Canadian 2016 Budget Earmarks Millions to Boost Tax Authority

By

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The Canada Revenue Agency is set to receive millions in funding over the next five years to boost its efforts to crack down on tax evasion and avoidance, as well as increase tax collections, according to the Liberal Party government's first federal budget.

Under Canada's 2016 budget plan, released on March 22, the government proposes investing C $444.4 million over the next five years to help the CRA address tax evasion and aggressive tax avoidance by individuals and businesses. The money would be used to hire extra specialists and auditors, increase verification activities, develop stronger business intelligence, and improve the quality of criminal tax evasion investigations, according to the plan.

"As the CRA has a proven track record of meeting expectations from targeted compliance interventions, Budget 2016 accounts for the expected revenue impact of C $2.6 billion over five years from these measures," the budget plan says.

Noting that the CRA's success in addressing tax evasion and aggressive tax planning would be diminished if it can't collect assessed revenue, the government also announced a proposal to give the CRA $351.6 million over five years to increase its ability to collect outstanding tax owed. "This strategy will complement existing efforts to encourage earlier payment of outstanding tax liabilities and work with those who cannot pay the full amount when due," the budget plan says.

The announcement drew a positive reaction from the tax community, including Canadians for Tax Fairness, which had recommended that the government invest C $50 million a year in the CRA. The budget announcement works out to about C $90 million a year, exceeding the organization's expectations, according to Executive Director Dennis Howlett.

However, there is concern about whether the CRA will be able to use all that money, according to Howlett. "It will take them a little while to ramp up," he told Tax Analysts. "What's really needed is highly skilled auditors who can deal with complex cases, and that's going to require training -- you're not going to find many off the street."

Howlett also called for more investment in the Canadian Department of Justice, which is severely understaffed to take on tax cases. Too often, big-time tax cheats have gotten off lightly, with many cases being settled out of court, he said. The government "needs a comprehensive approach" in addressing tax evasion and avoidance, Howlett added.

The CRA certainly needs more money to carry out its mandate on the front lines, according to Kim Moody of Moodys Gartner Tax Law LLP. "It's so obvious they need help," he told Tax

Analysts.

Moody noted that the previous Conservative government had cut the funding for many departments, including that of the CRA, over the past few budgets. The Liberal government's reversal of those cuts "makes good sense, but it's also very politically driven," Moody said, adding that many elements of the Liberal 2016 budget appeared to fly in the face of the former Conservative government.

For example, under the 2016 budget, the government said it would not proceed with a measure announced in the 2015 budget under the Conservative government. That measure would have provided a capital gains tax exemption for some dispositions of real estate or private corporation shares, when cash proceeds from the disposition are donated to a charity or qualified donation recipient within 30 days.

A lot of work had been done to move that proposal forward, and Canada's Joint Committee on Taxation, an influential advisory body that comments on draft tax legislation, had led the submission of the proposal, according to Moody. "All of a sudden, the government announced they're scrapping the whole thing," he said.

In general, Canada has a generous philanthropic taxation regime, which offers a capital gains tax exemption on direct donations of publicly traded stocks to charities. The 2015 budget proposal, which was the "brainchild" of the Conservative government, would have been parallel to that regime, Moody said. "For them to take it away like that so quickly smacks of politics to me," he said, adding that there is open hostility between the current and previous governments.

Moody also pointed to the 2016 budget's proposal to reverse the previous government's decision to change the Old Age Security (OAS) Act to increase the eligibility age from 65 to 67. Adjusting the OAS eligibility age "makes zero economic sense," but it was unpopular under the previous regime, according to Moody. That change, along with such proposed measures as a new Canada child benefit and an income-splitting credit for couples with at least one child under age 18, is "poking the eyes of the previous regime," he said.

Other Measures

While the budget in general was not a huge deal, according to Moody, there were still some surprises. For example, Canadian practitioners had expected major changes to the taxation of stock option benefits, which was part of the Liberal Party's election platform. Under the current regime, eligible employees effectively paid tax on just half of the economic benefits realized when their stock options are exercised -- a situation that the Liberal Party railed against as being unfair. However, the government didn't propose any changes to address the issue, which left many practitioners scratching their heads, Moody said.
The lack of follow-through on stock option benefit taxation came as a disappointment to Howlett, who noted that both the federal and provincial governments lose a collective C $1 billion a year under the current regime. "They caved to lobbying from the high-tech sector," Howlett said.

Another interesting turn was that the government proposed only minor changes to address the issue of wealthy individuals using private corporations, something that the Liberal government had criticized in the past as an inappropriate tax avoidance strategy, according to Moody. "So we were waiting to see what changes they would make, but the changes were pretty minor in the whole scheme of things," Moody said.

For example, the 2016 budget proposes amending the taxation regime for Canadian-controlled private corporations (CCPCs) to prevent the multiplication of the small business deduction. The proposed changes include "extending specific partnership income rules to partnership structures in which a CCPC provides . . . services or property to a partnership during a [tax] year of the CCPC where, at any time during the year, the CCPC or a shareholder of the CCPC is a member of the partnership or does not deal at arm's length with a member of the partnership," according to the budget plan.

Also under the 2016 budget is a proposal to keep the small business tax rate at 10.5 percent after 2016. Under the previous government, the small business tax rate was supposed to gradually decrease from 11 percent in 2015 to 9 percent in 2019. (Prior coverage.)

Howlett welcomed the proposal, saying that while it's fine for small businesses to have some preferential rates to stay competitive with bigger businesses, having too big a gap between the small business tax rate and the regular business tax rate creates a disincentive for growth.

Moreover, in line with its election platform, the Liberal government will move ahead with its plans to create a tax bracket of 33 percent on individual incomes exceeding C $200,000. Consequential amendments in the 2016 budget include the provision of a 33 percent charitable donation tax credit on donations exceeding C $200 to trusts subject to the 33 percent rate on all their taxable income and the application of the new tax bracket rate on excess employee profit-sharing plan contributions. (Prior coverage.)

The budget also provides for several international tax measures to implement the OECD's final base erosion and profit-shifting project recommendations. Those include a proposal to undertake the spontaneous exchange of tax rulings with partner countries starting in 2016 and plans to introduce country-by-country reporting legislation allowing Canada to start its first exchanges with partner jurisdictions starting in 2018. (Prior coverage.)