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Federal Budget 2022: What does it mean for personal income taxes?

The Tax & Estate team summarizes the key measures focusing on personal taxation, financial planning, and investment portfolios within Canada's Federal Budget 2022.

On April 7, 2022, Chrystia Freeland, Deputy Prime Minister and Minister of Finance, tabled Federal Budget 2022 (https://budget.gc.ca/2022/home-accueil-en.html). Below is our summary of the key measures focusing on personal taxation, financial planning, and investment portfolios.

Read our summary about the business tax measures contained in the budget.

Personal income tax measures

Tax-Free First Home Savings Account (FHSA)

Home Buyers' Tax Credit

Tax-Free First Home Savings Account (FHSA)

A new registered plan designed to help individuals save up for a down payment on their first home was proposed: the Tax-Free First Home Savings Account (FHSA). Expected to launch sometime in 2023, the FHSA will borrow features of existing registered plans. Contributions to the FHSA will be tax-deductible and withdrawals from the FHSA will be tax-free.

While more details are to follow on the plan's structure, the following details are known:

Eligibility requirements

- An individual must be 18 years of age or older and a resident of Canada
- An individual must not have lived in a home they owned at any time in either the current year or during the preceding four calendar years

Contributions

- Lifetime maximum contribution limit of $40,000, with an annual contribution limit of $8,000
- No carryforward of unused annual contribution room. In other words, if an individual contributes less than $8,000 to their FHSA in 2023, they would still be limited to a maximum contribution of $8,000 in 2024.

Withdrawals and Transfers

- Only withdrawals directly used to purchase a first home will be tax free. Withdrawals made for any other purpose will be taxable.
- Funds already held in an RRSP or a RRIF can be transferred to a FHSA on a tax-free basis in order to fund the FHSA, though doing so will not restore RRSP contribution room.
- The FHSA must be collapsed after a maximum of 15 years. Any unused FHSA contributions can be transferred on a tax-deferred basis to the individual's RRSP or RRIF without requiring the individual to have RRSP contribution room and without affecting their RRSP contribution limit.
- The Home Buyers' Plan (HBP), which enables qualifying first-time homebuyers to withdraw up to $35,000 from their RRSPs to purchase their first home, will still be offered. However, individuals purchasing a first home will not be able to participate in both the HBP and the FHSA: A withdrawal under only one of the schemes will be permitted.

Home Buyers' Tax Credit

Budget 2022 proposes to enhance the existing First-Time Homebuyers Tax Credit (HBTC). Under the current rules, the HBTC enables qualifying first-time homebuyers to claim a credit of up to $5,000 for the purchase of a home that they or their spouse or common-law partner intend to occupy as their principal place of residence. The

Budget proposes to double the maximum HBTC amount, bringing it up to $10,000.

Residential Property Flipping Rule and Ban on Foreign Property Investors

Property flipping is the act of buying real estate for the purpose of reselling it at a profit a short time later. Existing tax rules treat profits from property flipping as fully taxable income, as opposed to capital gains. As well, existing rules also prohibit property flippers from claiming the principal residence exemption (PRE) on the sale of a flipped property.

The Department of Finance has concerns that some property flippers are incorrectly reporting sales as capital gains and/or claiming the PRE. As a result, Budget 2022 proposes to implement a new deeming rule that will automatically treat the profits from the resale of residential property within 12 months of purchase as fully taxable income and will preclude the seller from claiming the PRE. This rule will apply to the sale of residential properties on or after Jan. 1, 2023.

There will be exceptions to the deeming rule if a property is sold within 12 months for any of the following reasons: death, additions of members to the same household, separation, personal safety concerns, disability or illness, employment change, insolvency, or involuntary dispositions (for example, if a natural disaster were to force the owner to relocate).

As part of the effort to curb housing speculation, the Department of Finance also announced its intention to ban foreign investors, both commercial and individual, from purchasing Canadian residential real estate for a two-year period. A variety of individuals who do not hold Canadian citizenship will be exempted from the ban, including refugees, permanent residents, certain international students on track to obtain permanent residency, and individuals residing in Canada on a work permit.

Medical Expense Tax Credit for Surrogacy and Other Expenses

Budget 2022 proposes to allow access to the medical expense tax credit (METC) for costs related to a surrogate mother or a sperm, ova, or embryo donor. The move expands access to the credit for individuals other the intended parents. Budget 2022 also proposes to allow fees paid to fertility clinics and donor banks in Canada in order to obtain donor sperm and ova to be eligible under the METC. The changes would be effective for the 2022 tax year and for subsequent years.

As a brief overview, the METC is available on qualifying medical expenses in excess of the lesser of $2,479 and 3% of the individual net income. The expenses must be in respect of products and services received by the taxpayer, their spouse or common-law partner or certain dependents of the taxpayer. Budget 2022 will broaden access to the METC in respect of these targeted measures.

Home Accessibility Tax Credit (HATC)

The federal HATC is a non-refundable credit for eligible expenses for a qualifying renovation of an eligible dwelling. Currently, the HATC can be claimed on eligible expenses up to $10,000 in a given taxation year, which equates to up to $1,500 in tax credits (the value of the credit is calculated by applying the lowest personal income tax rate (15% in 2022), to the eligible expenses. Budget 2022 proposes to increase the annual expense limit of the HATC from $10,000 to $20,000. The measure would apply to expenses incurred in the 2022 and subsequent tax years.

In order to claim the HATC, the taxpayer must be a qualifying individual **or** an eligible individual making a claim for a qualifying individual.

- ***Qualifying individual*** is an individual who is eligible for the disability tax credit for the particular taxation year and/or an individual who is 65 years of age or older at the end of the taxation year.
- ***Eligible individual*** includes a spouse, common-law partner, and certain supporting relatives of a qualifying individual.

- ***Eligible dwelling* is** generally a housing unit located in Canada that meets at least one of the following conditions:
  - It is owned (either jointly or otherwise) by the qualifying individual and it is ordinarily inhabited (or is expected to be ordinarily inhabited) in the year by the qualifying individual; or
  - it is **owned** (either jointly or otherwise) by the eligible individual (https://www.canada.ca/en/revenue-agency/services/tax/individuals/topics/about-your-tax-return/tax-return/completing-a-tax-return/deductions-credits-expenses/line-398-home-accessibility-expenses.html#lgbl_ndvdl) and is ordinarily **inhabited** (or is expected to be ordinarily inhabited) in the year by the eligible individual and the qualifying individual, and the qualifying individual does not throughout the year own (either jointly or otherwise) and ordinarily inhabit another housing unit in Canada
- *Qualifying renovation* is a renovation or alteration that is of an enduring nature and is integral to the eligible dwelling. In general, if the renovation or alteration is not permanent in nature, it will not qualify for the HATC. The renovation or alteration must allow the qualifying individual to gain access to or to be mobile/functional within the dwelling; or reduce the risk of harm to the qualifying individual within or in gaining access to the dwelling.

New Multigenerational Home Renovation Tax Credit

Budget 2022 proposes to introduce a new refundable tax credit, known as the Multigenerational Home Renovation Tax Credit The credit is applicable to the 2023 and subsequent tax years, in respect of work performed and paid for and/or goods acquired on or after Jan. 1, 2023.

The Multigenerational Home Renovation Tax Credit could be claimed by eligible claimants on eligible expenses of up to $50,000 for a qualifying renovation, which equates to up to $7,500 in tax credits.

Qualifying renovation

- Creates a secondary self-contained dwelling unit (private entrance, kitchen, bathroom facilities, and sleeping area) in addition to an eligible dwelling to permit an eligible person (i.e., a senior or an adult with a disability) to live with a qualifying relation.
- An eligible person includes seniors (65 or older at the end of the taxation year that includes the end of the renovation period) and adults with disabilities (18 years or older at the end of the taxation year that includes the end of the renovation period, and eligible for the Disability Tax Credit at any time in that year).
- A qualifying relation is a parent, grandparent, child, grandchild, brother, sister, aunt, uncle, niece, or nephew of the eligible person or their spouse. The qualifying relation must be 18 years or older at the end of the taxation year that includes the end of the renovation period.
- An eligible dwelling is a housing unit owned (either jointly or otherwise) by the eligible person or their spouse/common law partner or a qualifying relation. In addition, the eligible person and a qualifying relation must ordinarily reside or intend to ordinarily reside, within 12 months after the end of the renovation period.
- To be eligible, the appropriate building permits for establishing a secondary unit must be obtained and renovations must be completed in accordance with the laws of the jurisdiction where the eligible dwelling is located.
- Only one qualifying renovation would be permitted to be claimed with respect to an eligible person over their lifetime.

Eligible claimants

- An eligible person, a spouse/common-law partner or a qualifying relation of the eligible person, who ordinarily resides, or intends to ordinarily reside, in the eligible dwelling within 12 months after the end of the renovation period; or a qualifying relation who owns the eligible dwelling.

- More than one eligible claimant can make a claim on an eligible renovation. However, the total of all amounts claimed in respect of the qualifying renovation must not exceed $50,000.

Eligible expenses

- Expenses would be eligible for the credit if the expenses were made or incurred during the renovation period for the purpose of a qualifying renovation and are reasonable in the context of that purpose (i.e., the expenses enable an eligible person to reside in the dwelling with a qualifying relation).
- Eligible expenses could include the cost of labour and professional services, building materials, fixtures, equipment rentals, and permits.
- Ineligible expenses include items such as furniture, construction equipment, and tools would not be integral to the dwelling. Also, the cost of annual, recurring, or routine repair or maintenance, as well as payments for services such as outdoor maintenance and gardening, housekeeping, or security also would not qualify for the credit.
- Eligible expenses that would have been included in a claim must be reduced by any reimbursement or any other form of assistance that an individual is or was entitled to receive, including any rebates (e.g., Goods and Services Tax/Harmonized Sales Tax).
- Expenses would not be eligible for the Multigenerational Home Renovation Tax Credit if they were claimed under the Medical Expense Tax Credit and/or Home Accessibility Tax Credit.

Annual Disbursement Quota Changes for Registered Charities

A disbursement quota (DQ) is the minimum amount registered charities are generally required to expend each year on its own charitable activities, or on gifts to qualified donees (e.g., other registered charities). The DQ calculation is based on the value of a charity's property **not** used for charitable activities or administration. The DQ is currently set to 3.5% of the registered charity's property **not** used in directly for charitable activities or administration. Budget 20222 proposed to increase the DQ rate from 3.5% to 5% for the portion of property **not** used in charitable activities or administration that exceeds $1 million. Budget 2022 also proposes to amend the *Income Tax Act* so that expenditures for administration and management are not considered qualifying expenditures for the purposes of satisfying a charity's DQ. That said, the CRA will have the discretion to grant a reduction in a charity's DQ obligation for any particular year.

Currently, charities are allowed to apply to the CRA for permission to temporarily accumulate funds to make a major expenditure (e.g., buying a costly piece of equipment). If the application is approved, any property accumulated in accordance with the approval (including income earned) is not included in calculating a charity's DQ. Budget 2022 proposes to remove the accumulation of property rule, due to prior changes that simplified the DQ and existing provisions which provide relief to charities.

These measures would apply to charities with fiscal periods beginning on or after Jan. 1, 2023. The amendment to remove the accumulation of property rule would not apply to approved property accumulations resulting from applications submitted by a charity prior to Jan. 1, 2023.

Borrowing by Defined Benefit Pension Plans

Budget 2022 proposes more flexible borrowing rules in defined benefit pension plans administration. Applicable to amounts borrowed on or after the Budget Day, the new measure replaces one of the current borrowing *term* restriction (90-day) with a new *amount* limitation based on the plan's assets and liabilities, re-calculated at the beginning of each fiscal year.

Reporting Requirement for RRSPs and RRIFs

Financial institutions are required to report to the Canada Revenue Agency (CRA) on an annual basis, a comprehensive list of transactions that have occurred within each Tax-Free Savings Accounts (TFSAs). The information includes the fair market value of the property held in the account. Budget 2022 proposes to expand this requirement to apply to both Registered Retirement Savings Plans (RRSPs) and Registered Retirement Income Funds (RRIFs) that a financial institution administers. The information is sought to assist the CRA in its "risk-assessment activities" regarding qualifying investments held by RRSPs and RRIFs. The proposal appears to target very large RRSP/RRIF accounts that may subsequently involve further probes to determine whether the underlying investment activities withing the registered plans were qualified. The measure would apply starting in 2023.

Investments that may be held in registered plans are regulated by the *Income Tax Act.* Not all investments are "qualified" to be held within a registered plan but generally includes a wide variety of common investments such as traditional open-ended mutual funds and exchange traded funds. Where an individual acquires a non-qualifying investment, a 50% tax is imposed on the value of the investment. The punitive tax may be refundable in certain circumstances though the rules require the filing of a sperate tax return and to remit the tax on behalf of the registered plan, amongst other requirements. Further rules deal with "prohibitive investments" and attract similar punitive tax measures.

Minimum Tax for High Earners and Review of the Alternative Minimum Tax (AMT)

Budget 2022 proposes to introduce details (through the upcoming 2022 fall economic statement) on a minimum tax measure that will ensure high-income earners pay their fair share of income taxes. The government released information indicating that some high-income Canadians continue to pay relatively little in taxes including some 28% of filers with gross income above $400,000 paying an average federal income tax rate of 15% or less in 2019. The government further informs that more than one in 10 of top income earners pay less than 5% in federal income taxes. This rate is often less in federal taxes than the lowest income-earners in Canada. These Canadians make use of various tax incentives, deductions and credits, enabling to reduce their overall taxes payable. For reference, here are the 2022 federal tax rates:

Taxable income		
From	**To**	**Tax Rate**
$0	$50,197	15%
$50,198	$100,392	20.50%
$100,393	$155,625	26%
$155,626	$221,708	29%
$221,709	+	33%

As part of the introduction to establish a minimum tax for high income earners, the government will review The Alternative Minimum Tax (AMT) rules. The AMT has been in place since 1986 and was designed to prevent individuals from making disproportionate use of preferential tax treatments and ensuring a certain amount of tax remains payable despite targeted tax benefits claimed. AMT requires a separate tax calculation conducted along with an individual's regular income tax calculations by taking into consideration certain tax preferred treatments or deductions that an individual claimed in the tax year. In other words, the regular taxable income is recalculated based on a different set of assumptions to arrive at an adjusted taxable income for AMT purposes. This alternative calculation involves the add-back of specific targeted deductions to the taxable income otherwise determined and the exclusion of certain tax credits otherwise available. It is important to note that an individual (other than a trust) is entitled to a basic exemption of $40,000 when determining the adjusted taxable income under the AMT calculation. Instead of the progressive tax rates used in regular tax calculations, a flat rate of 15% is used to calculate the minimum tax payable. If the calculated AMT is greater than the regular tax otherwise payable, the individual must pay the AMT. The excess of AMT over the regular tax otherwise payable may be carried forward for up to 7 years and recovered against regular taxes, subject to certain limitations. Technically, an AMT calculation should be done for every individual each year in addition to the regular federal tax calculation. However, in most cases the regular federal tax payable would be greater than the AMT; therefore, in practice the AMT usually only applies to a small number of individuals.

The review of AMT indicates that thousands of Canadian still pay little to no personal income tax each year and Budget 2022 suggests a review of the AMT along with substantive changes.