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The Optimizer



2010 Federal Budget Canada's Economic Action Plan – Year 2

Recognizing that the challenges of the current economic environment continue to require significant economic stimulus spending, the government has reaffirmed its commitment (in the 2009 budget) to \$19 billion in second year stimulus spending for 2010. Also, included in this relief was \$3.2 billion of personal income tax relief.

Facing a current year deficit of \$53.8 billion, no new stimulus spending programs were announced for fiscal 2010 and beyond. While there was a significant number of tax measures introduced, the government did not undertake an overall attempt to attack the deficit with tax increases.

The government announced a multi-year plan to reduce the deficit through a combination of increased government revenues from economic growth and curbing increases in government program expenditures with the government hoping to get the deficit down to \$1.8 billion by 2014-15.

Corporate tax reductions

While the budget did not announce any new corporate rate reductions, the government restated its intention to collaborate with the provinces and territories to achieve a goal of a 25% combined federal-provincial corporate income tax rate.

The enacted Canadian federal corporate income tax rates are as follows:

	2010	2011	2012
General corporate rate	18.0%	16.5%	15.0%
Small business rate	11.0%	11.0%	11.0%

Employment Insurance Premiums

The government will freeze EI premiums at \$1.73 per \$100 insurable earnings to the end of 2010.

Mineral Exploration Tax Credit

The budget proposes to extend, for an additional year, the mineral exploration tax credit to flow-through share agreements entered into on or before March 31, 2011.

CCA for Clean Energy Generation

Class 43.2 provides 50 per cent capital cost allowance (“CCA”) per year on a declining balance basis for specified clean energy generation and conservation equipment. The budget expands Class 43.2 to include heat recovery equipment used in a broader range of applications and distribution equipment used in district energy systems that rely primarily on ground source heat pumps, active solar systems or heat recovery equipment.

Canadian Renewable and Conservation Expenses – Principal-Business Corporations

The budget proposes that the definition of a “principal-business corporation” be amended to clarify that flow-through share eligibility extends to corporations the principal business of which is producing fuel, generating energy or distributing energy. This measure will apply in respect of taxation years ending after 2004.

Television Set-top Boxes – Capital Cost Allowance

The budget proposes that satellite and cable set-top boxes that are acquired after March 4, 2010 and that have neither been used nor acquired for use before March 5, 2010 be eligible for a declining-balance-CCA rate of 40 per cent.

Interest on Overpaid Taxes

The budget proposes that, effective July 1, 2010, for corporations only, the interest rate payable on overpaid taxes will no longer be 2 percentage points higher than the average yield of three-month Government of Canada Treasury Bills. This new rate will apply in respect of income tax, GST/HST, EI and CPP.

Federal Credit Unions

Certain changes may be required to the Income Tax Act for the proposal to allow for the establishment of federal credit unions.

Specified Investment Flow – Through (“SIFT”) Conversion and Loss Trading

The budget proposes to impose restrictions on the use of losses where units of a SIFT are exchanged for shares of a corporation. The budget also proposes to amend the acquisition-of-control rules in the Income Tax Act to ensure that they do not inappropriately restrict the use of losses where a SIFT trust is wound up and distributes the shares of a corporation it holds.

Tax Loss Utilization Within Corporate Groups

Currently, it is difficult for companies within the same group to be able to transfer losses for utilization by profitable companies within the group, often requiring complicated transactions. The budget acknowledges that it may be possible to make improvements and the government is considering the introduction of a formal system of loss transfers or consolidated reporting. Any such changes will be subject to public consultation.

Employee Stock Options

The \$100,000 Deferral Disappears:

Currently, in certain circumstances, employees of publicly traded companies can defer the tax recognition of the benefit realized on exercising stock options up to \$100,000 per year of qualifying options.

Many employees have been left holding shares worth less than the tax owing.

Employees will no longer be able to defer the recognition of gains on options exercised after March 4, 2010.

Existing payroll withholding requirements will also be clarified to ensure that the tax on the benefit from exercising the option will be required to be remitted to the government when the option is exercised.

Relief For Prior Tax Deferral Elections:

The government is introducing special elective tax treatment for those taxpayers holding shares worth less than the tax owing.

Taxpayers will be able to elect to pay a special tax equal to the proceeds of disposition from selling the shares. The mechanism for doing so can be somewhat complicated as the tax relief from the use of capital losses on the shares against capital gains from other sources is taken into account as well.

For shares disposed of before 2010, the election must be made by the filing deadline for the employee’s 2010 tax returns. For post 2009 dispositions, the election must be made before 2015.

Cashing Out of Stock Options:

Previously, if an employee disposed of certain stock option rights for cash, the employee still received the stock option benefit deduction of one half of the gain on exercising while the cash payment was fully deductible to the employer.

After March 4, 2010, the employee would only be entitled to deduct one half of the gain if the employer makes an election to forgo the tax deduction for making the cash payment.

Charities: Disbursements Quota Reform

Dating back to 1976, registered charities have been required to meet a “disbursement quota” test to ensure that a significant portion of their resources and expenditures are devoted to charitable purposes. In general terms, 80% of receipted donations (“charitable expenditure rule”) and 3.5% of investment assets (“capital accumulation rule”) have to be spent each year on charitable purposes. These rules are particularly constraining on smaller and rural based charities.

Recent legislative and administrative efforts have enabled CRA to better police the operations of charities. As a result, for fiscal years that end on or after March 4, 2010, the government is eliminating the charitable expenditure rule. Additionally, the capital accumulation rule is being modified to increase the level of exempt assets from \$25,000 to \$100,000.

Anti-avoidance rules will also be put in place primarily to apply where it can be reasonably considered that a purpose of a transaction was to unduly delay or avoid the application of the disbursement quota rules, particularly restricting the ability to meet the test by transferring amounts between non-arms length charities.

Universal Child Care Benefit for Single Parents

The budget proposes to allow a single parent the option of including the aggregate Universal Child Care Benefit amounts received in his/her income or in the income of the eligible dependent for whom an Eligible Dependent Credit is claimed. This proposal applies beginning in 2010.

Benefits Entitlement – Shared Custody

The budget proposes to allow two eligible individuals to each receive 50% of the Canada Child Tax Benefit, Universal Child Care Benefit, and GST/HST credit amounts in respect of a child who lives with both individuals, who live separately. This proposal applies for benefits payable beginning July 2011.

Medical Expenses Tax Credit – Purely Cosmetic

The budget clarifies that expenses incurred for purely cosmetic procedures will not be eligible to be claimed as a medical expense tax credit. Reconstructive and medically required cosmetic procedures will continue to be eligible.

Rollover of RRSP Proceeds to an RDSP

Beginning on March 5, 2010, the budget proposes to allow the rollover of a deceased individual’s RRSP proceeds into a Registered Disability Savings Plan (RDSP) of a financially dependent infirm child or grandchild. The RDSP beneficiary or his/her legal representative will be required to make an election to rollover the RRSP proceeds into a RDSP.

Transitional Rules

The budget proposes that when the death of an RRSP annuitant occurs after 2007 and before 2011, an eligible individual can make an election to contribute up to the amount of a deceased annuitant’s RRSP proceeds to an RDSP of a financially dependent infirm child or grandchild of the deceased.

Transitional Rules, continued

An offsetting deduction will be allowed in either the deceased’s terminal tax return or of the contributor’s tax return, if the RDSP contribution is made before 2012.

Carry Forward of RDSP Grants and Bonds

Beginning in 2011, the budget proposes to amend the Canada Disability Savings Act to allow a 10-year carry forward of Canada Disability Savings Grants (CDSGs) and Canada Disability Savings Bonds (CDSBs) entitlements.

Provincial Payments into RESPs and RDSPs

The budget proposes to clarify that all payments made to a Registered Education Savings Plan or a Registered Disability Savings Plan through a program funded or administrated by a province will not use up contribution room and will not attract federal grants and bonds.

Scholarship Exemption and Education Tax Credit

Beginning in 2010, the budget proposes to clarify that a post-secondary program that consists principally of research will be eligible for the education tax credit, and the scholarship exemption, only if it leads to a college or CEGEP diploma, or a bachelor, masters or doctoral degree (or an equivalent degree).

U.S. Social Security Benefits

The budget proposes to reinstate the 50% inclusion rate, currently 85%, for Canadian residents who have been in receipt of U.S. Social Security benefits since before January 1, 1996 and for their spouses and common-law partners who are eligible to receive survivor benefits. This change will apply for benefits received in 2010 or later.

International

Section 116 and Taxable Canadian Property

In the absence of a certificate being issued under Section 116, withholding taxes may apply when a non-resident disposes of taxable Canadian property even if the sale is tax exempt under a tax treaty. The budget narrows the definition of taxable Canadian property to exclude shares of corporations, and certain other interests, that do not derive their value from real or immovable property situated in Canada and resource properties. This measure will remove the section 116 compliance requirements for these types of properties which is more in line with our tax treaties.

A second proposal also fixes a technical issue which prevented taxpayers in certain situations from getting refunds of overpayments of tax withheld under section 105 of the Income Tax Regulations or section 116 of the Income Tax Act.

Foreign Investment Entities and Non-Resident Trusts

The government continues to make efforts to develop rules that will prevent Canadians from using foreign intermediaries to avoid paying their fair share of tax. As a result, the budget contained revised proposals for public consultation with respect to both foreign investment entities and non-resident trusts.

Foreign Tax Credit Generators

Foreign tax credit generators are schemes that artificially create foreign taxes to be claimed against Canadian taxes payable in respect of interest income on loans made, indirectly, to foreign corporations. The budget introduces new measures that will deny claims for certain foreign tax deductions and should generally put the Canadian corporation in the same tax position as it had made a simple loan to a foreign corporation.

Customs Tariff Measures

Remaining tariffs on manufacturing inputs and machinery and equipment will be eliminated. The Most-Favoured Nation rates of duty will be reduced to "Free" for 1,160 tariff items as of March 5, 2010 and 381 tariff items will have rates gradually decreasing to "Free" by no later than January 1, 2015.

GST/HST

Purely Cosmetic Procedures

The budget aims to clarify that all purely cosmetic medical and dental procedures, and any related property or services, are subject to GST. Cosmetic procedures for medical and reconstructive purposes will continue to be exempt.

Direct Selling Industry

The budget confirms the government's intention to implement proposals for the simplification of the GST/HST for the direct selling industry and includes several enhancements and clarifications to previously announced measures.

Specified Leasing Property Rules

The budget proposes to extend the application of the specified leasing property rules to otherwise exempt property that is the subject of a lease to a government, other tax-exempt entity, or a non-resident if the total property value under the lease is greater than \$1 million.

Tax Avoidance, Tax Evasion and the Proceeds of Crime and Money Laundering

The budget announces a public consultation on proposals to require the reporting (often where a promoter is involved) of certain tax avoidance transactions to the Canada Revenue Agency.

The budget repeals the exclusion of indictable tax offences under the Income Tax Act, the Excise Tax Act, the Excise Act, and the Budget Implementation Act, 2000 from the definition of designated offence under the Criminal Code. Thus, the Crown will be able to persecute tax offences using the proceeds of crime and money laundering regime.

Online Notices

The budget proposes to allow for the electronic issuance of certain notices that can currently be sent by ordinary mail. These notices include notices under the Income Tax Act, Excise Tax Act, Excise Act 2001, Air Travellers Security Charge Act, Canada Pension Plan and Employment Insurance Act. The Canada Revenue Agency will inform taxpayers how to provide authorization to receive notices electronically by email.



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