INVESTMENT INDUSTRY ASSOCIATION OF CANADA
ASSOCIATION CANADIENNE DU COMMERCE DES VALEURS MOBILIÈRES

Summary of 2016 Federal Budget
Highlights Relevant to Canada's Investment Industry

For additional details on all the items below, refer to the 2016 Federal Budget available at: http://www.budget.gc.ca/*. Please note that Budget announcements requiring legislative amendment remain proposals until passed into law, and could be subject to change. The information in this summary is of a general nature and current as of publication. It should not be regarded as comprehensive or a substitute for professional advice.*

The Deficit and the Economic Outlook

- Using the February updated economic outlook for planning purposes, and accounting for budget measures, the budgetary balance is expected to show a deficit of $29.4 billion in 2016–17, gradually declining to a deficit of $14.3 billion in 2020– 21.

- The Department of Finance estimates that the measure contained in Budget 2016, along with the middle class tax cut announced in December 2015, will raise the level of real GDP by 0.5% in the first year and by 1.0% by the second year. The Government expects this to translate into 100,000 jobs created or maintained by 2017-2018.

- Risks around the economic outlook are largely external to the Canadian economy, stemming from uncertainty around the future of oil prices, failure of the U.S. economy to meet expectations and rebalancing in China. For these reasons, the Government is adjusting downwards the private sector forecast for nominal GDP by $40 billion per year for 2016 through 2020.

- The Government confirmed that they would be proposing legislative repeal of the *Federal Balanced Budget Act*, enacted under the previous government.

Infrastructure Investment

- The Government's $120 billion plan for infrastructure investment will be implemented in two phases:

    - Phase 1: $11.9 billion, mostly over the first two years, to focus on investments for modernizing public transit, water and wastewater systems and social housing.
    - Phase 2: The residual funding of over $100 billion will be focused on long-term infrastructure investment, after the Government engages in consultation with partners, investors and other stakeholders.

Canada Pension Plan and Measures Affecting Income for Seniors

- The Government proposes to increase the Guaranteed Income Supplement (GIS) top-up benefit by up to $947 annually for single seniors starting in July 2016. Single seniors with annual income (other than Old Age Security (OAS) and GIS benefits) of $4,600 or less will receive the full increase of $947. Above that income threshold, the amount of increased benefit will be gradually reduced, and completely phased out at an income level of $8,400. Benefits will be adjusted quarterly with increases in the cost of living.

- The Government will launch consultations on the potential enhancement of the Canada Pension Plan (CPP) in the coming months. The Government has been in discussions with the provinces and territories, with the goal of making a collective decision before the end of 2016.

- The Government intends to cancel the provisions in the *Old Age Security Act* that increase the age of eligibility for OAS and GIS benefits from 65 to 67 and Allowance benefits from 60 to 62 over the 2023 to 2029 period.

- The Government also intends to introduce amendments to the *Old Age Security Act* that will ensure that couples who receive Guaranteed Income Supplement and Allowance Benefits and have to live apart for reasons beyond their control (such as required long-term care) will receive higher benefits based on their individual incomes.

- The Government will look at developing a "Seniors Price Index" that could be used to ensure that OAS and GIS benefits keep pace with the actual cost of living faced by seniors.

Systemic Risk/*Capital Markets Stability Act* (CMSA)

- The Government intends to fulfill Parliament's role in the management of systemic risks in Canada's capital markets and Canada-wide data collection in a manner that is "collaborative and respectful of provincial and territorial jurisdiction".

- The Government will release a revised draft of the proposed federal *Capital Markets Stability Act* by summer 2016.

Legislative Review of Financial Sector Legislation and *Bank Act* Amendments

- The Department of Finance will undertake a review of federal financial sector legislation governing banking and insurance (as required every five years), and will begin consulting with stakeholders as part of this process. Budget 2016 provides funding to the Department of Finance over five years to undertake this review and will extend the statutory sunset date by two years to March 29, 2019.

- Amendments to the *Bank Act* will be proposed to add a new chapter, which will consolidate consumer protection provisions currently contained in the *Act*, and to provide a set of guiding principles for banks to "act fairly and responsibly". The Financial Consumer Agency of Canada (FCAC) will continue to oversee compliance with the regulatory framework and work with stakeholders to enhance financial literacy.

- The Government is proposing to introduce framework legislation to implement a "bail-in" regime that would allow authorities to convert eligible long-term debt of a failing systemically important bank into common shares to recapitalize the bank and allow it to remain open and operating. Regulations and guidelines setting out further features of the regime will follow, and stakeholders will be provided with an opportunity to comment on the elements of the regime.

Tax System Review

- In the coming year, the Government will undertake a review of the tax system, particularly aimed toward eliminating poorly targeted and inefficient tax expenditures.

Base Erosion and Profit Shifting (BEPS)/Common Reporting Standard (CRS)

- The Government will be acting on certain recommendations of the OECD Base Erosion and Profit Shifting (BEPS) project, in particular, proposing new legislation to introduce country-by-country reporting for large multinational enterprises, and spontaneous exchange with other jurisdictions of tax rulings that could give rise to BEPS concerns.

- Canada intends to implement the CRS starting on July 1, 2017, allowing for the first exchange of tax information with other countries in 2018, and the Government will issues legislative proposals for public comment in the near future.

Small Business Income Tax Rate

- The Government has decided to defer any further reduction in the small business income tax rate beyond the current 10.5% rate on the first $500,000 of active business income.

Labour-Sponsored Venture Capital Corporations Credit

- The Government will restore the Labour-Sponsored Venture Capital Corporations (LSVCC) tax credit to 15% for share purchases of provincially registered LSVCCs for 2016 and subsequent tax years.

Charitable Donation of Private Shares

- The Government confirmed that they would <u>not</u> proceed with the measure announced in the 2015 budget to provide an income tax exemption in respect of capital gains on certain dispositions of private corporation shares or real estate, where cash proceeds from the disposition are donated to a registered charity or other qualified done within 30 days.

Synthetic Equity Arrangements

- The Government intends to proceed with changes to "synthetic equity arrangements" under the dividend rental arrangement rules. As announced in last year's budget, the Government will modify the dividend rental arrangement rules in the *Income Tax Act* to deny the inter-corporate dividend deduction on dividends received by a taxpayer on a Canadian share in respect of which there is a synthetic equity arrangement as modified, to take into account consultations and deliberations since their announcement.

Other New Tax Measures

- The Government will extend eligibility for the 15% Mineral Exploration Tax Credit for an additional year, until March 31, 2017. This tax credit helps junior exploration companies raise capital by providing investors with an incentive in flow-through shares issues to finance mineral exploration, in addition to the deduction provided to the investor for the exploration expenses "flowed through" by the company that issues the shares.

- The Government proposes to amend the *Income Tax Act* so that an exchange of shares of a mutual fund corporation (or investment corporation) that results in the investor switching between funds ("switch fund shares") will be considered for tax purposes to be a disposition at a fair market value. Currently these switches are not deemed to be a disposition for income tax purposes. This measure will apply to dispositions of shares that occur after September 2016.

- The Government proposes to amend the Income Tax Act so that the return on a linked note retains the same character whether it is earned at maturity or reflected in a secondary market sale. A deeming rule will apply for the purposes of the rule relating to accrued interest on the sales of debt obligations, that will treat any gain on the sale of linked note as interest that accrued on the obligation. Furthermore, when a linked note is denominated in a foreign currency, currency fluctuations will be ignored for the purposes of calculating this gain. This measure will apply to sales of linked notes that occur after September 2016.

- The Government proposes to introduce rules so that any accrued foreign exchange gains on a foreign currency debt will be realized when a debt becomes a "parked" obligation. This measure will apply to a foreign currency debt that meets the conditions to become a "parked" obligation on or after March 22, 2016. There will be an exception where the meeting of these conditions occurs before 2017 and results from a written agreement entered into before March 22, 2016.

- The Government has also proposed measures that will affect the *de minimis* rules for treatment as a financial institution for GST/HST purposes, which will apply as of March 22, 2016.

Other Proposals of Interest:

- The Government proposes to eliminate income splitting for couples with children under the age of 18 for the 2016 and subsequent taxation years. Pension income splitting will not be affected by this change.
- The current child benefit system will be replaced with the Canada Child Benefit, which will provide a maximum annual benefit of up to $6,400 per child under the age of 6 and up and up to $5,400 per child for those aged 6 through 17.
- The Government proposes to reduce the maximum eligible expenses for the Children's Fitness and Arts Tax Credits by half for 2016 and eliminate both credits as of 2017.