

On March 29, 2012 the Honourable Jim Flaherty, Minister of Finance, presented his seventh Budget to the House of Commons.

The Government's fiscal positions include deficits in the years 2011/2012 (\$24.9 billion), 2012/2013 (\$21.1 billion), 2013/2014 (\$10.2 billion), 2014/2015 (\$1.3 billion), and a surplus in 2015/2016 (\$3.4 billion), and 2016-2017 (\$7.8 billion).

The Federal Government notes that:

- \$500 million over five years, starting in 2014-15, will be provided to the Canada Foundation for Innovation to support advanced research infrastructure.
- The penny will no longer be produced as of Fall 2012. It currently costs 1.6 cents to produce each coin.
- EI premium rate increases will be limited to 5 cents each year until the EI Operating Account is balanced.
- System-wide legislative improvements to the review process for major economic projects (such as the Northern Gateway project) to achieve the goal of “one project, one review” will be completed.
- \$400 million will be provided to help increase private sector investments in early-stage risk capital, and to support the creation of large-scale venture capital funds led by the private sector.
- Changes to the administration of the Scientific Research and Experimental Development Program through measures such as determining the feasibility of a formal pre-approval process and enhancing the existing online self-assessment eligibility tool will occur.
- The One-For-One rule was implemented whereby with every new regulation must come the elimination of an existing one.

	Projection (in billions of \$)						
	2010 - 11	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
Budgetary revenues	237.1	248.0	255.0	270.4	285.5	300.0	312.5
Program expenses	239.6	241.9	245.3	249.4	253.9	261.7	268.6
Public debt charges	30.9	31.0	30.8	31.1	33.0	34.9	36.1
Total expenses	270.5	272.9	276.1	280.6	286.9	296.6	304.7
Budgetary Balance	(33.4)	(24.9)	(21.1)	(10.2)	(1.3)	3.4	7.8

Note: Totals may not add due to rounding.

TAX HIGHLIGHTS

A. Personal Income Tax

B. Business Income Tax

C. International Tax

D. Sales and Excise Tax

E. Other Tax Measures

F. Customs Tariff Measures

G. Canada Pension Plan

H. Previously Announced Measures



A. Personal Income Tax

1. Medical Expense Tax Credit

Budget 2012 proposes to add blood coagulation monitors for use by individuals who require anti-coagulation therapy, including associated disposable peripherals to the list of devices eligible for the Medical Expense Tax Credit when they are prescribed by a medical practitioner.

This is effective for expenditures after 2011.

2. Registered Disability Savings Plans (RDSP)

Budget 2012 proposes to allow, on a temporary basis, certain family members to become the plan holder of the RDSP for an adult individual, who might not be able to enter into a contract.

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This measure will not apply where an RDSP has already been established and will apply from the date of Royal Assent to the enacting legislation until the end of 2016.

Proportional Repayment Rule

Budget 2012 proposes to introduce a new proportional repayment rule that will apply when a withdrawal is made from an RDSP.

The new rule will require that, for each \$1 withdrawn from an RDSP, \$3 of any Canadian Disability Savings Grants (CDSGs) or Canadian Disability Savings Bonds (CDSBs) paid into the plan in the 10 years preceding the withdrawal be repaid, up to a maximum of the assistance holdback amount.

This measure will apply to withdrawals made from an RDSP after 2013.

Maximum and Minimum Withdrawals

Budget 2012 proposes to increase the maximum annual limit for withdrawals from PGAPs (primarily government-assisted plans) to the greater of the amount determined by the lifetime disability assistance payment (LDAP) formula and 10 percent of the fair market value of plan assets at the beginning of the calendar year.

Non-PGAP RDSPs will now be subject to the same minimum limits as that which is imposed on PGAPs.

Rollover of RESP Investment Income

Budget 2012 proposes to allow investment income earned in a Registered Education Savings Plan (RESP) to be transferred on a tax-free (or “rollover”) basis to an RDSP

if the plans share a common beneficiary.

To qualify, the beneficiary must meet the existing age and residency requirements in addition to one of 3 specified situations.

The amount of RESP investment income rolled over to an RDSP may not exceed, and will reduce, the beneficiary’s available RDSP contribution room.

This measure will apply to rollovers of RESP investment income made after 2013.

Termination of an RDSP following Cessation of Eligibility for the Disability Tax Credit (DTC)

Budget 2012 proposes to extend, in certain circumstances, the period for which an RDSP may remain open when a beneficiary becomes DTC-ineligible.

A medical practitioner must certify in writing that the nature of the beneficiary’s condition makes it likely that the beneficiary will, because of the condition, be eligible for the DTC in the foreseeable future.

To take advantage of this measure, the plan holder will be required to elect in prescribed form and submit the election, along with the written certification, to the RDSP issuer.

This measure will apply to elections made after 2013.

3. Mineral Exploration Tax Credit for Flow-Through Share Investors

Budget 2012 proposes to extend eligibility for the 15% mineral exploration tax credit, available to individuals who invest in flow-through shares in agreements entered

into on or before March 31, 2013. Funds raised in one calendar year with the benefit of the credit can be spent on eligible exploration up to the end of the following calendar year.

4. Eligible Dividends – Split-Dividend Designation and Late Designation

Budget 2012 proposes to allow the corporation to designate, at the time it pays a taxable dividend, any portion of the dividend to be an eligible dividend.

Budget 2012 also proposes to allow the Minister of National Revenue to accept a corporation’s late designation of a taxable dividend to be an eligible dividend if the corporation makes the late designation within the three-year period following the day on which the designation was first required to be made. The Minister must also be of the opinion that accepting the late eligible dividend designation would be just and equitable in the circumstances.

These measures will apply to taxable dividends paid on or after Budget Day.

5. Group Sickness or Accident Insurance Plans

Budget 2012 proposes to include the amount of an employer’s contributions to a group sickness or accident insurance plan in an employee’s income for the year in which the contributions are made to the extent that the contributions are not in respect of a wage-loss replacement benefit payable on a periodic basis.

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This measure will not affect the tax treatment of private health services plans or other plans described in Paragraph 6(1)(a) of the Income Tax Act.

This measure will apply in respect of employer contributions made on or after Budget Day to the extent that the contributions relate to coverage after 2012.

6. Retirement Compensation Arrangements (RCAs)

Budget 2012 proposes new prohibited investment and advantage rules to directly prevent RCAs from engaging in non-arm's length transactions. These rules will be based very closely on existing rules for Tax-Free Savings Accounts and Registered Retirement Savings Plans (RRSPs). As well, Budget 2012 proposes a new restriction on RCA tax refunds in circumstances where RCA property has lost value.

Special taxes on prohibited investments and advantages on property acquired before Budget Day will be eligible for special transitional rules.

7. Employee Profit Sharing Plans (EPSPs)

Budget 2012 proposes a special tax payable by a specified employee on an "excess EPSP amount". An "excess EPSP amount" will be the portion of an employer's EPSP contribution, allocated to a specified employee that exceeds 20 percent of the specified employee's salary received in the year. A "specified employee" generally includes an employee who has a significant equity interest in their employer or who does not deal at arm's length with their employer.

The special tax will be made up of

the top Federal marginal tax rate of 29 percent in addition to the top marginal tax rate of the province of residence of the specified employee. The excess EPSP amount will not also be subject to regular income tax. A specified employee will not be able to claim any other deductions or credits in respect of an excess EPSP amount.

This measure will apply in respect of EPSP contributions made by an employer on or after Budget Day, other than contributions made before 2013 pursuant to a legally binding obligation arising under a written agreement or arrangement entered into before Budget Day.

8. Life Insurance Policy Exemption Test

The exemption test that determines whether a life insurance policy is an exempt policy was implemented to differentiate protection-oriented life insurance policies from investment-oriented life insurance policies.

Budget 2012 proposes to implement changes to update and simplify the test.

Amendments will apply to life insurance policies issued after 2013.

9. OAS/GIS

Eligibility for Old Age Security (OAS) and Guaranteed Income Supplement (GIS) benefits will shift from 65 to 67. This change will start in April 2023, with full implementation by January 2029. Therefore, this will not affect persons aged 54 or older as of March 31, 2012.

Receipt of OAS pension will also be eligible for a voluntary deferral of up to 5 years.

B. Business Income Tax

1. Clean Energy Generation Equipment: Accelerated Capital Cost Allowance

Budget 2012 proposes to further expand Class 43.2.

Waste-fuelled thermal energy equipment no longer is limited by the requirement that the heat energy generated from the equipment is used in an industrial process or a greenhouse.

Equipment that is part of a district energy system that distributes thermal energy primarily generated by waste-fuelled thermal energy equipment will also be eligible for this class.

These measures will apply to assets acquired on or after Budget Day that have not been used or acquired for use before that date.

Energy Generation from Residue of Plants

Budget 2012 proposes to add the residue of plants to the list of eligible waste fuels (i.e., biogas, bio-oil, digester gas, landfill gas, municipal waste, pulp and paper waste, and wood waste) that can be used in waste-fuelled thermal energy equipment included in Class 43.2.

This measure will apply to assets acquired on or after Budget Day that have not been used or acquired for use before that date.

Environmental Compliance

Budget 2012 proposes that equipment using eligible waste fuels not be eligible under Class 43.1 or Class 43.2 if the applicable environmental laws and regulations of Canada or of a province, territory, municipality, or

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a public or regulatory body are not complied with at the time the equipment first becomes available for use.

This measure will apply to assets acquired on or after Budget Day.

Corporate Mineral Exploration and Development Tax Credit

Budget 2012 proposes to phase out the corporate tax credit for preproduction mining expenditures. The credit will apply at a rate of 10 percent for exploration expenses incurred in 2012, 5 percent in 2013 and not available thereafter.

The corporate tax credit for preproduction development expenses incurred before 2014 will be 10 percent, 7 percent for 2014, 4 percent for 2015, and not available thereafter.

Pre-production development expenses incurred by before 2016 will be allowed under limited special circumstances.

2. Atlantic Investment Tax Credit (AITC)

Oil, Gas and Mining Activities

Budget 2012 proposes to phase out the AITC for a specific list of oil and gas and mining activities over a four-year period.

In regards to these specific activities, AITC will apply at a rate of 10 percent for assets acquired before 2014 and at a rate of 5 percent for such assets acquired in 2014 and 2015. Transitional relief may be provided in recognition of the long timelines involved in some oil and gas and mining projects.

Electricity Generation Equipment

Budget 2012 proposes to include

certain electricity generation equipment and clean energy generation equipment used primarily in an eligible activity as “qualified property”. “Qualified property” will include the following equipment:

- electricity generation equipment described in Class 17 or 48; and
- clean energy generation and conservation equipment described in Class 43.1 or 43.2.

This measure will apply to assets acquired on or after Budget Day that have not been used or acquired for use before that date.

3. Scientific Research and Experimental Development (SR&ED) Program

SR&ED Investment Tax Credit Rate

Budget 2012 proposes to reduce the general 20 percent SR&ED investment tax credit rate applicable to SR&ED qualified expenditure pool balances at the end of a taxation year to 15 percent. The 15-percent investment tax credit rate will apply in respect of taxation years that end after 2013, and pro-rated based on the number of days in the taxation year that are after 2013. The enhanced and potentially refundable 35-percent SR&ED investment tax credit rate for eligible Canadian Controlled Private Corporations (CCPCs) will remain unchanged on up to \$3 million of qualified SR&ED expenditures annually.

SR&ED Capital Expenditures

Budget 2012 proposes to exclude expenditures of a capital nature from eligibility for SR&ED deductions and investment tax credits. This measure will apply to property acquired on or after January 1, 2014.

SR&ED Overhead Expenditures

Budget 2012 proposes to reduce the rate at which the prescribed proxy amount is calculated to 60 percent (from 65 percent) for 2013 and to 55 percent after 2013. The proxy rate for periods including days in 2012, 2013 or 2014 will be pro-rated.

SR&ED Contract Payments

Budget 2012 proposes to disallow from the expenditure base for investment tax credits the profit element of arm’s length SR&ED contracts. It is proposed that only 80 percent of the cost to a payer of arm’s length SR&ED contracts will be eligible for SR&ED investment tax credits.

This measure will apply to expenditures incurred on or after January 1, 2013.

4. Partnerships

Tax Avoidance Through the Use of Partnerships

Budget 2012 proposes two measures to ensure that partnerships cannot be used to circumvent the intended application of Sections 88 and 100.

The first measure will generally deny a Section 88 bump in respect of a partnership interest to the extent that the accrued gain in respect of the partnership interest is reasonably attributable to the amount by which the fair market value of income assets exceed their cost amount.

This measure will apply to amalgamations that occur, and windups that begin on or after Budget Day. An exception will be provided where an amalgamation occurs before 2013, or wind up begins before 2013 in certain circumstances.

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Budget 2012 also proposes to extend the application of Section 100 of the Income Tax Act to the sale of a partnership interest to a non-resident person thereby ensuring that income assets held by a partnership are fully taxable on the sale of the partnership by a taxpayer to a tax-exempt or non-resident person.

This measure will apply to dispositions, of interests in partnerships that occur on or after Budget Day. Exception may be provided for an arm's length disposition made by a taxpayer before 2013.

5. Partnership Waivers

Budget 2012 proposes that a single designated partner of a partnership may be empowered to waive, on behalf of all its partners, the three-year time limit for making a determination under Subsection 152 (1.4) of the Income Tax Act. Waivers would not be required from each partner.

The measure will apply on Royal Assent to the enacting legislation.

6. Hiring Credit

Budget 2012 extends the Hiring Credit for small business for one year (2012) to help small business to defray the costs of hiring new workers.

7. Canada Revenue Agency (CRA)

Written Responses to Business Enquiries

Responses will be able to be received via My Business Account.

Web Forms

The CRA'S Web Forms electronic filing application for information returns will be expanded.

My Business Account Portal

Portal will be enhanced to include items such as address changes.

Graduated Penalties for Late Filing

Administrative policy will be adopted.

8. Taxation of Corporate Groups

Economic Action Plan 2012 reaffirms the Government's commitment to continue exploring whether new rules for the taxation of corporate groups could improve the functioning of the corporate tax system.

C. International Tax

1. Transfer Pricing Secondary Adjustments

Budget 2012 proposes to amend Section 247 of the Income Tax Act to confirm that secondary adjustments will be treated as dividends for Part XIII tax purposes.

2. Thin Capitalization Rules

The thin capitalization rules limit the deductibility of interest expense of a Canadian-resident corporation in circumstances where the amount of debt owing to certain non-residents exceeds a 2-to-1 debt-to-equity ratio.

Budget 2012 proposes to reduce the debt-to-equity ratio from 2-to-1 to 1.5-to-1, extend the scope to debts of partnerships, treat disallowed interest expense dividends for Part XIII withholding tax purposes, and prevent double taxation where a Canadian resident corporation borrows money from its controlled foreign affiliate.

3. Foreign Affiliate Dumping

Budget 2012 proposes that, where certain conditions are met, a divi-

dent will be deemed to be paid by a Canadian subsidiary to its foreign parent to the extent of any non-share consideration given by the Canadian subsidiary for the acquisition of the shares of a foreign affiliate. Any deemed dividend will be subject to non-resident withholding tax.

This measure will apply to transactions that occur on or after Budget Day, other than transactions that occur before 2013 between parties that deal at arm's length and that are obligated by an agreement in writing entered into before Budget Day.

4. Overseas Employment Tax Credit (OETC)

Budget 2012 proposes to phase out the OETC over four taxation years, beginning with the 2013 taxation year. The factor (currently 80 percent) applied to an employee's qualifying foreign employment income in determining the employee's OETC will be reduced to 60 percent for the 2013 taxation year, 40 percent for 2014, 20 percent for the 2015 and not available thereafter.

These phase-out rules will not apply to projects or activities to which the employee's employer had committed in writing before Budget Day.

D. Sales and Excise Tax

1. Health Care Sector

Budget 2012 proposes to apply the following changes relating to the health care sector.

Pharmacist's Services

To exempt from the GST/HST services rendered by pharmacists within a pharmacist-patient relationship for the promotion of the patient's health or for the prevention or treatment of

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a disease, disorder or dysfunction of the patient (Pharmacists' services of dispensing prescription drugs will continue to be zero-rated). Measures will apply to supplies made after Budget Day.

Corrective Eyewear

To zero-rate corrective eyeglasses or contact lenses supplied under the authority of an assessment record produced by a person who is entitled under the laws of the province in which the person practices to produce the record authorizing dispensing of corrective eyewear.

This measure will apply to supplies made after Budget Day and to supplies made on or before that day if GST/HST was not charged, collected or remitted in respect of the supply.

Blood Coagulation Monitoring Devices

To add blood coagulation monitoring or metering devices and associated items to the zero-rated medical device list.

This measure will apply to supplies made after Budget Day.

Medical and Assistive Devices Supplied on Written Order

To zero-rate supplies of the devices, that currently qualify for zero-rating only when supplied on the written order of a medical practitioner, when supplied on the written order of a registered nurse, occupational therapist or physiotherapist as part of their professional practice.

This measure will apply to supplies made after Budget Day.

2. GST Rebate for Books to be Given Away for Free by Prescribed Literacy Organizations

Budget 2012 proposes to allow charity and qualifying non-profit literacy organizations prescribed by regulation to claim a rebate of the GST (and the Federal portion of the HST) they pay to acquire printed books to be given away.

This measure will apply to acquisitions and importations of printed books in respect of which tax becomes payable after Budget Day.

3. Doubling GST/HST Streamlined Accounting Thresholds

Budget 2012 proposes to double the existing streamlined accounting thresholds as follows:

- Quick Method - the annual taxable sales threshold at or below which eligible businesses can elect to use this method will increase to \$400,000 (from \$200,000) of GST/HST-included taxable sales; and
- Streamlined Input Tax Credit Method - the annual taxable sales and taxable purchases thresholds at or below which businesses or Public Service Bodies (PSBs) can elect to use this method will increase.
 - to \$1,000,000 (from \$500,000) of taxable sales, and
 - to \$4,000,000 (from \$2,000,000) of taxable purchases.

This measure will be effective in respect of a GST/HST reporting period of a person (or a claim period of a person, in the case of the Prescribed Method for Calculating Rebates) beginning after 2012.

4. Tax Relief for Foreign-Based Rental Vehicles Temporarily Imported by Canadian Residents

Budget 2012 proposes to:

- fully relieve GST/HST on foreign-based rental vehicles temporarily imported by Canadian residents who have been outside Canada for at least 48 hours;
- levy GST/HST on a partial basis, as described below, on foreign-based rental vehicles temporarily imported by Canadian residents who have not been outside Canada for at least 48 hours;
- fully relieve the Green Levy and the automobile air conditioner tax on all foreign-based rental vehicles temporarily imported by Canadian residents.

This measure will apply to impact on or after June 1, 2012.

5. Consistent Application of the Green Levy on Fuel-Inefficient Vehicles

Budget 2012 proposes that the Excise Tax Act be amended so that the weighted average fuel consumption rating for the purposes of the Green Levy continues to be determined by reference to the current test method. Amendments will apply on Royal Assent to the enacting legislation.

E. Other Tax Measures

1. Gifts to Foreign Charitable Organizations

Budget 2012 proposes to modify rules for registering certain foreign charitable organizations as qualified donees. Foreign charitable organizations that receive a gift from the Government may apply for qualified donee status if they pursue activities:

- related to disaster relief or urgent humanitarian aid; or
 - in the national interest of Canada.
- Qualified donee status will be granted for a 24-month period.

This measure will apply to applications made by foreign charitable organizations on or after the later of January 1, 2013 and Royal Assent to the enacting legislation.

Intermediate Sanctions

Budget 2012 proposes to grant to the CRA the authority to suspend for one year the tax-receipting privileges of a charity that exceeds the limitations on political activities. It is also proposed that CRA be granted authority to suspend the tax-receipting privileges of a charity that provides inaccurate or incomplete information in its annual information return until the charity provides the required information.

2. Funding of Political Activities

Budget 2012 proposes that, where a gift is made by a charity and it can reasonably be considered that a purpose of the gift is to support the political activities of a qualified donee, the gift will be considered to be an expenditure made by the charity on political activities.

3. Tax Shelter Administrative Changes

Budget 2012 proposes to encourage tax shelter registration and reporting by:

- modifying the calculation of the penalty applicable;
- introducing a new penalty for a promoter who fails to meet their reporting obligations; and
- limiting the period for which a tax shelter identification number is valid to one calendar year.

4. Aboriginal Tax Policy

The Government reiterates its willingness to discuss and put into effect direct taxation arrangements with interested Aboriginal governments.

F. Customs Tariff Measures

1. Trade Measures to Support the Energy Industry

Budget 2012 will eliminate the 5 percent Most-Favoured-Nation (MFN) rate of duty on certain imported oils.

This tariff elimination will be effective in respect of goods imported on or after March 30, 2012.

2. Travellers' Exemptions

Budget 2012 proposes to increase the travellers' exemption (exemption which allows returning residents to bring back goods valued up to a specified dollar limit without having to pay duties) to \$200 from \$50 for those who are out of the country for 24 hours, and exemption levels from \$400 to \$800 for 48 hours or more.

The new exemption levels will be effective June 1, 2012.

G. Canada Pension Plan (CPP)

Prior to the 2012 Federal Budget, several significant changes were made to the CPP, most of which took effect on January 1, 2012. For example, workers aged 65 to 70 may be subject to CPP unless they elect otherwise.

This affects employees, employers, self-employed persons, and CPP recipients.

See the HRSDC website (www.hrsdc.gc.ca) or contact us for details.

H. Previously Announced Measures

Budget 2012 confirms the Government's intention to proceed with the following previously announced tax and related measures:

- July 16, 2010 proposals relating to income tax technical amendments;
- August 27, 2010 and August 19, 2011 proposals relating to foreign affiliates;
- November 5, 2010, income tax technical amendments proposals;
- December 16, 2010, real estate investment trusts proposals;
- January 28, 2011, GST/HST rules relating to financial institutions;
- March 16, 2011 proposals relating to deductibility of contingent amounts, withholding tax on interest paid to certain non-residents, and certain life insurance corporation reserves;
- July 20, 2011 measures relating to specified investment flow-through entities.
- October 31, 2011 income tax sales and excise tax technical amendments;
- November 10, 2011 caseload management of the Tax Court of Canada measures;
- GST/HST amendments to accommodate the Pooled Registered Pension Plans;
- December 29, 2011, Automobile expense amounts for 2012;
- February 17, 2012, transitional



rules for the elimination of the Harmonized Sales Tax in British Columbia.

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The preceding information is for educational purposes only. As it is impossible to include all situations, circumstances and exceptions in a newsletter such as this, a further review should be done by a qualified professional.

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