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AMT Overhaul: A Guide to the New Alternative Minimum Tax Rules

Written by: Nav Pannu, CPA

The 2023 federal budget announced significant changes to the Alternative Minimum Tax (AMT) regime to target high-income individuals better. On August 4, 2023, the Department of Finance released draft legislative proposals to modify the AMT regime, effective for taxation years beginning after 2023. The proposed changes would be the most extensive reforms to the AMT regime since it was introduced in 1986.

Today, we find ourselves grappling with this new set of AMT rules, which have unique nuances and implications for taxpayers. Familiarizing yourself with these changes is essential to making informed financial decisions, so we've compiled the following comprehensive guide to help you understand how it'll affect your tax situation going forward.

Understanding the Alternative Minimum Tax (AMT)
AMT is an alternative method of calculating your taxes payable each year to impose a minimum level of tax for both individuals and trusts. It's applicable in taxation years where you may have relied on certain tax exemptions and deductions to reduce your ordinary taxes payable meaningfully. AMT will be calculated in parallel with ordinary income taxes, and if the calculation under AMT is higher, you'll be required to pay AMT.

The New AMT Rules
Key changes to the AMT rules for taxation years after 2023 are as follows:

- **The AMT rate:** AMT currently calculates tax on adjusted taxable income (ATI) at a rate of 15%. This will now increase to 20.5%.
- **The AMT exemption:** This exemption is the amount of your ATI on which AMT will not apply. The current exemption is $40,000, increasing to $173,000 in 2024 (indexed annually).
- **Capital gains and losses:** Under the current AMT regime, the inclusion rate for the purpose of computing ATI is 80% for capital gains, capital losses and business investment losses (as compared to a 50% inclusion rate for computing ordinary taxable income). Under the new rules, the inclusion rate for the purpose of computing ATI will be 100% for capital gains, and 50% for capital losses and business investment losses.
- **Deductions:** Certain deductions such as employment expenses, moving expenses, childcare expenses, interest and carrying charges incurred to earn income from property and non-capital loss carryovers are 100% deductible under the current AMT rules. The new rules will limit the deduction to 50% for the purpose of computing ATI.
- **Non-refundable credits:** Non-refundable tax credits[1] reduce taxes payable but will not generate a refund beyond NIL taxes payable. Except for the dividend tax credit, these credits will be reduced to 50% under the new AMT rules.
- **Lifetime capital gains exemption (LCGE):** The LCGE shelters up to $971,190 (indexed for 2023) of a capital gain from the disposition of Qualified Small Business Corporation (QSBC) shares or Qualified Farm or Fishing Property from ordinary income tax. Under both the old and new AMT rules, the portion of a gain from the disposition of QSBC shares that is eligible for the LCGE is included in ATI at 30%. The AMT rate and AMT exemption under the new rules have changed, but the income inclusion percentage remains the same. Additionally, any portion of the gain that is not eligible for the LCGE is subject to the new 100% inclusion rate.

- **Donation of publicly listed securities:** Under the current rules, there is a zero-inclusion rate for capital gains realized on in-kind donations of publicly traded securities. Under the new rules, the inclusion rate will be 30%.
- **Employee Stock Options:** Stock option benefits are generally included as employment income. If the options qualify, the income inclusion may be reduced to 50% for ordinary taxes payable. The income inclusion under the current AMT rules is 80%, which will increase to 100% under the new AMT rules.

Impact to Trusts

The new AMT rules also extend to trusts. As it was before, the new AMT rules will not apply to certain trusts, such as mutual fund trusts and employee life/health trusts. In addition, the new rules will not apply to graduated-rate estates. Additionally, the new rules will allow qualified disability trusts to apply the basic exemption ($173,000 indexed for 2024) to their AMT calculation; however, no other trusts will have access to the exemption.

The limitation on certain deductions when computing ATI could cause some trusts to be subject to AMT. Generally, a trust that allocates all of its net income for the year to its beneficiaries will have no taxable income for the year, and thus no ordinary income tax payable. If the trust deducted interest incurred to earn income from property when computing its net income under ordinary rules, it has to include 50% of the interest deducted in its ATI and, therefore will be subject to AMT on that amount.

Tax Credit for AMT previously paid

AMT paid in a particular tax year may be claimed as a tax credit against ordinary income tax payable in any of the next seven taxation years, but only to the extent that ordinary income tax payable in a particular future tax year exceeds AMT payable for that future tax year. If the taxpayer has limited income in those next seven taxation years, they might not be able to use the AMT tax credit fully.

Effects on the average taxpayer and trust

The new AMT rules appear to better target high-income earners who would otherwise receive preferential tax rates through credits, deductions, and exemptions. However, in many instances, the new AMT rules will negatively affect all taxpayers regardless of income level.

For example, consider if your family relies on the sale of investments or properties as a retirement income. A large capital gain in a single year may trigger AMT under the new rules, and you may not have enough ordinary income tax payable in future years to fully utilize the tax credit for AMT paid in a prior year. This may mean that you could significantly impact your cash flow for retirement.

Additionally, the new rules will negatively impact the popular inter-vivos family trusts, which will suffer from the expanded tax limitations without having access to the increased AMT exemption amount as an offset. This will mean that many trusts will likely pay more tax, not just high-income earners' family trusts.

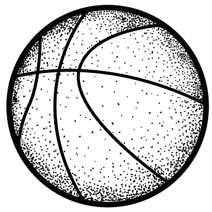
The bottom line

The new AMT rules represent a sizeable change in the Canadian tax landscape, and their effects will be far-reaching. To ensure you're up to date on how these changes will impact your situation, contact your CPA. They'll walk you through if and how these rules will apply to you and ensure you're well-positioned to their implementation.

[1] e.g., the basic personal amount, the spousal amount, the age amount, donations, medical expenses, etc.

Written by: Nav Pannu, CPA

Luxury Tax in Sports



Written by: Jonathan Couse

Effective September 1, 2022, the Canadian government implemented a luxury tax on the sale or import of specific vehicles, aircraft, and vessels. This luxury tax system bears similarities to those found in major North American sports leagues.

In the realm of professional sports, the luxury tax system is established through negotiations between the player's association and team owners, enshrined in each league's Collective Bargaining Agreement (CBA). Its primary aim is to curb excessive team spending and promote competitive balance. While akin to Canada's luxury tax, the sports version is notably more intricate, obliging owners to consider various factors when striving to assemble a championship-level team.

For instance, the National Basketball Association (NBA) sets a luxury tax threshold, which represents the predetermined limit of team salary expenditure beyond which teams become subject to the luxury tax. This threshold fluctuates annually based on league revenues. In the 2023-2024 season, the salary cap maximum is $136 million USD, with a luxury tax threshold of $165 million USD.[1] The NBA operates with a “soft” cap, permitting teams to surpass the salary cap maximum through various means, such as retaining their own players through Bird rights and various contract exceptions. The NBA's luxury tax system employs tiered rates, similar to Canada's income tax system. Additionally, it incorporates higher rates for repeater teams, defined as those that have paid the luxury tax in at least three of the previous four seasons.

For the current 2023-2024 season, the Golden State Warriors are expected to incur a[2] substantial luxury tax bill of $188 million USD in addition to their $207 million payroll. The system primarily targets wealthy owners and teams that can, or sometimes, choose to outspend others. To promote parity, teams that fall below the luxury tax threshold share half of the total tax penalty, which amounted to $15 million USD in the 2022-2023 season.

In contrast, Major League Baseball (MLB) doesn’t have a salary cap, but it implements a Competitive Balance Tax (CBT), functioning similarly to the NBA's luxury tax. The CBT tax rate increases for each consecutive year a team exceeds the threshold. In addition to financial penalties, teams surpassing the CBT threshold risk losing draft picks and international signing money, which can impede their ability to develop through young talent.

The implementation of a luxury tax is often advocated as a means to enhance competitive balance. Nevertheless, some contend that the National Hockey League (NHL) and the National Football League (NFL) are the two major North American leagues with the greatest competitive balance, and they employ a "hard" salary cap, preventing teams from surpassing a predetermined threshold on player salaries. This remains a topic of ongoing debate.

[1] https://www.spotrac.com/nba/tax/
[2] https://www.spotrac.com/nba/tax/

Written by: Jonathan Couse, CPA

Teleworking Policy: What You Need to Know

Written by: Natalie Beaudoin

What was uncommon before the pandemic, teleworking, is finally being integrated into the reality of many employees and employers. In recent years, several companies have resorted to teleworking when health restrictions made it necessary. In contrast, others have fully adopted it and could no longer do without this method of organizing work. While hybrid working is prevalent, some companies still need to adopt a clear policy regarding teleworking.

At a time when there is a labor shortage, teleworking is an advantage that allows you to attract and retain staff by giving, among other things, the opportunity to recruit employees at a greater distance from the usual workplace, offering a more flexible work schedule.

However, teleworking is not all positive. In particular, work accidents occurring at home have been recognized as work accidents (reference: Air Canada and Gentile-Patti, 2021 QCTAT 5829). In addition, the compulsory use of information technology has raised issues concerning the security and protection of personal and confidential data. Employees have also abused the situation at the company's expense by not providing the expected work performance.

What is the law, and what are the rules on teleworking?

There is no law specifically for teleworking in Quebec, but in 2021, a provision on teleworking was added to the Occupational Health and Safety Act:

"*Subject to any irreconcilable provision, in particular about the place of work, the provisions of this law apply to the worker who carries out teleworking and to his employer.*"

Please consider regulating teleworking within the law's guidelines.

Why do you need a teleworking policy?

Having a policy in place will help avoid the potential abuses of teleworking. It will enable you to oversee activities for teleworkers and remind remote or hybrid employees of the company policies and procedures that apply to people working from locations other than the company office. Details about the purpose of the teleworking policy can be listed under objectives. The policy will also be a tool to ensure you comply with the labor standards, pay equity, and occupational health and safety guidelines per CNESST.

Sometimes, teleworking may only affect a few employees in your organization. Still, regardless of the number of people, it's essential to provide some guidelines about remote working, which can be added to your teleworking policy.

Examples of topics to cover in the teleworking policy are:

- Policy objectives
- Scope of the policy
- Employees covered
- Policy framework and authorizations
- Teleworking code of conduct/ethics
- Communication and supervision
- Reminder of the rules, policies, and procedures that remain applicable (including those relating to OHS)
- Work schedule and overtime
- Workplaces
- Workspace and ergonomics
- Privacy and data protection
- Use of computer equipment
- Costs related to the purchase of equipment
- Consumption of drugs, alcohol and medication

What are the types of teleworking?
As an employer, you can use teleworking differently and include guidelines based on what's relevant to how your company structures it. The hybrid working model is quite common, consisting of an employee working approximately 50% remotely and 50% in-person at the workplace. Teleworking can, therefore, be full or part-time.

Some companies establish a quantity of remote hours for their employees, like a bank of hours they can choose when to use. In this setup, the employer ensures that their employees are on-site a certain percentage of the time. Other companies set specific days that employees must be in the office to bring employees together and foster collaboration.

The location where teleworking takes place can also vary. For example, employees can work from home, from another public place, or from another country. In this context, the form(s) selected by an employer will depend on the reality of a company by considering, among other things, the nature of the work, opening hours, confidentiality, and data protection. No policy is better than another; you'll need to find what works best for your company, set a clear policy framework, and specify the objectives.

What are the arguments in favor of teleworking?
- Greater flexibility in working hours
- A demonstration of trust in your employees
- Increased productivity
- Better work-family balance
- Avoid delays or absences
- Reduction of expenses

We want to remind you that we offer services to help you revise or write your employee handbooks for your internal HR and OHS procedures or policies!
You can also use our services as a bank of hours.

Written by: Natalie Beaudoin

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