

AIM Trimark Investments federal budget analysis 2007

A leader in the timely and thorough preparation of tax information on a range of issues, AIM Trimark has been providing a customized analysis of the federal budget for over a decade. Prepared from within the budget lockup in Ottawa by Jamie Golombek, AIM Trimark's Vice President of Tax & Estate Planning, the 2007 edition selectively focuses on several specific budget elements that will have the biggest impact on your personal finances and investments.

Increasing RRSP Age Limit to 71

Effective immediately, the age limit at which Registered Retirement Savings Plans (RRSPs), Registered Pension Plans (RPPs) and Deferred Profit Sharing Plans (DPSPs) must be converted either into a RRIF or an annuity has been increased to 71 from 69. While this will immediately benefit anyone who turns 69 in 2007, allowing them to defer conversion of their plans by two years, it will also benefit anyone who turns 70 or 71 this year.

Specifically, assuming the 70 or 71 year old has RRSP contribution room available, perhaps due to an unused RRSP carryforward that was never used by age 69 or on account of additional earned income (such as employment or rental income) currently being generated, a new RRSP could be opened this year to shelter such contributions from income and provide a tax deduction on a current or future year's tax return.

Alternatively, the 70 or 71 year old could transfer his or her existing RRIF back into an RRSP as long as it is then reconverted back to a RRIF before the end of the year in which he or she turns 71 (i.e., either in 2007 or 2008).

Finally, for those who choose not to reconvert their RRIF back to an RRSP, the government announced that it will be waiving the required minimum withdrawals for both this year and next year for RRIF annuitants who turn 70 in 2007 and similarly waiving the minimum withdrawal requirement this year for RRIF annuitants who turn 71 in 2007.

Changes to RESPs

The government has proposed two major changes to the contribution rules for RESPs: the elimination of the \$4,000 annual RESP contribution limit and the increase of the lifetime RESP contribution limit to \$50,000 from \$42,000.

This newfound ability to lump-sum fund an RESP for a child's post-secondary education may outweigh the benefits of collecting the annual Canada Education Savings Grant (CESG), generally equal to 20% per year on eligible contributions.



These CESG rules are also changing. The maximum annual RESP contribution that will qualify for the 20% CESG will be increased to \$2,500 from \$2,000, thereby increasing the maximum annual CESG per beneficiary to \$500 from \$400.

Consequently, if a beneficiary has unused CESGs carried forward from a prior year, by contributing \$5,000 in a particular year to an RESP, a total CESG of \$1,000 would now be available.

Note, however, that the \$7,200 lifetime CESG limit is unaffected by this change.

New Child Tax Credit

Last year's federal budget introduced the Universal Child Care Benefit (UCCB), which provided a payment equal to \$100 per month per child under the age of six.

This year's budget goes a step further in providing tax relief for families with children by introducing a brand new non-refundable child tax credit for parents based on an amount of \$2,000 (indexed annually for inflation) for each child under the age of 18. The tax credit is equal to 15.5% of \$2,000 or up to \$310 per child, effective in 2007.

Generally, either parent may claim the credit and any unused portion of the credit unnecessary to reduce a parent's tax payable to zero can be transferred by that parent to a spouse or common-law partner.

Note that just like the UCCB, the new child tax credit is available to all parents and is not income-tested.

Registered Disability Savings Plan (RDSP)

The government announced a new program to assist families to save for the long-term financial security of children with disabilities, which will be called the

Registered Disability Savings Plan (RDSP), along with a Canada Disability Savings Grant (CDSG) program and Canada Disability Savings Bond (CDSB) program.

The new RDSP will be largely based on the rules governing RESPs and will come into force in 2008.

Any Canadian resident who is either personally eligible for the disability tax credit (DTC) or is a parent or other legal representative of a disabled person will be eligible to establish an RDSP. The beneficiary of the RDSP will be the disabled person who must have a social insurance number in order to open a plan.

Contributions

As with RESPs, although contributions to an RDSP will not be tax deductible, any earnings or growth on such contributions will accrue tax-free. Contributions can also be withdrawn tax-free and only the deferred growth, along with any CDSGs and CDSBs (discussed below), will be included in the disabled beneficiary's income when ultimately withdrawn from the plan.

The lifetime RDSP contribution limit will be \$200,000 and, as is now the case with RESPs, there is no annual contribution limit. In addition, anyone can contribute to the plan up until the end of the year in which the beneficiary turns 59.

CDSGs and CDSBs

To further encourage RDSP contributions, the government will be providing grants, known as CDSGs, at various rates depending on the amounts contributed and the beneficiary's family net income.

Specifically, if the family's net income is below \$74,357, the government will pay a CDSG of 300% on the first \$500 contributed annually and 200% on the next \$1,000 contributed. For families with net income

above \$74,357, the CDSG will be 100% of the first \$1,000 contributed annually.

When the beneficiary is under age 18, the “family net income” will generally be the disabled child’s family. Once the beneficiary turns 18, however, the definition of “family net income” will be the disabled beneficiary and his or her spouse’s or partner’s combined net income.

The government has imposed a limit of \$70,000 on the total amount of CDSGs it will pay on behalf of an RDSP beneficiary. The CDSGs will be paid until the end of the year in which the beneficiary turns 49.

For low and modest income families with disabled beneficiaries under age 50, a new CDSB of up to \$1,000 will be paid annually (up to a lifetime maximum of \$20,000) to the CDSG, regardless of whether or not contributions have been made.

Withdrawals

Payments from an RDSP, which will be subject to an annual maximum withdrawal limit based on the beneficiary’s life expectancy and the fair market value of the plan, must begin once the beneficiary reaches age 60.

Unlike RESPs, contributors will not be entitled to a refund of their contributions. Rather, all RDSP contributions, CDSGs and CDSBs must be used to support the beneficiary.

Eligibility for income-tested benefits

Finally, the budget proposes that any amounts paid out of an RDSP will not be taken into account for the purposes of calculating federal income-tested benefits. It will not reduce Old Age Security nor Employment Insurance benefits.

While provinces and territories also provide income support for disabled persons, it remains to be seen whether the provinces will also commit to not disqualifying an RDSP beneficiary from receiving provincial income support because of the withdrawals under the new program.

Other changes

Donations to private foundations

Last year’s federal budget eliminated capital gains tax on donations of publicly-traded securities, including mutual funds, to registered charities and public foundations.

To encourage additional charitable donations to private foundations, this year’s budget proposes to eliminate capital gains tax on such donations to private foundations as well.

Elementary and secondary school scholarships

The 2006 budget exempted all post-secondary level scholarships and bursaries from tax. This year’s budget goes a step further by fully exempting from taxation scholarships and bursaries provided to students to attend elementary and secondary schools.

Spousal amount

For 2007, the basic personal amount, representing the amount of income that an individual can receive before paying personal tax, is set at \$8,929. The spousal amount that can be claimed in respect of a spouse or common-law partner is currently set at \$7,581 and is reduced on a dollar-for-dollar basis by the dependant’s net income above \$759.

The budget proposes to remove this so-called “marriage penalty” by increasing the spousal or dependent amount to \$8,929, the same level as the basic personal amount, while at the same time eliminating the threshold above which a dependant’s net income must be taken into account.

Based on the personal tax credit rate of 15.5%, this could result in a maximum benefit of an additional \$209 [i.e., $(\$8,929 - \$7,581) \times 15.5\%$].

Capital gains exemption

The budget proposes to increase the lifetime capital gains exemption to \$750,000 from \$500,000 for capital gains realized on the sale of qualifying small business shares and qualifying farm or fishing property.

Increase of instalment threshold

Under the current rules, individuals who receive income not subject to source deductions such as rental income, investment income, capital gains or self-employment income are required to pay quarterly instalments. Currently, instalments are required if your “net tax owing” is greater than \$2,000 (\$1,200 for residents of Quebec) in 2007 and was also greater than \$2,000 (\$1,200) in either 2006 or 2005.

The definition of “net tax owing” is complex but essentially refers to the net federal and provincial tax less income tax withheld at source.

The 2007 budget proposes to increase this threshold to \$3,000 (\$1,800 for Quebec residents), effective for the 2008 and future tax years.

No broad-based capital gains tax relief

Perhaps the biggest disappointment with Budget 2007 was that there was no announcement regarding the elimination (or at least the deferral) of capital gains tax on the reinvestment of proceeds within a six-month period. This was something that the Conservatives had promised during last year’s election campaign, but have so far failed to deliver.

In a similar vein, there was no mention of broad-based income splitting, as some had speculated, nor was there any update on the status of the “draconian” interest deductibility rules, originally proposed in 2003, but still in draft form.

For more information about this topic, contact your advisor,
call us at **1.800.874.6275** or visit our website at **www.aimtrimark.com**.

The information provided is general in nature and is provided with the understanding that it may not be relied upon as, nor considered to be, the rendering of tax, legal, accounting or professional advice. Readers should consult with their own accountants and/or lawyers for advice on the specific circumstances before taking any action. Commissions, trailing commissions, management fees and expenses may all be associated with mutual fund investments. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated. Please read the prospectus before investing. Copies are available from your financial advisor or from AIM Trimark Investments.

† AIM, the chevron logo and all associated trademarks are trademarks of A I M Management Group Inc., used under licence.

* Knowing Pays, TRIMARK and all associated trademarks are trademarks of AIM Funds Management Inc.

© AIM Funds Management Inc., 2007

TEFDBAE(03/07)

Knowing Pays:  **AIM TRIMARK[†]**

5140 Yonge Street, Suite 900, Toronto, Ontario M2N 6X7 • Telephone: 416.590.9855 or 1.800.874.6275
Facsimile: 416.590.9868 or 1.800.631.7008 • inquiries@aimtrimark.com **www.aimtrimark.com**