NEW GOVERNMENTS FIRST ROUND OF TAX CHANGES INTRODUCED IN PARLIAMENT

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New federal Finance Minister Bill Morneau has introduced a Notice of Ways and Means Motion in the House of Commons (the "**Motion**"). The Motion represents the first step taken by the new Government to formally enact several of the personal income tax changes that it proposed during the recent federal election campaign.

Personal Tax Rate Changes

As expected, the Government has proposed to reduce the tax rate in the second federal income tax bracket from 22% to 20.5%. The Government has also proposed to introduce a new top personal income tax rate of 33%, which will apply to the taxable income of an individual in excess of $200,000 each year[1]. The proposed changes to personal tax rates will be effective for the 2016 and subsequent taxation years.

A number of provisions in the *Income Tax Act* (the "**ITA**") levy tax, and compute credits, on the basis of the top personal income tax rate. The Motion proposes to amend several of these provisions to reflect the introduction of the new 33% tax rate. For instance, beginning in 2016, trusts and estates (other than certain special trusts, such as qualified disability trusts and graduated rate estates) will be subject to tax at a rate of 33%. Similarly, so-called "split income" paid or payable to a minor will be subject to tax at the new rate of 33%.

Charitable Donation Tax Credits

Individuals that make charitable donations to registered charities are typically eligible to claim a charitable donation tax credit. The federal charitable donation tax credit that an individual may claim in respect of a particular year has generally been equal to 15% of the first $200 of donations, and 29% of all donations in excess of $200, made in the year.

While the higher credit rate has historically corresponded with the highest marginal income tax rate, the Government does not propose to simply increase the 29% credit rate to 33% to reflect the new top personal income tax rate. Instead, a somewhat more complicated formula will be introduced that will generally provide that the higher credit rate will continue to be 29%, unless donations are made in a year by a taxpayer from income that is subject to the new 33% tax rate. In other words, the portion of charitable donations made in a particular year that exceeds $200 that will be eligible for a tax credit computed at the rate of 33% will be limited to the amount by which the taxable income of the taxpayer for the year exceeds $200,000.

Taxpayers that have previously taken advantage of the Canada Revenue Agency's administrative position that permits charitable donations made by spouses and common-law partners to be aggregated and reported by a single spouse/partner will need to be careful to ensure that such aggregation does not limit their entitlement to maximize the portion of their donations that are eligible for a credit computed at the new 33% rate.

Refundable Tax Provisions

The ITA also imposes special refundable taxes on the investment income earned by private corporations. The refundable tax rules were enacted with a view to limiting the ability of individuals to defer taxation by investing through a private corporation. The Government has proposed to increase the rates of such refundable taxes, and the related refund rates, effective January 1, 2016, to reflect the new highest marginal income tax rate of 33%. Specifically, the following rate changes have been proposed:

- The special refundable tax on investment income of "Canadian-controlled private corporations" ("**CCPCs**") will be increased by 4 percent to 10.67% (from 6.67%);
- The refundable portion of tax on investment income of CCPCs will be increased by 4 percent to 30.67% (from 26.67%);
- The refundable Part IV tax on portfolio dividends received by private corporations will be increased by 5% to 38.33% (from 33.33%); and
- The rate at which refunds will be paid to a private corporation out of the corporation's pool of refundable taxes previously paid (commonly referred to as the "refundable dividend tax on hand" or "RDTOH") will be increased by 5% to 38.33% of dividends paid by the corporation (from 33.33%).

The Government has indicated that further amendments will subsequently be made to the ITA to properly reflect the introduction of the new highest marginal rate of tax on individuals.

Tax-Free Savings Accounts

Consistent with the election platform of the new Government, the Motion also proposes to reduce, to $5,500, the annual limit on the contributions that may be made to a Tax-Free Savings Account (a "**TFSA**") by an individual.

The reduction in the TFSA contribution limit will take effect as of January 1, 2016. However, the annual contribution limit to a TFSA for 2015 will remain at $10,000. Accordingly, taxpayers that relied on the understanding that $10,000 could be contributed to their TFSA in 2015 will not be penalized.

The $5,500 contribution limit will be indexed to inflation in subsequent taxation years.

Future Measures

In conjunction with the release of the Motion, the Government also announced that it intends to introduce legislative amendments in the future to repeal the provisions of the ITA that permit the splitting of income between certain spouses and common-law partners that have children. The Government indicated that such legislative amendments will apply in respect of the 2016 and subsequent taxation years.

[1][ps2id id='1' target=''/] The Government has proposed that the $200,000 threshold will be indexed to inflation and, therefore, will increase in respect of the 2017 and subsequent taxation years.

A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.