

# New Federal Income Tax Changes – Effective January 1, 2016

In December 2015, the federal Liberal government tabled legislation to introduce tax initiatives from their election platform to take effect on January 1, 2016. While the legislation has not yet received Royal Assent, it is expected that these measures will formally be enacted into law shortly.

## Reduction of the TFSA annual contribution limit

Effective January 1, 2016, the TFSA contribution limit has been reduced to \$5,500. The TFSA contribution limit was increased to \$10,000 (from \$5,500) in the Conservative government's April 2015 Federal Budget; however, the Liberal government subsequently reverted the contribution limit back to \$5,500 for 2016 and future years. The TFSA contribution limit will be indexed to inflation, increasing in \$500 increments. The government also confirmed that the 2015 TFSA contribution limit will remain at \$10,000 and can be carried forward as part of an individual's lifetime TFSA contribution limit for use in future years.

## Changes to federal personal tax rates

In keeping with the government's campaign promise to strengthen the middle class, the Income Tax Act will be amended to lower the federal income tax rate for Canadians earning between \$45,282 and \$90,563 per year, from 22% to 20.5%. This reduced rate will translate into a maximum tax savings of approximately \$679 per individual. In addition, a new top federal tax bracket for taxable income over \$200,000 was introduced with a corresponding 33% income tax rate. The new rate is 4% higher than the previous top federal personal tax rate of 29%.

The table below compares the previous and the updated 2016 personal federal income tax brackets and rates:

Taxable Income	2016 Rate	Previous Rate
Up to \$45,282	15.0%	15.0%
\$45,282 - \$90,563	20.5%	22.0%
\$90,563 - \$140,388	26.0%	26.0%
\$140,388 - \$200,000	29.0%	29.0%
Over \$200,000	33.0%	29.0%

For further details regarding the combined top marginal tax rates by province, please refer to the **Appendix**.

Please note that the 4% federal tax rate increase for 2016 does not automatically translate into a 4% increase for incomes exceeding \$200,000 in all provinces. This is because some provinces have their own tax rate adjustments scheduled for 2016. Most notably, top rate taxpayers in Alberta will face a combined tax increase of 7.75% on ordinary income (e.g., salary, interest), resulting from the 2016 provincial and federal tax increases.

## Consequential tax changes

The government also announced the following consequential tax changes associated with the new 33% top federal tax rate, effective for 2016 and subsequent taxation years:

### Trust and estates

Another previously introduced tax measure that came into effect on January 1, 2016 was to align testamentary trusts (which are trusts created at death, typically in the deceased's Will) with inter-vivos trusts (i.e., trusts created during one's lifetime), and applying a flat tax rate at the top personal marginal rate – to any income retained in the trust. As a result, trusts and estates will also be subject to the new 33% federal tax rate. However, graduated rate estates and qualified disability trusts are not subject to this change and will continue to be taxed under the graduated tax rate system (including the 33% rate on taxable incomes exceeding \$200,000), effective in 2016.

### Kiddie tax

Certain income-splitting arrangements involving minor children, such as the payment of taxable dividends from private corporations directly (or indirectly through a trust) to a minor, may be subject to the 'Tax on Split Income.' This so-called "kiddie tax" will apply the new 33% top tax rate to the applicable income, instead of the child's marginal tax rate based on the child's lower income.

### Donation tax credits

Currently, individuals are able to claim a donation tax credit that is equal to the former top federal marginal tax rate of 29% on qualifying charitable donations over \$200. This is being amended to allow higher income donors to claim a 33% federal tax credit, but only on the portion of donations made from income that is subject to the new 33% top marginal tax rate. However, for those who qualify, this 33% donation tax credit rate will only be available for donations made after 2015 and will not be available for donations that are carried forward from a year prior to 2016.

## Investment income of private corporations

Given that corporate tax rates are generally lower than personal tax rates, special refundable taxes are imposed on the investment income of private corporations in order to limit the ability of individuals to defer taxation by holding investments in a private corporation. The 'integration' tax system for private corporations, which seeks to ensure consistency in taxation between individuals earning investment income personally or through a private company, will also be amended to ensure its alignment with the new top personal tax rate. Specifically, increases will be made to the (refundable) corporate tax rates on investment income and the rate at which corporate taxes are refunded from the Refundable Dividend Tax on Hand (RDTOH) on taxable dividend payments, effective January 1, 2016.

## Potential future tax changes and pledges

In addition to the changes discussed, the following is a list of potential future tax changes and pledges made by the Liberal government which could come into effect this year, or thereafter:

**Employee Stock Options** – In its election platform, the government indicated that potential changes to the taxation of employee stock options may be forthcoming. As such, new measures affecting stock option taxation may be included in the upcoming 2016 Federal Budget.

**Family Tax Cut** – The family tax cut (FTC) was introduced in 2014 and provided an additional potential federal non-refundable tax credit for couples with children under the age of 18. It is expected that the FTC will be repealed in the 2016 Federal Budget.

**New Canada Child Benefit (CCB)** – A new CCB plan is expected to be introduced to replace the current Universal Child Care Benefit, Canada Child Tax Benefit and National Child Benefit Supplement. The new CCB will be a tax-free benefit and tied to family income levels, with benefits being reduced as income levels increase. It is expected that families with a household income of \$200,000 or more will not receive any benefit under the new program.

**Home Buyers` Plan (HBP)** – It is expected that access to the HBP will be expanded to allow taxpayers affected by a sudden and significant life change to buy a house without a tax penalty through the HBP. Life changes would include a job relocation, the death of a spouse, marital breakdown or a decision to accommodate an elderly family member.

**Canada Pension Plan (CPP) /Old Age Security (OAS)** – The Liberal government has pledged to review the current CPP program along with the provinces and territories in order to potentially enhance the program. They have also pledged to retain OAS eligibility at age 65. The former Conservative government had proposed that the age requirement would increase to 67 years of age.

**Private Corporation Small Business Tax Rates** – In 2015, the former Conservative government implemented changes to gradually reduce the small business tax rate from 11% in 2015, to 9% by 2019, on the first \$500,000 of qualifying

active business income earned by a Canadian-Controlled Private Corporation (CCPC). The new Liberal government intends to proceed with this 2% reduction to the federal small business tax rate; however, they have not specified the implementation timeframe.



The tax changes, proposals and potential future changes outlined in this article are wide-ranging and may have significant implications to your particular tax situation. Please consult with your tax advisors for specific advice and direction on how you may be affected by these tax changes.

For more information on these measures, please ask your BMO Nesbitt Burns Investment Advisor for a copy of the article **Update on Liberal Federal Income Tax Changes**.

## Appendix – Comparison of 2016 and 2015 combined top marginal tax rates

Province	Ordinary Income		
	2016	2015	Increase
British Columbia	47.70%	45.80%	1.90%
Alberta	48.00%	40.25%	7.75%
Saskatchewan	48.00%	44.00%	4.00%
Manitoba	50.40%	46.40%	4.00%
Ontario	53.53%	49.53%	4.00%
Quebec	53.31%	49.97%	3.34%
New Brunswick	58.75%	54.75%	4.00%
Nova Scotia	54.00%	50.00%	4.00%
Prince Edward Island	51.37%	47.37%	4.00%
Newfoundland	48.30%	43.30%	5.00%
Northwest Territories	47.05%	43.05%	4.00%
Nunavut	44.50%	40.50%	4.00%
Yukon	48.00%	44.00%	4.00%

Province	Eligible Dividends		
	2016	2015	Increase
British Columbia	31.30%	28.68%	2.62%
Alberta	31.71%	21.02%	10.69%
Saskatchewan	30.33%	24.81%	5.52%
Manitoba	37.78%	32.26%	5.52%
Ontario	39.34%	33.82%	5.52%
Quebec	39.83%	35.22%	4.61%
New Brunswick	43.79%	38.27%	5.52%
Nova Scotia	41.58%	36.06%	5.52%
Prince Edward Island	34.22%	28.70%	5.52%
Newfoundland	38.47%	31.57%	6.90%
Northwest Territories	28.33%	22.81%	5.52%
Nunavut	33.08%	27.56%	5.52%
Yukon	24.81%	19.29%	5.52%

Province	Capital Gains		
	2016	2015	Increase
British Columbia	23.85%	22.90%	0.95%
Alberta	24.00%	20.13%	3.87%
Saskatchewan	24.00%	22.00%	2.00%
Manitoba	25.20%	23.20%	2.00%
Ontario	26.76%	24.76%	2.00%
Quebec	26.65%	24.98%	1.67%
New Brunswick	29.38%	27.38%	2.00%
Nova Scotia	27.00%	25.00%	2.00%
Prince Edward Island	25.69%	23.69%	2.00%
Newfoundland	24.15%	21.65%	2.50%
Northwest Territories	23.53%	21.53%	2.00%
Nunavut	22.25%	20.25%	2.00%
Yukon	24.00%	22.00%	2.00%

Province	Non-eligible Dividends		
	2016	2015	Increase
British Columbia	40.61%	37.99%	2.62%
Alberta	40.25%	30.84%	9.41%
Saskatchewan	40.06%	34.91%	5.15%
Manitoba	45.69%	40.77%	4.92%
Ontario	45.30%	40.13%	5.17%
Quebec	43.84%	39.78%	4.06%
New Brunswick	51.75%	46.89%	4.86%
Nova Scotia	46.97%	41.87%	5.10%
Prince Edward Island	43.87%	38.74%	5.13%
Newfoundland	39.40%	33.26%	6.14%
Northwest Territories	35.72%	30.72%	5.00%
Nunavut	36.35%	31.19%	5.16%
Yukon	40.18%	35.18%	5.00%

**Note:** The combined 2016 tax rates do not reflect potential changes that the provinces may introduce to their 2016 provincial tax rates in light of the federal tax rate changes announced.

**Source:** PWC Tax Insights from High Net Worth/Private Company Services Issue 2015-50



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