

JANUARY 2009 FEDERAL BUDGET COMMENTARY

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As widely expected, the Budget delivered on January 27th presented a broad package of provisions intended to stimulate the economy through dramatically increased spending on infrastructure and targeted programs. It also proposes a variety of tax measures aimed at increasing consumer spending and business investment, boosting employment, and providing some relief to those most affected by the current downturn.

The Budget signals the return of federal budget deficits. Deficits are forecast of almost \$34 billion for fiscal year 2009-10 and almost \$30 billion in 2010-11, although a small budget surplus is predicted by 2013-14.

In aggregate, the Budget proposes a series of new programs and tax incentives totaling approximately \$34.8 billion over two years, including \$7 billion of new spending on infrastructure such as roads, bridges, public transport, college and university upgrades, social housing, broadband Internet access and renewable-energy projects. Other stimulus measures include \$8 billion allocated for training and skills development, including a doubling of the Working Income Tax Benefit, and increased program spending of \$160 million for culture, \$302 million for heritage and tourism and \$170 million for forestry programs, as well as incentives targeted at farming, media, entertainment and small businesses. In addition, to help ease credit pressures, a variety of measures, including a new Extraordinary Financing Network, will give individuals and businesses access to up to \$200 billion in liquidity and financing.

Whether or not the Budget will pass in its present form is uncertain. The Liberal Party has announced they will seek amendments to the Budget, while the NDP and the Bloc are committed to voting against it.

PERSONAL TAX MEASURES

Personal Income Tax Rates

The previously announced federal personal tax brackets for 2009, based on taxable income, were as follows:

- 15% on the first \$38,832
- 22% between \$38,832 and \$77,664
- 26% between \$77,664 and \$126,264
- 29% over \$126,264

This Budget proposes the following increased personal tax brackets for 2009:

- 15% on the first \$40,726 (federal tax saving of \$132)
- 22% between \$40,726 and \$81,452 (federal tax saving of \$76)
- 26% between \$81,452 and \$126,264 (no tax saving)
- 29% over \$126,264 (no tax saving)

These tax brackets will be indexed to account for inflation in 2010 and subsequent years.

Basic Personal Amount

The basic personal amount, the spouse or common-law partner amount and the eligible dependant amount will be increased to \$10,320 (from \$10,100) for the 2009 taxation year and indexed to inflation for subsequent years. This will result in a federal tax savings of \$33 in 2009 for each applicable credit.

Age Credit

For 2009, the amount on which the age credit is based will be increased from \$5,408 to \$6,408, and indexed thereafter. This increase will provide up to an additional \$150 of federal tax savings, depending upon the individual's taxable income for the year. The income level at which

this credit is fully phased out will increase from \$68,365 to \$75,032.

Home Renovation Tax Credit (HRTC)

The Budget proposes a 15% non-refundable tax credit to individuals for eligible expenditures in excess of \$1,000 and less than \$10,000 made in respect of eligible dwellings. This will result in a maximum federal credit of \$1,350 (\$9,000 x 15%).

Work must be performed or goods acquired between January 28, 2009 to January 31, 2010. However, the credit will not be available for expenditures pursuant to an agreement entered into prior to January 28, 2009. The credit may be claimed on an individual's 2009 personal tax return, even with respect to qualifying expenditures incurred in 2010.

A renovation or alteration of an eligible dwelling qualifies for the HRTC provided it is of an enduring nature and is integral to the dwelling, including expenditures for the cost of labour and professional services, building materials, fixtures, equipment rentals and permits. Expenditures which do **not** qualify for the HRTC include (a) the cost of routine repairs and maintenance normally performed on an annual or more frequent basis, (b) expenditures for appliances and audio-visual electronics, and (c) financing costs.

Items such as furniture, draperies and other indirect expenditures for items that retain a value independent of the renovation, such as construction equipment and tools, will not qualify since they will not be considered integral to the dwelling.

Expenditures must be supported by receipts. Goods or services provided by a non-arm's length person will qualify only if that person is registered for GST purposes.

Home Buyers' Plan

The maximum eligible withdrawal permitted from an RRSP has been increased from \$20,000 to \$25,000 after January 27, 2009.

First-time Home Buyer's Tax Credit

The Budget proposes a new non-refundable tax credit for first-time home buyers who acquire a qualifying home after January 27, 2009. The tax credit is 15% of \$5,000 (or \$750 for 2009) and is claimable in the year in which the home is acquired.

A person will qualify as a first-time home buyer if neither the individual nor his or her spouse or common-law partner owned and lived in another home in the year of the home purchase, or in any of the previous four years. A qualifying home is one which the individual or the spouse or common-law partner intend to occupy as their principal residence within one year after acquisition. To be eligible for the credit, the home must be registered under the Ontario's land registration system.

RRSP/RRIF Losses After Death

In the absence of a spousal or dependant rollover, the fair market value of investments held in an RRSP or RRIF at the time of an annuitant's death is included in the income of the deceased for the year of death.

The Budget proposes to allow a deduction for a decrease in value of the investments held in an RRSP or RRIF subsequent to the annuitant's death and upon the final distribution of the property. This deduction would 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.

BUSINESS MEASURES

Small Business Deduction (SBD)

The SBD reduces the federal corporate income tax rate to 11% on the first \$400,000 of qualifying active business income earned by a group of associated companies in a year. The Budget proposes to increase this limit to \$500,000 for taxation years ending after December 31, 2008. For taxation years that straddle December 31, 2008 the \$100,000 increase is prorated based on the number of days after December 31, 2008.

Scientific Research and Experimental Development (SR&ED)

Corporations may earn enhanced investment tax credits (ITCs) equal to 35% of qualified current SR&ED expenditures and 40% of qualified capital SR&ED expenditures. The combined maximum amount of qualified SR&ED expenditures cannot exceed \$3 million. The Budget proposes that for taxation years that end after 2009, this entitlement will be phased out when taxable income is between \$500,000 (versus \$400,000) and \$800,000 (versus \$700,000) in the preceding taxation year. The phase-out will be prorated for taxation years that straddle December 31, 2008. The existing rule to phase out the entitlement to the enhanced ITC for taxable capital between \$10 and \$50 million is unaffected.

These enhanced ITCs may be fully refundable if the corporation does not have sufficient taxable income to utilize them. Similar rules as above reduce refundability to the extent that a corporation's taxable income exceeds \$500,000 (versus the current \$400,000).

Capital Cost Allowance (CCA)

Taxpayers acquiring new manufacturing equipment after March 19, 2007 and before 2010 are able to treat these assets as Class 29 assets (50% straight-line CCA rate, subject to the half-year rule). The Budget proposes to extend this treatment to qualifying assets acquired in 2010 and 2011.

Eligible computers and software acquired after January 27, 2009 and before February 2011 will be eligible for a 100% write-off in the first year the equipment is available for use.

COMPLIANCE

Electronic Filing of Corporate Income Tax Returns

The Budget proposes corporations with gross revenue exceeding \$1 million (other than atypical situations, such as non-resident corporations and corporations reporting in a functional currency) must file their T2 corporate income tax returns electronically for taxation

years ending after 2009. Failure to comply with these rules will make offending corporations liable for penalties depending on the corporation's year-end. The penalties will be \$250 in 2011, \$500 in 2012, and \$1,000 in subsequent years. These penalties will also apply for filing returns in an incorrect format.

Ward & Uptigrove intends to commence the electronic filing of corporate returns this summer, in advance of this requirement.

Information Returns

There will be a lower threshold requiring taxpayers to file information returns (such as T4s) electronically after 2009. The new threshold for T4s will be 50 (versus the current 500). Failure to comply with these new rules will make a taxpayer liable for a penalty, based on the number of information slips.

AGRICULTURE

Although no details were released, the government will implement a five year, \$500 million agricultural flexibility program for new initiatives. It will also work with interested provinces to improve client service for the delivery of the AgriStability program.

The Budget announced amendments to the Farm Improvement and Marketing Cooperatives Loans Act to help make credit available to new farms, support inter-generational farm transfers, and modify eligibility criteria for agricultural cooperatives.

Prior to the Budget release, the government announced an extension to repay cash advances under the Advance Payment Program (APP) to September 30, 2010. The first \$100,000 in advances remain interest-free. Producers can still apply for APP emergency advances until March 31, 2009. Regular APP advances continue to be available. Starting in April of 2009, producers meeting eligibility criteria can apply for 2009-2010 regular advances.