2009 Federal Budget Summary

Cunningham
Chartered Accountants

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www.cunninghamca.com

On January 27, 2009, the Honourable Jim Flaherty, Minister of Finance, delivered what was easily the most anticipated budget in recent years. From a tax initiatives perspective, there are few substantive measures proposed in the Budget.

The private, owner-managed business is vital to the health and success of the Canadian economy and we believe that the government fell short in providing significant tax relief to these taxpayers. In an attempt to kick start the economy though, the Budget did allocate money to infrastructure spending and included measures to strengthen credit for Canadian individuals and companies that require funds to invest, grow and create new jobs. Unfortunately the cost of these spending measures will be massive deficits in future years.

Corporate Income Tax Measures

Increase to the Federal Small Business Deduction Limit

The 2009 Budget proposes to increase the Federal Small Business Deduction Limit from $400,000 to $500,000 effective January 1, 2009. The Small Business Deduction Limit is the income amount that is afforded the lowest Federal corporate income tax rate of 11% (a combined rate of 16.5% in Ontario) on active business income that is earned by a corporation.

Concurrently, the Budget proposes to increase the income level where the enhanced 35% rate for purposes of claiming the scientific research and experimental development ("SR&ED") investment tax credit is reduced. The SR&ED expenditure limit will now be reduced when the taxable income of the associated group of companies reaches $500,000 for the prior year and will be completely eliminated when income exceeds $800,000 for the prior year.

As a result of the increase to the Federal Small Business Deduction Limit, some companies may now be eligible to pay any corporate income tax balance owing, 3 months after its fiscal year-end, rather than two months, and may be eligible for quarterly, rather than monthly, tax instalments.

Capital Cost Allowance ("CCA") Changes and Extensions

Manufacturing and Processing ("M&P") Machinery and Equipment

The Budget proposes that the temporary 50% straight-line CCA rate on M&P machinery and equipment announced in the 2008 Budget be extended to M&P machinery and equipment acquired in 2010 and 2011. Previously, the accelerated straight-line CCA rate was to apply only to acquisitions of M&P machinery and equipment made before 2010 with declining balance CCA rates to apply to 2010 and 2011 acquisitions. The "half-year rule" will continue to be applicable to M&P assets acquired subject to this measure.

Computer Equipment

The Budget proposes a temporary 100% CCA rate for eligible computers and software acquired after January 27, 2009 and before February 1, 2011. The "half-year rule" will not apply to computer acquisitions made in this period thereby allowing a full deduction of the purchase cost in the year of acquisition. The computers acquired must be situated in Canada.

Electronic Filing and Penalties

The Budget proposes to make electronic filing of corporate income tax returns mandatory for fiscal tax years that end after 2009. Electronic filing will apply to corporations with annual gross revenues over $1 million.

The penalty for filing a corporate income tax return in an incorrect format will be $250, $500 and $1,000 for fiscal years ending in 2011, 2012 and thereafter, respectively.

The number of any type of tax information return that can be electronically filed is to be reduced from 500 to 50. This measure will apply to returns required to be filed after 2009. It is expected that this measure will most often apply in respect of T4 information returns and slips.

Penalties for late electronically filed information returns will now be calculated based on the number of type of information returns required, rather than on the actual number of information returns filed.

Personal Income Tax Measures

Personal Tax Bracket Changes

The Budget proposes to increase the basic personal exemption amount and the two lowest personal income tax brackets by 7.5% effective January 1, 2009. In dollar terms, the basic personal exemption amount will increase from $9,600 in 2008 to $10,320 in 2009.

The upper limit for the first personal income tax bracket (15% Federal income tax rate) will increase from $37,885 in 2008 to $40,726 in 2009. The upper limit of the next income tax bracket (22% Federal income tax rate) will increase from $75,769 in 2008 to $81,452 in 2009. The increased amounts and income tax bracket thresholds will be indexed for inflation in subsequent years.

Age Credit

The Budget proposes to increase the Age Credit for Canadians 65 years of age and older for 2009 and subsequent years. For 2009, the Age Credit will increase by $1,000 to $6,408 from the current $5,408. There is no corresponding increase in the $32,312 net income level at which the Age Credit begins to be phased out; however, the upper limit at which the Age Credit is fully phased out will rise to $75,032 from the current level income level of $68,365.

Home Renovation Tax Credit

The government proposes to provide a non-refundable personal income tax credit for home renovation costs exceeding $1,000 up to a maximum of $10,000. This will result in a maximum Federal credit of $1,350. Work must be performed after January 27, 2009 and before February 1, 2010 and relate to a renovation or alteration of an enduring nature. It appears that eligible expenditures would include costs associated with renovating a basement, replacing a furnace or windows and building a deck. Expenditures not eligible for the new credit would include: routine repairs and maintenance normally performed on an annual or more frequent basis, appliances, audio-visual equipment and financing costs. Only renovations to the family's principal residence are eligible and only one claim can be made per family. Any eligible expenditures claimed must be supported by receipts.

Home Buyers Plan

The amount that first time home buyers can withdraw tax-free from their Registered Retirement Savings Plan ("RRSP") to purchase or build a new home will increase from $20,000 to $25,000. This is effective for RRSP withdrawals after January 27, 2009.

First Time Home Buyers' Tax Credit

First time home buyers will be entitled to a non-refundable personal income tax credit in connection with a home acquired after January 27, 2009. The credit, worth $750 in tax savings, is available only to first time home buyers and must be shared where more than one individual purchases the dwelling. The credit will also be available for purchases of dwellings by or for the benefit of individuals eligible for the disability tax credit in certain situations.

RRSP/Registered Retirement Income Fund ("RRIF") Losses after Death

In the year of death, a taxpayer's representative is required to include in the deceased taxpayer's final tax return (known as the "terminal return") the fair market value of the investments held in the deceased taxpayer's RRSP or RRIF. Any subsequent increase in the value of the RRSP/RRIF investments are generally included in the income of the beneficiaries of the RRSP or RRIF upon distribution or taxed in a return for the estate of the deceased. Losses from the date of death are currently considered "nothings" for income tax purposes.

The Budget proposes to allow, upon final distribution of the deceased's RRSP/RRIF, any loss in value post-death to be carried back to the terminal return and deducted against the income inclusion on death. This initiative will apply where the final distribution occurs after 2008.

Other Tax Related Measures

- Employment Insurance rates in 2010 will be frozen at 2009 levels ($1.73 per $100);

- The Budget proposes to correct an anomaly in the Income Tax Act retroactive back to 2006 which currently may prevent individuals from claiming certain tax benefits (namely, the Lifetime Capital Gains Exemption) when shares of a company are sold at a specific time in the day, but the Income Tax Act deems the shares sold at the commencement of the day;

- The Mineral Exploration Tax Credit on flow-through shares, which was set to expire on March 31, 2009, will be extended until March 31, 2010;

- Based on advice provided by the Advisory Panel on Canada's System of International Taxation, the government has proposed to repeal legislation which would have prevented Canadian companies from deducting interest in situations where the borrowed funds were used to finance foreign affiliates and the interest was also deductible in a foreign jurisdiction (i.e. "double dipping" financing structures);

- Again, based on advice from the Advisory Panel on Canada's System of International Taxation, the government will reconsider the proposed tax measures in connection with foreign investment entities, non-resident trusts and foreign affiliates.

2001 Sheppard Avenue E., Suite 810, Toronto, ON M2J 4Z8
Tel: (416) 496-1051 Fax: (416) 496-1546 Toll Free: 1-800-461-4618