2022 introduces a new refundable Multigenerational Home Renovation Tax Credit (MHRTC), which would account for certain eligible expenses for a qualifying renovation – meaning a renovation that creates a secondary dwelling unit for a senior or a person with a disability to live with a relative. Only one qualifying renovation is permitted for the MHRTC per individual over that individual's lifetime.

A secondary unit is defined as a self-contained unit that has a private entrance, kitchen, bathroom and sleeping area.

The MHRTC will be applicable for renovations occurring after January 1, 2023.

a) Eligibility

- The eligible senior would be 65 years or older, at the end of the taxation year, including the end of the renovation period, or
- Individuals 18 or older who are eligible for the Disability Tax Credit at the end of the taxation year, including the end of the renovation period.

A qualifying relative is an individual 18 years or older at the end of the taxation year, including the end of the renovation period. These individuals include the following relatives of the eligible person:
- Parent
- Grandparent

- Child
- Grandchild
- Brother
- Sister
- Aunt
- Uncle
- Niece
- Nephew

b) Eligible claims

The MHRTC can be claimed by the following persons:

An individual who ordinarily resides or intends to ordinarily reside in the property within 12 months of the renovation being completed. This could be an eligible person, the spouse or common law partner of an eligible person, a qualifying relative, or a qualifying relative who owns the house.

Claims cannot exceed $50,000 of qualifying renovations, irrespective of the number of claimants.

c) Eligible dwelling

This is a unit that is owned either solely or jointly by an eligible person, their spouse or common law partner, or in regard to a qualifying relative, if that individual ordinarily resides or intends to ordinarily reside in the property within 12 months of the renovation being completed.

d) Qualifying renovation

Qualifying renovation must be of:

- An enduring nature and integral to the dwelling, and
- Result in the creation of a secondary unit within the dwelling

e) Renovation period

Starts when the building permit is applied for and concludes when the renovation passes a final inspection and proof of completion.

f) Eligible expenses

Include:

- Cost of labour
- Building materials
- Fixtures
- Equipment rentals
- Professional services
- Permits

g) Ineligible expenses

Include:

- Items that retain their value (construction equipment and tools)
- Annual, recuring or routine repair or maintenance
- Cost of household appliances
- Cost of financing a renovation
- Goods or services provided by a person not dealing at arm’s length with the MHRTC claimant, unless the provider is registered for HST/GST

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Expenses claimed under the medical expense tax credit, or the home accessibility tax credit will not be eligible for the MHRTC.

4) Doubling the Home Accessibility Tax Credit

The Home Accessibility Tax Credit provides support to offset a limit of up to $10,000 in qualifying expenses associated with renovating a home to make it safer and more accessible.

Budget 2022 proposes to double the limit to $20,000 for the 2022 and subsequent tax years. This will mean a tax credit of up to $3,000, instead of $1,500 and includes renovations and alterations such as the purchase and installation of wheelchair ramps, walk-in bathtubs and wheel-in showers, and much more.

5) New residential property flipping taxation

Buying a house and selling it for much more than what was paid for it over a very short time period is known as property flipping. Budget 2022 expresses concern that some taxpayers may not be properly reporting these profits on their tax returns.

Budget 2022 proposes to introduce a new deeming rule to ensure profits from flipping properties held for less than 12 months would be fully taxable as business income, and not eligible for capital gains taxation, or the Principal Residence Exemption (PRE). There will be exceptions to the rule, including Canadians who sell their home due to certain life circumstances, such as a death, disability, the birth of a child, a new job or a divorce.

The rules are forthcoming, and Canadians will be consulted on the draft legislative proposals.

The measure will apply to residential properties sold on or after January 1, 2023.

6) Ban on foreign purchases

To make sure that housing is owned by Canadians instead of foreign investors, the budget announced the government's intention to propose restrictions that would prohibit foreign commercial enterprises and people who are not Canadian citizens or permanent residents from acquiring non-recreational, residential property in Canada for a period of two years. There will be exceptions for refugees fleeing international crises, international students on the path to permanent residency and others.

Non-resident, non-Canadians who own homes that are being underused or left vacant would be subject to the Underused Housing Tax once it comes into effect.

7) Changes coming to Alternative Minimum Tax (AMT)

The Alternative Minimum Tax (AMT) system is designed to ensure that taxpayers who claim significant tax preferential deductions or credits, such as the capital gains deduction, dividend tax credits or flow-through shares, pay at the very minimum the Alternative Minimum Tax. It's designed to ensure the wealthiest Canadians do not take advantage of the tax system to lower their federal tax bill. The government feels there are still too many wealthy Canadians paying little to no personal income tax each year.

As a result, the budget announced the government's commitment to examine a new minimum tax regime. The government will release details on a proposed approach in the 2022 fall economic and fiscal update.

8) Tax on real estate assignment sales

Assignment sales involve the resale of a home before it is constructed or lived in; GST/HST may or may not be applicable when there is an assignment sale. For example, GST/HST does not apply if the intention is for the buyer to live in the home. This creates an opportunity for speculators to be dishonest about their original intentions, and uncertainty for everyone involved in an assignment sale as to whether GST/HST applies.

To address these issues, the budget proposes to make all assignment sales of newly constructed or substantially renovated residential housing taxable for GST/HST purposes, effective May 7, 2022.

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9) Medical support for Canadians wanting to become parents

In Canada, it is illegal to pay consideration to surrogate mothers or donors, although surrogate mothers and donors may receive reinbursement from intended parents, which previously were not claimable as eligible medical expenses.The budget proposes to allow these reimbursements paid by a taxpayer to a surrogate mother or donor that are incurred in Canada for 2022 and subsequent taxation years to be claimed. This would also include costs that have been reimbursed to a surrogate for in vitro fertilization expenses. In addition, the budget proposes to allow fees paid to fertility clinics and donor banks in Canada in order to obtain donor sperm and ova to be eligible as a Medical Expense Tax Credit for 2022 and subsequent taxation years.

10) Measures for registered charities in Canada

Registered charities are generally required to spend a minimum amount each year in charitable activities, referred to as the disbursement quota. This is currently 3.5% of the charity's property that is not used directly in charitable activities or administration. The disbursement quota is designed to ensure timely disbursement of funds for charitable purposes, while allowing for reasonable asset growth over time. Budget 2022 proposes to increase the disbursement quota rate from 3.5% to 5% for the portion of property not used for charitable activities or administration exceeding $1 million annually. The budget also proposes to amend the Income Tax Act to clarify that expenditures for administration and management are not considered qualifying expenditures included in the 5% disbursement quota.

Charities not able meet the 5% quota may apply to the CRA and request relief. Other proposed rules are designed to simplify charity rules. All measures would apply to charities in respect of their fiscal year beginning on or after January 1, 2023.

In addition, the budget proposes a number of changes to improve the operation of charities conducting activities through an intermediary organization such as a donor-advised foundation. The budget proposes to allow charities to make qualifying disbursements to organizations that are not qualified donees, as long as these disbursements support the charity's charitable purposes and the charity ensures the funds are applied to charitable activities by the grantee. There are a number of conditions to this measure, which are yet to be determined. These measures will take effect upon royal assent of the budget.

Corporate tax changes

There are no changes to corporate federal income tax rates or income brackets.

1) Small business deduction

Canadian-controlled private corporations (CCPCs) have access to a reduced corporate income tax rate of 9% federally on the first $500,000 of active business income, compared to the general corporate income tax rate of 15%. This $500,000 limit is referred to as the "business limit" and is shared among all associated CCPCs.

Under the current rules, the business limit is gradually reduced if the taxable capital employed in Canada of the associated CCPCs combined exceeds $10 million, or the adjusted aggregate investment income ("AAII") of the associated corporations combined exceeds $50,000. The business limit is fully clawed back if the taxable capital is $15 million or more, or AAII is $150,000 or more.

Budget 2022 proposes to increase the taxable capital limit from $15 million to $50 million which would allow more CCPCs to benefit from the reduced corporate income tax rate. This would apply to taxation years that begin on or after April 7, 2022.

2) Investment tax credit for carbon capture, utilization and storage

Budget 2022 proposes to introduce a refundable tax credit for businesses that incur eligible expenses starting January 1, 2022. Eligible expenses include the cost of purchasing and installing equipment for use in projects that capture, transport, store or use carbon dioxide emissions for eligible uses.

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The project would be subject to a validation and verification process and financial disclosures before the tax credit can be claimed. The expenses incurred from 2022 through 2030 may be eligible for a tax credit rate of 37.5%, 50% or 60%, depending on the nature of the equipment. The tax credit rates would be cut in half for expenses incurred after 2030 through 2040.

3) Clean technology tax incentives: air-source heat pumps

Corporations earning income from eligible zero-emission technology manufacturing temporarily benefit from a 50% reduction in federal corporate tax rates (income that would otherwise be taxed at 9% would be taxed at 4.5%). The reduced tax rates apply to taxation years beginning after 2021, and the reduction would be gradually phased out between 2029 to 2031.

Budget 2022 proposes to include manufacturing of air-source heat pumps used for space or water heating, including manufacturing of components of an air-source heat pump, as eligible zero-emission technology manufacturing activity.

4) Capital cost allowance for clean energy equipment

The Income Tax Act allows taxpayers to deduct a portion of the capital cost of a depreciable property as a capital cost allowance (CCA) when they compute their income for each taxation year.

Classes 43.1 and 43.2 of Schedule II to the Income Tax Regulations provide accelerated CCA rates (30% and 50% respectively) for investments in specified clean energy generation and energy conservation equipment.

Budget 2022 proposes to expand eligibility under Classes 43.1 and 43.2 to include air-source heat pumps primarily used for space or water heating. The expansion of these classes applies to property that is acquired and becomes available for use on or after budget day.

5) Critical Mineral Exploration Tax Credit

Currently there is a Mineral Exploration Tax Credit (METC) that provides additional income tax benefits for individuals who invest in mining flow-through shares which augments the tax benefits associated with the deductions that are flowed through.

The METC is equal to 15% of specified mineral exploration expenses incurred in Canada and renounced to flow-through share investors.

Budget 2022 proposes to introduce a new 30% Critical Mineral Exploration Tax Credit (CMETC) for specified minerals including copper, nickel, lithium, cobalt, graphite, rare earth elements, scandium, titanium, gallium, vanadium, tellurium, magnesium, zinc, platinum group of metals and uranium.

The CMETC would apply to expenditures renounced under eligible flow-through share agreements entered into after budget day and on or before March 31, 2027.

6) Intergenerational share transfers

Bill C-208 received royal assent on June 29, 2021, which allowed certain qualifying small business owners to benefit from a capital gains treatment when transferring their shares to the next generation and access their unused lifetime capital gains exemption (LCGE) to minimize taxation. Prior to this legislation, certain anti-avoidance rules under the Income Tax Act applied to tax the income as dividends resulting in a higher tax liability (compared to generally lower-taxed capital gains) and not allowing the small business owners to access their LCGE.

The Department of Finance expressed concerns about this bill and indicated that a revised legislation would be introduced to clarify the rules to support “genuine intergenerational business transfers” only and safeguard against unintended tax loopholes caused by this bill. The department originally stated that the revised legislation would apply as of the later of either November 1, 2021 or the date of publication of the revised legislation.

Budget 2022 announced an extension of the consultation process to review the rules, allowing all stakeholders to provide their

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comments to the Department of Finance by June 17, 2022. The government expects to introduce the revised bill in the fall after the consultation process has concluded.

7) Deferring tax using foreign entities

Passive income earned through a CCPC is subject to a high tax rate due to the refundable tax mechanism that aims to tax income earned through a corporation at roughly the same rate that would apply to a Canadian resident individual and eliminate any tax-deferral advantage of earning investment income through a private corporation. The refundable taxes may be partially or fully refunded to the CCPC when it issues taxable dividends to its shareholders.

Budget 2022 proposes to target taxpayers that manipulate the status of their corporation to avoid qualifying as a CCPC by taxing "substantive CCPCs" under the same refundable tax mechanism that apply to CCPCs. Substantive CCPCs would include private corporations resident in Canada that are ultimately controlled by Canadian-resident individuals directly or indirectly. Corporations that are not considered CCPCs under the current rules because a non-resident or public corporation has a right to acquire its shares would also be considered a substantive CCPC under the new rules.

This measure would apply to taxation years that end on or after April 7, 2022.

If you have any questions please talk to your wholesaling team or a member of the Tax and Estate Planning Team.

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