

# 2009 Federal budget highlights

January 27, 2009

Today the Minister of Finance, James M. Flaherty, tabled the Conservative government's fourth federal budget.

As previously announced, the days of budget deficits are back, with a projected shortfall of approximately \$64 billion over the next two years (\$34 billion for 2009-2010 and \$30 billion the year after) and an expectation to emerge from the deficit and return to a surplus within five years.

The budget will provide for almost \$30 billion this year in stimulus programs targeted at the economic crisis. These programs focus on job retraining, housing and social programs, spending on roads and infrastructure and initiatives to protect the environment.

The budget provides for measures to restore confidence, encourage lending and improve access to financing, including tax relief to stimulate consumer spending by lowering the tax brackets for low to middle income Canadians and increasing the amount of income eligible for the small business tax rate.

The following is a summary of the tax measures proposed in the budget. It should be noted that these measures are not yet law and may undergo revisions before receiving Royal Assent.

We invite you to contact your local Grant Thornton office to discuss any questions you have regarding the changes proposed in this budget.



# Business measures

## Small business limit increase

Effective January 1, 2009, it is proposed that the small business limit (the annual amount of active-business income earned by Canadian-controlled private corporations (CCPCs) eligible for the low federal small business corporate rate of 11%) will increase from \$400,000 to \$500,000. The increase will be pro-rated for non-calendar year-ends.

## Phase-out of SR&ED expenditure limits

CCPCs are also eligible to earn investment tax credits at an enhanced rate of 35% on up to \$3 million of scientific research and experimental development expenditures annually. This \$3-million expenditure limit is reduced as a CCPC's taxable income for the previous year increases from \$400,000 to \$700,000 and taxable capital of the previous year increases from \$10 million to \$50 million. Consistent with the above proposal to increase the small business limit, the \$3-million expenditure limit will begin to be reduced at the proposed small business limit of \$500,000 and will be fully eliminated where taxable income in the previous year is \$800,000 or more. This change will apply where the previous taxation year ends after 2008. The reduction of the expenditure limit based upon taxable capital will not be changed.

## Accelerated CCA for manufacturing and processing (M&P) equipment

Both the 2007 and 2008 budgets provided the M&P sector with a temporary ability to claim an accelerated capital cost allowance (CCA) rate for M&P equipment used primarily in Canada.

Qualifying M&P equipment acquired on or after March 19, 2007 and before 2010 is eligible for an accelerated straight-line 50% CCA rate. Last year's budget provided for accelerated CCA treatment on a declining-balance basis for eligible M&P assets acquired in 2010 and 2011.

This year's budget proposes to replace the declining-balance basis CCA for assets acquired in 2010 and 2011 with 50% straight-line treatment.

## Temporary 100% CCA rate for computer hardware and systems software

A temporary 100% CCA rate is proposed for eligible computer hardware and systems software acquired after January 27, 2009 and before February 1, 2011, provided that the equipment and software would otherwise be included in Class 50 (55% CCA rate). The equipment will not be subject to the half-year rule in the year of acquisition, thereby permitting a full write off of the equipment in the year of acquisition.

The 100% CCA rate will also apply to property that is currently included in Class 29, that would otherwise be described in Class 50 and that meets other qualifying conditions.

## Freezing of employment insurance (EI) rates

It is proposed that the EI premium rate of \$1.73 per \$100 of insurable earnings will be frozen for both 2009 and 2010.

### Acquisition of control of a corporation—time of acquisition

Under the Income Tax Act (the Act), control of a corporation is deemed to have been acquired at the beginning of the day of acquisition. In a 2006 Federal Court of Appeal case, *La Survivance v. The Queen*, this deeming rule was interpreted to apply strictly to the issue of control. This means that where an individual sells shares of a CCPC that would otherwise qualify for the enhanced capital gains exemption to a non-resident, the CCPC's control is deemed to be acquired at the beginning of the day. As a result, the company is no longer a CCPC at the time of sale, and the vendor will not be able to claim the capital gains exemption.

It is proposed that the deeming rule for the timing of the acquisition of control will be amended to ensure that the timing of the sale will not affect the status of a corporation as a CCPC at the time of the transaction that caused the change in control. It is also

proposed that this amendment will apply retroactive to acquisitions of control that occur after 2005 (subject to an election that can be made not to have this proposed amendment apply to acquisitions of control occurring prior to January 28, 2009).

### International taxation—interest deductibility

In December 2008, the federal government received the final report of the Advisory Panel on Canada's System of International Taxation (the Panel). In response to the Panel's recommendations, it is proposed that section 18.2 of the Income Tax Act will be repealed. This section, scheduled to come into force in 2012, constrains the deductibility of interest in certain situations where a Canadian corporation uses borrowed funds to finance a foreign affiliate and a second deduction for that interest is available in the foreign jurisdiction (so-called "double-dip" interest deductions). The Panel was concerned about the potential effects of this provision on foreign investment by

Canadian multinational firms, particularly in the context of the current global financial environment.

---

## Personal tax measures

### Personal amounts and income tax brackets

Effective January 1, 2009 it is proposed that the basic personal amount and the two lowest personal income tax brackets will be increased as follows:

- the basic personal amount, the spousal and common-law partner amount and the eligible dependant amount will increase to \$10,320 (from \$9,600 in 2008);

- the upper limit of the first personal income tax bracket (15% tax rate) will increase to \$40,726 (from \$37,885 in 2008); and
- the upper limit of the second personal income tax bracket (22% tax rate) will increase to \$81,452 (from \$75,769 in 2008).

The above amounts will be indexed to inflation for 2010 and subsequent years.



### Age credit

Canadian taxpayers 65 or older are entitled to claim an age credit that is reduced at the rate of 15% where a taxpayer's income exceeds a prescribed threshold. It is proposed that the relevant amounts for 2009 will be as follows:

- The age amount will increase to \$6,408 (from \$5,276 in 2008);
- The net income level at which the age credit begins to be phased out will remain unchanged at \$32,312; and
- Due to the increase in the age amount, the income level at which the credit will be fully phased out will increase to \$75,032.

### Home renovation tax credit

To encourage taxpayers to invest in improvements to their homes, it is proposed that a temporary Home Renovation Tax Credit (HRTC) will be introduced. The rules will operate as follows:

- A family (comprised of an individual, his or her spouse or common-law partner and any children <18 yrs) will be able to claim a 15% non-refundable tax credit for eligible expenditures made after January 27, 2009 and before February 1, 2010 in respect of eligible dwellings.
- The credit will apply to expenditures in excess of \$1,000, but not more than \$10,000, resulting in a maximum credit of \$1,350 (\$9,000 x 15%).
- Where one person in the family does not claim the entire credit, any unused portion can be claimed by one of the other family members.
- The credit will not be available in respect of expenditures for work performed or goods acquired in that period if the expenditure is made pursuant to an agreement entered into before January 28, 2009.

The credit will apply only to the 2009 taxation year and will be claimed on the individual's 2009 income tax return (including expenditures made in January 2010). It must be supported by receipts.

- The HRTC will not be reduced by any other tax credits or grants to which a taxpayer is entitled under other government programs (for example, the Medical Expense Tax Credit).
- An eligible dwelling is a dwelling that is the taxpayer's "principal residence" at any time during the period (as defined under existing tax law).
- Only eligible expenditures that relate to the personal-use areas of the residence will qualify and where the residence is used for business or rental income, the expenditures will need to be allocated between personal and income-earning use.
- Eligible expenditures include amounts incurred for labour, material, equipment rentals and permits in relation to a renovation or alteration of an eligible dwelling, provided it is of an enduring nature and is integral to the eligible dwelling.
- The following expenditures will not qualify for the credit:
  - the cost of routine repairs and maintenance normally performed on an annual or more frequent basis;
  - expenditures for appliances and audio-visual electronics;
  - financing costs associated with a renovation;
  - other indirect expenditures that retain a value independent of the renovation (e.g. furniture and draperies); and
  - expenditures for goods and services provided by a non-arm's length person, unless that person is registered for the GST/HST.

### Measures for first-time home buyers

The following measures are proposed to assist first time home buyers:

- The maximum amount that can be withdrawn from an RRSP under the Home Buyers' Plan will increase to \$25,000 from \$20,000. This measure will apply to withdrawals made after January 27, 2009. The increase will also apply to amounts withdrawn to facilitate the acquisition of a home that is more accessible for an individual who qualifies for the disability tax credit.
- A new, non-refundable, First-Time Home Buyers' Tax Credit is introduced. This \$5,000 credit will apply to first-time buyers who acquire a qualifying home after January 27, 2009 (i.e., the closing is after this date). Since it is based on the lowest marginal tax rate of 15%, this new credit will reduce income taxes by \$750. The qualifying rules are the same as those that apply under the Home Buyers' Plan.

### RRSP/RRIF losses after death

The fair market value of investments held in a RRSP or RRIF at the time of an annuitant's death is generally included in the income of the deceased for the year of death. However, there is currently no tax provision to recognize any decrease in the value that occurs after the death and before the investments are distributed to beneficiaries (the post-death decrease).

The budget proposes to allow the amount of the post-death decrease in value to be carried back and deducted against the year-of-death RRSP/RRIF income inclusion. This measure will apply where the final distribution from the RRSP or RRIF occurs after 2008.

### Mineral exploration tax credit

The mineral exploration tax credit is currently scheduled to expire at the end of March 2009. The budget proposes to extend eligibility for this credit to flow-through share arrangements entered into on or before March 31, 2010. Under the existing “look-back” rule, funds raised with the credit during the first three months of 2010 can support eligible exploration until the end of 2011.

### Child tax benefit and supplement

For the 2009-10 benefit year, it is proposed that the income levels on which benefits under the Canada Child Tax Benefit (CCTB) and the National Child Benefit supplement are based will be increased as follows:

- the income level at which the phase-out of the CCTB begins will increase to \$40,726; and
- the income level at which the phase-out of the supplement begins will increase by \$1,894, such that it will be completely phased out by \$40,726 for most families.

### Working income tax benefit

To provide incentives for lower income Canadians to enter or remain in the workforce, the 2007 federal budget introduced a working income tax benefit (WITB). For the 2008 tax year, this benefit was comprised of a refundable tax credit of up to 20% for each dollar earned in excess of \$3,000 to a maximum credit of \$510 for single individuals and \$1,019 for couples and single parents. The credit is reduced by 15% of net family income in excess of a specified amount.

The government announced that it plans to double the tax relief provided by this benefit. The final design parameters of the enhanced WITB for the 2009 taxation year will be announced later this year following consultation with the provinces and territories.

---

## Sales tax measures

### Direct selling industry

Measures are introduced to simplify the operation of the GST/HST to the direct selling industry. This industry generally employs two models; a buy and resell model whereby contractors buy and resell goods to the consumer for a mark-up and a commission based model where a sales representative receives a commission for arranging for the sale of the seller's goods. The Excise Tax Act currently provides for an alternative collection method for contractors purchasing goods from a direct seller under the buy and resell model but this method is not allowed for a commission based model.

A new simplified method is announced whereby a seller under the commission based model may now obtain approval from the Minister of National Revenue and jointly elect with all sales representatives to use the new method if certain conditions are met. As a result of the election, commissions and bonuses will not be subject to GST/HST and such income will be ignored for purposes of determining if the sales representative is a small supplier for registration purposes. Certain supplies of sales aids and host gifts to the sales representatives would also not be subject to GST/HST if the election is made. GST/HST

will apply under the normal rules on the sale of goods to the final consumer.

This special accounting method will be available in respect of fiscal years of the seller commencing after 2009. Strict conditions must be met to be eligible to make the election. Adjustments will be made to the seller's net tax if conditions are not met during a fiscal year the election is in effect, or if the seller fails to notify a sales representative that the election has ceased to have effect.

---

# Other measures

## Mandatory electronic filing

To increase filing efficiencies, for taxation years that end after 2009, corporations with annual gross revenues in excess of \$1 million for a taxation year will be required to file their income tax returns in electronic format. Certain exceptions may be provided where no efficiency is generated through electronic filing such as for non-resident corporations, insurance corporations and corporations filing in a functional currency.

In addition, electronic filing of information returns will be required after 2009 for taxpayers filing more than 50 slips (currently 500) related to a particular return (such as T4s and T5s).

## Penalties

To ensure compliance with the mandatory electronic filing changes, new penalties will be gradually introduced for filing a corporate tax return in an incorrect format commencing with returns required to be filed after 2010.

The budget also proposes a reduction in penalties for certain information returns which are either late filed or filed in incorrect format.

## Non-resident trusts, foreign investment entities and foreign affiliate proposals

There are a number of outstanding proposals, first introduced in Budget 1999, that pertain to non-resident trusts and foreign investment entities. There are also other proposals, first announced in February 2004, that pertain to foreign affiliates. This year's budget provides that the government will review the recommendations made by the Panel before proceeding with measures in this area.

## Custom tariff measures

Effective in respect of goods imported into Canada from outside of North America on or after January 28, 2009, the budget proposes to eliminate tariffs on a range of machinery and equipment, thereby assisting Canadian industry by lowering costs of acquiring such goods.

The information contained herein is prepared by Grant Thornton LLP for information only and is not intended to be either a complete description of any tax issue or the opinion of our firm. Changes in tax laws or other factors could affect, on a prospective or retroactive basis, the information contained herein. You should consult your Grant Thornton LLP adviser to obtain additional details and to discuss whether the information in this article applies to your specific situation.

A listing of Grant Thornton offices and contact information can be found on our Web site at: [www.GrantThornton.ca](http://www.GrantThornton.ca)

---

## About Grant Thornton in Canada

Grant Thornton LLP is a leading Canadian accounting and advisory firm providing audit, tax and advisory services to private and public organizations. Together with the Quebec firm Raymond Chabot Grant Thornton LLP, Grant Thornton has more than 3,100 people in offices across Canada. Grant Thornton LLP is a Canadian member of Grant Thornton International Ltd, whose member and correspondent firms operate in over 100 countries worldwide.