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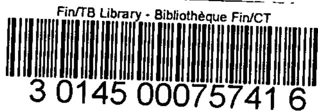
Budget Papers

Notices of Ways and Means Motions
and supplementary information
on the Budget

November 16, 1978

Department of Finance
Canada

Ministère des Finances
Canada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Notice of Ways and Means Motion

Income Tax Act

Notice of Ways and Means Motion To Amend the Income Tax Act

That it is expedient to amend the Income Tax Act and to provide among other things:

Employment Expense Deduction

(1) That for the 1979 and subsequent taxation years, the maximum amount that may be claimed as an employment expense deduction be increased to $500.

Investment Tax Credit

(2) That the investment tax credit be modified in the following ways:

(a) the credit be extended by repealing the June 30, 1980 termination date for qualifying property and expenditures,

(b) the credit be increased for qualifying property acquired after November 16, 1978 to 7%, 10% and 20% depending on location of use of the qualified property in Canada,

(c) a credit of 7% apply to acquisitions after November 16, 1978 of prescribed transportation equipment for use in a taxable business carried on in Canada, and

(d) the credit for eligible current and capital scientific research expenditures incurred after November 16, 1978 be increased

(i) to 25% for a Canadian-controlled private corporation which qualifies in the year in which the expenditure is made for the small business deduction, and

(ii) in any other case, to 20% for research carried on in the Atlantic provinces and the Gaspé Peninsula of Quebec and 10% for research carried on elsewhere in Canada.

Employment Tax Credit of Cooperative Corporations

(3) That for taxation years ending after November 16, 1978, a cooperative corporation be required to include in its income for a year the employment tax credit to the extent that it offsets the deduction at source on patronage dividends.

Inventory Adjustment

(4) That for taxation years ending after November 16, 1978, an annual inventory adjustment be introduced

(a) requiring the inclusion in income for a year of an amount equal to the depreciation, obsolescence or depletion included in the cost of the inventory on hand at the end of the year or its fair market value, whichever is lower, and

(b) permitting the deduction of that amount in the following year.

Investment Tax Credit of Cooperative Corporations (5) That for taxation years ending after November 16, 1978, a cooperative corporation be required to reduce the cost of property to it to the extent that its investment tax credit offsets the deduction at source on patronage dividends.

Income Bonds and Income Debentures (6) That with respect to payments on income bonds or income debentures made after November 16, 1978, the reference in subsections 15(3) and 15(4) of the Act to "an annual or other periodic amount" be replaced by a reference to "interest or dividends."

Interest and Taxes on Land (7) That the Act be amended to permit a deduction for interest and property taxes incurred after November 16, 1978 with respect to land held primarily for the purpose of resale or development by a taxpayer in the ordinary course of his business.

Underwriting Expenses (8) That

(a) a unit trust be permitted to deduct expenses incurred after November 16, 1978 in the course of issuing its units, and

(b) a commission, bonus, fee or other amount paid or payable after November 16, 1978 for or on account of services rendered by a person as a salesman, agent or dealer in securities in the course of selling shares or units or borrowing money be permitted as a deduction.

Interest on Borrowed Funds (9) That for the 1978 and subsequent taxation years, in computing his income, a taxpayer be entitled to deduct interest paid on money borrowed before 1978 to purchase an annuity contract before 1978 provided that

(a) the money was not borrowed from the issuer of the contract, and

(b) annuity payments under the contract commence not later than the date on which the annuitant becomes 75 years of age.

Crown Corporations (10) That for the 1978 and subsequent taxation years, the tax status of any crown corporation specified in Schedule D to the *Financial Administration Act* be extended to any corporation it controls.

Restricted Farm Loss (11) That for taxation years ending after 1977, the additional allowance for scientific research not be limited by the rules in section 31 of the Act relating to restricted farm losses.

Research Allowance (12) That for taxation years ending after 1977 and before 1989, in determining the research allowance,

(a) qualified expenditures on scientific research in Canada be reduced by government grants only to the extent that they relate to qualified expenditures on a research property, and

(b) qualified expenditures include the repayment of government research grants.

Definition of Capital Loss and Business Investment Loss (13) That for the 1978 and subsequent taxation years,

(a) the definition of capital loss in paragraph 39(1)(b) of the Act be amended to include a business investment loss, and

(b) the definition of business investment loss in paragraph 39(1)(c) of the Act be amended to exclude the loss on any share issued before 1972 or any share substituted or exchanged therefor.

Registered Retirement Income Funds

(14) That for the 1978 and subsequent taxation years, a right to any payment under a registered retirement income fund be excluded from the property to which subsection 48(1) of the Act applies when a person ceases to be resident in Canada.

Capital Loss

(15) That where subsection 85(4) of the Act denies a capital loss on the disposition of a property to a corporation, subsection 53(1) of the Act be amended

(a) in the case of a disposition after March 31, 1977, to permit the disallowed loss to be added to the corporation's cost of the property where the vendor does not own shares of the corporation, and

(b) in the case of a disposition after 1971, to ensure that the disallowed loss is added to the vendor's cost of the shares where he owns shares of the corporation.

Termination Payments

(16) That an amount not otherwise included in income and received with respect to the termination after November 16, 1978 of an office or employment be included in the recipient's income except to the extent that it exceeds one-half of the employee's remuneration for a preceding twelve month period.

Unemployment Insurance Benefit Repayments

(17) That for the 1979 and subsequent taxation years,

(a) the benefit repayment of an unemployment insurance claimant be deductible in computing the taxable income of the claimant for the taxation year to which the benefit repayment relates, and

(b) such benefit repayment not be deductible in computing the claimant's income for the taxation year in which it is paid

provided that an Act entitled *"An Act to amend the Unemployment Insurance Act, 1971"* is assented to during the Fourth Session of the Thirtieth Parliament.

Income-Averaging Annuity Contract

(18) That for the 1979 and subsequent taxation years, the amount qualifying for the purchase of an income-averaging annuity contract by an individual in a year be reduced by his allowable business investment loss for the year.

Canadian Exploration Expense

(19) That the provisions of the Act permitting the deduction of Canadian exploration expenses incurred before July, 1979 by individuals and non-principal-business corporations be extended to expenses incurred before 1982.

Mine Development Expense

(20) That expenses incurred after November 16, 1978 relating to the development of a mine qualify as Canadian exploration expense.

Oil and Gas Well Recompletion Expenses

(21) That

(a) the definitions of Canadian development expense and Canadian exploration expense be clarified to ensure that, for taxation years ending after May 6, 1974, they include the expense of completing an oil or gas well in Canada, and

(b) the definition of Canadian development expense be extended to include expenses relating to the recompletion of an oil or gas well in Canada incurred after November 16, 1978.

Cumulative Canadian Development Expense

(22) That for the 1977 and subsequent taxation years, where a successor or second successor corporation has acquired a resource property from another corporation, any proceeds from its disposition be deducted from the cumulative Canadian development expense so acquired.

Successor Corporation

(23) That the rules in sections 66, 66.1 and 66.2 relating to predecessor, successor and second successor corporations apply to an acquisition of property after November 16, 1978 only if the purchaser and vendor elect jointly to have the rules apply.

Storage Rights

(24) That, after November 16, 1978, a right, licence or privilege to store petroleum, natural gas or other related hydrocarbons be included in the definition of Canadian resource property.

Exploration and Development Expenses

(25) That after Royal Assent to any measure giving effect to this paragraph, the references to associations and syndicates be deleted in the definitions of "foreign exploration and development expenses", "Canadian exploration expense" and "Canadian development expense".

Winding-up of a Corporation

(26) That subsection 69(5) of the Act be amended to ensure that the rules in subsection 85(4) of the Act not apply to an appropriation of property to shareholders after November 16, 1978 on the winding-up of a corporation.

Definition of Small Business Corporation

(27) That, for the purposes of the rules relating to the transfer after May 25, 1978 of shares of a small business corporation,

(a) a qualified business be defined as an active business within the meaning of section 125 of the Act as modified by paragraph (42) of this Motion, and

(b) the definition of small business corporation be amended to include a Canadian-controlled private corporation whose property consisted both of assets used in a qualified business and of shares of one or more other small business corporations connected with it.

Small Business Corporation

(28) That for transfers after November 16, 1978 of shares of a small business corporation, the rules in subsection 73(5) of the Act be applicable only if the attribution rules in subsection 74(2) of the Act do not apply thereto.

Housing Loans

(29) That the definition of housing loan be amended to exclude a loan made at any time after November 16, 1978 to an individual if, immediately after that time, his spouse had a housing loan.

Provincial Indemnities

(30) That any indemnity received after 1977 by an individual under prescribed provisions of provincial law be exempt.

Non-Arm's Length Sale of Shares

(31) That, in respect of a disposition of shares after April 10, 1978 to which the rules in sections 84.1 and 212.1 of the Act apply, in determining whether a taxpayer is a member of a controlling group of less than 6 persons, only shares of a corporation that are owned by the taxpayer, his spouse, a trust referred to in paragraph 73(1)(c) of the Act or a controlled corporation be deemed to be owned by him.

Exempt Corporations (32) That the rules in sections 87 and 88 of the Act not apply to an amalgamation or winding-up after November 16, 1978 involving any corporation that is not a taxable Canadian corporation.

Amalgamations (33) That for the 1978 and subsequent taxation years, a corporation formed on an amalgamation be deemed to be a continuation of each predecessor corporation for the purposes of the treatment of interest referred to in paragraph 81(1)(m) of the Act.

Amalgamations (34) That section 87 of the Act be amended to include a statutory amalgamation after November 16, 1978 of two or more taxable Canadian corporations as a result of which

(a) the amalgamated corporation is a wholly-owned subsidiary of another taxable Canadian corporation (the "parent"), and

(b) all of the shareholders of the predecessor corporations, other than the parent, receive, from the parent, shares of its capital stock,

and to provide a rollover for shareholders in respect of the surrender of their shares of a predecessor corporation in exchange for shares of the parent.

Winding-up of Canadian Corporations (35) That in respect of a winding-up commencing after November 16, 1978,

(a) the increase to a parent corporation in the cost of assets acquired on the winding-up of its subsidiary under paragraph 88(1)(d) of the Act be limited by any taxable dividends or capital dividends received by the parent, or by a corporation with which the parent was not dealing at arm's length at any time, on shares of the subsidiary, and

(b) for the purposes of paragraphs 88(1)(c) and (d) of the Act, where a parent has acquired control of a subsidiary in a non-arm's length transaction, the parent be deemed to have last acquired control of the subsidiary at the time a related corporation last acquired control (within the meaning assigned by subsection 186(2) of the Act) of the subsidiary.

Winding-up of Canadian Corporations (36) That where a debt obligation of a parent corporation is substituted for a debt obligation of its subsidiary on a winding-up after November 16, 1978, the rules in subsection 88(1) of the Act be amended to permit a rollover of the adjusted cost base of the obligation.

Sale of Shares of a Foreign Affiliate (37) That after Royal Assent to any measure giving effect to this paragraph, the section 93 election in respect of gains on the sale of shares of a foreign affiliate be permitted at any time within two years of the due date upon payment of a late-filing penalty on the amount designated in the election of 1/4 of 1% per month to a maximum of $2,500.

Currency Gains and Losses of Foreign Affiliates (38) That for the 1976 and subsequent taxation years, any foreign exchange gain or loss arising on the settlement of inter-affiliate debt be excluded from foreign accrual property income.

$1,000 Investment Income Deduction (39) That amounts received after November 16, 1978 that are deemed by section 84 of the Act to be dividends be excluded from income qualifying for the $1,000 investment income deduction.

Dividends from Foreign Affiliates

(40) That for the 1976 and subsequent taxation years, subparagraph 113(2)(b)(ii) of the Act be repealed with respect to dividends received from a foreign affiliate.

Cumulative Deduction Account

(41) That the cumulative deduction account of a corporation at the end of any taxation year ending after November 16, 1978 be reduced by 4/3 of the amount by which its qualifying taxable dividends in the year exceeds 4 times its dividend refund for that year.

Small Business Deduction

(42) That for taxation years commencing after 1978, the small business deduction apply only to the income from manufacturing, processing, mining, operating an oil or gas well, prospecting, exploring or drilling for natural resources, construction, logging, farming, fishing, leasing property other than real property, selling property as a principal, transportation or other qualifying business.

Foreign Tax Deduction

(43) That for the 1978 and subsequent taxation years, for the purposes of the foreign tax credit formula, the amount of the income earned in the year in a province be the amount thereof as determined for the purposes of section 120 of the Act.

Dividend Refund to Private Corporations

(44) That

(a) for taxation years commencing after 1978, a taxable dividend paid out of the income from a business and, in the case of a corporation that is controlled by one or more non-residents, income from the rental of real property not qualify for a dividend refund to a private corporation, and

(b) interest and dividends paid after November 16, 1978 on income bonds and income debentures or on shares that would, if they were issued after that date, be term preferred shares, not qualify for a dividend refund to a private corporation.

Investment Corporations

(45) That stock dividends paid by an investment corporation after November 16, 1978 not qualify as a distribution to shareholders for the purposes of subsection 130(3) of the Act.

Mutual Fund Corporations

(46) That for taxation years ending after November 16, 1978, the capital gains refund to a mutual fund corporation be computed by reference to a federal tax rate of 36%.

Policy Reserves of Life Insurers

(47) That

(a) the portion of a life insurer's policy reserves in respect of its segregated fund policies deducted in computing its income for its 1977 taxation year be included in the amount referred to in paragraph 138(4.2)(a) of the Act for its 1978 taxation year, and

(b) a life insurer be permitted to deduct in its 1978 taxation year the portion of any policy reserve in respect of segregated fund policies deducted under subparagraph 138(3)(a)(i) of the Act for its 1977 taxation year.

Shareholder Dividends of Life Insurers

(48) That the rule requiring a life insurer resident in Canada to add to its taxable income an amount determined by reference to dividends paid to its shareholders be amended to ensure that the amount so added will not be increased in respect of dividends paid before 1978 to the extent such increase would not have occurred under the rule as it read in its application to the 1976 taxation year.

Property Passing on Death

(49) That the Act be amended to provide that

(a) where an annuitant under a matured registered retirement savings plan dies after June 29, 1978, the surviving spouse, who is entitled during his or her lifetime to all the benefits payable under the plan, may become the annuitant under the plan,

(b) on the death after June 29, 1978 of the last annuitant under a registered retirement savings plan or a registered retirement income fund, any residue in the plan or fund be included in the income of the annuitant for the year of his death except for the following amounts included in the income of the recipient:

(i) that portion of the residue that passes to his surviving spouse, and

(ii) if the annuitant is not survived by a spouse, that portion of the residue that passes to a child or grandchild of the annuitant who was financially dependent on him, to the extent that the aggregate of all such amounts that pass to any one such child or grandchild does not exceed (except in the case of a recipient who is dependent by reason of mental or physical infirmity) $5,000 times the number of years until the child or grandchild becomes 26 years of age, and

(c) in respect of the death of an annuitant after November 16, 1978, the recipient of an amount out of or under a registered retirement savings plan or a registered retirement income fund that is included in the annuitant's income be jointly and severally liable for the tax payable thereon by the annuitant.

Exempt Status

(50) That for the 1979 and subsequent taxation years,

(a) a trust under a registered retirement savings plan or a registered retirement income fund cease to be exempt from tax after the end of the year in which the last annuitant thereunder dies, and

(b) any annuity under a registered retirement savings plan be required to be commuted on the death of the last annuitant thereunder.

Non-Qualified Investments

(51) That the references in the Act to cost in connection with the acquisition or holding, after November 16, 1978, of non-qualified investments by a registered retirement savings plan, a registered home ownership savings plan or a registered retirement income fund be changed to references to the fair market value of such investments at the time of acquisition.

Transfer of Funds

(52) That the rules in subsection 146(16) of the Act relating to the transfer of funds of a registered retirement savings plan apply only to those transfers after 1978 that are made before the year in which the annuitant attains 72 years of age.

Registered Education Savings Plan

(53) That

(a) for the purposes of the provisions relating to registered education savings plans, a qualifying trust not include a trust that makes a payment after November 16, 1978 to another trust for the purpose of paying scholarships, and

(b) any amount received after 1978 by or on behalf of a beneficiary from a registered education savings plan or from a trust to which any such plan has made a payment be included in computing the beneficiary's income and not qualify for the $1,000 investment income deduction.

Registered Home Ownership Savings Plan

(54) That for the 1978 and subsequent taxation years, the deduction allowed in a year in respect of funds withdrawn from a registered home ownership savings plan that were included in a taxpayer's income for a previous year be allowed only if an amount has not previously been deducted in respect thereof.

Transfer of Funds

(55) That after Royal Assent to any measure giving effect to this paragraph,

(a) the rules relating to registered home ownership savings plans provide for a transfer of funds to a new plan with the same trustee, and

(b) the rules relating to registered retirement income funds provide for a transfer of funds to a new fund with the same carrier.

Life Annuities

(56) That any payment (other than an annuity payment, a policy loan or a policy dividend) received after 1979 by a taxpayer under a life annuity contract entered into after 1977 be deemed to be proceeds of the disposition of an interest in a life insurance policy unless the contract was issued pursuant to a registered pension fund or plan, a registered retirement savings plan, an income-averaging annuity contract or a deferred profit sharing plan.

Life Insurance Policy Loans

(57) That the portion of any policy loan made after March 31, 1978 representing accumulated policy dividends or interest thereon be excluded for the purposes of determining the proceeds of disposition of an interest in a life insurance policy.

Limited-Dividend Housing Corporation

(58) That for taxation years commencing after 1978, a limited-dividend housing corporation qualify for exemption only if all or substantially all of its business is the construction, holding and management of low-rental housing projects.

Pension Fund Corporations

(59) That for taxation years commencing after 1978, the exemption in section 149 of the Act for pension fund corporations be restricted to

(a) corporations incorporated and operated solely for the administration of a registered pension plan and accepted as a "funding medium" for the purposes of the registration of the plan, and

(b) a corporation to which paragraph 149(1)(o) of the Act applied on November 16, 1978 or any qualifying corporation incorporated after November 16, 1978 only if it was held exclusively for the benefit of such pension plans since the later of November 16, 1978 and the date of incorporation.

Charitable Organizations

(60) That after Royal Assent to any measure giving effect to this paragraph, the Minister be given authority to publish an annual listing of all registered or previously registered charities.

Common Questions

(61) That after Royal Assent to any measure giving effect to this paragraph, the rules in section 174 of the Act relating to the reference by the Minister to the Federal Court or Tax Review Board of questions of law or fact common to assessments of two or more taxpayers be modified

(a) to make clear that the questions may concern assessments or proposed assessments,

(b) to enable appeals against determinations of such questions to be made under the Act or the *Federal Court Act,* and

(c) to change the time-stop rules provided in subsection 174(5) thereof for the purposes of assessing tax, interest or penalties, serving a notice of objection or instituting an appeal.

Part IV Tax

(62) That the election to pay Part IV tax not be permitted in respect of dividends received by a corporation after November 16, 1978 from a corporation it controls.

Part XI.I Tax

(63) That

(a) for the 1973 and subsequent taxation years, the Part XI.1 tax not apply in respect of certain life insurance policies held under a registered retirement savings plan or a deferred profit sharing plan, and

(b) for the 1978 and subsequent taxation years, the provisions of Part XI.1 of the Act relating to the filing of returns and the payment of tax apply to registered retirement income funds.

Stock Dividends

(64) That the non-resident withholding tax be extended to stock dividends paid after November 16, 1978 by a public corporation to non-resident shareholders, other than stock dividends paid in shares of the same class as that on which the dividend was paid.

Standby Charges and Commitment Fees

(65) That standby charges and commitment fees paid after 1977 under an agreement to lend money be exempt from the non-resident withholding tax where interest payable on any obligation issued under the agreement would be exempt.

Recovery of Amounts Owing to the Crown

(66) That after Royal Assent to any measure giving effect to this paragraph, where there is an amount owing by a person to Her Majesty under the Act, the Minister be authorized to require the retention by way of deduction or set-off of any amount payable to such person by Her Majesty.

Information Returns

(67) That after Royal Assent to any measure giving effect to this paragraph, section 233 of the Act be amended to allow a demand by the Minister for an information return to be served personally.

Definition of Canadian Partnership

(68) That after Royal Assent to any measure giving effect to this paragraph, the definition of "Canadian partnership" in section 102 of the Act apply for all purposes of the Act.

Income Bonds and Term and Retractable Preferred Shares

(69) That interest and dividends on

(a) income bonds, income debentures, and term and retractable preferred shares issued pursuant to an agreement in writing entered into on or before November 16, 1978 cease after that date to qualify for dividend treatment on the date that the conditions thereof are altered, the term is extended or the holder waives his right to redeem, and

(b) income bonds, income debentures, and term and retractable preferred shares, other than those referred to in paragraph (a), be denied dividend treatment except in restricted circumstances.

Compound Interest

(70) That compound interest or similar amounts payable after November 16, 1978 on interest or dividends owing on an income bond, income debenture or share of the capital stock of a corporation be deemed to be interest on a bond.

Notice of Ways and Means Motion to Amend the Income Tax Application Rules, 1971

That it is expedient to amend the Income Tax Application Rules, 1971 and to provide among other things:

Stock Dividends from a Foreign Affiliate

(1) That, for the 1972 and subsequent taxation years,

(a) the option provided in subsection 26(8.3) of the Rules in respect of a stock dividend on a share of a foreign affiliate owned on December 31, 1971 be extended to shares received as a stock dividend on shares previously received to which that subsection applies, and

(b) a corporation formed on an amalgamation be deemed to be a continuation of each predecessor corporation for the purposes of the treatment of stock dividends provided in subsection 26(8.3) of the Rules.

Successor Corporations

(2) That the rules in section 29 of the Rules relating the predecessor, successor and second successor corporations apply to an acquisition of property after November 16, 1978 only if the purchaser and vendor elect jointly to have the rules apply.

Notice of Ways and Means Motion

Excise Tax Act

Notice of Ways and Means Motion an Act to Amend the Excise Tax Act

That it is expedient to introduce a measure to amend the Excise Tax Act and to provide among other things that:

1. The ad valorem consumption or sales tax imposed under the said Act be set at the following rates:

(a) twelve per cent on the sale price of wines and goods on which a duty of excise is imposed under the Excise Act or would be imposed under that Act were the goods produced or manufactured in Canada,

(b) five per cent on the sale price of articles enumerated in Schedule V, and

(c) nine per cent on the sale price of all other goods to which subsection 27(1) of the Act presently applies.

2. The 5% special excise tax on large motorcycles and the 10% special excise tax on boat motors exceeding twenty horsepower and on aircraft, be repealed.

3. Schedule IV of the said Act be repealed and the following substituted therefor:

" Schedule IV

1. Petroleum products, namely,

(a) gasoline, premium, no lead . . . 1.3 cents per litre
(b) gasoline, grade 1 . . . . 1.2 cents per litre
(c) gasoline, grade 2 . . . . 1.1 cents per litre
(d) gasoline, no lead . . . . 1.1 cents per litre
(e) diesel fuel . . . . 1.0 cents per litre

and for the purposes of this section, the expressions "gasoline, premium, no lead", "gasoline, grade 1", "gasoline, grade 2", "gasoline, no lead" and "diesel fuel" have the meanings assigned thereto by regulation of the Governor in Council."

4. Section 12.1 of Schedule I to the said Act be repealed and the following substituted therefor:

"12. Gasoline and aviation gasoline . . . 1.5 cents per litre."

5. The said Act be amended to specify the time period within which any amount owing to Her Majesty in right of Canada pursuant to section 47.1 shall be payable and to impose a penalty upon default in payment of the said amount within the time limit specified.

6. The said Act be amended to make a person who files false or deceptive tax refund claims, guilty of an offence and liable to a penalty.

7. The said Act be amended to provide authority in section 47 of the Act for the Minister of National Revenue to pay to such persons as the Governor in Council may by regulation prescribe, an amount equal to the special excise tax paid on aviation gasoline which is for the sole use of the purchaser and not for resale and to provide for extension of the rules in subsections 47(2) and (4) of the said Act to payments in respect to aviation gasoline.

8. Subsection 21(2) of the said Act be repealed and the following substituted therefor:

"(2) Where the goods are imported, such excise tax shall be paid by the importer or transferee who takes the goods out of bond for consumption at the time when the goods are imported or taken out of warehouse for consumption, and where the goods are manufactured or produced and sold in Canada, such excise tax shall be payable by the manufacturer or producer at the time of delivery of such goods to the purchaser thereof."

9. The said Act be amended to provide that

(a) the excise tax on gasoline and the consumption or sales tax on gasoline and diesel fuel shall be payable not later than at the time of delivery of these products to a retail outlet, and

(b) where gasoline or diesel fuel is held in inventory at a retail outlet and the consumption or sales tax or the excise tax thereon has not been paid or become payable on or before November 16, 1978, the said gasoline or diesel fuel shall be deemed to have been delivered to the purchaser thereof on November 17, 1978.

10. Part XVIII of Schedule III to the said Act be amended by repealing section 5 thereof and substituting therefor the following:

"5. Thermal insulation materials designed exclusively for insulation of buildings and having a thermal resistance as installed (R value) greater than 2.4 per inch of material, but not including board and sheet materials of a thickness which provides a total thermal resistance of less than 3."

11. Part XVIII of Schedule III to the said Act be further amended by repealing section 7 thereof.

12. The following goods be made exempt from the consumption or sales tax:

(a) devices designed to convert sound to light signals for use by the deaf, when purchased on the written order of a registered medical practitioner; and

(b) solar water heaters.

13. The exemption from consumption or sales tax of twenty-five per cent of the sale price or duty paid value, as the case may be, of trailers for use as homes, be repealed.

14. Subsection 59(4) of the said Act be repealed.

15. Subsection 31(2) of the said Act be amended to provide that the Governor in Council, on the joint recommendation of the Minister of Finance and the Minister of National Revenue, may make regulations exempting any class of small manufacturer or producer from the payment of consumption or sales tax on goods manufactured or produced by them.

16. Paragraphs (1)(p) and (q) of Part XIII of Schedule III to the said Act be repealed and the following substituted therefor:

> "(p) photocopiers and other office type reproduction equipment for use by persons exempted from consumption or sales tax under subsection 31(2) and whose principal business is other than printing; office equipment;
>
> (q) motor vehicles except those described in paragraphs (e) and (h); or
>
> (r) goods for use by persons exempt from payment of consumption or sales tax under subsection 31(2), other than those persons prescribed by regulation of the Governor in Council."

17. The ad valorem tax imposed on the amount paid or payable for transportation of a person by air within the taxation area, as defined for purposes of Part II of the said Act, be increased to the lesser of 15% and such amount as may be prescribed by order of the Governor in Council on the recommendation of the Minister of Transport.

18. The specific tax imposed on the amount paid or payable for transportation of a person by air from a point within the taxation area, as defined for purposes of Part II of the said Act, to a point outside of the taxation area, be increased to the lesser of $15.00 and such amount as may be prescribed by order of the Governor in Council on the recommendation of the Minister of Transport.

19. Part II of the said Act, and references thereto or provisions related thereto in sections 44, 52, 53, 59 and 70, be repealed on a day to be fixed by Order of the Governor in Council, which Order would be subject to negative resolution of Parliament.

20. Any enactment founded on

> (a) paragraphs 1, 2, 4, and 7 to 16 shall be effective November 17, 1978, except that any enactment founded on paragraph 4 shall be read and construed in the case of the period commencing on November 17, 1978 and ending on December 31, 1978, as if the reference to 1.5 cents per litre therein were a reference to 7 cents per gallon;
>
> (b) paragraph 3 shall be effective January 1, 1979; and,
>
> (c) paragraphs 17 and 18 shall be effective on April 1, 1979 in the case of a tax imposed on an amount paid or payable in Canada, and in respect of emplanements on and after July 1, 1979 in the case of a tax imposed on an amount paid or payable outside of Canada.

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Supplementary Information

Federal Revenue Effects of Budget Tax Measures

	Effective Date	Revenue Effect First Full Year	Revenue Effect Fiscal Year 1979-80
		($ Millions)	
1) Reduction in the rate of federal sales tax	Immediate	−1000	−1015
2) *Increase in employment expense deduction	1979 Taxation Year	−230	−270
3) Investment and R & D tax credits			
– Increase in the rates of credit	Immediate	−100	−100
– Extension of credit to transportation equipment	Immediate	−30	−30
– Increase in rates of credit for research and development and special rate of 25 per cent for small firms	Immediate	−25	−25
– Indefinite extension of the credit	July 1, 1980	−500	—
4) Mining and oil and gas			
–*Extension of drilling fund incentive from June 30, 1979 to Dec 31, 1981	July 1, 1979	−80	−60
–*Development expenses in mining to be deductible at 100 per cent rate and social capital expenditures in mining to qualify for depletion allowance	Immediate	−25	−25
5) *Indefinite extension of two-year write-off for pollution control investments	Jan 1, 1980	−15	−5
6) *Change in treatment of income debentures and term preferred shares issued after budget date	Immediate	+150	+150
7) **Increase in air transportation tax	After Mar 31, 1979	**	**
8)***Other measures	Immediate unless otherwise indicated	***	***
– Elimination of special excise taxes on private airplanes, motorcycles and boat motors			
– Extension of the 7 cent gasoline tax to aviation fuel for non-commercial aircraft			
– Redefinition of insulation material for purposes of sales tax exemption			
– Elimination of sales tax exemption on storm doors and windows			
–*Change in the definition of active business income for purposes of small business deduction	Tax years after 1978		

	Effective Date	Revenue Effect First Full Year	Revenue Effect Fiscal Year 1979-80
		($ Millions)	
— Elimination of sales tax exemption for timer-control devices			
— Exemption of sales tax on signalling devices for the deaf			
— Exemption of sales tax on solar water heaters			
— Conversion of excise tax and sales tax on gasoline to metric system			
— Amendment of sales tax to reflect introduction of premium no lead gasoline			
—*Depreciation adjustment related to inventory			
—*Tax relief for RRSP funds passing to minor children	June 30, 1978		
—*Deduction for underwriting fees and expenses			
—*Change in tax treatment of payments on termination of employment			
—*Allowance of costs of recompleting an oil or gas well to earn depletion			
—*Permission of costs of clearing or removing overburden at mine sites to be capitalized			
—*Extension of preferential treatment of investments in multiple-unit residential buildings for one year	Jan 1, 1979		
—*Current deduction of interest and property taxes on land held for resale or development			
Net Total			– 1380

The net effect of the measures will be a reduction in federal revenues of some $310 million in 1978-79.

* Measures marked with an asterisk also affect provincial revenues. Assuming that all the provinces make the necessary accommodating changes in their legislation, taxpayers will save an additional $60 million in reduced provincial revenues in the 1979-80 fiscal year.

** The proposed increases in air transportation tax will yield $72 million per annum in additional revenues. These revenues are earmarked for air transport services and thus do not affect federal budgetary revenues.

*** The revenue effects of changes are offsetting; their net revenue impact is marginal.

Sales and Excise Tax Changes

General Sales Tax Reduction

Currently a range of imported and domestically manufactured goods are subject to a general federal sales tax of 12 per cent.

Effective immediately, this rate will be reduced to 9 per cent for all goods except alcohol and tobacco products.

The new rate will apply to sales by manufacturers and licensed wholesalers on goods sold or delivered to the purchaser, and on goods imported into Canada or taken out of warehouse for consumption, after November 16, 1978. The reduction in the general rate does not have a termination date.

Automobiles and parts, furniture, stoves, refrigerators, washing machines, stereo equipment, radios, television sets, sporting goods, boats, tools, toys and games, and a variety of household goods such as soap, cosmetics, waxes, pots and pans, are examples of goods that will be affected by this sales tax reduction.

The tax is levied on manufacturers and importers. It is expected that these tax savings will be passed on to distributors and retailers and in turn to consumers in the form of lower prices.

This measure will reduce federal revenue in 1979-80 by $1,015 million.

The tax on construction materials was reduced from 11 per cent to 5 per cent in 1974, and these materials will continue to be taxed at the low rate.

Major items such as clothing and footwear, foodstuffs, pharmaceuticals and heating fuels, are completely exempt from the federal tax.

In accordance with standard practice, no claims will be entertained for refunds of tax in respect of inventories of goods on which the 12 per cent tax has already been paid.

Tax Changes Related to Energy Conservation

The Excise Tax Act will be amended to remove the 5 per cent special excise tax on large size motorcycles and the 10 per cent special excise tax on marine motors over 20 horsepower and personal and corporation aircraft. The special excise tax of seven cents per gallon which now applies to motor vehicle gasoline for personal use will be extended to apply to aviation gasoline. Regulations will be introduced to authorize a refund of the tax on aviation gasoline used in the provision of public air transportation services for passengers, freight or mail, and air services related directly to exploration and development of natural resources, agricultural applications, fire fighting, fire protection and aerial construction.

Exemption from the new 9 per cent federal sales tax will be provided for solar powered water heaters. The 5 per cent sales tax will be reimposed on storm windows and doors and the new 9 per cent sales tax will be imposed on timer-controlled thermostats.

The exemption for storm windows and doors was originally intended to be confined to these goods for installation on existing buildings. This was not found to be practicable, however, and as a result, all double glass windows and glass cladding material became exempt from the tax. Given that glass is less efficient in energy conservation than solid wall construction, the exemption did not achieve its original intent. The exemption for automatic timer controls has also caused serious interpretational problems as these goods are capable of being used in a variety of applications not linked to energy conservation.

Exemption for Thermal Insulation Clarified

Thermal insulation materials have been exempted from the sales tax since 1975. A change is proposed to clarify which insulation materials are entitled to exemption by reference to the efficiency factor (R value) of the product in restricting heat loss. Thermal insulation marketed as bulk material or as batts will continue to enjoy exemption if it has an R value greater than 2.4 per inch of material. For thermal insulation material marketed in the form of boards and sheets, the exemption will be conditional upon the individual board or sheet providing a total thermal resistance of three or more.

Tax Changes Affecting Other Goods

Exemption from the tax is proposed for devices which convert sound to light signals, for use by the deaf, in conjunction with telephones, doorbells and stove timers and in other similar applications. This will be an addition to the range of goods for which tax exemption is provided when for use by handicapped persons.

Time of Imposition of the Levies on Gasoline and Diesel Fuel Clarified

Motor vehicle fuels are normally taxed at time of delivery by the manufacturer of the fuel to independent retail service stations. But when the manufacturer operates the retail service station, the law now allows him to defer the tax until the fuel is sold to individual consumers. The budget proposals include a provision which will require the tax to be imposed on motor vehicle gasoline and diesel fuel at time of delivery to retail service stations, irrespective of whether the station is operated by the manufacturer or by any other person.

Refund Claim Provisions Modified

Refunds of the tax arising out of Tariff Board decisions are now restricted to one year from the time the tax was paid. The budget includes a proposal to extend the refund claim period to four years.

Also included is a proposal under which claimants who have requested refund of the special excise tax on gasoline, and the federal sales tax on taxable goods, will be treated in the same manner as taxpayers licensed under the Act. The effect of this change is that fraudulent refund claims for recovery of tax, and failure to return excess refund payments, will attract the same penalties as now apply to licensed taxpayers.

Exemption for Production Equipment for "Small Manufacturers" Clarified

The Excise Tax Act was amended in May 1978 to provide tax exemption for production equipment acquired by small manufacturers who are excluded from licensing under the provisions of subsection 31(2) of the Excise Tax Act. Changes are proposed in Schedule III of the Act and in the Small Manufacturers' Regulation which will ensure that the benefits contemplated in May 1978 will accrue only to persons who are genuine "small manufacturers". In particular, large businesses that produce printed matter for their own use will be denied exemption on their printing equipment unless the value of that printed matter produced is sufficient to require them to be licensed for the production of printed matter.

Special Status Enjoyed by Travel Trailers is Eliminated

Hard wall recreational trailers now attract federal sales tax on 75 per cent of their sale price, which is equivalent to a rate of 9 per cent. The proposals include a provision which will eliminate this special treatment. As the general rate of tax is being reduced to 9 per cent, the effect of this provision is that travel trailers will continue to attract the same rate of tax as before.

Conversion of Levies on Gasoline and Diesel Fuel to Metric Measure

It is proposed that effective January 1, 1979, the seven cents a gallon special excise tax on gasoline and the specific tax levies on gasoline and diesel fuel be expressed in metric units. Also, a new specific rate of 1.3 cents per litre is being established for premium no lead gasoline, a relatively new product on the market.

	Present Rates in Imperial Measure	New Rates in Metric Measure
	Cents per gallon	Cents per litre
Special Excise Tax on Gasoline	7	1.5
Gasoline, Grade 1	5.507	1.2
Gasoline, Grade 2	4.918	1.1
Gasoline, No Lead	5.132	1.1
Gasoline, No Lead Premium	-	1.3
Diesel Fuel	4.618	1.0

Increase in the Employment Expense Deduction

The budget proposes to double, to $500, the maximum employment expense deduction that individual taxpayers will be able to claim, starting in the 1979 taxation year.

The change, which benefits individual taxpayers with income from employment, will mean aggregate savings of an estimated $315 million in their federal and provincial income tax. Over 6,200,000 taxpayers will benefit from the change. Of these, some 2,800,000 will receive the maximum proposed deduction of $500.

Under the current provisions of the Income Tax Act, individuals are allowed a deduction of 3 per cent of wage and salary income to a maximum of $250.

This deduction is in recognition of the fact that all working Canadians have to incur some expenses in the context of their employment, and is available automatically to all without any receipts to support the expense claim. The maximum limit for the deduction was increased from $150 to $250 in the March 31, 1977 budget.

Personal Income Tax Indexing in 1979

Indexing of personal exemptions and tax brackets in relation to the consumer price index (CPI) commenced with the 1974 taxation year. Indexing eliminates the tax increases that would otherwise arise from inflation interacting with a system of graduated tax brackets. Indexing thus acts to ensure that taxpayers are not pushed into higher tax brackets by increases in income that merely keep pace with inflation.

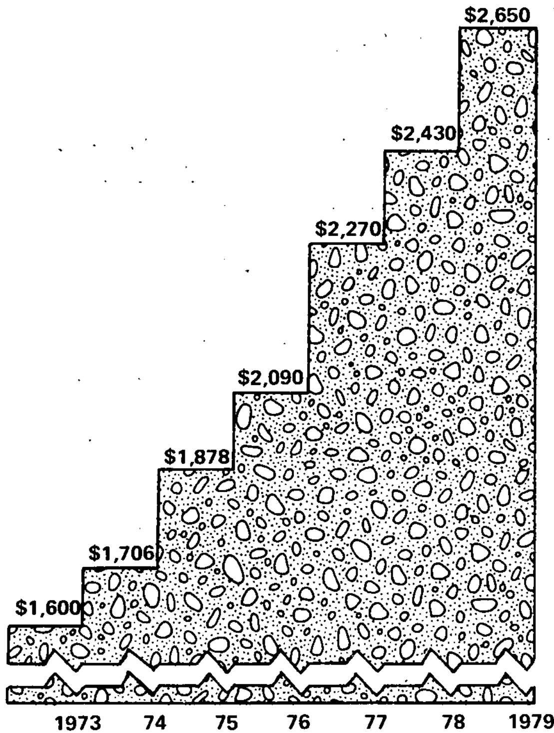
The indexing adjustment for each year is based on the average annual increase in the CPI for the 12-month period ending in September. For the 1979 taxation year personal exemptions and tax bracket limits will rise by 9.0 per cent commencing January 1, 1979.

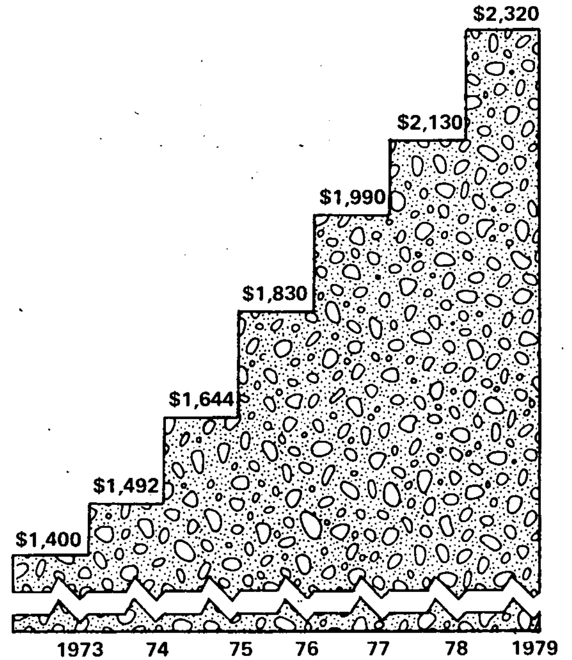
Tax indexing in 1979 will raise personal exemptions as follows:

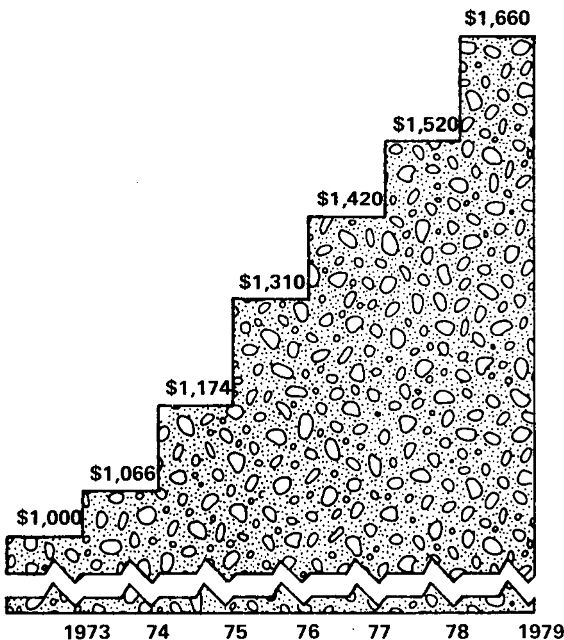
	1978 Levels	1979 Levels	Increase
		(dollars)	
Basic Personal Exemption	2430	2650	220
Married Exemption	2130	2320	190
Exemption for dependants under age 17	460	500	40
Exemption for dependants age 17 or over	840	910	70
Age Exemption	1520	1660	140
Exemption for blindness and disability	1520	1660	140

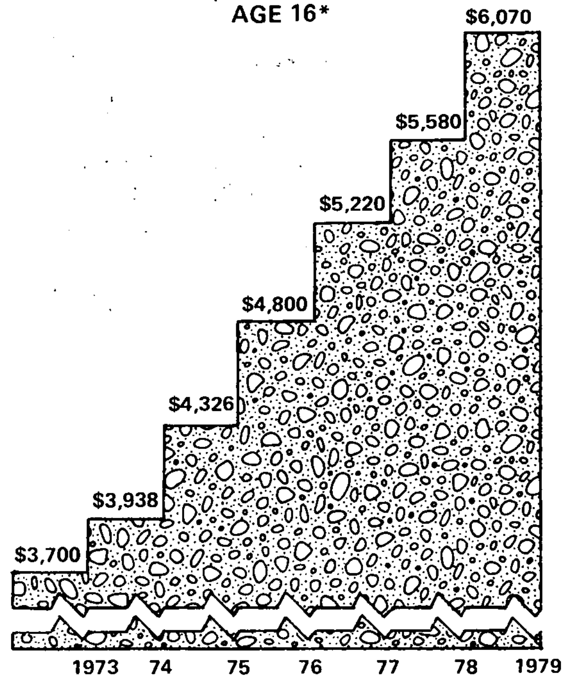
The increase in exemptions since indexing began is shown graphically in the chart. Table 1 shows the new federal income tax schedule with widened tax brackets.

INCREASES IN VARIOUS EXEMPTIONS AND DEDUCTIONS AS A RESULT OF INDEXING, 1973 – 1979









*This includes the basic personal exemption, the married deduction, the standard $100 deduction in respect of medical and charitable contributions and the deduction applicable to children under age 17 in 1979 and under the age of 16 for the preceding years. No account is taken of other exemptions and deductions applicable to the family such as the employment expense deduction of 3 percent of wage and salary income to a maximum of $250 or those deductions in respect of CPP/QPP and UI contributions.

Table 1
1979 Federal Income Tax Rates
Based on an Indexing Factor of 1.658

Taxable Income			Tax
$829 or less			6%
In excess of			
$ 829	$ 50	+	16% on next $ 829
$ 1,658	$ 182	+	17% on next $ 1,658
$ 3,316	$ 464	+	18% on next $ 1,658
$ 4,974	$ 763	+	19% on next $ 3,316
$ 8,290	$ 1,393	+	21% on next $ 3,316
$11,606	$ 2,089	+	23% on next $ 3,316
$14,922	$ 2,852	+	25% on next $ 3,316
$18,238	$ 3,681	+	28% on next $ 4,974
$23,212	$ 5,073	+	32% on next $16,580
$39,792	$10,379	+	36% on next $24,870
$64,662	$19,332	+	39% on next $34,818
$99,480	$32,911	+	43% on remainder

The refundable child tax credit, introduced on August 24, 1978, is also indexed to changes in the CPI. As a result of 1979 indexing of 9.0 per cent, the credit for the 1979 taxation year, payable in 1980, will rise from $200 per child to $218. The threshold family income level up to which full child tax credit benefits are paid will rise from $18,000 to $19,620. As a result, the real value of child credit benefits will not be eroded by inflation.

Savings to Typical Taxpayers

The benefits of indexing to typical families and single individuals are shown in Table 2.

As can be seen from the table, all taxpayers benefit from indexing. Tax savings are significant. In the middle-income ranges, indexing reduces tax liabilities of individuals by $200 to $400. Even though the dollar amounts of tax savings are larger in higher-income brackets, the savings represent a much larger percentage cut in tax for lower-income persons.

Table 2
Tax Savings in 1979 as a Result of Indexing

Earned Income	1979 Federal and Provincial Tax: Without 1979 Indexing	1979 Federal and Provincial Tax: With 1979 Indexing	Tax Savings: Amount	Tax Savings: Per Cent
$	$	$	$	%
Single Taxpayer—No Dependants				
3,000	8	2	6	75.0
5,000	202	137	65	32.2
7,000	677	604	73	10.8
10,000	1440	1358	82	5.7
12,000	1989	1881	108	5.4
15,000	2889	2753	136	4.7
20,000	4511	4340	171	3.8
30,000	8644	8262	382	4.4
50,000	18440	17857	583	3.2
Married Taxpayer—Two Dependants under Age 17				
5,000	−400	−436	36	9.0
7,000	−328	−402	74	22.6
10,000	340	162	178	52.3
12,000	853	660	193	22.6
15,000	1684	1459	225	13.4
20,000	3325	2982	343	10.3
30,000	7462	6987	475	6.4
50,000	17108	16385	723	4.2

Tax savings include those arising from indexing of exemptions, tax bracket limits and the refundable child tax credit. Negative amounts of tax represent a payment of the refundable child tax credit.

Taxpayers are assumed to be under age 65 and to receive earned income. Family allowance payments, at 1979 rates, are added to earned income in calculating tax liability where applicable. In addition to personal exemptions the employment expense deduction of 3 per cent of wage and salary income to a maximum of $500 and CPP/QPP and UI contributions, calculated at 1979 rates, are deducted in computing tax. Taxpayers are assumed to take the optional standard deduction of $100 in respect of medical expenses and charitable contributions. No account is taken of other potential deductions such as child care expenses or contributions to private pension plans. For purposes of computing child credit benefits, income is assumed to accrue to one spouse.

The provincial tax is calculated at a standard rate of 44.0 per cent of federal basic tax. As rates of provincial tax vary from province to province, taxpayers in some provinces will experience tax savings that differ from those given above. No provision is made in the calculations for any provincial tax cuts or tax credits.

Revenue Impact

The additional indexing of *exemptions and tax brackets* by 9.0 per cent will reduce federal revenues by some $1,050 million for the 1979 taxation year. Revenues of the provinces under the tax collection agreements will be reduced by some $410 million. The current-year (federal) tax savings to individuals, associated with the cumulative increase in exemptions and tax bracket limits that has occurred since the inception of indexing in 1974 amounts to over $6 billion.

The indexing of the child tax credit will reduce federal revenues by $150 million for the 1979 taxation year. The total federal revenue cost of indexing the personal income tax is thus some $1.2 billion. Provincial revenues are not affected by the indexing of the child tax credit.

Distribution of Aggregate Indexing Savings

Table 3 provides a distribution of aggregate savings to individuals in federal and provincial tax from the 1979 indexing of *personal exemptions and tax bracket limits*, by income class. Approximately two-thirds of these savings accrue to those earning less than $25,000. The percentage share of low-income individuals in these savings is considerably higher than their percentage share in tax otherwise payable.

All of the benefits of the indexing of the refundable child tax credit accrue to low and middle-income families. These benefits are not included in the distributions shown in Table 3.

Comparisons with the United States

In countries such as the United States where personal income taxes are not indexed, substantial discretionary tax reductions are needed merely to offset the effects of inflation interacting with a progressive tax system. The study of comparisons of tax levels in Canada and in the United States, which is contained in the budget material, shows that automatic indexing and other discretionary tax cuts have significantly increased the after-tax incomes of Canadians.

As a result of adjustments in deductions at source, Canadians will begin experiencing the benefits of indexing of exemptions and tax bracket limits in January 1979. The benefits from indexing of the child tax credit will be reflected in 1979 child credit claims which will be filed with Revenue Canada early in 1980.

Table 3
Distribution of aggregate federal and provincial benefits from 1979 indexing of exemptions and tax brackets

Individual Income Level	Federal and Provincial Tax Savings From 1979 Indexing of Exemptions and Tax Brackets		Share in Federal and Provincial Tax
($)	Amount ($ million)	Share in Total (%)	(%)
Under 10,000	200.7	13.7	5.7
10,000-15,000	258.9	17.7	14.7
15,000-20,000	290.1	19.9	20.3
20,000-25,000	228.5	15.7	16.8
25,000-50,000	376.0	25.8	28.2
50,000 and over	105.1	7.2	14.3
Total	1459.3	100.0	100.0

Source: Department of Finance estimates.

Sectoral and Regional Incentives

The budget proposes major tax incentives for private investment that will lead to improvements in productivity and help contain cost increases. They will encourage modernization in important sectors of the economy and act to promote more balanced patterns of development across Canadian regions.

The incentives are provided through extension and enrichment of the federal investment tax credit. All of these changes take effect November 17, 1978.

Current Structure of Investment Tax Credit

The federal income tax system provides for an investment tax credit on qualified purchases of new buildings, machinery and equipment. The present rate of credit varies by region, with a basic rate of 5 per cent and rates of 7½ and 10 per cent applicable in designated slower-growth regions of the country.

The credit applies for assets acquired for use in manufacturing or processing businesses; in the petroleum, industrial mineral and mineral industries and in logging, farming, fishing and grain storage. Both current and capital expenditures on scientific research and development also receive the credit.

Individuals, including small businessmen, farmers and fishermen, as well as corporations may use the credit to reduce federal income taxes.

Removal of Expiry Date

The current credit applies to investments made before July 1, 1980. The budget proposes to extend the credit indefinitely. This will eliminate uncertainty in long-term investment planning and will provide for the continuation of this significant investment incentive.

Increases in Rates

The rates of investment tax credit are to be increased, maintaining the regional variation.

The basic rate of credit is being raised from 5 to 7 per cent. This rate applies generally in Southern Ontario, Southwestern Quebec, and most of Alberta and British Columbia.

The rate of tax credit will be increased from 7.5 to 10 per cent in areas designated under the Regional Development Incentives Act in Saskatchewan, Manitoba, Northern Ontario and Quebec other than the Gaspé region. Investments in the northern parts of Alberta and British Columbia, and the Yukon and Northwest Territories will also qualify for the credit at this rate.

The rate of tax credit will be doubled from 10 to 20 per cent in the Atlantic Provinces and the Gaspé region of Quebec.

The new 20 per cent rate of credit in the Atlantic Provinces and the Gaspé is almost as large as the maximum DREE grants of 25 per cent of the cost of capital investment. DREE grants are also available in relation to direct job creation.

In its economic impact, the investment tax credit has an effect similar to a direct reduction in the purchase price of investments by the amount of the credit. A credit of 20 per cent, for example, on a piece of machinery costing $1,000 is equivalent to a reduction in the purchase price to $800.

Extension of Coverage to Transportation

The coverage of the investment tax credit is to be expanded to include expenditures on rail, air, water and long-haul road transportation equipment. The basic rate of credit of 7 per cent will apply for all such qualified expenditures. It is not possible to provide different credit rates for transportation investments in designated areas due to the difficulty of determining the region where such equipment is used.

Major new investments are required in transportation in order to improve productivity and contain cost increases. To achieve this it will be important to rely upon the market mechanism and the ability of carriers themselves to respond to new possibilities for productivity improvement and to meet new capacity requirements where they emerge.

The new measure is consistent with the government's intention to contain the rate of increase in direct government expenditures and avoid undue reliance on regulatory measures.

Railways are of special importance for the movement of heavy and bulk commodities such as grain, coal, lumber, metallic ores and concentrates, sulphur and potash over long distances. This measure follows up on the accelerated capital cost allowances on railway assets announced in the last budget.

Road transportation is important in the movement of processed and manufactured goods. The investment tax credit for trucking will reduce over-all distribution costs for the products of Canadian industry. The measure will help particularly in those areas of the country where there is an increasing shift from rail to truck in the movement of freight.

The measure will benefit Canadian shipping and encourage replacements and additions to the existing Canadian Great Lakes and coastal fleets.

The credit will provide incentive to air carriers to replace old equipment with new, more energy-efficient aircraft and to take advantage of technological

improvements. Air carriers at all levels will benefit, including the smaller carriers which provide service in the more remote and less heavily populated areas of the country.

Inclusion of intercity bus transport in the credit will assist the development of better services with more modern equipment. It will be important in those areas of the country where the size and distribution of the population make the bus an attractive and flexible mode of transport.

Revenue Impact

The total federal revenue cost of increasing the rates of credit and extending their coverage to transportation will be $130 million in 1979-80. The extension to transportation accounts for $30 million of this amount.

The extension of the credit beyond June 30, 1980, reduces federal revenues by some $500 million in a full year. This amount represents the total federal cost of the credit in the 12 months following June 30, 1980.

Research and Development

Research and development (R&D) is vitally important to the structure of the Canadian economy over the medium-term. The sectoral task forces, and the Second Tier Committee have drawn further attention to Canada's R&D needs.

The government has taken tax action in the past two budgets to ensure that our R&D effort will act to enhance economic performance. Under the present income tax system, current and capital expenditures on R&D qualify for a 100 per cent write-off in the year they are made. Since 1977, R&D has qualified for the investment tax credit. Eligible expenditures include those of a capital nature, such as buildings and equipment, as well as current expenditures such as salaries of research personnel. The April 10, 1978, federal budget permitted a firm to claim an additional 50 per cent deduction for R&D expenditures that exceed its average expenditures on R&D for the previous three years. This deduction is to apply for a period of 10 years.

This budget proposes a special measure for R&D expenditures undertaken by small, Canadian-controlled private corporations that qualify for the low rate of corporation tax. These firms will receive an investment tax credit of 25 per cent on all their R&D expenditures. This special incentive for small business R&D will be available throughout Canada.

The budget also doubles the basic federal investment tax credit for R&D from 5 per cent of expenditures to 10 per cent for all other businesses. Thus the basic rate of credit will be higher for R&D than for other investments. This rate will apply to R&D investments in all of Canada except for the Atlantic Provinces and the Gaspé region of Quebec. In these areas, R&D expenditures will qualify for a credit of 20 per cent.

The increased tax credit for R&D will reduce federal revenues by $25 million a year. The measure reinforces the government's commitment to increasing the relative importance of R&D in the Canadian economy. Total value of additional federal tax incentives for R&D (not counting the tax advantage of the basic 100 per cent write-off) now exceeds $100 million per annum.

Resource Taxation

The budget proposes a series of measures to stimulate investment in exploration and development, and new mining ventures in Canada. The changes significantly reduce taxation for businesses participating in these activities.

First, the provision to permit the immediate deduction of Canadian exploration expenses for individuals and non-resource corporations is to be extended until December 31, 1981. This provision, originally introduced on May 25, 1976, would otherwise have terminated on June 30, 1979.

Second, the costs incurred after November 16, 1978, for the development of new mines may be written off at 100 per cent. Previously, these costs could be written off at a maximum rate of 30 per cent.

Third, the capital cost of social assets and townsite facilities acquired after November 16, 1978, for new mines will be eligible to earn depletion, at a rate of $100 depletion for every $300 expenditure. These costs will in future be treated in the same way as other costs relating to new mines.

Fourth, costs incurred after November 16, 1978, relating to the recompletion of a producing oil or gas well will be included in the definition of Canadian development expense and will be eligible to earn depletion. Recompletion involves work necessary to maintain or extend the life of a producing well.

In addition, a number of technical relieving changes are proposed in the rules relating to predecessor and successor corporations. Any proceeds of disposition of a resource property acquired by a corporation from a predecessor corporation will be applied against the cumulative Canadian development expense acquired from the predecessor corporation. Previously, such proceeds were included in an income account for the purpose of calculating the write-off of the Canadian development expense acquired by the successor corporation. To the extent that such proceeds from a resource property exceed the balance of the cumulative Canadian development expense so acquired, they will be applied against the cumulative Canadian development expense of the successor corporation.

The budget also proposes to permit the costs of clearing and removing overburden at a mine site, after the mine has commenced production, to be capitalized as a Class 12 asset, allowing the costs to be written off at a 100 per cent rate. This change will permit taxpayers to defer the deduction of such costs during periods of little or no profits to a later period when profits are higher.

The above changes and the enrichment of the investment tax credit are of significant benefit to businesses which are developing additional natural resources in Canada, or are expanding production at existing sites.

The extension of the deductibility of Canadian exploration expense by individuals and non-resource companies will reduce federal revenues by $60 million in the coming year. The 100 per cent write-off of development expenses plus the depletion earned on social assets will reduce federal revenues by an additional $25 million. The increases in the rates of investment tax credit in the designated areas are of particular benefit to the mining sector. Investments made on these activities in the coming year will earn an additional $35 million in investment tax credits.

Pollution Control Equipment

The income tax provisions currently contain a fast write-off for capital expenditures incurred to control air and water pollution. Such expenditures (on both structures and machinery and equipment) may be fully written off over two years at 50 per cent per year as opposed to a write-off at rates ranging between 5 and 20 per cent (on a declining balance basis) that would otherwise apply. The incentive is scheduled to expire at the end of 1979.

This two-year write-off provision will be extended indefinitely. The tax incentive reduces federal and provincial revenues by some $20 million a year.

Pulp and paper and mining companies are the primary users of this measure. In 1975, the latest year for which data are available, the pulp and paper industries claimed some 43 per cent of the total $72 million in accelerated capital cost allowance for water pollution control equipment.

Of the $67 million of fast write-off for air pollution control equipment claimed in 1975, mining, the primary metals, and non-metallic mineral products industries accounted for some 51 per cent.

This measure will lessen any impediments that pollution control requirements put on the expansion and operation of resource-based industries.

Over the next few years the pulp and paper industry is embarking on a major program of investment in pollution abatement equipment. In addition to the two-year write-off, such investments also qualify for the federal investment tax credit. This credit is being extended indefinitely and the rates of credit are being increased from the current 5, 7½ and 10 per cent to new levels of 7, 10 and 20 per cent. The higher rates apply to designated slower-growth areas.

Housing Measures

The special provision in the capital cost allowance regulations designed to stimulate the construction of multiple-unit residential buildings, (MURB) which would otherwise expire at the end of this year, is to be extended to December 31, 1979.

This provision has assisted in increasing the supply of housing across Canada. This extension is designed to increase the number of multiple-unit residential starts in 1979 and provide employment opportunities during the coming winter months.

The MURB provision permits the offset against other income of rental losses generated by capital cost allowances.

Provision is made in the budget for the deduction of interest and property taxes on land held for development or resale by taxpayers in the ordinary course of their business. This will apply to such expenses incurred after November 16, 1978. It will provide developers an opportunity for planning more projects in Canada.

The Small Business Tax Incentive

The budget proposes a more precise definition of who may benefit from the low tax rate on small business, to ensure that this tax incentive will serve its original purpose of promoting expansion of small business and not be used as a tax shelter by others.

Incorporated Canadian small business enjoys very favourable tax treatment. Canadian-controlled private corporations qualify for a federal tax rate of 15 per cent on the first $150,000 of annual business earnings (10 per cent for small manufacturing firms). These tax rates compare with the 36 per cent federal tax rate (30 per cent for manufacturing) which applies to corporations not qualifying as small businesses. Since 1972, the government has tripled the annual amount of income eligible for the small business tax rate. The low tax rate applies as long as the small corporation's retained business income is less than $750,000. Once this limit is reached, the small business can continue to qualify for the low tax rate by paying dividends to shareholders.

This low tax rate on small business results in a reduction of some $900 million annually in federal tax revenues.

Last summer the government introduced other measures for small business. They included a deferral on up to $200,000 of capital gains when small family businesses are transferred from parents to children or grandchildren. Losses on investments in Canadian-controlled private companies were made deductible against income from other sources without limit, compared with the $2,000 limit for other investments. Small manufacturers with sales under $50,000 were exempted from federal sales tax.

The low tax rate on small incorporated businesses allows the shareholder-manager, who would otherwise be taxed at personal income tax rates exceeding the small business rate, to defer personal income tax by retaining income in the corporation. In conjunction with the dividend tax credit, the combined personal and corporate tax on small business income earned in a private corporation and distributed to shareholders is well below that on the

same amount of income earned as salaries or wages or as unincorporated business income.

The small business incentive is intended to enable and assist growing, Canadian-controlled firms to accumulate funds for expansion. It was never intended to be a tax shelter device for employment, professional and investment income. Yet, in part, this is what it has tended to become.

More specifically, the corporate tax advantages to small business have caused many individuals and groups of professionals to consider incorporating themselves. In recent years, a number of businesses have been incorporated to provide the personal services of athletes and entertainers or to provide professional or management services. For example, some lawyers, chartered accountants, doctors, dentists and other professionals have formed private companies to provide administrative services to their professional practices. The fees charged by such service companies effectively convert professional earnings into income qualifying for the small business tax rate. Typically, these companies are owned by other members of the professional's family.

Generally speaking, the principal reason for incorporating these types of businesses is to realize the tax saving from the lower tax rate applying to small businesses. Other advantages of the corporate form of organization, such as limited liability, are usually a secondary consideration. For example, limited liability is not generally available to professionals setting up a professional corporation in those jurisdictions where it is permitted. They seek only the tax advantages of incorporation.

When the small business deduction was introduced, provincial legislation did not generally allow individuals to carry on their professional practice through a corporation. There is now greater pressure on provinces, who do not permit professionals such as doctors and lawyers to incorporate, to introduce enabling legislation. If action is not taken, a situation could develop whereby virtually all professional earnings in Canada would be taxed at a federal corporate tax rate of 15 per cent.

It was never intended that an individual providing a personal service be permitted to defer and reduce his taxes by setting up a corporation and leaving part of his earnings in the corporation.

This growing practice has given such individuals an unfair tax advantage in comparison with employed persons who cannot use the same tax advantage.

There are also other areas where the application of the small business tax rate is not appropriate. As a result of court decisions, the income eligible for the small business deduction (that is, active business income) has been broadened to include passive investment-type income. For example, it has been held that income from the holding of mortgages and real estate rentals qualifies for the low tax rate applicable to small businesses.

Changes are proposed in order to ensure that the original intention of these tax benefits is preserved. The term "active business" will be defined so as to direct the benefits of the small business incentives to those Canadian-controlled private corporations that engage in specified activities. These changes will eliminate the undue deferral and reduction of tax in other cases.

"Active business" will include the business of manufacturing, processing, mining, operating an oil or gas well, prospecting, exploring or drilling for natural resources, construction, logging, farming, fishing, leasing property other than real property, retailing, wholesaling, transportation and other prescribed businesses.

In this way the very favourable tax provision will apply to small businesses that need funds to expand and create jobs.

These changes are effective for taxation years beginning after 1978.

Income Bonds and Certain Preferred Shares

The budget will remove a favourable tax treatment for income bonds or debentures and term or retractable preferred shares that are issued after November 16, 1978.

Income bonds and debentures are obligations on which interest is payable only when the borrower has made a profit. They were originally provided for in the Income Tax Act in the 1930s to help companies in serious financial difficulty. Retractable preferred shares, of more recent origin, may be redeemed at the holder's option, and term preferred shares are now frequently issued for a limited period, often less than 10 years.

These types of securities have been considered for tax purposes as equity investments, although they are essentially debt obligations. As a result, income earned by banks and other financial institutions on such securities is received as tax-free dividends rather than as fully taxable interest.

Increasingly, however, these types of securities have been used instead of traditional debt financing, principally for major loans by chartered banks to large corporations. The annual cost of this favourable tax treatment to federal and provincial treasuries has increased to an estimated $500 million. This form of financing is growing rapidly and so the revenue loss is increasing.

The budget proposes legislation to ensure that, except in limited circumstances, interest and dividends paid on new issues of such securities will be treated as interest for tax purposes. This will not apply to a security issued pursuant to a written agreement made prior to November 17, 1978.

The new provision will, however, apply after today whenever the conditions of any existing income bond or debenture, retractable or term preferred share are altered, the term is extended, or the holder waives his right to redeem.

The amendment will not affect the tax treatment of common shares or ordinary preferred shares, nor will it affect term preferred shares issued for a period exceeding 10 years.

To allow the present favourable tax treatment to continue would mean that the revenue loss involved would have to be made up by higher taxes on individuals and on the large majority of other Canadian businesses not in a position to take advantage of such securities.

The new provision will prevent a further erosion in 1979-80 of an estimated $150 million in federal corporation tax revenues.

These types of securities have represented an attractive form of financing to borrowers who do not have taxable income. But the situation no longer arises only because a company is in financial difficulties. It also arises because of significant tax incentives, including fast write-offs for business properties.

Most of the funds borrowed through these securities have gone to large multinational and Canadian corporations, and have been provided by the chartered banks. A large part is going to refinance existing debt and in some cases to finance take-overs of other companies rather than to finance new projects. Some non-financial corporations have even proposed issuing these securities simply to raise funds for investment in higher-yielding debt obligations. The effect of the financing has been to permit the transfer to lending institutions of some part of the benefits of unused tax savings from incentive deductions.

In order to accommodate standard estate planning techniques for transferring a family corporation to children, the new legislation will not affect retractable preferred shares issued by a corporation to a related shareholder.

In certain cases, these securities are used legitimately to assist a borrower in financial difficulty in order to permit payments on debt only when profits are made. The current tax treatment will continue to apply to such cases.

Air Transportation Tax

The budget proposes increases in the air transportation tax, whose proceeds are allocated to help finance the air transport service provided by the Department of Transport.

It is proposed that the existing tax on transportation of a person by air within the taxation area—that is, Canada, the United States and the Islands of St. Pierre and Miquelon—be increased to 15 per cent from 8 per cent, with a maximum of $15 (presently $8). The specific tax on international air travel between Canada and points outside the taxation area would be increased by regulation to $12 from the current $8. The allowable statutory maximum for this tax would be increased to $15 from $10. In order to reduce the level of double taxation of air travel between Canada and the United States, the regulations will be amended to provide a reduced rate of Canadian tax where the 8 per cent ad valorem tax imposed by the United States also applies.

The proposed increases will take effect April 1, 1979, for tickets purchased in Canada, and on July 1, 1979, for emplanements on and after that date with respect to tickets purchased outside Canada.

These increases will provide an additional $72 million in fiscal year 1979-80 toward the cost of air transport services which would otherwise have to be paid from general tax revenues. This is a major step in the ongoing program to shift the costs of financing the air program from the general taxpayer to the users of the system.

It is also proposed that the air transportation tax which is imposed under the Excise Tax Act, will eventually be converted to a user charge to be levied on the carriers under authority of the Aeronautics Act. To permit this conversion, the Excise Tax Act will be amended to provide authority to repeal the air transportation tax on a date to be fixed by Order of the Governor in Council, subject to negative resolution of Parliament.

The proposal to convert to a user charge is consistent with the cost-recovery systems adopted in the late 1960s by a number of European countries. The timing and details of the conversion of the Canadian tax to a user charge will be determined through extensive consultations between the Department of Transport and the air industry. Consequently, only the broad outlines of this proposal are being announced at this time.

Registered Retirement Savings Plans

The April 1978 budget increased significantly the alternatives for realizing retirement benefits out of registered retirement savings plans. Changes were also introduced for determining the tax liability when the benefits under such plans are transferred on death. These changes required any balance in a plan on the death of an annuitant to be included in his income in the year of death except to the extent that the balance was transferred to a surviving spouse. Accordingly, only the after-tax proceeds would pass to an annuitant's heirs other than his spouse. This treatment recognized that the tax saving and deferral allowed in connection with a registered retirement savings plan is intended to assist the taxpayer to provide an income in retirement for himself and his spouse and is not intended to subsidize the creation of estates.

Since the presentation of the April budget, the government has concluded that some accommodation should be made in the rules to deal with the situation where both parents die, leaving behind minor or disabled children.

Accordingly, where there is no surviving spouse, specified amounts passing to a dependent child or grandchild of the annuitant will be included in the income of that child or grandchild, and not in the income of the deceased annuitant, and such amounts will qualify for the purchase of an income-averaging annuity contract. The amounts qualifying for this treatment are related to the age of the child. These rules will apply as of June 30, 1978.

Life Annuities

Under the existing Income Tax Act rules, it is possible to avoid income tax on interest income by investing in certain types of life annuity contracts.

Normally, life annuity contracts provide monthly annuity payments starting when the purchaser reaches a specified age and continuing until his death or the death of a named beneficiary. The contract may also provide that the annuity payments will be made over a guaranteed term. The Income Tax Act provides that the interest portion of each annuity payment is taxed and the balance, representing a return of capital, is not taxed.

Recently, some annuity contracts have been structured in such a way as to ensure that the interest portion thereof may pass tax-free after the death of the purchaser of the contract. This is achieved by arranging annuity payments to commence on a date well beyond the purchaser's normal life expectancy. At the time of death, any funds accumulated under the contract would ordinarily be distributed tax-free to a beneficiary even though a substantial portion of the amount represents interest income accumulated over the life of the contract.

The budget proposes that after 1979 the accumulated interest income realized on any lump sum or other payment under a life annuity will be included in income. This proposal will not affect life annuity contracts issued before 1978 or any annuity under a registered retirement savings plan or other statutory deferred income plans.

The measures, of course, will not affect death benefits under ordinary life insurance.

Termination Payments

Some confusion has arisen out of the difficulty in separating the different component parts of a payment from an employer on the termination of employment, particularly where the employee alleges wrongful dismissal. In order to remove the uncertainty and to curtail certain abuses, special rules are proposed that will apply to amounts received by an employee on a termination of his office or employment after November 16, 1978. Such amounts, to a maximum of 50 per cent of his employment income for the preceding twelve months, will be taxable but will qualify for the purchase of an income-averaging annuity contract. The tax treatment of the excess will depend upon the nature of the payment.

Unemployment Insurance

Amendments to the Unemployment Insurance Act now before Parliament would require an individual who has received unemployment insurance benefits in a year and who has income for the year in excess of a stated limit to repay a portion of excess benefits on the filing of his tax return.

A consequential amendment to the Income Tax Act is needed to allow a taxpayer in such a case to claim a deduction for the benefit repayments in the taxation year to which the benefit repayment relates rather than in the year in which it is actually repaid.

Corporations and their Shareholders

Refundable Tax

The refundable dividend tax account of a private corporation consists of a portion of the tax paid by it on certain categories of its income. This tax is refunded to the corporation at such time as the income is distributed to shareholders by way of a dividend. Consequently, the combined corporate and shareholder tax on investment income passed through a private corporation is the same as the income tax that would apply if the income had been received directly by the shareholder. This tax refund mechanism permits what is generally referred to as the integration of the corporate and shareholder tax.

The refundable tax was originally intended to apply only to investment income of private corporations. Changes proposed in the budget will ensure that for taxation years commencing after 1978 the refund will not apply to the tax on business income or, in the case of a corporation controlled by non-residents, to the tax on real property rental income. This will ensure that only the tax on investment income will be refunded. In addition, interest and dividends paid on income bonds and term preferred shares will not qualify for a tax refund to the corporation.

Definition of Business Investment Loss

Shareholders of Canadian-controlled private corporations may deduct as an "allowable business investment loss" one-half of any loss realized on the sale of their shares. The value of shares existing on Valuation Day may be reduced by reason of dividend payments. This presents opportunities for abuse and the budget proposes to deny the deduction of an allowable business investment loss on shares issued before 1972. However, any losses on such shares would continue to qualify for deduction as a capital loss.

$1,000 Investment Income Deduction

The Income Tax Act provides a $1,000 deduction for Canadian investment income—interest, dividends and capital gains. This measure, introduced to offset the impact of inflation, has provided an unintended benefit to certain deemed dividends arising on the redemption of shares. Such dividends received after November 16, 1978 will no longer qualify for the $1,000 investment income deduction. This change will not affect the normal $1,000 deduction for ordinary dividends.

Stock Dividends Paid to Non-Residents

At present, a stock dividend paid by a public corporation to a foreign shareholder is subject to the non-resident withholding tax only when the shareholder owns more than 10 per cent of the class of shares on which the stock dividend is paid. These rules permit the issue and immediate redemption of a stock dividend on a portfolio shareholding without the imposition of the tax which would normally apply to dividends paid abroad.

The budget proposes changes that will require the withholding tax to apply to all stock dividends to non-residents paid on portfolio shareholdings except those which are paid in shares of the same class as that on which the dividend has been paid.

Amalgamations

The Income Tax Act provides special rules that apply on the amalgamation of Canadian corporations. Changes in these rules have been proposed in the budget to recognize developments in Canadian corporate law.

In addition, changes are proposed to the rules applying to the amalgamation and winding-up of a corporation to restrict their application to corporations that are taxable Canadian corporations.

Underwriting Expenses

The present Act denies the deduction of certain expenses incurred by taxpayers in the course of borrowing funds or issuing shares. The budget proposes to broaden the application of the deduction for a commission, bonus, fee or other amount paid or payable after November 16, 1978 on account of services rendered by a person as a salesman, agent or dealer in securities in the course of borrowing funds or issuing or selling shares. In addition, the deduction will apply to the corresponding expenses incurred by a unit trust.

Inventory Adjustment

The income tax system permits the deduction of capital cost allowances rather than depreciation reflected in the taxpayer's financial statements. Under most cost accounting systems, depreciation is included along with labour, raw material and overhead charges in determining the cost of goods manufactured. Accordingly, such costs are ordinarily reflected in the cost of unsold inventories at the end of a fiscal period. Thus, these costs do not enter into the computation of profits reflected in the financial statements until the inventory is sold.

The budget proposes that the same rules will apply for the computation of income for tax purposes. As a result, the amount of depreciation included in a taxpayer's inventory at a year-end will be required to be included in income for that year and will be deductible in the subsequent year.

This measure will not in any way affect the rules relating to the capital cost allowance system.

Pension Fund Corporations

The Income Tax Act presently exempts from tax corporations "incorporated solely in connection with, or for the administration of, a registered pension fund or plan".

This limitation is less restrictive in practice than the words imply. As a consequence, the definition of an exempt pension trust or corporation is to be modified.

The new definition will include only existing corporations all of the shares of which are held at all times after November 16, 1978 for the exclusive benefit of registered pension plans. The exemption for pension fund corporations will also apply to any new corporations formed by them for the purpose of investing in properties which would be qualified investments if they were owned directly by the pension fund corporation.

International Taxation

The foreign accrual property income (FAPI) provisions in the Income Tax Act are designed to discourage the use of tax havens to avoid tax on investment income. These provisions were not intended to interfere with bona fide international operations of Canadian companies. The existing rules produce inappropriate results for certain currency gains or losses resulting from foreign exchange fluctuations. In recognition of this, the budget proposes that for the 1976 and subsequent taxation years any currency gain or loss on inter-affiliate debt be excluded from FAPI provisions.

Under the existing Act, a corporation may elect to treat a portion of any proceeds of disposition on the sale of a share in a foreign affiliate as a dividend. Recognizing that the information on which the election is made may not be readily available, the budget proposes a two-year extension of the due date for the filing of the election, subject to a late filing penalty.

Taxation Proposals of Industry Sector Task Forces

The First Ministers' Conference in February started a process of private sector consultations on measures to improve the performance of and outlook for the manufacturing, construction and tourism sectors in the Canadian economy. Some 23 industry Task Forces composed of representatives of management, labour and the academic community, with provincial representatives (excepting Alberta) acting as observers, were formed. They produced reports reflecting conditions in their industries. These reports covered a broad range of themes and the information and proposals contained in them will be an important element in the development of future industrial policies.

Following the work of the industry sector Task Forces, a Second Tier Committee was established consisting of a Chairman from the business sector and representatives from the Canadian Labour Congress, business and the academic community. This group worked from the sector reports, identifying common viewpoints, and presented policy recommendations applicable both to the economy generally and to specific industries.

One of the themes receiving considerable emphasis was taxation policy. A number of recommendations for relieving tax action are made in the 23 individual Task Force reports and in the report of the Second Tier Committee. The proposals, which are summarized in Table 1, cover enhancement and extension of tax incentives provided in the past as well as special new incentives for specific sectors.

The taxation proposals in the Task Force reports are directed primarily toward providing greater incentives for investment and economic activity. Taken together, the proposals would represent a major restructuring of the federal corporation income tax and commodity tax systems in support of these objectives.

This budget paper brings together in one document the government's response to these tax proposals, so as to facilitate their consideration in the perspective of over-all tax policy. This also provides the opportunity to relate the present budgetary changes and other recent tax measures to the concerns identified by the Task Forces.

While the provision of special tax incentives can be an important instrument of government policy, this use must be carefully balanced against other functions and objectives of the tax system, and against the possiblity that desired results can be achieved more effectively through other means. In this respect, the

Second Tier Committee expressed three concerns that arise from the strong emphasis in the Task Force reports on the incentive to invest and concentration on opportunities for individual sectors' economic progress. These concerns are shared by the government.

First, the Committee noted the need for taxation policy to contribute to social policy in such areas as the redistribution of income to lower-income groups. This role is weakened by the availability of extensive tax concessions. The government has always believed that it is necessary to balance concerns of equity with the need to provide tax incentives to promote particular economic ends.

Second, the Committee observed that "If all the tax recommendations in the Task Force reports were implemented, a massive reduction in government revenues would follow". This would necessarily lead either to increased taxation for individuals and businesses not receiving the incentives, or to reduced services from governments or to some combination of both. Hard choices are required. There will always be genuine room for disagreement about where a balance should be struck.

Finally, the Second Tier Committee recommended that special tax concessions for particular industries should be based only on a clearly established rationale. This principle recognizes the importance of all types of industry to Canada and enunciates the philosophy that special tax incentives should exist only where exceptional national priorities can be identified. The government is in full agreement with this viewpoint. Proliferation of a large number of tax incentives tailored to individual sectors or circumstances will in the end dilute the effectiveness of each incentive and risk serious harm to the efficiency of the Canadian economy while adding to the complexity of the tax system. In cases where special tax treatment now exists—for example, for small businesses, manufacturing, exploration, research and development—important national priorities have been identified. A corollary to assuring that incentives are introduced only where a major priority exists is that incentives should be frequently reviewed as action may be needed from time to time to reallocate resources to other areas. This budget contains its share of such measures.

For the reasons noted above, it is neither practicable nor desirable to adopt in a broad fashion the many proposals in the Task Force reports. Nevertheless, the nature of the proposals and the discussions in the reports clearly identify six major areas of concern involving tax policy. These are related to inflation accounting, investment incentives, the level of taxation, international competitiveness, research and development and certain industry situations. This budget has introduced tax measures which respond to some of these concerns. In others, there are good reasons why the federal government has not responded. With respect to some of these concerns, there are current, but unresolved, developments which the government believes have a bearing on the direction policy should take. In a few cases, there are strong reasons for continuing the existing tax treatment.

The major tax policy concerns identified in the 23 Task Force reports are discussed below in conjunction with government actions and policy in each

area. A brief discussion is also presented in some cases for concerns that were raised by only a few Task Forces or that are more technical in nature.

Inflation Accounting

The sectoral Task Forces directed considerable attention to the effect of inflation on the measurement of business income for tax purposes. Proposals included the adoption of a comprehensive inflation accounting system and various ad hoc changes in inventory accounting and in the capital cost allowance system.

The government has recognized that distortions in income measurement do arise from the use of historic cost accounting in an inflationary environment and has publicly stated its interest in a comprehensive solution to this problem. As accounting data are used for more than tax computation, this is an issue on which the private sector must take the lead. The government has, however, actively supported the activities of accounting bodies and business groups in Canada in their review of the issue. In the interim, tax changes such as the 3 per cent inventory adjustment, the investment tax credit and accelerated capital cost allowances have been a positive response, substantially mitigating the impact of inflation on business taxation.

That inflation adjustment of financial statements presents complex problems is evident from the fact that no country has so far adopted a widely-accepted, comprehensive inflation accounting system. This is despite intensive international efforts to develop such a system. Nevetheless, some conclusions have been forthcoming. In particular, it has now come to be generally accepted that inflation not only leads to an overstatement of profits because of first-in-first-out (FIFO) inventory and historic cost depreciation accounting, but also to an understatement of profits because accounting conventions overstate the real cost of corporation borrowing during an inflationary period. This latter point is discussed fully in the studies which have been carried out by the Economic Council of Canada and by the Ontario Committee on Inflation Accounting. When the implications of debt financing are recognized along with the full implication of tax changes that have been adopted, the over-all level of Canadian corporation taxation does not differ greatly from what it would be under a comprehensive system of inflation accounting.

The government will, however, continue to support the development of appropriate inflation accounting systems in the private sector because of the importance of accurate information on business operations for the efficient operation of the economy, and the possibility that the existence of such information would allow a fairer distribution of the total corporation tax burden among sectors.

Incentives for Investment

Weakness in capital investment has been a feature of the current period of slow growth. Recent budgets have introduced tax measures to stimulate

capital investment including extension and enhancement of the investment tax credit, capital gains rollovers on replacements of business property and incentives for transportation and energy development. These latter are particularly important in that they act indirectly to produce a more favourable investment climate throughout the economy.

A primary emphasis of the Task Forces was on the need for investment incentives, and the reports contained various proposals to provide additional stimulus to capital spending. These included enrichment of both the investment tax credit and the capital cost allowance system. Some of these measures if applied to all sectors could reduce federal corporation tax revenues by billions of dollars.

This budget, however, does respond in a very positive manner to the suggestions made by the Task Forces. It extends the investment tax credit indefinitely. The rates of credit are increased, most notably for investments in designated areas. The coverage of the credit is broadened to include transportation. The extension and enrichment of the investment tax credit and the two-year write-off for manufacturing and processing, which has been permanent since 1975, provide a very attractive environment in which to undertake modernization and expansion. Other broad-based fiscal measures introduced in the budget will help sustain growth in consumer demand, thus making investment far more attractive and profitable for the private sector.

Several sectoral reports suggested that the effective rate of the investment tax credit be raised by removing the requirement that the credit received reduce the capital cost allowance (CCA) base. The rates of investment tax credit have been chosen with regard to the degree of incentive provided and government revenue requirements. The reduction of the CCA base by the credit received has been recognized in the choice of rates and is desirable in order to provide neutral treatment of longer- and shorter-lived assets. In the United States, where the credit is not deducted from the capital cost allowance base, a similar result is achieved by giving only partial credits to assets with a life of less than seven years. The more appropriate method of enhancing the value of the credit is through increasing the credit rates directly, as proposed in this budget.

The budget proposes that the two-year write-off of water and air pollution equipment scheduled to expire in 1979 be extended indefinitely. This responds to a concern raised by the forest products industry and is of significant benefit to the mining industry. The incentive for construction of multiple-unit residential buildings has been extended for one year.

Carry-Forward of Losses and Investment Tax Credit

Business losses and the investment tax credit may be carried forward to reduce tax for up to five years. Given the discretion in timing available to taxpayers in claiming capital cost allowances, this provides for full utilization of the amounts in all but exceptional circumstances. Many sectors, in arguing for extension of the carry-forward, referred to the United States, where the period is seven years. However, it should be noted that in that country CCA must be claimed in full in each year, giving taxpayers significantly less flexibility in the claiming of deductions.

The five-year time period in Canada matches the period for tax reassessments. To change the connection among the two types of carry-forwards and the reassessment period would entail considerable administrative difficulties for taxpayers and taxation authorities, without significantly aiding many taxpayers.

Corporation Income Tax Rates

The top statutory federal corporation income tax rate is 36 per cent. This represents a reduction from the 40 per cent rate prevailing before 1972. Special deductions provide lower federal rates of 30 per cent for manufacturing and processing and 15 per cent for small business (10 per cent if engaged in manufacturing). Although Table 1 refers to a few recommendations for reductions in tax rates, these were not as prevalent as proposals for inflation adjustment or particular investment incentives.

The accompanying budget paper, *The Tax Systems of Canada and the United States*, indicates that the combination of tax rates, incentive deductions and exemptions and tax credits produces a Canadian corporation tax structure that is not at all out of line with that existing in the United States. In manufacturing and for small businesses, the Canadian system compares very favourably. Manufacturing, in particular, enjoys effective tax rates in Canada, as a percentage of corporation pre-tax profits, that average some 10-12 percentage points lower than those in the United States. Given these facts, the need for broad-based reductions in tax rates is unclear. As the Second Tier Committee noted, tax differentials must be evaluated against other cost differentials in areas such as labour and transportation costs. While these latter costs may or may not be higher in Canada, a good argument can be made for attacking any problems in these areas directly, and on a broad front, rather than by acting to offset the effects on particular sectors through tax reductions.

The Second Tier Committee recommended that the inconsistencies in corporation tax rates between industries be reviewed. The low tax rate on small business is intended to offset some market disadvantages faced by smaller firms and provide an environment for dynamic new businesses. The differential rates in favour of manufacturing and processing were introduced to contribute to industrial development, maintain our competitive position and enhance cash flows available for investment in a sector with a high degree of value added. Both of these provisions are generally accepted as desirable elements in the Canadian tax structure.

Consolidated Tax Returns

A few sectoral reports recommended that consolidated tax returns be allowed for related corporation groups in order to allow losses in one or more operations to be offset against income in related, profitable companies. In response to this, it should be recognized that in a majority of cases companies can utilize losses within present tax laws. The provisions for consolidated tax returns are generally very complex and would require significant amendments to the Income Tax Act.

A system of consolidated tax returns would allow considerable flexibility for corporations under common control to transfer losses, and thereby tax deductions, within the corporation group. In Canada, there are some significant variations in the rates of federal and provincial taxes applicable to corporation income. Strong incentives would arise to create a number of corporation entities to take advantage of the flexibility provided by consolidation to minimize tax liabilities. This could result in substantial loss in tax revenues.

Any system of consolidation which attempted to deal with this major problem would likely be very complex. This is at a time when the government is attempting to simplify the body of technical rules applying to business. However, the existing situation does produce some undesirable results and attempts are being made to develop reasonable solutions.

Research and Development (R&D)

A significant number of sectors proposed increased tax incentives to industrial research and development. The Second Tier Committee recommended increased government assistance that would involve a package of tax measures and direct shared-cost grant programs.

The federal government shares the goal of increasing Canada's R&D effort with emphasis on development and use in Canada. To this end, significant income tax incentives for those engaging in any level of R&D expenditure have been combined with additional incentives for those increasing their R&D expenditures.

Current and capital expenditures on R&D qualify for a 100 per cent write-off in the year they are made. Since 1977, R&D expenditures have qualified for the investment tax credit. This budget proposes that the basic rate of investment tax credit for R&D be doubled from 5 to 10 per cent. The rate of credit will be set at 20 per cent in the Atlantic provinces and the Gaspé.

The budget contains a special provision to encourage R&D by small Canadian businesses. Such businesses qualifying for the low rate of corporation tax will get an investment tax credit of 25 per cent on all their R&D expenditures irrespective of their location in Canada.

The budget of April 10, 1978 provided for an additional deduction from income for tax purposes of 50 per cent of the costs of R&D expenditures in excess of their average levels for the preceding three years.

The total tax value of these special incentives (not including the 100 per cent write-off) is over $100 million per annum. In addition, the government provides a variety of expenditure grants and subsidies to industrial R&D.

International Competitiveness

The budget paper, *The Tax Systems of Canada and the United States*, indicates that most Canadian industries enjoy a lower rate of tax than do their American counterparts. As the U.S. is our principal trading partner, this helps to place both import-competing and exporting firms in a competitive position.

Some sectoral groups expressed concern about prospective tariff changes and export-incentive programs in other countries. The maintenance of international competitiveness is obviously a critical concern to Canadians. When tariffs have been changed in the past or other countries adopted new export-oriented programs, these were followed by significant changes in Canadian tax or expenditure policy to provide for industrial adjustment and maintain competitiveness as required.

Other Incentives Affecting Specific Industries and Other Recommendations on Corporation Income Taxation

The sectoral Task Forces presented a large number of recommendations applicable to specific industries. In the interest of avoiding complexity in our tax system and keeping provisions as broad as possible to maintain fairness, it would not be desirable to develop a tax system which contains numerous incentives applicable to individual sectors.

There are situations in which special consideration is required. As in the past, the government will review these individually, although always from the position that a very strong case needs to be presented for special treatment.

This budget, for example, proposes increased incentives for new mine development. These changes are responsive to sector concerns and to identified weaknesses in exploration and new mine development. They are being adopted after a federal-provincial review of economic conditions and taxation in the mining sector. The changes represent a federal government initiative in an industry where provincial governments are also major collectors of revenues.

Some Task Forces suggested that a system of value-added taxation be considered. While such a change would not be without merit, it would not solve all our economic problems and would introduce new uncertainties. It needs to be recalled that the last six years have seen dramatic changes in the tax system. At this time attention needs to be given to stability in taxation and simplification of the tax system. Changes of a far-reaching nature need to be resisted. It would not serve a useful purpose to embark on an extensive review of the value-added tax proposal at the present time.

A number of Task Forces referred to the need for federal and provincial cooperation in fiscal policy. While it would not be possible nor desirable to have a rigid, uniform system of tax and expenditure policies in a diverse federation such as Canada, some important avenues for cooperation do exist. The consultative industry task force process itself arose from a meeting of First

Ministers on economic issues. Finance Ministers meet on a regular basis to exchange information and discuss economic matters. Joint federal and provincial reviews of issues of common concern are also carried out frequently. A recent example is the review of resource taxation. The federal government is committed to these avenues of cooperation and will continue to support them.

Incentives for Equity Investment and Other Forms of Financing

In common with the other industrialized countries, Canada has experienced a period of business uncertainty with a corresponding weakness in the markets for equity financing. There have been signs of significant improvement in equity markets this year, including the relatively strong performance of Canadian stock markets.

To some extent, this undoubtedly reflects the major changes that have been made in the tax treatment of businesses and their shareholders in the past few years. Of particular and direct importance to equity investors are the enhanced dividend gross-up and tax credit, the deferral of capital gains tax on inter-generational transfers of shares in small businesses and on dispositions of business property for relocation purposes and the opportunity to make a permanent election of capital gains treatment on most types of Canadian securities.

The tax changes referred to above along with other changes in corporation taxation provide attractive opportunities for equity investment in Canada. Indeed, income from capital is in many cases taxed at significantly lower rates than employment income.

Personal Taxation

The proposals of the Task Forces were understandably concentrated in the area of business taxation. A few did, however, advance recommendations for lower personal taxes.

The Second Tier Committee recommended a review of mortgage interest deductibility, particularly in the context of providing greatest benefits to lowest income groups. The government has presented its view of such a deduction. A consideration of proposals made to date for mortgage interest deductibility shows them to be generally regressive, discriminatory against tenants and to produce economically perverse effects on housing prices, capital markets and interest rates.

Other recommendations for personal tax reductions were based on such reasons as their beneficial effect on labour costs or their effect in enhancing personal incentives to work or invest.

The government has introduced signficant personal tax cuts. Automatic indexing is a unique feature of Canada's tax system resulting in substantial automatic annual reductions in personal income tax levels. This budget further

reduces personal taxes on employees by increasing the employment expense deduction. The study of the U.S. and Canadian tax systems, contained in the budget material, shows that personal tax levels in Canada are lower than in the United States in a majority of cases. That study also shows that, through the dividend tax credit and other measures, Canada's tax treatment of personal investment income is also favourable.

The potential effects of taxation in decreasing personal initiatives must always be kept in mind in framing budgetary policy. Responding to such concerns must also take into account the equity and complexity of the tax system and whether the revenue foregone could be more productively directed to other areas.

Sales Taxation

Most of the recommendations in this area were for an expansion of the exemption provisions of the Excise Tax Act, and for structural changes in the commodity tax system. The Standing Committee of the House of Commons on Finance, Trade and Economic Affairs will be considering the *Report of the Commodity Tax Review Group* with a view to recommending some modification to the structure of Canada's commodity tax system. The report makes many specific recommendations which directly address the concerns raised, such as those related to the effect of the federal sales tax in discriminating between imports and domestically-produced goods. As that study progresses, it will be appropriate for the government to also consider the range of goods and activities which should enjoy exemption from commodity taxes.

The budget proposes a reduction in the general rate of manufacturers' sales tax from 12 per cent to 9 per cent. This measure was adopted for stimulative purposes and will have a beneficial effect on price and cost pressures.

Table 1
Industry Sector Task Force Recommendations on Federal Government Taxation Policy*

Recommendation	Sectors Making Recommendation
1. *Inflation Accounting*	
—The Federal Government should amend corporate tax legislation to recognize and allow for the impact of inflation on corporate profits.	—Electrical —Fertilizers —Petrochemicals —Plastics Processing
—A new system of inventory allowance or of inventory accounting for tax purposes should be adopted in response to inflation. (Specific proposals are given below under *Deductions for Corporate Income Tax Purposes: Inventories*).	—Forest Products —Iron and Steel —Non-Ferrous Metals —Textiles and Clothing —Plastics Processing
—New methods of adjusting for inflation should be adopted in relationship to the capital cost allowance system. (Specific proposals are given below under *Deductions for Corporate Income Tax Purposes: Capital Cost Allowances*).	—Cement and Concrete —Commercial Printing —Non-Ferrous Metals —Textiles and Clothing
2. *Deductions for Corporate Income Tax Purposes*	
(a) *Inventories*	
—The 3 per cent inventory adjustment should be increased.	—Furniture —Iron and Steel —Plastics Processing —Textiles and Clothing
—LIFO inventory valuation should be introduced for tax purposes.	—Forest Products —Iron and Steel —Non-Ferrous Metals —Plastics Processing
—The definition of the inventory allowance should be extended to include the air transportation sector and such items as furnishings.	—Tourism
(b) *Capital Cost Allowances*	
—The Government should make permanent or guarantee the permanence of its present system of accelerated write-offs.	—Commercial Printing —Forest Products —Iron and Steel —Petrochemicals
—Fixed assets should be indexed to inflation for capital cost allowance purposes.	—Non-Ferrous Metals
—The two-year write-off of pollution control expenditures, currently scheduled to expire at the end of 1979, should be extended indefinitely.	—Forest Products
—The period in which the cost of eligible capital expenditures can be written off for tax purposes should be reduced from two years to one year.	—Electrical

* This table summarizes the recommendations for federal government taxation policy presented in the 23 Sector Task Force reports. Proposals which are essentially similar have been grouped together under a general description. Therefore, the actual proposal from a particular sector may include additional details or specify some limitations. Reference should be made to the individual reports for a full description of particular recommendations.

Recommendation	Sectors Making Recommendation
2. *Deductions for Corporate Income Tax Purposes* (Cont'd)	
—Capital cost allowances for buildings and older fixed assets should be accelerated.	—Cement and Concrete —Electrical —Textiles and Clothing
—The fast write-off for manufacturing and processing assets should be extended to all industrial sector capital expenditures, logging equipment and renovation and conversion costs for existing properties in the accommodation industry.	—Electrical —Forest Products —Tourism
—A capital cost allowance rate of 100 per cent should be applicable to housekeeping and other small equipment in the accommodation industry and to equipment purchased for primary use in offshore operations or for use in the manufacture or development of offshore hardware.	—Tourism —Ocean
—Greater flexibility in claiming the 33 ⅓ per cent allowance for new construction and major alterations or conversions of vessels should be granted.	—Shipbuilding
—There should be an increase in the capital cost allowance rate for commercial air carriers and for buses used for sightseeing.	—Tourism
—A study should be carried out to determine an equitable method whereby the benefits of capital cost allowances available to existing companies could be made available to new companies.	—Petrochemicals
3. *Investment Tax Credits*	
—Consideration should be given to an increase in the rate of investment tax credit.	—Cement and Concrete —Electrical —Forest Products —Iron and Steel —Petrochemicals —Textiles and Clothing
—The capital cost of the asset used for computing depreciation should not be reduced by the amount of the tax credit.	—Electrical —Forest Products —Iron and Steel —Petrochemicals —Textiles and Clothing
—The cost of restructuring within the industry for production efficiencies should be recognized within investment incentives definitions.	—Electrical
—Pollution control assets should be granted a higher rate of investment tax credit than that available on production machinery and equipment.	—Cement and Concrete —Iron and Steel
—Logging equipment should be included in the category of qualified assets for the investment tax credit.	—Forest Products
—The 5 per cent tax credit for investment in renovations and conversions should be available in the accommodation sector.	—Tourism
—A study should be carried out to determine an equitable method whereby the benefits of the investment tax credit available to existing companies could be made available to new companies.	—Petrochemicals

Recommendation	Sectors Making Recommendation
4. *Carry-Forwards of Losses and Investment Tax Credits*	
—The five-year limitation on loss carry-forwards should be extended.	—Ocean —Textiles and Clothing
—There should be more generous carry-back and carry-forward provisions for unused amounts of investment tax credit.	—Cement and Concrete —Iron and Steel —Petrochemicals —Textiles and Clothing
5. *Corporate Tax Rates*	
—Governments should be prepared to reduce the tax on corporate profits to about 35 per cent while maintaining the current level of taxation for small business.	—Plastics Processing
—Logging income and construction activity should receive the manufacturing and processing deduction.	—Construction —Forest Products
—Profits from new businesses or on products resulting from R & D innovation should be subject to reduced tax rates.	—Electronics
—Federal and provincial corporate taxes on profits of firms in the footwear and allied manufacturing sectors should be reduced until stabilization is achieved in these industries. The net federal tax rate should be reduced from 30 per cent to 26 per cent.	—Footwear
—The inconsistencies in the corporate tax rate and tax concessions from industry to industry should be reviewed and their continuation should be dependent on a more clearly established rationale.	—Second Tier Committee
6. *Consolidated Tax Returns*	
—Within a corporate group which can demonstrate a major degree of common (equity) interest, provisions in the Income Tax Act should be changed to allow losses in one (or more) of its companies to be offset against income in other profitable operations.	—Food and Beverages —Forest Products —Iron and Steel
7. *Research and Development*	
—There should be greater tax incentives for industrial research.	—Electrical —Electronics —Food and Beverages —Forest Products —Machinery
—The present R & D tax incentives should be applied to "base" as well as incremental expenditures.	—Electrical —Electronics —Forest Products
—The definition of R & D expenditures eligible for the above treatment should be broadened to cover expenses which are essential to the development of new or improved products or processes.	—Electrical
—Governmental assistance to R & D should be in the form of a package of available measures (i.e. tax measures in the form of write-offs and/or tax	—Machinery —Second Tier Committee

Recommendation	Sectors Making Recommendation
7. *Research and Development* (Cont'd) credits, or direct shared-cost grant programs) that can be applied flexibly depending on the characteristics of individual projects.	
8. *International Competitiveness*	
—Government should ensure that higher costs which cannot be overcome by industry, such as those due to climate, will continue to be offset by tax arrangements now in existence, such as accelerated depreciation, investment tax credits and lower corporate tax rates than now exist in the U.S.	—Fertilizers
—The Federal Government should provide a special tax incentive for high risk exports of manufactured goods such as allowing an accelerated write-off of "export derived losses" at (say) 150 per cent of actual costs.	—Urban Transportation Equipment
—The Federal Government should examine the feasibility of introducing specific measures to counteract the effect of foreign export subsidies such as the DISC program in the U.S.	—Machinery
—Special investment allowances should be considered for the replacement or modernization of facilities threatened by tariff reductions.	—Forest Products
—Changes in corporate taxation should be evaluated in the context of all the factors that determine international competitiveness. The differential treatment of corporations from country to country (whether in terms of the direct tax rate, or in terms of tax concessions such as accelerated write-offs, tax credits, etc.) are as crucial as other cost items, including wages, transportation, and tariffs, and should be considered in that light.	—Second Tier Committee
9. *Other Incentives Affecting Specific Industries*	
—The three year tax exemption for new mines, automatic depletion allowances and depletion allowances on dividends should be reinstituted.	—Iron and Steel
—The 25 per cent resource allowance currently allowed on profits accruing from domestic iron-ore processing should be extended to the processing of foreign ores in Canada.	—Iron and Steel
—Federal and provincial governments should provide stable tax policies and, particularly for the potash industry, should coordinate total taxation at a level which will enable the industry to retain sufficient profits to re-invest and expand.	—Fertilizers
—The sale of family and small privately owned footwear manufacturing companies to children and/or employees should be facilitated by tax forgiveness or deferment on dividends to purchasers up to purchase costs.	—Footwear
—Regional loans and incentives to encourage plant location in designated areas should be combined with a corporate tax holiday for any five years of the first ten years of existence.	—Footwear

Recommendation	Sectors Making Recommendation
9. *Other Incentives Affecting Specific Industries* (Cont'd)	
—Equity investors in resident corporations engaged in the high technology, high risk ocean industry should be allowed a 150 per cent tax deduction against ordinary income. Such investments, when sold, should be subject to capital gains tax on the entire value received upon such sales.	—Ocean
—The tax deferral previously available on the disposition of vessels should be re-introduced.	—Shipbuilding
—The capital cost allowance restrictions regarding the leasing of aircraft by airlines and the withholding tax on aircraft lease and loan payments to non-residents should be removed.	—Tourism
—The electronics sector should be exempt from capital gains tax. There should be realistic phasing-out procedures for carry-forward of losses for taxpayers with capital losses.	—Electronics
—Furniture purchases should be reinstated as an allowable expenditure with the proceeds from a Registered Home Ownership Savings Plan.	—Furniture
—There should be a 15 per cent bonus valuation for the next three years for renovations and conversions in the accommodation sector.	—Tourism
—In order to encourage intensive forestry practices beyond those eligible for the stumpage offsets, a tax credit of 150 per cent should be provided for these additional expenditures.	—Forest Products
10. *Other Recommendations on Corporate Income Taxation*	
—The Federal Government should undertake to produce a green paper on corporate taxation within twelve months and the proposals should then be subjected to a full and public process of consultation with the private sector. The impact of personal income taxes on competitiveness and labour supply, capital gains taxation and employee stock options should be included in the review.	—Textiles and Clothing
—The feasibility of incorporating the most desirable features of the proposed Toronto-Dominion inverse value-added tax system into the existing corporate tax system should be considered.	—Plastic Processing
—The Federal Government should give serious consideration to a basic modification of its corporate tax structure in order to generate growth and create jobs in the manufacturing sector.	—Footwear
—Government policies should be aimed at creating a stable tax structure to minimize uncertainty and to facilitate a rationalized long-range planning program in the business sector.	—Iron and Steel
—There should be a greater degree of fiscal harmony between federal and provincial governments leadng to the adoption of a uniform income tax act for both federal and provincial purposes in order to reduce administrative costs.	—Iron and Steel

Recommendation	Sectors Making Recommendation
10. *Other Recommendations on Corporate Income Taxation* (Cont'd)	
—If programs implemented by governments are not of a permanent nature, these should contain specific commencement and termination dates which will be adhered to in normal circumstances.	—Commercial Printing
—The recently introduced employment tax credit program should become a permanent program to encourage continued increase in employment.	—Footwear
—Money for expansion should be made available by not taxing corporate profits until they are passed on to shareholders.	—Fertilizers
—Unrealized foreign exchange losses on capital accounts should be deductible from taxable income on an accrual basis.	—Textiles and Clothing
—The change in the Income Tax Act which no longer allows the offsetting of capital cost allowance against other income should be reversed.	—Shipbuilding
—Future legislation should recognize the advantages of leasing to the Canadian economy.	—Shipbuilding
—A greater degree of co-ordination of fiscal policy should exist among levels of government to meet national goals.	—Second Tier Committee
—An in-depth study should be made of the feasibility of implementing value-added based taxes in place of existing taxes.	—Second Tier Committee
11. *Incentives for Equity Investment and Other Forms of Financing*	
—Capital gains tax should be eliminated	—Cement and Concrete —Fertilizers
—Tax-free rollovers (i.e. deferral of tax through reinvestment) should be allowed for all investors.	—Non-Ferrous Metals
—Loss flow-throughs to investors in newly incorporated private companies should be permitted so that the losses earned by a new company in its starting years could be pro-rated through to the investors to be used in computing their personal tax situation.	—Electronics
—Capital instruments to provide tax-free income for a period of years with no erosion of the original capital invested should be allowed.	—Electronics
—The existing methods available to assist a new company with its initial financing problems such as income debentures and preferred shares should be maintained.	—Petrochemicals
—The government should encourage innovative forms of equity financing such as floating-term preferred shares.	—Iron and Steel
—Provisions of the Income Tax Act which relate to "undistributed income" and "the valuation of business assets" in connection with the sale or transfer of a business from one owner to another should be further simplified in order to remove those regulations which frustrate appropriate consolidations.	—Food and Beverages

Recommendation	Sectors Making Recommendation
12. *Personal Income Taxation*	
—Amendments should be made to the Income Tax Act to allow deduction of mortgage interest and municipal taxes from taxable income.	—Cement and Concrete —Furniture
—The deductibility of mortgage interest payments should be reviewed; such a review should give careful consideration to delivering the greatest benefits to the lowest income groups.	—Second Tier Committee
13. *Sales Taxation*	
—The current discrimination against Canadian manufactured products under the federal sales tax should be removed as soon as possible.	—Furniture —Second Tier Committee —Textiles and Clothing
—There should be consideration of sales tax cuts or the extension of current exemptions on products such as footwear and clothing.	—Footwear —Second Tier Committee
—All machinery and equipment used directly or indirectly in manufacturing and processing operations should be exempt from federal and provincial sales taxes.	—Iron and Steel
—Equipment purchased by a Canadian corporation primarily for leasing to companies engaged in offshore operations should be exempt from payment of federal sales tax at the time of acquisition regardless of the length of the equipment's initial offshore use.	—Ocean
—All construction materials should be exempt from sales tax.	—Cement and Concrete —Construction —Second Tier Committee
—Federal sales tax should be eliminated or reduced for a number of selective items of interest to foreign visitors.	—Tourism
—Provincial and federal sales taxes should be eliminated on equipment used in food preparation.	—Tourism
—Private aircraft should be exempt from the special excise tax on purchase of aircraft.	—Tourism
—The air transport tax should be removed completely from visitors originating outside the country or the tax should be reduced for all air travellers.	—Tourism
—Aviation fuel consumed in Canada should be exempt from the 12 per cent federal sales tax.	—Tourism
—The through-put charge on gallonage which is part of Transport Canada lease arrangements with fuel distributors should be excluded from the federal sales tax.	—Tourism