



## Federal Budget 2007 - Not a “bring down the government” kind of budget

### Introduction

Finance Minister, Jim Flaherty, introduced the Conservative government’s second budget on March 19, 2007. The Bloc has agreed to support the budget so there is no risk of the budget precipitating an election.

The budget does not contain any broad based tax reduction measures like rate reductions or bracket realignments. The tax measures can best be described as targeted to specific groups or initiatives.

What received a lot of attention but is noticeable by its absence are any measures eliminating or deferring capital gains tax liabilities on dispositions of capital property. So, if you were waiting to sell the cottage until after the budget, there’s no good news in it for you.

The budget materials also highlighted many items which were previously announced and that are in various stages of implementation: the increase in the age credit; pension income splitting; corporate tax reductions, to name a few.

We will highlight measures of note from a financial industry and consumer perspective and will point out any opportunities or implications from a life insurance and investment planning perspective.

### Child Tax Credit

A non-refundable child tax credit is proposed for each child under the age of 18 years at the end of the year. The amount used to calculate the tax credit will be \$2,000. At the lowest personal tax rate it will be worth about \$310 per child. It will take effect in 2007.

### Spousal and other amounts

The budget proposes to increase the amount used to calculate the spousal and wholly dependant tax credit (currently at \$7,581) to match the basic personal amount of \$8,929 for 2007. The credit amounts will increase to match announced increases in the basic personal amounts.

### Lifetime Capital Gains Exemption

The budget proposes to increase the lifetime capital gains exemption from \$500,000 to \$750,000. The exemption will apply to dispositions of qualified small business corporation shares and qualified farm or fishing property that occur on or after March 19, 2007.

### Donations to Private Foundations

Last year’s Federal Budget reduced the capital gains inclusion rate to zero on the donation of publicly-listed securities (including mutual funds and segregated funds) to a public charity. It also eliminated the tax on the employment benefit when an employee donates a publicly-listed security acquired under an option if it is donated to a public charity within 30 days.

The 2007 Budget proposes to extend these rules to gifts made to private foundations on or after March 19, 2007. However, limitations on holdings will apply. In general a foundation

and all non-arm's length persons together cannot hold more than 20 per cent of all outstanding shares in any share class of a corporation. Transitional rules will allow foundations to comply with the 20 per cent limitation where they have excess holdings present on March 18, 2007.

Capital gains (or employment benefits) arising from donations of publicly-listed securities to private foundations will be eliminated as a result of this measure. Taxpayers may consider purchasing insurance or other investments with the tax savings derived from gifting publicly-listed securities to private foundations.

### **Registered Disability Savings Plan**

A new Registered Disability Saving Plan (RDSP) is introduced to help parents and others save for long-term financial security of people with severe disabilities. Commencing in 2008, the plan will be roughly similar in design to the existing registered education savings plan (RESP). Those individuals that qualify for the disability tax credit, their parent or other legal representative may establish an RDSP.

RDSP contributions may qualify for a Canada Disability Savings Grant (CDSG) and a Canada Disability Savings Bond (CDSB). Eligibility is based on family income ranges.

Contributions to an RDSP will not be deductible to the contributor. Contributions will be limited to a lifetime maximum of \$200,000 with no annual limit. The investment income on contributions in the plan, CDSGs and CDSBs will accumulate tax free. CDSGs, CDSBs and investment income earned will be included in the beneficiary's income for tax purposes when paid out of an RDSP. Payments must commence by age 60.

Repayment of CDSGs and CDSBs and income inclusion of RDSP funds will be required upon death or cessation of disability of the beneficiary.

Only the plan beneficiary or their legal representative will be entitled to receive payments from the plan. Payments from the plan will not affect other benefits such as the Canada Child Tax Benefit, the Goods and Services Tax credit, Old Age security and Employment Insurance benefits.

### **Pension Income Splitting**

While no new details were provided, the budget confirmed that the government will enact the pension income splitting provisions announced on October 31, 2006 in the Tax Fairness Plan. Commencing in 2007, Canadian residents receiving pension income that qualifies for the pension income credit can allocate up to half of this income to their spouse or common-law partner. The transferor will deduct the amount allocated and the transferee will include the amount allocated. Both parties must agree to the allocation in their tax returns.

For individuals age 65 and older\* the following qualify as eligible sources of income:

1. A life annuity out of a Registered Pension Plan (RPP)
2. Annuity payments out of an RRSP
3. Withdrawals from a RRIF
4. Annuity and installment payments out of a Deferred Profit Sharing Plan (DPSP)
5. Income from some foreign pension arrangements and U.S. IRAs
6. The interest element of a non-registered annuity contract (prescribed & non-prescribed), and
7. Accrued (interest) income from a non-registered deferred annuity contract such as a GIC with an insurance company.

\*A life annuity from a RPP also qualifies for the pension tax credit for any individual under age 65. Payments described in items 2 to 7 may also qualify for the credit under age 65 if the income is received because of the death of the individual's spouse.

### **Increasing the Age Limit for Maturing RRSPs and RPPs**

The Income Tax Act currently requires that RRSPs, RPPs and DPSPs mature by the end of the year in which an individual turns age 69. The budget proposes to increase the conversion age

from 69 to 71 starting in 2007. For individuals who turn 70 in 2007, contributions are permitted to their RRSP in 2007 and 2008, provided contribution room is available. For individuals who turn 71 in 2007, contributions are permitted to their RRSP in 2007, provided contribution room is available.

In addition the requirement that a specified minimum amount be withdrawn from a RRIF the year after it is established will be waived for 2007 and 2008 for individuals that turn 70 in 2007 and for 2007 for individuals who turn 71 in 2007.

A RRIF annuitant who is 71 years or younger at the end of 2007 may convert the RRIF back to an RRSP so long as the plan is converted back to a RRIF before the end of the year the individual turns 71.

### **Registered Education Savings Plans (RESPs)**

The budget proposes several measures to provide more flexibility to families who save through RESPs, and to make RESPs more responsive to the changing needs of education today. The \$4,000 annual RESP contribution limit will be eliminated, and the lifetime RESP contribution limit will be increased to \$50,000 from \$42,000. The maximum annual RESP contribution qualifying for the 20-per cent Canada Education Savings Grant (CESG) will be increased to \$2,500 from \$2,000, thus increasing the maximum annual CESG per beneficiary for 2007 and subsequent years to \$500 from \$400. The maximum CESG for a year will increase to \$1,000 from \$800 if there is unused grant room from previous years. The lifetime CESG limit of \$7,200 will be unaffected by this change.

The budget also proposes to relax the Education Assistance Payment eligibility requirement to accommodate qualifying part-time programs beginning in 2007.

### **Conclusion**

All in all, from a financial services perspective, the 2007 Budget only provided a few tax measures of significance. No broad based tax reductions -- just tax measures targeted at small business owners, families with children, seniors, and the disabled.

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