Editorial Comment on Notice of Ways and Means Motion Resolutions and Supplementary Budget Information

Notice of Ways and Means Motion to Amend the *Income Tax Act*

That it is expedient to amend the *Income Tax Act* to provide among other things:

Resolution 1: Basic Personal Amount

(1) That, for the 2009 taxation year, the basic personal amount, the spouse or common law partner amount, and the eligible dependant amount be increased to $10,320 and be indexed to inflation for subsequent taxation years.

CCH Editorial Comment: Resolution 1 proposes that the basic personal amount, the spouse and common-law partner amount, and the eligible dependant amount be increased to $10,320 for the 2009 taxation year (up from $9,600 in 2008). Normal indexation will apply to this amount for 2010 and subsequent taxation years.

Resolution 2: Personal Income Tax Rates

(2) That, for the 2009 and subsequent taxation years, subsection 117(2) of the Act be replaced by the following:

(2) The tax payable under this Part by an individual on the individual's taxable income or taxable income earned in Canada, as the case may be (in this subdivision referred to as the "amount taxable") for a taxation year is

(*a*) 15% of the amount taxable, if the amount taxable is equal to or less than $40,726;

(*b*) if the amount taxable is greater than $40,726 and is equal to or less than $81,452, the maximum amount determinable in respect of the taxation year under paragraph (*a*), plus 22% of the amount by which the amount taxable exceeds $40,726;

(*c*) if the amount taxable is greater than $81,452, but is equal to or less than $126,264, the maximum amount determinable in respect of the taxation year under paragraph (*b*), plus 26% of the amount by which the amount taxable exceeds $81,452; and

(*d*) if the amount taxable is greater than $126,264, the maximum amount determinable in respect of the taxation year under paragraph (*c*), plus 29% of the amount by which the amount taxable exceeds $126,264.

CCH Editorial Comment: Resolution 2 proposes the following changes to the two lowest personal income tax brackets, as of the 2009 taxation year:

- an increase in the upper limit of the lowest personal income tax bracket (subject to an income tax rate of 15%) to $40,726 (up from $37,885 in 2008); and
- an increase in the upper limit of the middle income tax bracket (subject to an income tax rate of 22%) to $81,452 (up from $75,769 in 2008).

Normal indexation will apply to these amounts for 2010 and subsequent taxation years.

Resolution 3: Age Credit

(3) That, for the 2009 and subsequent taxation years, the formula in subsection 118(2) of the Act be replaced by the following:

$$A \times (\$6,408 - B)$$

CCH Editorial Comment: Currently, an individual who is 65 years of age or older in the taxation year may claim the Age Credit. The amount of this credit is reduced by 15% of net income over a certain threshold.

Resolution 3 proposes to increase the amount on which the Age Credit is based by $1,000 to $6,408 for the 2009 taxation year. This amount will be indexed for 2010 and subsequent taxation years.

The Budget also announced that the net income threshold at which the credit begins to be phased out will remain at $32,312. Thus, for the 2009 taxation year, the income level at which the Age Credit is fully phased out rises to $75,032.

Resolution 4: Home Renovation Tax Credit

(4) That the Act be modified consequential on the introduction of the Home Renovations Tax Credit in accordance with proposals described in the budget documents tabled by the Minister of Finance in the House of Commons on January 27, 2009.

CCH Editorial Comment: One of the pre-budget ideas floated by the Minister of Finance was a tax credit for individual taxpayers who renovate their homes. Quebec's recent announcement of a similar tax credit seemed to support the possibility that the Federal Budget would contain this type of measure in order to help stimulate the economy.

Those predictors turned out to be accurate, as the Budget includes a temporary Home Renovation Tax Credit (HRTC) which permits individuals to claim a 15% non-refundable tax credit for eligible expenditures made in respect of eligible dwellings. The maximum credit is $1,350 and will apply to expenditures that are greater than $1,000, but do not exceed $10,000.

The restrictions applicable to claiming the HRTC are very specific. First, the HRTC will only apply for expenditures for work performed, or goods acquired, after January 27, 2009 and before February 1, 2010. However, the HRTC may not be claimed in respect of work performed or expenditures incurred under a contract that was entered into before January 28, 2009. The HRTC will be available to be claimed only in an individual's 2009 tax return.

Secondly, the HRTC is limited to one per family. This means that family members will be subject to a single limit based on their pooled expenditures. A family is considered to include an individual, the individual's spouse or common-law partner and children who are under 18 years of age. To the extent that an individual is unable to utilize the entire HRTC, the unused portion may be used by other family members. Where two or more families share ownership of an eligible dwelling, each family will be entitled to claim its own HRTC, as if the family owned the dwelling alone.

Thirdly, in order to claim the HRTC, the dwelling must be eligible to be a principal residence (within the meaning of section 54 the Act) of the individual or of one or more of the individual's other family members. For condominiums and co-operative housing corporations, an individual's share of eligible expenditures incurred in respect of common areas will also qualify for the HRTC. Where an individual earns business or rental income from part of his or her principal residence, expenditures that relate to common areas or that benefit the housing unit as a whole will qualify as eligible expenditures for HRTC purposes, subject to limits established under existing CRA administrative practices which apply when determining how

business or rental income and expenditures are allocated between personal use and income-earning use.

Fourthly, the types of expenditures that will qualify for HRTCs will be subject to a variety of restrictions. Eligible expenditures must be incurred in relation to renovations or alterations of an eligible dwelling that are of an enduring nature and are integral to the eligible dwelling. This test would exclude expenditures for routine repairs and maintenance. Furthermore, financing costs of a renovation are specifically excluded. Eligible expenditures include building materials, fixtures, equipment rentals, permits, labour and professional services.

The Budget documents indicate that a taxpayer's entitlements to a HRTC will not be affected by other tax credits, grants or other programs including the medical expense tax credit program. Finally, the Budget briefly describes taxpayer compliance issues relating to the HRTC. To support a taxpayer's claims for HRTCs, eligible expenditures must be supported by receipts and expenditures will not be eligible in circumstances where goods or services are provided by a person not dealing at arm's length with the individual unless that person is registered for GST/HST purposes.

Resolution 5: Home Buyers' Plan — Increased Withdrawal Limit

(5) That, for the 2009 and subsequent calendar years, in respect of withdrawals made after January 27, 2009, the Home Buyers' Plan limits described in paragraph (*h*) of the definition "regular eligible amount", and in paragraph (*g*) of the definition "supplemental eligible amount", in subsection 146.01(1) of the Act be increased to $25,000.

CCH Editorial Comment: In the 1992 federal Budget, the Home Buyers' Plan (the "HBP") (set out in section 146.01) was introduced to allow a first-time home buyer to withdraw $20,000 from an RRSP on a tax-free basis if such amount was used to acquire a qualifying home. The scope of the HBP was subsequently amended to allow a participant an additional tax-free withdrawal if such amount was used to acquire a home for a disabled individual related to the participant.

Withdrawn amounts must be repaid to the RRSP by the participant within a 15 year period, subject to minimum annual repayments. To the extent a required repayment is not made, such amount is included in the participant's income for the year.

Continuing on the theme of this Budget to boost the economy by way of the housing market, it is proposed to increase the amount that can be withdrawn by a participant for these purposes from $20,000 to $25,000. The requirements to repay withdrawn amounts remain unchanged.

Resolution 6: First-Time Home Buyer's Tax Credit

(6) That the Act be modified consequential on the introduction of the First-Time Home Buyer's Tax Credit in accordance with proposals described in the budget documents tabled by the Minister of Finance in the House of Commons on January 27, 2009.

CCH Editorial Comment: The final of three budget measures designed to stimulate the economy through the housing market is the First-Time Home Buyers' Tax Credit (the "FTHBC") The FTHBC is a new non-refundable tax credit based on an amount of $5,000 and will be available to first-time home buyers who complete a purchase of a home after January 27, 2009. The FTHBC will be calculated by reference to the lowest personal income tax rate for the year and can be claimed for the taxation year in which the home is acquired.

An individual will be considered a first-time home buyer if neither the individual nor the individual's spouse or common-law partner owned and lived in another home in the calendar year of the home purchase or in any of the four preceding calendar years. A qualifying home is

one that is currently eligible for the Home Buyers' Plan that the individual or individual's spouse or common-law partner intends to occupy as the principal place of residence not later than one year after its acquisition. It is interesting to compare this with the Ontario land transfer tax refund for first-time home buyers, which contains notable differences. For instance, to quality for the Ontario land transfer tax refund for first-time home buyers, the purchaser cannot have previously owned a home, or had any ownership interest in a home, anywhere in the world, at any time. Therefore, a person who qualifies for the FTHBC may not qualify for the Ontario land transfer tax refund for first-time home buyers.

The FTHBC will also be available with respect to purchases made for the benefit of individuals entitled to the disability tax credit (a "DTC eligible person"), if the purchase was made to enable the DTC eligible person to live in a home better suited to his or her personal needs. In order to claim the FTHBC, the home must be intended to be the principal residence of the DTC eligible person within one year after acquisition.

The individual acquiring the home, or the individual's spouse or common-law partner can claim the FTHBC. An ownership interest in the particular home for which the FTHBC is claimed must be registered in the applicable provincial land registration system.

Any unused portion of the FTHBC relating to an individual can be claimed by such individual's spouse or common-law partner. A home jointly acquired by two individuals will only create one full FTHBC.

Resolution 7: Registered Retirement Savings Plans

(7) That, in the case of a registered retirement savings plan or a registered retirement income fund from which the final payment out of or under the plan or fund is made after 2008 and after the death of the annuitant under the plan or fund,

(a) the Act be amended to allow the annuitant's legal representative to claim a deduction, in computing the annuitant's income for the year in which the annuitant died, of an amount not exceeding the amount determined by the formula

$$A - B$$

where

A is the total of all amounts each of which is

(i) the amount deemed by subsection 146(8.8), or subsection 146.3(6), of the Act, to have been received by the annuitant out of or under the plan or fund,

(ii) an amount (other than an amount described in clause (iii)) received, after the death of the annuitant, by a taxpayer as a benefit out of or under the plan or fund and included, because of subsection 146(8) or subsection 146.3(5) of the Act, in computing the taxpayer's income, or

(iii) a tax-paid amount (within the meaning assigned by subsection 146(1) of the Act) in respect of the plan, or in the case of a registered retirement income fund, an amount that would, if the fund were a registered retirement savings plan, be a tax-paid amount in respect of the fund, and

B is the total of all amounts paid out of the plan or fund after the death of the annuitant;

(b) that the deduction described in subparagraph (*a*) not be available, except to the extent acceptable to the Minister of National Revenue, in circumstances where

(i) at any time after the death of the annuitant, the plan or fund held a non-qualified investment, or

(ii) the last payment out of or under the plan or fund was made after the year following the year in which the annuitant died.

CCH Editorial Comment: Under subsections 146(8.8) and 146.3(6), the fair market value of investments held in an annuitant's RRSP or RRIF (each referred to as a "Plan") at the time of the annuitant's death is generally included in the income of the deceased for such year (unless there is a transfer to a spouse or common-law partner). A subsequent increase in the value of the investments held in the Plan is generally included in the income of the beneficiaries of the Plan upon distribution.

Pursuant to the Budget, a loss realized in a Plan after death of the annuitant (a "Plan Loss") can now be carried back and deducted when computing income for tax purposes of the annuitant in the year of death. The amount of a Plan Loss available for carry back is expressed as the formula (A - B) where:

A is the total of (i) all amounts included in the annuitant's income from the Plan as a result of death, (ii) all amounts received from a Plan, after the death of an annuitant, by a taxpayer as a benefit out of the Plan pursuant to subsections 146(8) and 146.3(5) of the Act, and (iii) all "tax-paid amounts" in respect of the Plan, as such term is defined in subsection 146(1) of the Act, and

B is the total of all amounts paid out of the Plan after the death of the annuitant.

The ability to carry back a Plan Loss to the year of death will not be available, except to the extent acceptable by the Minister of National Revenue if, at any time after death of the annuitant, the particular plan held a non-qualified investment or the last payment out of the particular plan was not made within the year after the year in which the annuitant died.

This amendment applies with respect to Plans where the final distribution occurs after 2008.

Resolution 8: Mineral Exploration Tax Credit

(8) That, for expenses renounced under a flow through share agreement made after March 2009,

(a) paragraph (*a*) of the definition "flow-through mining expenditure" in subsection 127(9) of the Act be replaced by the following:

(*a*) that is a Canadian exploration expense incurred by a corporation after March 2009 and before 2011 (including, for greater certainty, an expense that is deemed by subsection 66(12.66) to be incurred before 2011) in conducting mining exploration activity from or above the surface of the earth for the purpose of determining the existence, location, extent or quality of a mineral resource described in paragraph (*a*) or (*d*) of the definition "mineral resource" in subsection 248(1),

and

(b) paragraphs (*c*) and (*d*) of the definition "flow-through mining expenditure" in subsection 127(9) of the Act be replaced by the following:

(*c*) an amount in respect of which is renounced in accordance with subsection 66(12.6) by the corporation to the taxpayer (or a partnership of which the taxpayer is a member) under an agreement described in that subsection and made after March 2009 and before April 2010, and

(*d*) that is not an expense that was renounced under subsection 66(12.6) to the corporation (or a partnership of which the corporation is a member), unless that renunciation was under an agreement described in that subsection and made after March 2009 and before April 2010.

CCH Editorial Comment: The flow-through share regime permits an investor to enter into an agreement to subscribe for shares of a corporation, and the corporation uses the subscription funds to incur certain qualifying resource expenses which it renounces or "flows through" to the investor. Certain individuals who invest in flow-through shares are also entitled to an additional benefit equal to 15 per cent of certain qualifying expenses incurred in Canada as described in the definition of "flow-through mining expenditure" in subsection 127(9). This mineral exploration tax credit was introduced as part of the October 18, 2000 Budget and is currently scheduled to expire at the end of March 2009.

Resolution 8 of the 2009 Budget proposes to extend the eligibility for the mineral exploration tax credit for one year by amending the definition of "flow-through mining expenditure" to include qualifying expenses incurred before 2011, pursuant to agreements entered into before April 1, 2010. Qualifying expenses will include expenses incurred in 2011 and expenses deemed to be incurred before 2011 by virtue of the "look-back" rule in subsection 66(12.66).

Resolution 9 to 11: Small Business Limit

(9) That, for taxation years that end after 2008, the rules in subsections 125(2) and (3) of the Act determining the business limit of a Canadian-controlled private corporation (CCPC) be modified such that

(*a*) subject to subparagraph (*b*), the business limit of a CCPC for a taxation year be the total of

(i) that proportion of $400,000 that the number of days in the taxation year that are in 2008 is of the number of days in the taxation year, and

(ii) that proportion of $500,000 that the number of days in the taxation year that are after 2008 is of the number of days in the taxation year; and

(b) for the purpose of subsection 125(3) of the Act, associated CCPCs allocate a business limit for taxation years beginning after 2008 by allocating a total business limit of $500,000.

(10) That, in applying paragraph 125(5)(*a*) of the Act, the business limit of a CCPC in respect of each of its second and subsequent taxation years that end in 2009 (where it has more than one taxation year that ends in 2009 and is associated in two or more of those taxation years with another CCPC that has a taxation year that ends in 2009) be determined as if its business limit for its first taxation year that ends in 2009 was determined based on the amount referred to in subsection 125(3) that applies for taxation years that begin after 2008.

(11) That, for fiscal periods of a partnership that end after 2008, the references in the description of M in the definition "specified partnership income" in subsection 125(7) of the Act to "$400,000" and "$1,096" be replaced with references to "$500,000" and "$1,370".

CCH Editorial Comment: Budget 2009 increases the small business income limit, as set out in subsection 125(2) for Canadian-controlled private corporations (CCPCs) from $400,000 to $500,000, effective January 1, 2009. Corporations whose taxation years straddle the end of calendar 2008 will pro-rate their small business limits based on the number of days in the taxation year after 2008 and before 2009. The current 11% federal tax rate will continue to apply to the small business income (that is, the regular 28% corporate rate minus the 17%

reduction amount for CCPCs). The 11% rate on small business income has applied since the beginning of 2008.

The increase in the small business limit is the latest of a series of increases going back to the 2003 budget, which phased in an increase in the limit from $200,000 to $300,000, the 2004 budget which accelerated that phase-in, and the 2006 budget which increased the limit from $300,000 to $400,000 beginning in the 2007 taxation year.

Resolutions 12 and 13: Small Business Limit — SR&ED

(12) That, subject to paragraph (13), the expenditure limit in subsection 127(10.2) of the Act in respect of a corporation for the 2010 and subsequent taxation years be determined as if,

(a) the formula in subsection 127(10.2) of the Act were the following:

$$(\$8 \text{ million} - 10A) \times [(\$40 \text{ million} - B) / \$40 \text{ million}]$$

and

(b) the reference to "$400,000" in paragraph (*a*) of the description of A in subsection 127(10.2) of the Act were a reference to "$500,000".

(13) That, for a corporation's 2010 taxation year that begins before 2010, the expenditure limit in subsection 127(10.2) of the Act of the corporation be determined by the formula,

$$A + [(B-A) \times (C/D)]$$

where

A is the expenditure limit of the corporation for the taxation year determined in accordance with the formula in subsection 127(10.2) of the Act as that subsection read in its application to taxation years that end in 2009;

B is the expenditure limit of the corporation for the taxation year determined in accordance with the formula in subsection 127(10.2) of the Act, as provided for in paragraph (12) without reference to this paragraph;

C is the number of days in the taxation year that are after 2009; and

D is the total number of days in the taxation year.

CCH Editorial Comment: A related change to the increase in the small business limit applies to the refundable scientific research and experimental development (SR&ED) investment tax credit available to CCPCs. Under subsection 127(10.1) of the Act, a CCPC is eligible for an enhanced investment tax credit (ITC) equal to an extra 15% (in addition to the regular 20% rate) of certain eligible expenditures not exceeding a $3 million expenditure limit per taxation year. The enhanced credit is reduced if the CCPC's taxable income (along with the taxable income of any associated corporations) in the previous taxation year was over $400,000 and it is eliminated completely if the taxable income was $700,000 — in other words, the expenditure limit for the current year is reduced by $10 for every $1 of taxable income of the CCPC (and its associated corporations) in excess of the $400,000 small business limit for the previous year.

As a result of the increase to the small business limit to $500,000, the phase-out of the expenditure limit will now begin when the taxable income for the previous year was over $500,000 and the expenditure limit will be eliminated completely at $800,000 of taxable income for the previous year. This change will apply to the 2010 taxation year, although pro-rating transitional rules will apply where the 2010 taxation year began before the beginning of 2010.

Since the refundable tax credit in section 127.1 is based on the CCPC's expenditure limit, it will be affected to the extent that the expenditure limit is affected in the manner described above.

Resolutions 14 and 15: Small Business Limit — Refundable Investment Tax Credit

(14) That, subject to paragraph (15), in respect of the 2010 and subsequent taxation years, the reference to "$400,000" in the formula in the definition "qualifying income limit" in subsection 127.1(2) of the Act, as proposed in subclause 33(2) of the Notice and Ways and Means Motion tabled in Parliament on November 28, 2008, be replaced by a reference to "$500,000".

(15) That, for 2010 taxation years that begin before 2010, the reference to "$400,000" in the formula in the definition "qualifying income limit" in subsection 127.1(2) of the Act, as proposed in subclause 33(2) of the Notice and Ways and Means Motion tabled in Parliament on November 28, 2008, be replaced by a reference to the amount determined by the following formula

$$\$400,000 + [\$100,000 \times (A/B)]$$

where

A is the number of days in the taxation year that are after 2009; and

B is the total number of days in the taxation year.

CCH Editorial Comment: A "qualifying corporation" is eligible for the refundable investment tax credit under subsection 127.1(1). A "qualifying corporation" (taking into account draft proposed changes first announced in last year's budget) for a particular taxation year is a CCPC, the taxable income of which for its preceding taxation year, together with the taxable incomes of all associated corporations for their preceding taxation years, does not exceed the "qualifying income limit" of the corporation. Currently, the qualifying income limit is $400,000, and is reduced if the corporation's taxable capital employed in Canada in the previous year exceeds $10 million. Resolution 14 of this year's budget increases the $400,000 amount to $500,000, effective for 2010 and subsequent taxation years. Resolution 15 provides that if the 2010 taxation year straddles the end of 2009, the amount is pro-rated based on the number of days in the taxation year before 2009 and those after 2008. (The reduction of the qualifying income limit by the taxable capital in excess of $10 million is not affected by the change.)

Resolutions 16 and 17: Small Business Limit — Instalments

(16) That, subject to paragraph (17) in respect of taxation years that end after 2008, a reference to "$400,000" in paragraph 157(1.2)(*a*) of the Act be replaced by a reference to "$500,000."

(17) That for 2009 taxation years that begin before 2009, paragraph 157(1.2)(*a*) of the Act be read as follows:

(*a*) for which the amount determined under subsection 157(1.3) of the Act

(i) for the taxation year does not exceed an amount that is the total of

(A) that proportion of $500,000 that the number of days in the taxation year that are in 2009 is of the number of days in the taxation year; and

(B) that proportion of $400,000 that the number of days in the taxation year that are before 2009 is of the number of days in the taxation year; or

(ii) for the preceding taxation year does not exceed $400,000;

CCH Editorial Comment: Pursuant to subsection 157(1.1), a "small-CCPC" is generally allowed to make quarterly instalments of tax (rather than monthly instalments as is the case for other corporations) and must pay any remaining balance owing within three months after its year end (rather than two months in the case of other corporations). Subsection 157(1.2) defines a small-CCPC at a particular time in a taxation year as a CCPC that, among other things, had taxable income (along with taxable income of any associated corporations) not exceeding $400,000 for the year or the immediately preceding taxation year. As a result of the increase to the small business limit (noted above), the $400,000 threshold is increased to $500,000, starting with the 2009 taxation year. If the 2009 taxation year straddles the end of the 2008 calendar year, the threshold is pro-rated based on the number of days in the taxation year before 2009 and the number of days after 2008, while the threshold for the taxation year immediately before that year will remain $400,000.

Resolution 18: Acquisition of Control of a Corporation

(18) That subsection 256(9) of the Act not apply for the purposes of determining if a corporation is, at any time, a small business corporation or a Canadian-controlled private corporation (CCPC), and that

(a) this paragraph apply in respect of acquisitions of control of a corporation that occur after 2005, other than in respect of such an acquisition of control that occurs before January 28, 2009 in respect of which the taxpayer elects on or before the taxpayer's filing-due date for the taxpayer's 2009 taxation year that this measure not apply; and

(b) a taxpayer be deemed to have made the election described in subparagraph (*a*) in respect of an acquisition of control of a corporation if it can reasonably be considered that the position taken in respect of the acquisition of control in a return of income, notice of objection or notice of appeal filed or served under the Act before January 28, 2009 relies upon an interpretation of that subsection of the Act to the effect that the subsection applies for the purposes of determining if the corporation was a small business corporation or a CCPC at the time of the transfer of shares of the corporation that caused the acquisition of control to occur.

CCH Editorial Comment: Subsection 256(9) of the Act provides that where control of a corporation is acquired by a person or group of persons, absent a specific election otherwise, the timing of the acquisition of control is deemed to be at the commencement of the day, regardless of when during the day control was actually acquired. This means that for purposes of computing the corporation's income tax circumstances for the taxation year that ends immediately before the acquisition of control, by virtue of subsection 249(4), the day when control is acquired should not be included and instead that day becomes the first day of the corporation's post-acquisition of control taxation year, unless the corporation elects otherwise.

In 2006, the Federal Court of Appeal decision in *La Survivance v. The Queen* held that where subsection 256(9) applied in respect of the acquisition of control of a public corporation that did not elect out of the deeming rule, and such corporation was acquired by a private corporation, for purposes of the Act the corporation would be considered to be a Canadian-controlled private corporation (CCPC) at the time the acquisition of control actually occurred (see Tax Topics No. 1881). This decision raised concerns among tax practitioners that a CCPC that did not elect out of subsection 256(9) could lose its CCPC status at the commencement of the day if it were acquired by a non-resident or a public corporation and thereby fail to qualify for the capital gains exemption available for dispositions of qualified small business corporation shares. The Canada Revenue Agency confirmed this concern was legitimate in a technical interpretation issued on February 22, 2008 (doc. no.

2006-0214781E5). The CRA pointed out that this result can be avoided by electing to opt out of subsection 256(9). However, in some cases, an acquisition of control in the middle of a business day can create certain practical tax issues for the corporation. In the technical interpretation the CRA stated:

"we will bring this matter to the attention of the Department of Finance for consideration as to whether a legislative change is necessary."

The Department of Finance has responded to this issue with a legislative solution. The Notice of Ways and Means provides that subsection 256(9) no longer applies for the purposes of determining if a corporation is, at any time, a small business corporation or a CCPC. This new rule will apply in respect of acquisitions of control of corporations that occur after 2005 except for transactions that occurred before January 28th, 2009 where the taxpayer elects in its 2009 tax return that this new rule should not apply. This permits taxpayers who have relied on the decision in *La Survivance* to elect to have the Federal Court of Appeal's interpretation apply to them notwithstanding these Budget proposals. Further, a corporation will be deemed to have made this election in respect of an acquisition of control if it can reasonably be considered that the corporation's tax filing position in respect of a tax return, notice of objection or notice of appeal filed or served under the Act prior to January 28, 2009 relies upon an interpretation of subsection 256(9) to the effect that the subsection applies for purposes of determining if the corporation was a small business corporation or a CCPC at the time the shares were transferred giving rise to the acquisition of control.

Resolution 19 to 22: Mandatory Filing of Return by Electronic Transmission

(19) That, for taxation years that end after 2009, corporations that meet conditions prescribed by the Minister of National Revenue be required to file the return of income required to be filed under section 150 of the Act by way of electronic filing.

(20) That, for taxation years that end after 2010, the Act be amended to provide that every person who fails to file a return of income for a taxation year by way of electronic filing as required by paragraph (19) be liable to a penalty of

(a) where the taxation year ends in 2011, $250;

(b) where the taxation year ends in 2012, $500; and

(c) where the taxation year ends after 2012, $1,000.

(21) That, for information returns that are prescribed for the purposes of this paragraph and required to be filed after 2009, the Act be amended to provide that every person (other than a registered charity) or partnership who fails to file such an information return when required by the Act or the Income Tax Regulations is liable to a penalty of the greater of

(a) $100; and

(b) where the taxpayer is required to file on a day one or more such information returns and the number of those information returns of a particular type so required to be filed is

(i) less than 51, $10 for each day during which the failure continues, not exceeding 100 days,

(ii) more than 50 but less than 501, $15 for each day during which the failure continues, not exceeding 100 days,

(iii) more than 500 but less than 2,501, $25 for each day during which the failure continues, not exceeding 100 days,

(iv) more than 2,500 but less than 10,001, $50 for each day during which the failure continues, not exceeding 100 days, and

(v) more than 10,000, $75 for each day during which the failure continues, not exceeding 100 days.

(22) That for information returns that are prescribed for the purposes of this paragraph and required to be filed electronically after 2009, the Act be amended to provide that every person (other than a registered charity) or partnership who fails to file such an information return by way of electronic filing is liable to a penalty of, where the number of those information returns of a particular type so required to be filed is

(a) more than 50 but less than 251, $250;

(b) more than 250 but less than 501, $500;

(c) more than 500 but less than 2,501, $1500; and

(d) more than 2500, $2,500.

CCH Editorial Comment: The Budget contains measures that will require certain income tax returns and information returns to be filed electronically. The Budget documents provide that corporations that have annual gross revenues in excess of $1 million in a taxation year will generally be required to file their income tax returns electronically, applicable for taxation years that end after 2009. It is noted that exceptions to this requirement may be provided with respect to non-resident corporations, insurance corporations, and corporations filing in a functional currency.

Furthermore, existing mandatory electronic filing provisions will be amended. The current requirements to file information returns electronically will be reduced from 500 to 50, applicable to information returns required to be filed after 2009. It is noted in the Budget documents that this measure will apply most often with respect to T4 information returns for employment income.

New penalties will be introduced, and existing penalties amended, to deal with non-compliance of these requirements.

With respect to the requirement to electronically file an income tax return, the new penalty will not apply before 2011. The penalty for taxation years that end in 2011 will be $250, increased to $500 with respect to 2012 and to $1,000 for taxation years ending after 2012.

With respect to the existing requirements relating to the filing of information returns, the Budget proposes to reduce the existing penalties for late filing, which are computed by reference to the number of returns required. In particular, the penalties for late filing will be reduced to the greater of $100 and the following amounts:

(i) $10 per day where the number of returns required to be filed is less than 51;

(ii) $15 per day where the number of returns required to be filed is more than 50 but less than 501;

(iii) $25 per day where the number of returns required to be filed is more than 500 but less than 2,501;

(iv) $50 per day where the number of returns required to be filed is more than 2,500 but less than 10,001; and

(v) $75 per day where the number of returns required to be filed is more than 10,000.

In all cases, the late filing period is capped at a maximum of 100 days. Accordingly, these new provisions will cap penalties for late filing in the range of $1,000 and $7,500, depending on the number of returns required. These penalties will be applicable to returns required to be filed after 2009.

With respect to the failure to file prescribed information returns electronically, new penalties will be added, applicable for returns required to be filed after 2009, as follows:

(i) $250, where more than 50 but less than 251 returns are required;

(ii) $500, where more than 250 but less than 501 returns are required;

(iii) $1,500, where more than 500 but less than 2,501 returns are required; and

(iv) $2,500, where more than 2,500 returns are required.

Resolutions 23 and 24: Interest Deductibility

(23) That section 18.2 of the Act be repealed in respect of interest and other borrowing costs paid or payable in respect of a period or periods that begin after 2011.

(24) That, consequential to the repeal of section 18.2 of the Act:

(a) subsection 20(3) be amended, in respect of interest paid or payable in respect of a period or periods that begin after January 27, 2009, to remove the scheduled reference to section 18.2;

(b) subparagraphs 53(1)(*e*)(xiv) and 53(2)(*c*)(xiii) and subsections 91(5.1) to (5.3) of the Act be repealed applicable after 2011; and

(c) subsection 92(1) be amended, applicable after 2011, to repeal subparagraph 92(1)(*a*)(ii) and to remove the reference to section 91(5.1) in subparagraph 92(1)(*b*)(ii).

CCH Editorial Comment: Effective January 1, 2012, section 18.2 was to restrict the deductibility of interest and other borrowing costs incurred by a Canadian corporate taxpayer on borrowed money used to invest in foreign affiliates, where such borrowing would give rise to a second interest deduction for foreign tax purposes. This type of arrangement is commonly referred to as "double-dip" financing because two interest deductions are provided in respect of different sources of income in two jurisdictions. Resolution 23 proposes the repeal of section 18.2. The Budget papers state that this step was taken in response to the December 2008 final report of the Advisory Panel on Canada's System of International Taxation, specifically with respect to its conclusions on the potential effects section 18.2 would have on foreign investment by Canadian multi-national firms, particularly taking into account the current global economic crisis.

Resolution 24 contains a number of consequential amendments resulting from the repeal of section 18.2. Specifically:

- an amendment to subsection 20(3) to remove the scheduled reference to section 18.2;
- the repeal of subparagraphs 53(1)(e)(xiv) and 53(2)(c)(xiii);
- the repeal of subsections 91(5.1) to (5.3); and
- the repeal of subparagraph 92(1)(a)(ii) and an amendment to subparagraph 92(1)(b)(ii).

Other Tax Matters Not In the Notice of Ways and Means Motion

In response to the December 2008 report of the Advisory Panel on Canada's System of International Taxation, the Government indicated that it is studying the report and offered its response in respect of some issues raised. Firstly, section 18.2 will be repealed (see Budget Resolutions 23 and 24, above). Secondly, the Government has said that the proposals relating to non-resident trusts and foreign investment entities which were first introduced 10 years ago in the 1999 Budget, will be reviewed in light of the Advisory Panel's submissions, before proceeding further with these controversial measures. (The last version of these proposals was set out in Bill C-10 which generally proposed that they would come into effect for years commencing after 2006. There is no indication whether this date will remain in any new proposals to be introduced, leaving taxpayers with a significant level of uncertainty.) In addition, the Government will consider the Advisory Panel's recommendations relating to foreign affiliates before proceeding with the February 2004 foreign affiliate amendments and subsequent modifications resulting from consultations and deliberations.

The Budget Papers also describe proposals to amend the Regulations in order to further enhance the availability of accelerated capital cost allowance (CCA) for machinery and equipment used primarily in Canada for manufacturing and processing goods for sale or lease, which would ordinarily be included in Class 43. Accelerated CCA for this type of depreciable capital property was first proposed in the 2007 Budget and in the 2008 Budget it was extended to permit a 50% straight-line CCA rate for eligible assets acquired before 2010 followed by a CCA treatment on a declining balance basis for eligible assets acquired in 2010 and 2011. The 2009 Budget Papers propose to extend the 50% straight-line CCA for eligible assets acquired in 2010 and 2011.

A temporary 100% CCA rate for eligible computers and software acquired after January 27, 2009 and before February 2011 is also provided for in the Budget Papers. In addition, the half-year rule will not apply to these amounts, allowing the taxpayer to fully deduct the cost of an eligible computer in the first year that the CCA deductions are available. Property that would be described in Class 29 or 50 will qualify for these deductions provided that it is situated in Canada, it has not been used or previously acquired for use prior to being acquired by the taxpayer, and is acquired by the taxpayer (i) for use in a business carried on by the taxpayer in Canada or for the purpose of earning income from property situated in Canada, or (ii) for lease by the taxpayer to a lessee for use by the lessee in a business carried on by the lessee in Canada or for the purpose of earning income from property situated in Canada. These CCA deductions remain subject to the computer tax shelter property rules. While the Budget Papers do not contain specific proposals dealing with CCA for carbon capture and storage assets, the Government does state that it will consult with stakeholders to identify specific assets used for this purpose with a view to providing accelerated CCA in the future.

WHAT IS NOT IN THE 2009 BUDGET?

It is interesting to note that the 2009 Budget did not follow up on several previous budget proposals. For example, the 2009 Budget did not contain any proposals relating to cross-border share-for-share exchanges. This was first discussed in the 2005 Budget. In addition, the 2003 interest deductibility proposal set out in draft section 3.1 (which has still not been updated despite comments from the Department of Finance that revised draft legislation had been prepared) was not discussed in the 2009 Budget.

It is also interesting to note that during the last federal election, the Conservatives promised to index the capital gains exemption and create a new refundable children's art tax credit and that the Conservatives did not live up to these election promises. However, they did fulfil their election promises to increase the small business deduction limit, extend the mineral exploration tax credit and provide a new first time home buyer tax credit.

The 2009 Budget will be remembered by Canadian tax professionals as a budget which only made a few technical changes to the Income Tax Act, and for that, tax professionals will be grateful. However, as announced by the Department of Finance at the 2008 Canadian Tax Foundation Conference, it is likely that a Technical Bill, which would deal with many of the "comfort letters" issued by the Department of Finance over the past several years, will be introduced in Parliament early this year.

Customs and Excise Tax Measures

CCH Editorial Comments: Notice of Ways and Means Motion to Amend the Excise Tax Act re: GST/HST

The 2009 Budget included a Notice of Ways and Means Motion to Amend the Excise Tax Act with respect to direct / network sellers.

Simplification for Network Sellers

New section 178 has been proposed in recognition of the various forms of distribution in the direct selling business. The two business models described are supply-and-resupply through contractors, and direct supplies to customers using the services of commissioned sales representatives.

Supplies under the first model, referred to as the "buy and resell model", are subject to simplified processes currently in place, including an "Alternate Collection Method" (ACM) which allows the direct seller to account for GST collected, as if the direct seller had collected from the final consumer on the suggested retail price. The contractor is not required to account for the GST collected, thereby in many cases avoiding the necessity for contractors to register for GST.

Budget 2009 extends simplification, albeit in a different form, to the second model, referred to as the "network selling" model. If the parties jointly elect, the sale by the network seller to the final customer would be subject to the normal rules, and the supplies of the representative's sales services, payments of commission, and certain supplies of sales aids would be effectively ignored. This will have the effect of simplifying the GST accounting for the network seller and essentially eliminating the obligation of the sales representative. Many more sales representatives will not be required to register for GST. Recognizing this, proposed new subsection 242(2.3) allows the cancellation of registration of a sales representative which has jointly elected with a network seller. Enforcement provisions have also been proposed, as subsections 236.5(1) and (2), such that if an electing network seller does not meet the conditions for election, the net tax calculation for the network seller will include an amount equal to the interest that would be payable on the uncollected GST on sales representatives commissions. Similar provisions apply if the election is revoked under the authority of the Minister.

The amendments are proposed to apply to any reporting period of a network seller that begins after 2009.

Previously Announced Measures

Financial Institutions

The Budget confirmed the government's intention to proceed with proposed amendments to the financial services sector, announced on January 26, 2007.

CCH Editorial Comments: Notice of Ways and Means Motion to Amend the Customs Tariff

Customs Relief on Machinery and Equipment

Amendments to the Customs Tariff are proposed to eliminate tariffs on most machinery and equipment which is not currently imported duty free. Indication of further steps to improve the Customs Tariff rules were also included in the budget.

CCH Editorial Comment: Other

Provincial Sales Tax Harmonization

Under the heading “Provincial Sales Tax Modernization”, the budget documents confirm the government’s commitment to working with the provinces which continue to impose retail sales taxes (RST), toward a federal-provincial harmonized GST. To promote a harmonized tax, the paper boasts one of the benefits of harmonization as a significant reduction in the marginal effective tax rate for new business investment in the five remaining RST provinces.