

Providing fiscal stability to foster growth and investment: 2014–2015 federal budget highlights

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The big picture

The 2014 federal budget stays the course to achieve a balanced budget by 2015–2016. With continued political and economic uncertainty in the U.S., Europe and emerging markets, a fiscal policy directed towards stability and prudence should help support investors' confidence in the Canadian capital markets.

The budget projects a \$6.4 billion surplus in 2015–2016, higher than the \$3.7 billion forecast in the November 2013 Fiscal Update. It is expected there will be an \$8–10 billion budget surplus each year through 2018–2019. The federal debt-to-GDP ratio is projected to fall to 27.0% in 2017–2018; this is below pre-recession levels and on the path to the government's target ratio of 25% in 2021. The projected deficit and debt trends will continue to place Canada at the forefront of fiscal prudence among developed countries, helping to insulate Canada against potential external economic shocks in the future, while providing a more predictable economic environment that attracts and fosters investment.

New tax rules

While there were no major tax announcements in this budget, there were a number of proposals put forth to enhance the fairness, integrity and neutrality of the tax system. These proposals include the following:

- **Elimination of graduated rate taxation of trusts and estates** – The use of graduated rates on trusts created by will (and certain grandfathered inter-vivos trusts) is eliminated to prevent the multiple uses of graduated rates. Instead, flat top-rate taxation will apply, with two exceptions: 1) the graduated rates will apply for the first 36 months after death; and 2) certain testamentary trusts set up for the benefit of disabled persons (e.g., Henson Trusts) will continue to benefit from graduated rate taxation.
- **Non-resident trusts** – Until now, new residents to Canada were able to benefit from the use of non-resident trusts to shelter income from Canadian tax for up to 60 months. New rules eliminate this exemption.
- **Foreign Account Tax Compliance Act (FATCA)** – An intergovernmental agreement was signed on February 5, 2014, to implement FATCA. The budget provides an update on the exchange of tax information between Canada and the U.S. Fidelity encourages clients to seek the advice of their financial advisor or tax advisor to better understand how FATCA affects them.

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Retirement discussion and continued pension reform: More to come

While retirement wasn't the focus of this budget, the national discussion of retirement savings vehicles and retirement income is not over. The next round of this discussion may occur in this year's Ontario budget, which could contain details of a proposed supplementary pension plan, and may well continue in next year's federal budget. As well, the government continues to redress private sector funding and public sector pension issues. Implicit in these changes is the call to all Canadians to take additional responsibility for their retirement income.

- **Targeted initiative for older workers:** The renewal is for a three-year period and is intended to encourage labour market participation by older workers. Working in retirement is becoming increasingly prevalent as both a source of income and a source of social satisfaction.
- **Extending changes to the pension transfer limits:** The government has extended and refined previous changes to pension transfer limits, allowing a larger tax-free transfer to an RRSP from a RPP where the contribution is from a lump-sum payout from a defined benefit pension plan that has been reduced due to plan underfunding.
- **Crown corporation pensions:** The budget continues the initiative to align Crown corporations' pension plans with the public service pension plan. Specifically, it plans to implement a 50:50 employer/employee cost-sharing model and raise the retirement age for new hires, as well as the age other retirement benefits are available, to 65.
- **Go Canada! Amateur athlete trusts:** With the winter Olympics underway, the budget proposes to allow income contributed to an amateur athlete trust to qualify as earned income for the purpose of determining an athlete's annual RRSP contribution limit.

Encouraging competitive financial services

The budget proposed a number of measures intended to reinforce stability and encourage greater competition in financial services.

- **National regulator:** The budget renewed the government's commitment to forming a national securities regulator and to wait for further commitment from all provinces. To date, only British Columbia and Ontario have signed on.
- **Small banks:** The government will improve the ability of smaller banks to access funding from Canada Mortgage and Housing Corporation (CMHC).
- **Credit unions:** The government will support provincial credit unions that wish to move to the federal credit union framework by streamlining the process for amalgamations. This will enable credit unions to better compete and broaden choices for consumers by providing their financial services across Canada.

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Other measures

- **Immigrant Investor Program:** Previously, the program provided a pathway to Canadian citizenship in exchange for significant investments in Canada. The government has officially ended the program and will be introducing a new pilot project, with more details coming at a later date.
- **Over-the-counter derivatives and financial benchmark regulation:** The government proposes to amend the Bank Act to create an explicit regulation-making authority for banks regarding over-the-counter derivatives and to provide a regulation-making authority that would apply to Canadian banks in their submissions to financial benchmarks.
- **Cross-border price discrimination:** The budget proposes to address the gap in consumer prices between Canada and other countries through legislation addressing market power, which will be enforced by the Competition Bureau.
- **Telecommunications:** The government will cap wholesale domestic wireless roaming rates until the CRTC makes a decision on roaming rates.

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