The J Thomas McCallum Letter

advancing the understanding of income tax and valuation matters

Federal Budget Edition March 19, 2007

This special release reviews only the income tax measures contained in today's federal budget. It also ignores the items already announced and re-iterated in the budget. Those interested in other aspects of the budget can download the budget document from www.budget.gc.ca/2007/index_e.html

Personal Tax Changes

Working Income Tax Benefit

Basic

It's estimated that more than 1.2 million Canadians will benefit from a new *refundable* tax credit of 20% of their earned income in excess of $3,000. The maximum credit will be $500 for single taxpayers who have no dependants and $1,000 for families, including single parents. "Earned income" is employment and business income, excluding losses.

The credit will be reduced by 15% of income in excess of $9,500 (single taxpayers) and $14,500 (families). The income 'cap' then is $12,833 for singles and $21,167 for families.

Single persons need to be at least 19-years of age at the end of the taxation year, but a single parent need only be the primary caregiver to a dependent child. Students without children will not be eligible for this tax credit if they are enrolled as full-time students for more than three months in the year.

Supplement

There will be a supplementary amount added for persons, other than dependants, who are eligible for the disability tax credit and who have at least $1,750 in earned income. Each $1 of income in excess of that will be eligible for an additional 20% tax credit (maximum $250).

Prepayment

Taxpayers who receive a GST credit will be eligible to apply for 50% of their anticipated WITB and have it paid with their quarterly GST credit.

Registered Disability Savings Plan

Those eligible for the disability tax credit, or their parents, will be able to establish a RDSP. There will be no annual limit on contributions — which will not be tax deductible — but there will be a $200,000 lifetime contribution limit. The beneficiary of the RDSP cannot be older than 59-years of age and must be the individual enabling the disability tax credit.

The government will provide matching grants (Canada Disability Savings Grant) of 100%, 200% and 300% depending on family income and RDSP contributions:—

- 300% on first $500 (up to $74,357 income)
- 200% on next $1,000 (same income level), and

- 100% on first $1,000 (over $74,357 income).

Additionally, Canada Disability Savings Bonds of up to $1,000 annually will be paid into the RDSPs of low-income families. The $1,000 CDSB will be paid to those with family income less than $20,833, and on a graduated basis for those with income up to $37,178.

There will be a lifetime limit of $20,000 paid as CDSBs and only up to and including the year the beneficiary of the RDSP turns 49-years of age.

Taxation

Withdrawals from the RDSP must begin the year the beneficiary turns 60 years of age. The non-deductible contributions will be returned tax-free but the grants, bonds and accumulated investment income (which was sheltered in the RDSP) will be taxable to the beneficiary. However, this will not count as income for income-tested benefits, such as the GST credit, delivered through the income tax system. The maximum annual withdrawal amount will depend on life expectancy and the fair market value of the RDSP; however, encroachments on capital/income will be permitted.

Private Foundations Added

The zero capital gains inclusion rate on publicly-traded securities which have been donated to public charities will be extended to those donated to private foundations. This begins with donations made after March 18, 2007. To avoid undesired consequences, limits will be placed on private foundation holdings.

Registered Educations Savings Plans

The $4,000 annual limit is eliminated and the lifetime limit is increased to $50,000 from $42,000. The maximum annual RESP contribution eligible for the 20% Canada Education Savings Grant is increased to $2,500 from $2,000, but the $7,200 lifetime maximum is unchanged..

For 2007 the RESP's Educated Assistance Payments system is revised for part-time students. A qualifying program will now be one requiring 12-hours per month, rather than 10-hours per week.

Personal Tax Amounts

The spouse/wholly dependent relative tax credit base amount will be increased (for 2007 on) so that it's the same as the basic personal tax credit amount.

Beginning in 2007 there will be non-refundable tax credit for each child under 18-years of age at the end of the year. The base amount for this credit is $2,000. Note: this is restoration of the 'old system' where a taxpayer could claim children as dependents.

The public transit credit will be revised to allow, rather than just monthly passes:—

- electronic payment cards which provide for at least 32 one-way trips in a 31-day period, and
- weekly passes, provided that passes have been purchased in at least 4 consecutive weeks

Scholarships
The 100% tax-free nature of scholarships and bursaries is extended (as of 2007) to those for elementary and secondary school.

Capital Gains Deduction
The CGD allowed on fishing property, farm property and small business shares is increased to $750,000 from $500,000 effective with dispositions after March 18, 2007.

RRSPs, RPPs and DPSPs
Beginning with 2007, the age limit is increased to 71 from the existing age 69 when it becomes mandatory to convert these plans to an annuity or other permitted option. Note: again this is a restoration of the 'old' system which went to age seventy-one.

The list of qualified investments permitted to be held by these plans is expanded as at March 19, 2007 to add two items.

Northern Residents Deduction
The NRD is expanded to include British Columbia's District Municipality of MacKenzie in the "intermediate zone". This will allow residents there to deduct one-half of the NRD.

The Vancouver Olympics
The *Income Tax Act* is to be amended for 2005 through 2011 to eliminate withholding taxes on certain income paid to the IOC and the IPC. The Act is further amended to exempt non-residents — athletes, Olympic team support staff, games officials, and accredited media — from Canadian tax on monies earned in the context of the Olympics. Lastly, there will be no customs duties, excise taxes, or GST/HST on goods imported in connection with the Olympics.

Mineral Tax Credit
The MTC, which was scheduled to expire at the end of March 2007, is extended to March 31, 2008.

Long Haul Truck Drivers
The deduction for meals by long-haul truckers (including employers) will be increased, starting in 2007, to 80% (rather than 50%) of their costs. This increase will be phased-in over a 5-year period:—

- 60% for meals in 2007 after March 18th
- then increasing by 5 points annually thereafter until 2011.

To be a long-haul truck the vehicle must have a GVW of greater than 11,788kg.

Only trips where the trucker is away at least 24-hours from their home terminal/city and the trip is beyond a radius of 160km from that point are eligible for this higher deduction.

Business Tax Changes

Capital Cost Allowances
The annual CCA rates for some assets are revised:—

- computers: increased from 45% to 55% for computers acquired after March 18, 2007

- natural gas distribution pipelines: increased from 4% to 6% for pipelines acquired after March 18, 2007

- liquid natural gas facilities (acquired after March 18, 2007): increased from 4% to 8%
- changes to many other items, generally energy-specific, were also made.

M&P Equipment/Machinery

Machinery and equipment used in manufacturing/processing which is acquired after March 18, 2007 but before 2009 will be eligible for a new *fast* write-off on a 50% straight-line basis, but with the half-year rule applied. This essentially means a three year write-off period.

Some Buildings

The CCA rate on buildings used in manufacturing/processing will be increased from 4% to 10%, and the CCA rate on non-residential buildings generally will be increased to 6% from 4%. These increases are brought in as additional or 'supplementary' allowances, which are [also] subject to the half-year rule.

In order to be eligible for this 'supplementary' CCA the building needs to be put into a separate Class. Taxpayers can continue to put the building into the 'old' Class but they'll lose the ability to claim the 'supplementary' CCA.

To be eligible for the 'supplementary' rate/Class at least 90% of the building, as measured by square feet, must be used for the designated purpose. If a building used for M&P doesn't qualify under that 90% usage rule, then it can still qualify for the 6% rate allowed for non-residential buildings as long as 90% is used for non-residential purposes.

The new rules on buildings apply to buildings acquired after March 18, 2007.

Donations of Medicine

Corporations which donate medicines from inventory, after March 18, 2007, will be allowed an *additional* deduction, set at the lesser of two measures. Only donations made under or pursuant to certain CIDA programs qualify.

Interest to/from the U.S.

The withholding tax on interest, currently 10% under the Canada-US Tax Treaty, will be reduced to zero over a three-year period, beginning the year after entry-into-force of the amendments to the Treaty.

International Tax 'Fairness'

An initiative paper was included with the Budget which includes a number of proposals relative to foreign affiliates and similar. These will be studied by a special committee of tax professionals, and eventually some or all of the proposals might find their way into law.

Prescribed Stock Exchanges

The current system of prescribed stock exchanges is to be replaced by new categories (which will serve different purposes):—

- designated stock exchanges
- recognized stock exchanges, and
- stock exchanges.

Child Care Space ITC

An investment tax credit will be provided to businesses for eligible expenditures (after March 18, 2007) incurred to create *licensed* child care space. The ITC will be 25% of the eligible expenses, with a maximum ITC of $10,000. All non-child care businesses are eligible for this ITC.

Remittances, Filing Thresholds

Starting with taxation years beginning after 2007, corporate tax instalments will only be required where the base amount is $3,000 rather than $1,000.

CCPCs which (in either the prior or current year) qualified for the small business deduction *and* whose taxable income didn't exceed $400,000 *and* whose taxable capital didn't exceed $10 million, will be eligible to pay their corporate tax instalments quarterly, rather than monthly, starting with the taxation year beginning after 2007.

Starting next year (2008) the threshold for individuals required to pay their income tax in quarterly instalments is increased to $3,000 from $2000.

The employer remittance of source deductions can be made quarterly, rather than monthly, if a threshold of $1,000 isn't exceeded. Beginning in 2008, that threshold is increased to $3,000.

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I will be presenting my annual Federal Budget Update for the Toronto Chapter of the Certified General Accountants Association of Ontario on May 24th at the Radisson Toronto East.