

Tax Alert – Canada



Federal budget redux: a modest fine-tuning of the original

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As widely speculated, federal Finance Minister Jim Flaherty today reintroduced the budget tax measures that he tabled in the House of Commons just over two months ago. We have compared the two documents and confirm that there are no substantive revisions to the March budget tax proposals. All measures are effective as of 22 March 2011, the original budget date, unless otherwise noted.

The minister noted that at his meeting with Canada's leading private-sector economists on 31 May, they confirmed the government's economic planning assumptions remain on track. Based on the latest revenue and expense estimates, the fiscal 2010–11 deficit is projected to be \$36.2 billion, which is lower than the 22 March estimate of \$40.5 billion, largely due to lower program spending.

The only significant new measures in the second iteration are the setting aside of \$2.2 billion in compensation for Quebec for sales tax harmonization, subject to the conclusion of a satisfactory agreement, and the four-year phase-out of the per-vote subsidy to political parties.

Following are the highlights of the measures announced in the original 2011–12 budget. For further details, see our [Tax Alert 2011 Issue No. 11](#), our related [economic analysis](#) and our archived [webcast](#).

Business income tax measures

- ▶ **Corporate tax rates** – reaffirmed enacted general corporate rate reductions to 16.5% in 2011 and 15% in 2012.
- ▶ **Manufacturing and processing equipment (Class 29)** – extended for eligible assets acquired in 2012 and 2013.
- ▶ **Clean energy generation equipment (Class 43.2)** – expanded to include energy generated from waste heat sources such as industrial processes.
- ▶ **Intangible capital expenses in oilsands projects** – more closely aligned with the treatment of like expenditures in the conventional oil and gas sector.
- ▶ **Stop-loss rules on the redemption of a share** – extended to certain transactions that were not previously caught by the existing stop-loss rules.

Corporate tax deferral using partnerships

The budget includes extensive proposals to eliminate the corporate tax-deferral/absolute tax savings advantages where the partnership's fiscal period did not coincide with the corporation's tax year end. It's estimated that elimination of this deferral would increase government revenues by \$2.85 billion over the next five fiscal years.

There are relieving provisions that will permit corporate partners to spread over a five-year period the one-time tax cost of reporting the deferred income.

Tax relief for individuals and families

- ▶ **Personal tax rates confirmed**, no personal tax rate changes.
- ▶ **New tax credits** effective 2011 for Children's Arts Tax Credit and Volunteer Firefighter Tax Credit.
- ▶ **Enhancements to existing tax credits** effective 2011 for Medical Expense, and Child and Tuition Tax Credits, and effective 2012 for Family Caregiver Tax Credit.
- ▶ **Mineral Exploration Tax Credit** extended to flow-through share agreements entered into on or before 31 March 2012.

Other personal measures

- ▶ **Tax on split income ("kiddie tax")** – extended to apply to capital gains realized by or included in the income of a minor from the disposition of shares to a person who does not deal at arm's length with the minor, if taxable dividends on those shares would have been subject to kiddie tax.
- ▶ **Tax assistance for study abroad** – reduction in minimum course duration from 13 to three consecutive weeks. Applies to tuition, education and textbook tax credits and educational assistance payments from a registered education savings plan (RESP).

Changes for registered plans

- ▶ **Registered disability savings plan (RDSP)** – a beneficiary with a life expectancy of five years or less is permitted to withdraw up to \$10,000 in taxable amounts annually from their RDSP without triggering the repayment of any Canada Disability Savings Grants (CDSGs) and Canada Disability Savings Bonds (CDSBs) received by the RDSP in the preceding 10 years.

- ▶ **Registered education savings plan (RESP)** – amendments to provide flexibility of a family plan to individual plans for siblings.
- ▶ **Registered retirement savings plan (RRSP)** – introduction of a number of anti-avoidance rules that currently apply to tax-free savings accounts (TFSA's).
- ▶ **Individual pension plan (IPP)** – new rules regarding annual minimum withdrawals once the beneficiary reaches the age of 72, and restrictions on past service contributions.

Charities

- ▶ **Donation of publicly listed flow-through shares** – the tax-exempt portion of the capital gain arising at the time of the donation to be limited to generally the amount by which the cumulative capital gain exceeds the original cost of the flow-through shares.
- ▶ **Public information reporting and other regulatory requirements** – extended to organizations that may issue donation receipts without being registered charities (e.g., municipalities, registered Canadian amateur athletic associations), to combat fraud and abuse and ensure compliance with respect to charitable donations.
- ▶ **Refusal or revocation of charitable registration** – at the minister's discretion if a representative of a charity has been found guilty of criminal offences involving financial dishonesty, or was involved with other non-compliant entities for which registration has been revoked within the last five years.

Sales and excise taxes

- ▶ **Customs tariff simplification** – to include reduction in the number of tariff items and the elimination of many tariff items with "end use" provisions.

Previously announced measures

The government confirmed its intention to reintroduce a number of previously announced corporate measures. At the earliest, these measures will be tabled in House of Commons this fall. However, the Department of Finance may release draft legislation for public consultation during the summer.

Outstanding corporate measures include:

- ▶ **Response to Federal Court of Appeal decisions**, released 16 March 2011 concerning the deductibility of contingent amounts, withholding tax applicable to interest payments made to non-residents, and the tax treatment of a life insurance corporation's reserves in respect of its segregated fund policies.
- ▶ **GST/HST provisions for investment plans and pensions** dated 28 January 2011.
- ▶ **Revised real estate investment trust (REIT) rules** dated 16 December 2010.
- ▶ **Outstanding March 2010 federal budget legislation**, including 27 August 2010 draft legislative proposals in respect of foreign affiliates, foreign tax credit generators, income trust rules, foreign investment entity (FIE) and non-resident trust (NRT) provisions, and aggressive tax planning.
- ▶ **Outstanding technical amendments**, including draft legislative proposals released 16 July 2010.
- ▶ **Foreign affiliates**, including those announced on 27 February 2004 and 18 December 2009, which were not included in other legislative proposals.

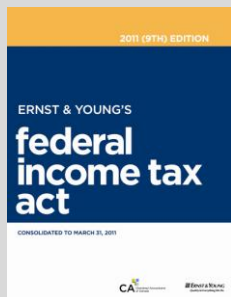
Consultation papers

- ▶ **Federal support for business research and development** announced 21 December 2010. Read more in our [Tax Alert 2011 Issue No. 01](#).
- ▶ **Taxation of corporate groups**, including 23 November 2010 consultation paper. Read more in our [Tax Alert 2010 Issue No. 40](#).

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