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the newsletter of Prentice Yates & Clark

Income tax measures in the 2022 Federal Budget

On April 7, 2022 the Honourable Chrystia Freeland introduced her second Budget (Budget 22). Here is a summary of the individual and corporate income tax changes that were included in the budget.

Personal income tax changes

Several of the tax changes affecting individuals dealt with improving house affordability for first-time home owners in particular. These are covered in the "Government programs to support first-time home buyers" article in this edition of *Business Matters*. Some additional measures were proposed to improve housing affordability in general.

Multigenerational Home Renovation Tax Credit

In addition to the support for first-time home buyers, Budget 22 proposes a new refundable credit for up to \$50,000 of eligible expenses to renovate a home to create a secondary residential unit for a qualifying relative who is senior or person with a disability. The maximum tax savings would be \$7,500 (15% times \$50,000).

Home accessibility tax credit

The home accessibility tax credit is a non-refundable tax credit for up to \$10,000 of eligible home renovation expenses to make a home more accessible for a person eligible to claim the Disability Tax Credit or who is 65 years or older at the end of the taxation year. Budget 22 proposes to double the annual renovation expense limit to \$20,000, which will increase the maximum tax savings from \$1,500 to \$3,000. The increased limit will be effective for 2022 and subsequent years.

Residential property flipping rule

Budget 22 proposes a new deeming rule to ensure that profits from flipping residential real estate are always treated as business income. This means that profits are fully taxable, rather than capital gains that are 50 per cent taxable or offset by the Principal Residence Exemption.

The new rule will apply when you sell a residential property, including a rental property, that you owned for less than 12 months. Exceptions to this rule will be available when there are "life events" that necessitate the sale of the home. Examples of



life events include death, marriage, separation, new baby or senior coming to live with you, a new job in a different location, insolvency, or a threat to personal safety. This new deeming rule would apply for all sales on or after January 1, 2023.

Labour Mobility Deduction for Tradespeople

Expenses associated with temporary relocations that are common in the construction industry often do not qualify for the current deductions for moving or travel expenses. Budget 22 proposes to introduce new Labour mobility deductions for tradespeople and apprentices who make such temporary locations to obtain or maintain employment in a construction activity at a particular work location in Canada. The relocation must be for a minimum of 36 hours and the temporary lodging must be at least 150 kilometres closer to the work location than the ordinary residence. Expenses eligible for this deduction include temporary lodging, transportation and meal expenses for the tradesperson for one round trip from their ordinary residence, up to a maximum of \$4,000 per year. This deduction would apply for 2022 and subsequent taxation years.

Medical Expense Tax Credit

The list of eligible expenses for the non-refundable Medical Expense Tax Credit is proposed to be expanded to include the reimbursement of medical expenses incurred by a surrogate mother or sperm, ova or egg donor. It would also include fees paid to fertility clinics or donor banks in Canada to obtain sperm or ova. These changes would be effective for 2022.

More changes to come for high-income Canadians

In addition to the personal tax changes noted above, Budget 22 announced a review of a new or amended minimum tax regime for high-income Canadians. More details are expected to be released in the 2022 fall economic and fiscal update.



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Corporate tax changes

Expansion of the small business deduction

The small business deduction (SBD) allows small Canadian-controlled private corporations (CCPCs) to benefit from a lower corporate tax rate on the first \$500,000 per year of qualifying active business income in the associated group of CCPCs. There are two “size” tests applied to the CCPC and its associated companies to ensure that the SBD targets small companies. The \$500,000 limit is reduced on a straight-line basis when:

- The combined taxable capital employed in Canada is between \$10 million and \$15 million.
- The combined adjusted aggregate investment income is between \$50,000 and \$150,000.

When both business limit reductions apply, the lesser of the two amounts will apply. To make more mid-sized businesses eligible for the SBD, Budget 22 proposes to change taxable capital criteria so that it would continue to start reducing the SBD at \$10 million, but not be fully eliminated at \$50 million. Since the reduction is calculated on a straight-line basis, this means that each \$1 million of taxable capital over the \$10 million threshold would reduce the SBD limit by \$12,500 instead of \$100,000 under the current rules. This measure would apply to taxation years beginning on or after April 7, 2022.

Substantive CCPCs

CCPCs pay a refundable tax on investment income earned in the corporation; this tax is fully or partially refunded when taxable dividends are paid to the shareholders. This process, known as integration, is designed to ensure that income earned directly by an individual is taxed at approximately the same rate as if it was earned through a corporation.

Some taxpayers have attempted to manipulate status of private corporations to avoid being a “Canadian” corporation, and thereby avoid these refundable taxes. Budget 22 introduces the concept of “substantive CCPCs” that are in law or in fact controlled by Canadian-resident individuals. The taxation of substantive CCPCs would be aligned with the rules for actual CCPCs. This would be effective for taxation years that end on or after April 7, 2022.

Foreign resident corporations

Budget 22 proposes some changes to the way investment income earned by CCPCs and substantive CCPCs through foreign subsidiaries or affiliates is taxed. These changes would apply to taxation years beginning on or after April 7, 2022.

Canada Recovery Dividend

Budget 22 proposes to introduce a new one-time 15 per cent tax on the 2021 taxable income of bank and insurance company groups in excess of \$1 billion for the taxation year ending in 2021. The proposed Canada Recovery Dividend would be calculated in 2022 and payable in equal instalments over five years.



Additional tax on banks and life insurers

The budget proposes an additional 1.5 per cent tax on bank and life insurer groups on taxable income in excess of \$100 million. This would apply to taxation years ending after April 7, 2022, and would be prorated for taxation years that include that date.

Investment tax credit for carbon capture, utilization and storage

Budget 22 proposes a new refundable tax credit for the cost of purchasing and installing eligible equipment used in eligible projects where the captured carbon dioxide is used for eligible uses. Projects would be subject to a validation and verification process, and rates for expenses incurred after 2021 would vary from 60 per cent for equipment used in a direct air capture project, 50 per cent for all other capture equipment, and 37.5 per cent for transportation, storage and use equipment. Those rates would be halved for expenditures after 2030 and before 2040.

Clean technology tax incentives for air-source heat pumps

The capital cost allowance rules for investments in specified clean energy generation and energy conservation equipment provide accelerated deductions for these assets. Budget 22 proposes to expand the definition of these assets to include purchases of air-source heat pumps primarily used for space or water heating after April 7, 2022.

Budget 22 proposes that the tax rate reductions introduced in the 2021 budget for qualifying zero-emission technology manufacturing and processing income will be extended to include the manufacturing of air-source heat pumps and related components.

Critical Mineral Exploration Tax Credit

Flow-through share agreements allow corporations to renounce certain expenses to investors, who can deduct the expenses on their own tax returns. In addition to the deduction of the renounced expenses, a new Critical Mineral Exploration Tax Credit (CMETC) is proposed for companies that mine minerals used in the production of batteries and permanent magnets which are used in zero-emission vehicles. This credit will flow-through to the shareholder based on 30 per cent of the renounced exploration expenses, and apply to eligible flow-through share agreements entered into between April 7, 2022 and March 31, 2027. Eligible expenses will not be able to benefit from both the new CMETC and the existing 15 per cent flow-through Mineral Exploration Tax Credit.

Flow-through share for oil, gas and coal activities

The government proposes to eliminate the flow-through regime that allows shareholders to deduct renounced oil, gas and coal exploration and development expenses. This change is effective for flow-through share agreements entered into after March 31, 2023.



Income tax measures in the 2022 Federal Budget - continued

Anti-avoidance measures

Several changes are proposed in Budget 22 to address transactions that the government considers to be aggressive or abusive. The government proposes introducing specific changes to the *Income Tax Act* to prevent financial institutions from realizing artificial tax deductions through hedging and short selling Canadian shares. It is also proposing amendments that would specifically extend the general anti-avoidance rule (GAAR) to include tax attributes that had not yet been used to reduce taxes (a 2018 Federal Court of Appeal decision had limited the application of GAAR to circumstances where the tax attribute had been utilized). This change would be effective for notices of determination issued on or after April 7, 2022.

Future consultations

The budget included announcements on several consultation projects on tax legislation. These include the following:

- A review of the alternative minimum tax regime for individuals noted above.
- A review of how the rules to prevent people from converting taxable dividends into capital gains, which are taxed at a lower rate, can facilitate genuine intergenerational share transfers in a more targeted manner.
- Engaging with stakeholders on the development of tax rules for Employee Ownership Trusts – a new dedicated type of trust to support employee ownership of a business.
- Consulting with experts on the design of a new 30 per cent investment tax credit for investments in net-zero technologies, battery storage solutions and clean hydrogen.
- A review of the Scientific Research and Experimental Development program to improve program efficiency and effectiveness.
- A review of whether Canada should seek to adopt a “patent box” regime, which provides lower effective tax rates on income derived from intellectual property.

More details on many of these consultations are expected to be released in the fall economic and fiscal update. ♦



Inside PYC

Congratulations to **Katya Bell** in reaching the 15-year milestone of service at PYC. Katya is a dedicated and valuable member of the firm and is responsible for managing all aspects of the firm's administrative support.

We would like to welcome **Heeshini Rajasinh** as a new member of our professional staff.



What to consider before lending money to loved ones

Loaning money to a friend or child may be well-intentioned, but it's important to consider all the implications, especially in the current context, experts suggest.

The COVID-19 pandemic has wreaked havoc on many Canadians' finances. By April, 2020 the economy had lost **more than three million jobs** and the unemployment rate rose to 13 per cent. During stressful financial times like this, it's inevitable people will turn to loved ones for monetary help. How do you respond to such a request? We asked the experts.

Rule 1: Put yourself first, especially now

According to Doretta Thompson, CPA Canada's financial literacy leader, the first question you should ask yourself is whether you can afford to lend the money.

"Everyone wants to help their friends and family, but this crisis is hard on us all and that may be a good reason for you to turn them down," she says. "Who knows what tomorrow will bring? Extending a loan shouldn't make it difficult for you to make ends meet. Your loved one should start by looking into the many government programs available, including those for small business owners."

Your primary concern, Thompson says, should be to maintain the cash you need and plan for the worst. "Loans are always risky," she says. "If a loved one comes to you, you're probably their last resort, which may mean the risk is even greater."

CPA Pierre Leblanc, president of bankruptcy trustee firm Groupe Leblanc Syndic, agrees: "Of course you want to help your child, but you shouldn't sacrifice your retirement plans, for example, to do so. You should be realistic about their ability to pay you back."



What to consider before lending money to loved ones - continued

Rule 2: Be prepared to never see your money again

If you can lend money, accept that the loan may become a gift.

“Whatever the amount, make sure you don’t need it in the short- or medium-term ... or ever again,” says Leblanc. “The borrower may be trustworthy, but they could get sick, go through a divorce or lose their job. From one day to the next, they may no longer be able to pay you back.”

For your psychological well-being, proceed with caution. “A loan can always be secured, by real estate, for example. But how far are you willing to go to collect? Your goal should be to protect the relationship, even if you never see your money again,” he adds.

In other words, says Thompson, you have to determine whether you’re ready to jeopardize the relationship if the money disappears.

“A parent who lends a child money also needs to consider other family members, like brothers and sisters,” says Leblanc. “For everyone’s sake, the loan shouldn’t be viewed as a debt if the lender dies, but as an advance on the borrower’s inheritance.”

Rule 3: Ask why

Questioning someone you care about and trust to tell you why they need money is awkward but necessary, says Leblanc.

“You have a right to know what you’re getting into,” he says. “You have to consider the risks in order to make an informed decision.”

Thompson agrees. “Close to 40 per cent of Canadians live paycheque to paycheque. They tend to confuse the lifestyle they can afford with the one they would like to have,” she says. “In the current economic conditions, their first step should be to minimize their financial obligations.”

By asking questions, you can understand their circumstances better and may be able to help in other ways, such as buying groceries, housing or babysitting, says Thompson.

“Transparency may not be the norm when it comes to money, but now’s the time to be honest about your situation and the assistance you can offer,” she adds. “This crisis is unprecedented and may lead people to make different decisions than they normally would.”

Rule 4: Set the terms

Under such circumstances, establishing terms for the loan, an IOU of sorts, is essential. Specify the total amount, set a due date or a repayment schedule, and determine whether you’ll be charging interest, even if the rate is nominal.

“Money may still be a taboo topic, but you shouldn’t be shy about asking for information, in the same way a bank would,” says Leblanc. “What’s their current debt level? Do they have a credit report? Can they give you an idea of their actual budget?”

“This is a tough conversation for anyone to have,” acknowledges Thompson. “But you can always say that times are tough for everyone and that you don’t have enough cash.” If you’re honest, your loved one will better understand where you’re coming from and the help you can provide is limited.

“You can also secure a loan by registering an asset as collateral, such as a home or a debt-free vehicle,” says Leblanc. “Or the borrower can name you as an irrevocable beneficiary in a life insurance policy. This

makes it possible to protect the loaned amount up front from other creditors, in the event of bankruptcy, for example.”

Rule 5: Think twice before guaranteeing a loan

Guaranteeing a loved one’s loan is just as risky. In addition, you can be on the hook for not only the debt, but also any accrued interest.

“Guarantors feel like they aren’t as involved as if they’d directly provided the funds, but that’s not the case,” says Leblanc. “They take on a new debt obligation if the borrower defaults.”

Some may have their eyes on their parents’ or grandparents’ home equity or other lines of credit and wear them down with emotional blackmail to get what they want. “If you’ve never told them no in the past, it’s difficult to start when money is involved,” says Leblanc.

Under the current conditions, many parents may be tempted to help children whose businesses are in trouble. However, warns Leblanc, “With \$10,000, you may be able to put out the fire by paying rent, employee salaries and creditors. But, it’s quite likely that three months from now, business won’t be back to normal in restaurants, for instance. Is this the best way to help? It’s hard to say.”

Decisions like these are all about the numbers and a professional like a CPA or a trustee in bankruptcy can be of assistance. With guidance, lenders will be in a better position to get their money back in the future. ♦



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We hope that you find *info@pyc* a useful source of information. If you should ever have any specific questions or concerns regarding your own business or personal finances, please call us. We will gladly help in any way that we can.

If you would like to contact us by e-mail, we can be reached at *info@pyc.net*. Some of the articles appearing in this issue of *info@pyc.net* were prepared by the Chartered Professional Accountants of Canada for the clients of its members.