The Budget

presented by
the Honourable Jean Chrétien
Minister of Finance
in the
House of Commons
April 10, 1978

Department of Finance
Canada

Ministère des Finances
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Budget Speech

Mr. Speaker,

The purpose of my budget tonight is to take positive and responsible action to deal with the problems which face the Canadian economy in a very troubled world. These problems are complex and difficult. We are being held back by serious unemployment and inflation, and we must do all we can to deal with them. But we also face longer-term problems and opportunities calling for structural adjustment in many industries, sectors and policies. These were the challenges brought out very clearly by the recent Conference of First Ministers.

In the past days and weeks I have sought the advice of many individual Canadians. I have spoken to all provincial Finance Ministers. I have benefitted from vigorous public discussion of our economy. My cabinet colleagues and I have considered briefs from groups large and small, national and regional.

Many of the suggestions made to me for this budget would be popular politically but unwise economically. I will not follow such suggestions. I believe this is a time for Canada to face our problems critically and realistically. If we do, we can turn the tide against inflation and unemployment. The measures of this budget should secure and reinforce the progress we have already made.

It is now clear that many of our current difficulties have their roots in the period of extraordinary growth Canada experienced between the mid-1960s and the mid-1970s. With the great advantage of hindsight, we can see that we did not always use our good fortune wisely.

Our economy boomed. The world environment was good to us. Canadians enjoyed a very large increase in their standard of living.

But we all came to expect too much of the economy. Governments increased their spending too quickly. The money supply was increased too fast.

Too much was asked and given at the wage bargaining table. Other forms of income also rose too rapidly. Too little attention was paid to the long-run efficiency of the Canadian economy, and its ability to compete.

And so Canadians were not well prepared to deal with the shocks of the early 1970s. Sharp increases in the price of oil, food and other major world commodities speeded up our inflationary spiral.

World recession arrived and compounded our loss of competitiveness. A large deficit opened up in our balance of payments. Our growth slowed down. The loss of sales meant the loss of jobs.

At the same time, we experienced more conflict and confrontation in Canada. Conflict between the provinces and Ottawa. Conflict between separatist and federalist forces. Conflict between employers and employees. All of these things breed uncertainty and weaken the economy.

The Signs of Progress

By the fall of 1975 it was clear that strong economic action had to be taken. The anti-inflation program launched at that time has made a major contribution in turning our situation around.

The expenditures of all levels of government in Canada have since been brought under better control. In our own case we have cut back the growth in our total outlays from 26 per cent in 1974-75 to 18 per cent in 1975-76 to 10 per cent or less since then.

The Bank of Canada has brought down the rate of increase of the money supply in line with its announced targets for continued growth and declining inflation.

Wage increases have returned to more realistic levels. New settlements came down from 17 per cent in 1975 to 10 per cent in 1976 and under 8 per cent in 1977. They are now down to the guideline of 6 per cent.

The underlying rate of inflation has also been reduced. We can see this in the trend of non-food prices which has been improving steadily. Another indication is the fact that the average price of *all* the goods and services which Canada *produces* rose only 6.5 per cent last year, compared with 9.5 per cent in 1976 and 11.2 per cent in 1975.

The controls program has played a key role in these developments. Controls over prices and incomes cannot succeed unless they are supported by the right setting of fiscal and monetary policy. But the underlying rate of inflation would not have been brought down so quickly without the controls. Without their help, we would have had less growth and more unemployment.

Given the erosion that our competitive position suffered over several years, it was inevitable that an adjustment of the exchange rate would be required sooner or later. That adjustment has taken place in several stages. The government has permitted it to occur by allowing the exchange value of the Canadian dollar to move in response to changes in the balance of supply and demand in the foreign exchange market. That continues to be our policy.

It also continues to be our policy to intervene directly in the market to moderate short-term fluctuations in the rate of exchange. This intervention dampens the more erratic short-term movements. It also provides resistance to appreciable movements of the rate in either direction. The intervention does not prevent the exchange rate from moving in response to the market situation. It moderates the speed of change.

Such intervention gives rise to changes in Canada's official reserves. In the event of a sustained declining trend in the exchange rate, such as we have been experiencing, the drain on the official reserves can be considerable. In such circumstances it is prudent for the government to replenish the foreign exchange component of reserves by borrowing foreign currency. As Honourable Members know, we have been following just such a policy.

Changes in the official reserves arising from exchange market interventions reflect the overall balance in Canada's international payments. When, as at present, we have a deficit in the current account of our balance of international payments, changes in official reserves can be regarded as adjusting the net inflows of capital that finance the current account deficit.

In recent months the net inflow of capital to Canada, particularly that arising from the usual foreign borrowing of Canadian provinces, municipalities and corporations, has been low in relation to the size of the deficit on current transactions in goods and services. For seasonal reasons, this deficit is normally much larger in the first several months of the year than in the other months. In these circumstances the Government of Canada has used exchange reserves to supplement the inflow of capital. The Bank of Canada has raised the bank rate on two recent occasions to encourage Canadian borrowers to raise funds abroad. In summary, it is our policy to undertake such foreign borrowings as are required to replenish our reserves and to provide assurance that the government is in a position to supplement the net inflow of capital to Canada.

With our costs now under better control and a lower exchange rate, we have become more competitive internationally. This has helped us to turn around our trade balance from a deficit of $500 million in 1975 to a surplus of almost $3 billion in 1977.

In other ways, our progress has been no less important, but perhaps harder to measure. Expectations have changed. Hopefully they are more realistic. Some of the divisions in our society have been narrowed or closed.

We have also seen a remarkable improvement in relations between labour and management. In 1976 we lost 11.6 million man-days in strikes. Last year that number fell 70 per cent to only 3.4 million man-days. More important, labour and business are talking to each other about their common problems.

There is also a more effective dialogue among governments and between governments and business, labour and other groups in our society. It is not a matter of choice whether we pursue this dialogue. We *must* achieve more agreement on economic issues and find more ways to co-operate, or we cannot get the best out of our economy.

The Challenge of Structural Reform

The federal government discussed co-operation and structural change in the paper entitled *Agenda for Co-operation.* The First Ministers' conference was a milestone in federal-provincial relations both in terms of the range of policy agreement and the commitment to structural reform. A comprehensive work program is now underway as a result of the meeting. For example, studies are proceeding with the private sector in 22 manufacturing industry categories. A major effort is underway to cut down the burden of government regulation. Measures have been taken to help arrest and reverse the tourist deficit. Food and agricultural policies are under review. We are looking forward to developing the potential created for our fisheries by the 200-mile limit.

For my part, I can encourage useful structural adjustment as Minister responsible for tariffs and tax policy.

Commercial Policy and the Tariff

The multilateral trade negotiations now taking place in Geneva have longer-range potential for the productive sectors of our economy. We are participating actively in the talks, and seeking reductions in both tariff and non-tariff barriers to give us better access for our exports, especially highly processed resources and manufactured goods. We will also be prepared to reduce Canadian tariffs, but only in return for concessions of real value. Canada's development in the 1980s will depend very largely on the ability of our industries to grasp significant new export opportunities and compete more effectively against imports at home. As First Ministers have urged, we will be ready to support the private sector adjustments that will be needed for our success in the trading environment of the decade ahead.

The Geneva talks are moving ahead quickly and we hope for a successful conclusion in the coming months. In the meantime I am not submitting any major amendments to the Customs Tariff. However, I am proposing tonight that most of the temporary tariff reductions introduced in 1973 on a broad range of consumer products be extended for another year beyond their scheduled expiry date of June 30. The extension will contribute, as it has in the past, to our efforts to minimize inflation.

I am also proposing to withdraw the British Preferential rate from certain goods imported from Britain and Ireland, including certain diesel engines, radio and television apparatus, truck-mounted cranes, knitted goods and confectionery products.

To assist Canadian producers, increases in the MFN rates are being proposed for certain chemicals and industrial tires and tubes.

I have received a number of enquiries about implementation of the Tariff Board's proposals for changes in the tariffs on fruits and vegetables. We have notified our trading partners that we intend to renegotiate certain GATT commitments which currently prevent us from increasing existing rates of duty on products covered by the Board's report. The government will try to conclude these negotiations as soon as possible and then introduce legislation to provide for a new schedule of rates for fresh and processed fruits and vegetables.

The Tax Structure

Our tax system is another instrument which can support innovation and change. I want to proceed immediately with major structural changes in three areas of industrial policy highlighted by First Ministers. They are research and development, transportation and energy.

Research and Development

We must continue to encourage Canada's research and development efforts. An adequate level of R&D is crucial to achieve gains in productivity and to strengthen Canada's position in an increasingly competitive world. At present, corporations are allowed to write off immediately 100 per cent of all R&D capital and operating expenditures. Last year these outlays also became eligible for the federal investment tax credit of from 5 to 10 per cent. In many cases they also qualify for direct assistance under significant federal grant programs.

I now propose that for 10 years starting this year, taxpayers be allowed to deduct from their income a further 50 per cent of additional R&D expenditures. The deduction will apply to both current and capital expenditures to the extent that they exceed the average amount over the preceding three years. This means that there will now be a special incentive for companies to *expand* their R&D. I want to emphasize that this special allowance comes on top of the incentives already in place. ✓

The new allowance will make Canada's tax treatment of research and development one of the most generous in the world. The after-tax cost to companies of one dollar's worth of additional expenditure will be reduced to as little as 20 cents. I hope this incentive will lead to significant improvements in R&D performance by the private sector. And I look to companies to ensure that the resulting new technology is used within Canada to create new jobs.

Railway Investments

Discussions at the First Ministers' conference underlined the importance of transportation for industrial and regional development in Canada. Railways continue to be a crucially important mode of transportation, particularly for long hauls and heavy commodities. Recently, the government has announced significant changes in the organization of the CNR to improve the efficiency of its operations. Measures were introduced in the last budget to encourage track and grading investments by railways. Looking to the medium term, major new investments are needed in this sector if efficiency and productivity gains are to be captured.

I am therefore proposing a significant increase in the capital cost allowance for railway investments. This will take the form of an additional depreciation allowance of 6 per cent per year for five years for most capital expenditures of a railway. It will apply to investments undertaken after tonight and before 1983. The measure will help improve the railway system in all regions of Canada and will be of benefit to suppliers of railway equipment.

Energy Development Incentives

We must also continue to place high priority on our national energy policy, and in particular the need to extend self-reliance for oil and gas. We are fortunate in our existing and potential resources, and many tax incentives and other measures have been put in place to encourage their development. But increasing attention is now focussed upon the heavy oil reserves and oil sands deposits of the western provinces which can be tapped only by advanced technology and multi-billion dollar investments. These are projects requiring long lead times for planning, organization, design and construction. It is important to get them moving now, and I have concluded that some modification and clarification of their tax treatment can be helpful in that regard.

First, I want to make clear that the up-grading plants to process the heavy oil produced from wells into a type of oil similar to conventional crude will be treated as a manufacturing facility, eligible for fast write-offs and the reduced tax rate.

Second, it will be important to extract as much oil as technologically possible from all deposits. It has already been established that enhanced recovery systems can greatly increase total production. After today, therefore, special machinery, equipment and other facilities acquired for enhanced recovery systems — specifically, so-called "tertiary" recovery — will be able to earn depletion at a rate of $1 for every $2 of expenditure as compared to the normal earning rate of $1 for $3.

Finally, earned depletion may be applied at present only to reduce taxable resource profits, and only up to a ceiling of 25 per cent. This provision will be significantly improved. Effective immediately, corporations may deduct depletion earned through certain qualifying investment in non-conventional oil projects up to the extent of 50 per cent of total income — both resource and other profits. The qualifying investment will include expenditures on tertiary recovery equipment and certain depreciable property acquired for use in a bituminous sands mining project.

I am confident that these measures, added to the ones already in place, will in future years help reduce our dependence on imported oil, especially in eastern Canada.

I would like also to say a word about the mining industry. The First Ministers' conference directed Finance and Resource Ministers to undertake an early review of the taxation of the mineral industry. The government is proceeding with its review and looks forward to further consultation with the provinces in the near future.

Retirement Income

Almost two million Canadians have Registered Retirement Savings Plans, enabling them to set aside funds to provide income after retirement. The wide range of choice allowed in setting up these plans and the generous tax treatment for contributions have made them very popular.

I have some concern, however, over the limited choice available to RRSP holders when the time comes to turn their savings into retirement income. A taxpayer is now required to invest his RRSP proceeds in a life annuity with an insurance company prior to his 71st birthday. The only alternative he has is to withdraw the funds in a lump sum and pay income tax on this amount in the same year.

I propose to introduce two additional alternatives that will increase flexibility while retaining the basic principle that RRSP funds are intended to be used for retirement income. ✓

The first alternative will allow the purchase of a fixed-term annuity to provide benefits to age 90.

The second alternative will allow the taxpayer to have his RRSP savings placed in a new kind of investment vehicle to be known as a Registered Retirement Income Fund. Each year a set fraction of the total assets in the Fund — capital plus accumulated investment earnings — will be withdrawn and taken into income. This fraction will be determined by a formula designed to provide benefits to age 90. Payments would grow over time at a rate reflecting the investment performance of the Fund and thus provide a degree of protection against future inflation. There will be provisions enabling a taxpayer to manage his investments in much the same way as he can now with a self-administered RRSP.

Institutions with the right to issue RRSPs will be permitted to sell fixed-term annuities or retirement income funds. At present this includes mainly life insurance and trust companies.

The transfer of an RRSP into any of the retirement income options must occur between age 60 and age 71.

I am confident that the added alternatives will provide the range of choice that taxpayers desire in planning for retirement. They respond to concerns expressed to me by many Canadians.

Family Law Reform

A number of provinces have introduced fundamental changes in the laws relating to the division of certain properties between marriage partners. These changes in law raise a number of important issues which are far from being resolved. Because they affect several provisions of the Income Tax Act, I am monitoring the developments in this area very closely. In the meantime, I am proposing a change in the provisions so that transfers of property between spouses pursuant to provincial family laws will not give rise to taxable capital gains.

The Ways and Means Motion contains several other important changes. First, the current provisions which permit the transfer of farm land and buildings by a farmer to his children without payment of capital gains tax will be extended to incorporated family farms. Second, single employees will now receive the same tax exemption as married employees on the value of free board and lodging provided at logging camps and other remote work locations. Third, I am proposing certain tax changes to further promote the production of good Canadian films.

Problems of the Past Year

In addition to measures which will encourage structural changes in the economy, I have also had to consider what measures will be helpful in dealing with the immediate problems that confront us.

Although the prices of the things we produce continued to slow down last year, the prices of the things we consume have risen more sharply. There were two major factors — higher prices of imported foods and the decline in the exchange rate. I do not believe the price surge will last. I believe the direct impact of our dollar's decline is now largely behind us. Further, an improving supply situation should help to slow the rise in food prices.

The growth of output was disappointing last year. The rate dropped from about 5 per cent in 1976 to 2.6 per cent in 1977, according to the preliminary estimate. The most unfortunate consequence was the rise in unemployment. Unemployment has reached unacceptable levels despite a substantial increase in the number of Canadians who are working. Employment has increased more than 3 per cent in the past year. Almost 300,000 more Canadians are working today than one year ago. But our labour force has also been growing rapidly, much more rapidly than in other countries. Since 1970, our labour force has increased by about 3 1/2 per cent a year, compared with 2 per cent in the United States and well under 1 per cent in the United Kingdom, France and Japan. In Germany, the labour force has actually dropped over this period.

An important reason for the growth of our labour force has been the growing number of Canadian women who are working. Since 1970 the number of adult women in the labour force has increased from 1.9 million to 2.7 million, a rise of more than 40 per cent. There has also been a surge of young people coming into the labour market. This surge will not last; in many schools, there are now empty desks. But the immediate challenge is to create enough jobs for all our young people. Youth unemployment is one of our most serious problems. It cannot be dealt with only by general economic policies. Our manpower training and direct job creation programs are pointed specifically to this problem.

In 1978-79 a total of $458 million will be spent for the Canada Works, Young Canada Works and other continuing job creation programs. Some of these programs, notably Young Canada Works, Summer Job Corps, Youth Apprenticeship and Job Experience Training are directed exclusively to young people. However, this does not represent our total effort in favour of young people. I must stress that the young also have complete access to our general programs such as Canada Works and the Canada Manpower Training Program where they represent roughly half of the clientele. I estimate our job creation effort for young people under these programs to be over $225 million.

Further, an additional $150 million is being provided for seasonal works projects with a high employment content in high unemployment areas. The new employment credit will directly stimulate private sector employment.

The stimulus will be especially strong for jobs which young people are most likely to fill. We are also making a manpower training investment of the order of $500 million, about half of which is to be spent on youth.

Mr. Speaker, if I may summarize, we are going through a difficult period of adjustment, with some recent factors working against the pace of our recovery. Forecasts for 1978, including my own, have been shaded down. But the recovery is proceeding. Employment is rising. Confidence is improving, although not as quickly as I would like to see. The question now is whether the gradual recovery that has been established should be given an added push from policy. I have decided that it should.

The size of such a push must take into account the forces of expansion that are already in place. Much of the tax action I took last winter has not yet worked through the system. Moreover, the decline in the exchange rate over the past year, by improving the competitiveness of our exports and domestic industry, will have an impact of major dimensions — provided we do not waste it through cost increases. Very large resource projects lie ahead of us. So while further action is desirable, it must be responsible action, and action aimed at the right target.

The Action We Need Now

Any further stimulus should obviously be fast-acting. It should encourage consumer spending, not more spending by government. It should offset some of the temporary factors which are pushing up prices. This is particularly important now, on the eve of the start of decontrol.

A reduction of retail sales taxes fits these requirements best, and has the added advantage of benefitting all those who spend in Canada, even those who do not pay income tax. It will stimulate retail sales and therefore benefit, among others, the many small businessmen in this sector. The idea has been advocated widely by economists, business associations and others. Indeed, I made a proposal to the provinces last fall under which the federal government would compensate them for half of the cost of reducing retail sales taxes by two percentage points. Most provinces were unable to accept the proposal at that time in view of their fiscal positions, and I therefore proceeded with an income tax cut of up to $100 per person for this year.

Tonight I want to announce that I have made a broader proposal to my provincial colleagues.

I have offered to compensate them for a reduction of two percentage points in their retail sales taxes for a period of six months. In return, I have asked them to bear the cost of *either* a further one percentage point for the same period, *or* an extension of the two-point cut for a further three-month period.

I recognize that the Atlantic Provinces are less able than the other provinces to bear this additional cost. I have therefore offered to compensate them for the full cost of three percentage points for six months.

To focus the tax cut on essential items, the reductions will not apply to amusements, tobacco products and alcoholic beverages for home consumption.

The federal compensation to the provinces will be made in the form of a temporary transfer of $800 million in personal income taxes, with small balancing payments in cash where necessary. Equalization payments will be insulated from the impact of the retail sales tax and the personal income tax changes.

Alberta does not have a sales tax and therefore will not benefit in the same way as the other provinces. However, the fiscal position of Alberta is very strong as a result of its oil and gas revenues and this has permitted significant further cuts in other provincial taxes. The Government of Alberta has raised no objection to our proceeding with the proposed arrangement.

Mr. Speaker, this measure can be an outstanding example of federal-provincial fiscal co-ordination and I want to express my deep appreciation of the co-operation I have received from provincial colleagues. If all provinces accept the federal offer, this will mean a tax cut to the economy of about $1.1 billion. About one-third would be paid for by the stronger provinces, about a third by federal deficit financing, and about a third by a cut in federal expenditures to which I will refer in a moment. The measure will boost real income by holding prices below the level which would otherwise be expected. The impact on the average price level should be about one per cent for the period the cut is in effect. This cut provides a

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Inserted addition to the Budget speech:

On page 14, insert after the fifth full paragraph ...Income tax changes.

With this measure now officially committed in the budget tonight, I am glad to report that the four Atlantic provinces, Ontario and Manitoba all propose to reduce their retail sales tax rates by three percentage points for six months. The provinces of British Columbia and Saskatchewan propose to apply the federal compensation to a two-point reduction for the first six months and to make their own contributions over subsequent periods.

I understand that the province of Quebec is still considering the federal offer. I have asked my colleague in Quebec to let me know his decision within two weeks.

Under these cooperative arrangements, provincial governments respectively will take steps to reduce retail sales taxes from 11 per cent to 8 per cent in Newfoundland; from 8 per cent to 5 per cent in New Brunswick, Nova Scotia and Prince Edward Island; from 7 per cent to 4 per cent in Ontario; from 7 per cent to 5 per cent in British Columbia; from 5 per cent to 2 per cent in Manitoba; and from 5 per cent to 3 per cent in Saskatchewan.

Alberta ... picking up sixth paragraph of the printed text.

specific incentive to consumers to take advantage of temporarily lower prices. Its impact will be reflected in an early stimulus to retail and wholesale business, a call on output from the production line, and a lowering of tax cost on business.

Fiscal Position and Outlook

Mr. Speaker, I would like now to table the Notice of Ways and Means Motion, projections of the government's revenues and expenditures, and supplementary information outlining details of the measures proposed tonight. This material also provides background to the tables on the government's accounts and information on the relation between domestic borrowing, foreign borrowing and our financial requirements.

On the basis of close to final information, financial requirements excluding foreign exchange transactions totalled $8.5 billion in 1977-78. This is $300 million less than I forecast recently, mainly because it now appears likely that our total outlays were $200 million below the budgeted amounts.

For 1978-79, we have reduced our expenditure ceilings by $350 million below the total announced by the President of the Treasury Board when he tabled the Main Estimates. This will require very tight control over spending under existing programs and over the introduction of new programs. Taking last year and this year together, our financial requirements will be $550 million lower than they would otherwise have been as a result of these expenditure savings.

Taking into account the measures announced tonight, which will reduce revenues for this year by some $900 million, I now expect 1978-79 financial requirements to total about $9.5 billion if one excludes the $2 billion of accrued interest on Canada Savings Bonds which will be encashed this year. While the total requirement of $11.5 billion is large, I am confident it can be financed without creating undue pressures on markets, particularly in light of our very large cash balances at the present time.

The revenue side of the 1978-79 fiscal outlook is based on a forecast increase in total output in current dollars of about 11 per cent.

I expect about 6 per cent of this increase to consist of price changes, as measured by the price index of total gross national expenditure, and close to 5 per cent of growth in real output. This rate of real growth should bring about some modest decline in unemployment. Whether we in fact obtain as much output growth and as little price increase will be influenced by wage and price behaviour in the decontrol period, as well as by international developments. The increase in the consumer price index is likely to be about 7 per cent because it includes import prices which are directly affected by higher food prices and the decline in the exchange rate.

Conclusion

In summary, this budget is aimed at creating the proper conditions for a strong and prosperous economy. In conjunction with the provinces, in the short term I have taken steps to increase consumer demand and to lower consumer prices; in the medium term, I have put into place tax changes designed to meet some of the major challenges of the future — in energy, transportation and research and development. In doing these things, my objective has been to strengthen the private sector without government interference.

Mr. Speaker, I am convinced that Canada has a potential for economic growth and higher living standards second to none in the world. We have the skills, the natural resources and the proven ability to work together in solving our problems.

To translate promise into reality we must meet certain conditions.

First and foremost, we must keep Canada united.

Second, we must carry through structural reforms in the Canadian economy to make it more efficient and competitive.

Third, we must restore reasonable cost and price stability. The experience of recent years has made it very clear that inflation is the enemy of growth, because it weakens consumer and business confidence and erodes our ability to compete in world markets.

Individual Canadians must accept the need to be reasonable in their wage and salary demands at a time when the issue for more than a million Canadians is not getting a pay increase but getting a job. There will be times when we will have to pay more for some of the things we buy without expecting any offsetting increase in our incomes. It is futile and damaging to try to compensate ourselves for the higher costs of imported goods.

I look to the business community to explore markets aggressively and demonstrate the faith in Canada that is merited by its great material and human resources and its sound institutions.

Governments must pursue with discipline the policies that will encourage as much growth as possible at declining rates of inflation. We shall continue to restrict the growth of our own spending to less than the trend growth of the gross national product. In doing so, we will continue to pursue greater efficiency in government. In setting the wages and salaries of our own employees, we will follow — not lead — the private sector.

If we all play our part, we can advance into the 1980s with rising investment, declining unemployment, an improving balance of payments and strong growth in all parts of this country.

There is only one way to get out of our difficulties and that is for all Canadians to apply themselves diligently to build a better future for our children and our grandchildren. It is through hard work, imagination, determination and discipline that we will succeed.

Tonight, despite the prospect of an early election, I have refused to make irresponsible promises to the people of Canada because I respect the intelligence of those who will be choosing the next government. The theme of the budget which I have brought down tonight is responsibility, and responsibility is what Canadians deserve.

Table 1
Government of Canada
Summary Statement of Transactions
Public Accounts Presentation

	1976-77 Actual	1977-78 Estimate(1)	1978-79 Forecast(1)
		($ millions)	
Budgetary transactions			
Revenues	32,640	32,700	36,000
Expenditures(2)	-38,930	-43,000	-46,900
Surplus or deficit (–)	-6,290	-10,300	-10,900
Non-budgetary transactions			
Loans, investments and advances(2)	-2,148	-1,250	-1,550
Annuity, insurance and pension accounts	2,368	1,570	2,250
Other transactions	676	1,480	-1,300
Net source or requirement (–)	896	1,800	-600
Financial requirements			
(Excluding foreign exchange transactions)	-5,394	-8,500	-11,500
Foreign exchange transactions	1,122	1,170(3)	
Total financial requirements	-4,272	-7,330	

(1) Numbers in these columns should be interpreted as mid-points of ranges of estimates.
(2) Total outlays are composed of budgetary expenditures plus loans, investments and advances.
(3) This figure reflects actual transactions to the end of fiscal year 1977-78. No forecast is made of foreign exchange transactions in fiscal year 1978-79.

Table 2
Government of Canada
Fiscal Position
Public Accounts Budgetary Revenues

	1976-77 Actual	1977-78 Estimate(1)	1978-79 Forecast(1)
		($ millions)	
Personal income tax	14,620	13,575	14,915
Corporation income tax	5,377	5,775	6,270
Non-resident tax	451	500	540
Customs duties	2,097	2,280	2,660
Sales tax	3,929	4,355	4,905
Other duties and taxes	2,681	2,465	2,325
Total tax revenues	29,155	28,950	31,615
Non-tax revenues	3,485	3,750	4,385
Total budgetary revenues	32,640	32,700	36,000

(1) Numbers in these columns should be interpreted as mid-points of ranges of estimates.

Table 3
Government of Canada
Summary, Extended National Accounts Presentation

	1976-77 Actual	1977-78 Estimate(1)	1978-79 Forecast(1)
		($ millions)	
Current transactions			
A. Revenues	36,599	36,400	40,525
B. Expenditures	-40,458	-45,200	-49,775
Surplus or deficit (–)	-3,859	-8,800	-9,250
Loans and other transactions			
A. Loans, investments and advances	-2,030	-1,375	-1,150
B. Cash vs accrual	486	1,325	-1,225
C. Other transactions	9	350	125
Net source or requirement (–)	-1,535	300	-2,250
Total financial requirements (Excl. foreign exchange transactions)	-5,394	-8,500	-11,500
Foreign exchange transactions	1,122	1,170(2)	
Total financial requirements	-4,272	-7,330	

(1) Numbers in these columns should be interpreted as mid-points of ranges of estimates.
(2) This figure reflects actual transactions to the end of fiscal year 1977-78. No forecast is made of foreign exchange transactions in fiscal year 1978-79.

Table 4
Government of Canada
Revenues and Expenditures
National Accounts Basis

	1976-77 Actual	1977-78 Estimate[1]	1978-79 Forecast[1]
		($ millions)	
Revenues			
Direct taxes, persons	18,535	17,455	19,305
Direct taxes, corporations	5,810	5,685	6,320
Direct taxes, non-residents	522	555	625
Indirect taxes	8,596	9,090	9,820
Other current transfers from persons	9	10	10
Investment income	2,611	3,015	3,780
Capital consumption allowances	516	590	665
Total revenues	36,599	36,400	40,525
Expenditures			
Current goods and services	10,139	11,300	12,400
Transfer payments to persons	11,803	13,400	14,650
Subsidies	2,431	2,500	2,400
Capital assistance	312	400	525
Current transfers to non-residents	574	675	775
Interest on the Public Debt	4,672	5,425	6,650
Transfers to provinces	9,048	9,750	10,475
Transfers to local governments	197	350	375
Gross capital formation	1,282	1,400	1,525
Total expenditures	40,458	45,200	49,775
Surplus or deficit (–)	–3,859	–8,800	–9,250

[1] Numbers in these columns should be interpreted as mid-points of ranges of estimates.

Table 5
Government of Canada
Revenues, Public Accounts and
National Accounts Reconciliation

	1976-77 Actual	1977-78 Estimate(1)	1978-79 Forecast(1)
		($ millions)	
Budgetary revenues —			
Public Accounts	32,640	32,700	36,000
Deduct			
Post Office revenues and deficit	-1,103	-1,240	-1,310
Deficit of government business enterprises(2)	-144	-175	-130
Excess of accruals over collections			
Corporate income tax	496	-30	110
Oil export charge	-64	-40	-20
Add			
Government pension and social security receipts(3)	4,676	5,310	5,900
Capital consumption allowance	516	590	665
Miscellaneous adjustments(4)	-418	-715	-690
Total revenues —			
National Accounts	36,599	36,400	40,525

(1) Numbers in these columns should be interpreted as mid-points of ranges of estimates.
(2) In the Public Accounts, deficits of government business enterprises are a charge to budgetary expenditures whereas in the National Accounts, these deficits are deducted from remitted profits of other government business enterprises.
(3) In the Public Accounts, these government pension and social security receipts and disbursements are treated as non-budgetary transactions whereas in the National Accounts, these transactions are included in government revenue and expenditure.
(4) These miscellaneous adjustments arise as a result of conceptual differences between the two forms of presentation. These items represent, for example, the proceeds from the sales of existing capital assets; budgetary revenue items offset against budgetary expenditures; imputed items; and, an adjustment for the treatment of revenue in the supplementary period.

Table 6
Government of Canada
Expenditures, Public Accounts and
National Accounts Reconciliation

	1976-77 Actual	1977-78 Estimate(1)	1978-79 Forecast(1)
		($ millions)	
Budgetary expenditures —			
Public Accounts	38,930	43,000	46,900
Deduct			
Transfers to funds and agencies(2)	-2,896	-2,885	-3,475
Post Office expenditures	-1,103	-1,240	-1,310
Deficit of government business enterprises(3)	-144	-175	-130
Add			
Expenditures of funds and agencies(2)	1,500	1,510	2,065
Government pension and social security disbursements(4)	4,115	5,130	5,450
Capital consumption allowance	516	590	665
Miscellaneous adjustments(5)	-460	-730	-390
Total expenditures —			
National Accounts	40,458	45,200	49,775

(1) Numbers in these columns should be interpreted as mid-points of ranges of estimates.
(2) In the National Accounts, budgetary appropriations to various funds and agencies are replaced by the expenditure actually made by the funds and agencies.
(3) In the Public Accounts, deficits of government business enterprises are a charge to budgetary expenditures whereas in the National Accounts, these deficits are deducted from remitted profits of other government business enterprises.
(4) In the Public Accounts, these government pension and social security receipts and disbursements are treated as non-budgetary transactions whereas in the National Accounts, these transactions are included in government revenue and expenditure.
(5) As in the case of revenues, the miscellaneous adjustments arise as a result of conceptual differences between the two forms of presentation. These items represent, for example, reserves and write-offs; purchase of existing capital assets; budgetary revenue items offset against budgetary expenditure; expenditures of reserve accounts and revolving funds; imputed items; and, an adjustment for the treatment of expenditures in the supplementary period.

Table 7
Government of Canada
Non-Budgetary, Public Accounts and
Extended National Accounts Reconciliation

	1976-77 Actual	1977-78 Estimate(1)	1978-79 Forecast(1)
		($ millions)	
Non-budgetary transactions –			
Public Accounts	896	1,800	-600
Deduct			
Loans and advances to funds and agencies	118	-125	400
Government pension and social security accounts	-2,366	-1,585	-2,190
Excess of accruals over collections			
Corporate income tax	-496	30	-110
Oil export charge	64	40	20
Miscellaneous adjustments(2)	249	140	230
Loans and other transactions –			
Extended National Accounts	-1,535	300	-2,250

(1) Numbers in these columns should be interpreted as mid-point of ranges of estimates.
(2) As in the case of revenues and expenditures, the miscellaneous adjustments arise as a result of conceptual differences between the two forms of presentation. These items represent, for example, the adjustments for the treatment of revenues and expenditures in the supplementary period; the change in the reserves and revolving funds; and the adjustment required to bring financial requirements of entities included in the national accounts government sector in line with the requirements of these entities which are met through the Consolidated Revenue Fund.

Notes to Fiscal Tables

Status of 1977-78 Figures

Although the fiscal year ends on March 31, the books remain open for some time to permit payments made up to April 30 in discharge of debts incurred before March 31, together with receipts in transit at March 31, to be included in the accounts for the fiscal year. Since the books are not yet closed, the 1977-78 figures in the fiscal tables should be regarded as estimates. The government's preliminary financial statement for 1977-78 will be published this summer in The Canada Gazette.

Fiscal year-end levels of cash balances are already known and the preliminary data on debt and foreign exchange transactions should be subject to only minor revisions. Thus, close to final figures for "Total Financial Requirements" and "Financial Requirements (excluding foreign exchange transactions)" may be derived. Budgetary revenues and expenditures, the resulting budgetary deficit, and the figures for non-budgetary transactions are based on actual data for the first 11 months of the fiscal year, estimates for March, and forecasts for the supplementary period.

Differences from Forecast in October Economic and Fiscal Statement

The current estimate of 1977-78 budgetary revenues is $350 million lower than the forecast provided in the October 20, 1977 Economic and Fiscal Statement of the Minister of Finance. The individual revenue category showing the largest difference is personal income tax revenue which is $525 million below the October forecast. Of this reduction, $260 million reflects a transfer to the provincial tax collection account in respect of 1976 assessments. Adjustments in respect of prior years' entries to this account are calculated every January when data from individual tax returns for the taxation year which ended 13 months earlier become available. While reducing budgetary revenues, this transfer does not increase financial requirements as it constitutes a non-budgetary source of funds. The remaining part of the reduction in personal income tax revenues reflects a slightly lower tax base growth than expected earlier and the latest available collections information.

Total outlays, i.e., budgetary expenditures and non-budgetary loans, investments and advances, are now estimated to total $200 million less than the target level of $44,450 million established last March and restated in October. Budgetary expenditures on certain statutory programs, such as public debt charges and payments to provinces under the new Established Programs Financing arrangements, were higher than originally expected but more than offsetting reductions occurred in the loans, investments and advances categories. In addition, it was decided to provide budgetary appropriations to write off loans totalling $444 million to the Canadian Dairy Commission and Atomic Energy of Canada Limited, and to forgive loans totalling $232 million to least developed countries under the foreign aid program. These additional increases in budgetary expenditures resulted in no increase in total outlays, as they gave rise to corresponding reductions in net loan requirements.

The decrease in budgetary revenues and the increase in budgetary expenditures resulted in an estimated budgetary deficit which is $1.1 billion higher than the deficit forecast in October. The reduction in loan requirements and the increase in non-budgetary receipts turned out to balance this increase in the budgetary deficit, leaving financial requirements at the same level as in the October forecast.

Foreign Borrowing, Foreign Exchange Transactions and Domestic Borrowing

There was a significant amount of foreign borrowing in 1977-78 for the first time in several years. The following table shows how such borrowing is reflected in the Summary Statement of Transactions (Table 1), and also provides summary information on the domestic borrowing record.

Financial Requirements and Debt Transactions

	1976-77	1977-78
	($ millions)	
Financial requirements		
(Excl. foreign exchange transactions)	-5,394	-8,500
Foreign exchange transactions		
Unmatured debt outstanding — payable in foreign currency (increase (+)/decrease-)	-2	850
Other	1,124	320
Total	1,122	1,170
Total financial requirements	-4,272	-7,330
Unmatured debt transactions (increase (+)/decrease-)		
Marketable bonds	2,270	3,443
Treasury bills	1,760	3,040
Canada Savings Bonds	787	1,747
Total	4,817	8,230
Change in cash balance	545	900
Cash balance at end of period	3,597	4,497

Foreign currency borrowing is shown under "Foreign Exchange Transactions". At the time of the borrowing, assuming the funds are not immediately converted into Canadian dollars, there are two offsetting entries: a positive entry under the "Unmatured Debt Outstanding — Payable in Foreign Currency" sub-heading which represents the Canadian dollar value of the foreign currency borrowed, and a negative entry included in "Other Foreign Exchange Transactions" which reflects the 'use' of the funds to add to our foreign exchange reserves. The $850 million positive entry shown for "Unmatured Debt Payable in Foreign Currency" in 1977-78 represents the value, in Canadian dollars, of the $750 million U.S. drawing in 1977-78 under the standby credit facility with the Canadian chartered banks. (The recent borrowing of $750 million U.S. through an issue of marketable securities dated April 1, 1978 will appear in this category in 1978-79.) The $320 million shown for "Other Foreign Exchange Transactions" in 1977-78 is the net result of the source of funds which arose from exchange market intervention and other transactions, and the 'use' of funds corresponding to the replenishment of the reserves from the foreign currency borrowing.

"Total Financial Requirements" represents the total requirements for Canadian funds arising from budgetary and non-budgetary transactions and foreign exchange transactions. These requirements are equal to the increase in unmatured debt less the increase in cash balances.

Direct Borrowing by Government Agencies

Direct market borrowings, of $463 million in 1976-77 and some $350 million in 1977-78, by agent Crown corporations, specifically Petro-Canada, the Export Development Corporation, and Eldorado Nuclear, which have been authorized to borrow under their respective statutes, are not included in Government of Canada financial requirements. In the projection of financial requirements for 1978-79, it is envisaged that such direct borrowings by agent corporations will continue, and that in particular the Export Development Corporation will raise the bulk of its requirements through direct borrowing. In addition, the 1978-79 requirement for loans to Central Mortgage and Housing Corporation is reduced due to the anticipated sale of mortgages by CMHC from its existing holdings.

Canada Savings Bond Interest and Financial Requirements in 1978-79

Provision for interest on Canada Savings Bonds, including an allowance for the accumulating liability under the compound interest and bonus interest features of bonds issued prior to 1974, is made each year on an accrual basis and forms part of the "public debt charges" component of total budgetary expenditures. To the extent that interest accruals exceed interest actually paid in a particular year, because some holders of Canada Savings Bonds allow coupons to accumulate uncashed and/or because the compound coupon or the bonus payment do not come due in that year, the government is provided with a source of funds which is included in "Other non-budgetary transactions" in Table 1. The accumulated amounts of "interest accrued" and "interest due and outstanding" are recorded as components of the public debt in the statement of the government's assets and liabilities.

In a year in which the compound interest coupon and/or bonus interest payment on a Canada Savings Bond series come due, cash interest payments will exceed interest accruals on that series; there is then a use of funds under "Other non-budgetary transactions". There is a corresponding reduction in the "interest accrued" and "interest due and outstanding" components of the total public debt.

The SR series of Canada Savings Bonds (issued May, 1968, $120 million estimated outstanding) and the large S24 series (issued November, 1969, $2.5 billion estimated outstanding), mature in 1978. Both series have compound interest provisions and are eligible for bonus interest. It is estimated that in 1978 compound interest coupons and bonus interest totalling $850 million will be paid on these series, together with $1,450 million in regular interest coupons. Only $300 million will correspond to interest accruing on these bonds during fiscal year 1978-79. Thus, unlike recent years in which the excess of interest accruing over interest encashment on these two series provided a substantial source of funds (some $350 million in 1977-78), in 1978-79 the excess of encashment over accruals gives rise to a requirement of some $2 billion. On other series of CSBs, accrued interest continues to exceed cash payments. Overall, the interest accounts switch from giving rise to a source of funds of almost $800 million in 1977-78, to giving rise to an estimated requirement of $1,300 million in 1978-79.

The unusually high level of interest encashment in 1978-79 affects financial requirements but not the budgetary deficit. Nor does it affect the National Accounts deficit (Tables 3 and 4) as interest on the public debt is also treated on an accrual basis in the National Accounts.

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:

Remote work sites

(1) That for the 1978 and subsequent taxation years, an individual be entitled to exclude from income the value of board and lodging received in respect of employment at a remote work site at which he could not reasonably be expected to maintain a self-contained domestic establishment.

Shareholder loans

(2) That a loan made by a corporation after March 31, 1977 to an employee to enable him to purchase from a related corporation fully paid shares of its capital stock, not be included in income.

Interest on policy loans

(3) That for the 1978 and subsequent taxation years, the rules relating to the deductibility of interest on policy loans made after March 31, 1977 apply to all policy loans.

Additional allowance for scientific research

(4) That for taxation years ending after 1977 and before 1988, in computing its income from a business carried on in Canada, a corporation be permitted to deduct an extra allowance equal to 50% of the amount by which its qualified current and capital expenditures on scientific research in Canada exceed the average of such expenditures made by it during a base period and that for the purposes of the allowance

(a) the base period in respect of a year be the three immediately preceding taxation years or such lesser number of years as ended after 1976,

(b) the deduction for the 1978 taxation year be calculated by reference to the number of days in the year after 1977, and

(c) rules be provided to determine the amount of the deduction where the corporation is a member of an associated group and to recapture an appropriate part of the allowance when a research property is disposed of.

Family farm corporations and partnerships

(5) That where, after April 10, 1978, a taxpayer transfers to his child resident in Canada shares of a qualifying farm corporation or an interest in a qualifying farm partnership, substantially all of the assets of which were used in the business of farming in Canada, any capital gain that would otherwise arise be

(a) deferred, in the case of a transfer on death, and

(b) determined on the basis of the lesser of the proceeds actually received and the fair market value, in the case of an *inter-vivos* transfer.

Transfers of property pursuant to provincial legislation

(6) That for the 1978 and subsequent taxation years, the provisions of section 73 of the Act relating to the transfer of property by a taxpayer to his spouse be extended to apply to transfers of property under provincial legislation relating to marital property.

Agricultural quotas

(7) That the rules in subsection 73(3) of the Act applicable to the *inter-vivos* transfer of property by a farmer to his child be extended to apply to the transfer after April 10, 1978 of agricultural quotas and other eligible capital property.

Employee loans

(8) That for the 1979 and subsequent taxation years, subsection 80.4(2) of the Act be amended:

(a) to extend the definition of "excluded loan" and "housing loan" to include a loan received by an employee from a person other than his employer, and

(b) to extend the definition of "housing loan" to include a loan made to an employee who has moved from a location outside Canada.

Reduction of capital

(9) That any amount paid by a public corporation after April 10, 1978 as a reduction of paid-up capital in respect of a share of its capital stock be treated as a dividend unless the amount was paid on the redemption or cancellation of the share, on the winding-up of the corporation or in the course of the reorganization of the capital stock of the corporation.

Non-arm's length sale of shares

(10) That the rules in sections 84.1 and 212.1 of the Act be modified to apply to a non-arm's length sale of shares of the capital stock of a corporation after April 10, 1978 to another corporation with which it is connected within the meaning of section 186 of the Act as modified by paragraph (18) of this Motion.

Losses of certain insurers

(11) That, for the purpose of computing the taxable income of a life insurer for its 1978 and subsequent taxation years, its non-capital loss for the 1977 taxation year be determined as the amount, if any, by which its 1977 carry-forward deduction exceeds the aggregate of the amounts referred to in subparagraphs 138(4.2)(a)(i) and (ii) of the Act.

Northwest Territories

(12) That sections 120 and 124 of the Act be amended effective January 1, 1978 to recognize the introduction of an income tax by the Northwest Territories.

Abatement for provincial sales tax reduction

(13) That for the 1978 taxation year the tax otherwise payable by an individual resident in a prescribed province on December 31, 1978 be reduced by $100.

Cumulative deduction account

(14) That in computing the cumulative deduction account of a Canadian-controlled private corporation, no deduction be made in respect of a dividend paid after April 10, 1978 to another corporation (other than a corporation associated with it) with which it is connected within the meaning of section 186 of the Act as modified by paragraph (18) of this Motion.

Cost basis of life insurance policy

(15) That in computing the adjusted cost basis of a life insurance policy after March 31, 1978, the premium paid on the policy exclude any interest paid before 1978 on a policy loan.

Registered retirement savings plan

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

(a) a registered retirement savings plan shall mature only after the annuitant attains 60 years of age and before the end of the year in which he attains 71 years of age;

(b) benefits under a registered retirement savings plan that matures after April 10, 1978, may be received as

(i) an annuity for life,

(ii) an annuity for a fixed term equal to the number of years remaining before the annuitant attains the age of 90, or

(iii) an annuity under a new plan to be known as a registered retirement income fund out of which payments shall be made to the beneficiary in each year equal to the fraction of the value of the property of the fund at the beginning of the year that one year is of the number of years then remaining before the annuitant attains the age of 90; and

(c) except where the spouse is the beneficiary, benefits pursuant to a registered retirement savings plan shall be required to be commutable at death and the annuitant shall be deemed to have received the value thereof immediately before death.

Penalties

(17) That the penalty provided in subsection 163(2) of the Act for a false statement or omission made by a person after April 10, 1978 be calculated by reference to all unreported income or overstated expenses.

Part IV tax

(18) That subparagraph 186(4)(b)(ii) of the Act be deleted with respect to dividends received after April 10, 1978.

Interest on Part X tax

(19) That for the 1972 and subsequent taxation years, interest on the refundable portion of the Part X tax on non-qualified investments of a deferred profit sharing plan not accrue after the plan disposes of the non-qualified investment.

Insurers branch tax

(20) That for the 1978 and subsequent taxation years,

(a) subsections 219(5) and (6) of the Act be deleted, and

(b) the rules in subsection 219 (4) of the Act be amended to limit the amount by which a non-resident insurer may reduce its Canadian investment fund by paying the 25% tax to the portion of its surplus that exceeds a minimum required level to be prescribed by regulation.

Notice of Ways and Means Motion
Customs Tariff

1. (1) That *An Act to amend the Customs Tariff (No. 2)*, being c. 14 of the Statutes of Canada, 1976-77, be amended, except with respect to tariff items 805-1, 810-1, 825, 8901-1, 9001-1, 9002-1, 32606-1, and 93402-1 listed in subsection 3(1) thereof, by deleting all references in subsections 7(3) and 7(4) thereof to the year 1978 and replacing them with references to the year 1979.

(2) That Schedule A to the *Customs Tariff* be amended by striking out tariff items 805-1, 810-1, and 825-1 and the enumerations of goods and the rates of duty set opposite each of those items, and by inserting in Schedule A to the said Act the following items, enumerations of goods and rates of duty:

					Rates in Effect Prior to February 20, 1973		
Tariff Item	Description	British Preferential Tariff	Most-Favoured-Nation Tariff	General Tariff	B.P. Tariff	M.F.N. Tariff	General Tariff
805-1	Canned pork	15 p.c.	15 p.c.	35 p.c.	15 p.c.	25 p.c.	35 p.c.
810-1	Canned hams	15 p.c.	15 p.c.	35 p.c.	15 p.c.	20 p.c.	35 p.c.
825-1	Canned meats, n.o.p.	15 p.c.	15 p.c.	35 p.c.	15 p.c.	20 p.c.	35 p.c.

2. That Schedule A to the *Customs Tariff* be amended by striking out tariff items 2300-1, 7802-1, 7804-1, 14100-1, 18405-1, 40960-1, 42701-1, 42815-1, 44043-1, 44047-1, 44205-1, 44533-1, 44540-1, 56805-1, 61810-1, 68205-1, 85000-1, and 91510-4, and the enumerations of goods and the rates of duty set opposite each of those items, and by inserting in Schedule A to the said Act the following items, enumerations of goods and rates of duty:

Tariff Item	Description	British Prefer-ential Tariff	Most-Favoured-Nation Tariff	General Tariff	Rates in Effect Prior to Rates Proposed in this Budget		
					B.P. Tariff	M.F.N. Tariff	General Tariff
2300-1	Preparations of cocoa or chocolate, n.o.p., and confectionery coated with or containing chocolate	10 p.c.	15 p.c.	35 p.c.	10 p.c.	15 p.c.	35 p.c.
	Except that in the case of any such goods that are the growth, produce or manufacture of the United Kingdom of Great Britain and Northern Ireland, the Channel Islands, the Isle of Man, or Eire, the Most-Favoured-Nation Tariff applies.						
7802-1	Gladiolus corms, *n.o.p.*	15 p.c.	17 1/2 p.c.	25 p.c.	15 p.c.	17 1/2 p.c.	25 p.c.
7804-1	Hydrangeas and other pot-grown plants, n.o.p.; rose stock and other stock for grafting or budding, n.o.p.; bulbs, corms, *including gladiolus corms*, tubers, rhizomes and dormant roots, n.o.p.; dwarf polyantha rose bushes;						
	All the foregoing for use by florists or nurserymen for bona fide forcing purposes or growing on prior to disposal	Free	Free	20 p.c.	Free 15 p.c.	Free 17 1/2 p.c.	20 p.c. 25 p.c.
14100-1	Sugar candy and confectionery, n.o.p., including sweetened gums, candied popcorn, candied nuts, flavouring powders, custard powders, jelly powders, sweetmeats, sweetened breads, cakes, pies, puddings and all other confections containing sugar	12 1/2 p.c.	20 p.c.	35 p.c.	12 1/2 p.c.	20 p.c.	35 p.c.
	Except that in the case of any such goods that are the growth, produce or manufacture of the United Kingdom of Great Britain and Northern Ireland, the Channel Islands, the Isle of Man, or Eire, the Most-Favoured-Nation Tariff applies.						
18405-1	Periodical publications, *bound* or unbound, printed and issued at regular intervals, not less frequently than four times a year, and bearing dates of issue	Free	Free	25 p.c.	Free	Free	25 p.c.

Tariff Item	Description	British Preferential Tariff	Most-Favoured-Nation Tariff	General Tariff	Rates in Effect Prior to Rates Proposed in this Budget		
					B.P. Tariff	M.F.N. Tariff	General Tariff
40917-1	*Articles of any material designed to be ejected from aircraft for use as markers in crop spraying or crop dusting operations*	Free	Free	Free	15 p.c.	17 1/2 p.c.	35 p.c.
40960-1	Roofs, chutes, ladders, wall sections with or without doors incorporated therein, materials and parts; all of the foregoing for the construction or repair of silos for storing ensilage	10 p.c.	10 p.c.	25 p.c.	10 p.c.	10 p.c.	25 p.c.
42701-1	Articles which otherwise would be classified under tariff item 42700-1, namely: compressor sets, electricity generating sets, fork lift trucks, front-end loaders or tractor shovels, gear reducers, pumps and pump sets, motor operated valves, positive displacement blowers and vacuum pumps, metal working lathes, metal working milling machines, cutting tools for use with metal working machines, *articulated folding boom-type cranes designed for mounting on trucks*; accessories, attachments and control equipment for use therewith; parts of the foregoing	2 1/2 p.c.	15 p.c.	35 p.c.	2 1/2 p.c.	15 p.c.	35 p.c.
	Except that in the case of any such goods that are the manufacture of the United Kingdom of Great Britain and Northern Ireland, the Channel Islands, the Isle of Man, or Eire, the Most-Favoured-Nation Tariff applies. Except that in the case of the importation into Canada of any goods enumerated in this item, the Governor in Council on the recommendation of the Minister of Industry, Trade and Commerce may, whenever he considers that it is in the public interest and that the goods are not available from production in Canada, remit the duty specified in this item applicable to the goods, and subsections 17(2), (3), (4), (5) and (8) of the *Financial Administration Act* apply in the case of a remission granted under this provision.						

Tariff Item	Description	British Preferential Tariff	Most-Favoured-Nation Tariff	General Tariff	Rates in Effect Prior to Rates Proposed in this Budget		
					B.P. Tariff	M.F.N. Tariff	General Tariff
42815-1	Diesel and semi-diesel engines, *of a class or kind made in Canada,* and parts thereof, n.o.p.	Free	15 p.c.	30 p.c.	Free	15 p.c.	30 p.c.
	Except that in the case of any such goods that are the manufacture of the United Kingdom of Great Britain and Northern Ireland, the Channel Islands, the Isle of Man, or Eire, the Most-Favoured-Nation Tariff applies.						
42816-1	*Diesel and semi-diesel engines, of a class or kind not made in Canada, and parts thereof, n.o.p.*	Free	15 p.c.	30 p.c.	Free	15 p.c.	30 p.c.
	Aircraft, not including engines, under such regulations as the Minister may prescribe:						
44043-1	When of types or sizes not made in Canada	Free	Free	27 1/2 p.c.	Free	Free	27 1/2 p.c.
	on and after July 1, 197*9*	Free	7 1/2 p.c.	27 1/2 p.c.	Free	7 1/2 p.c.	27 1/2 p.c.
					(on and after July 1, 1978)		
	Aircraft engines, when imported for use in the equipment of aircraft:						
44047-1	When of types or sizes not made in Canada	Free	Free	27 1/2 p.c.	Free	Free	27 1/2 p.c.
	on and after July 1, 197*9*	Free	7 1/2 p.c.	27 1/2 p.c.	Free	7 1/2 p.c.	27 1/2 p.c.
					(on and after July 1, 1978)		
44205-1	Materials, including all parts, wholly or in chief part of metal, of a class or kind not made in Canada, when imported for use in the manufacture of goods entitled to entry under tariff items 41100-1, 41105-1, 41110-1, 42723-1, 42726-1, 42729-1, 42732-1, 42733-1, 42741-1, 42805-1, 42815-1, *42816-1*, 42817-1, 44037-1, 44040-1, and 44705-1, under such regulations as the Minister may prescribe	Free	Free	10 p.c.	Free	Free	10 p.c.

					Rates in Effect Prior to Rates Proposed in this Budget		
Tariff Item	Description	British Prefer-ential Tariff	Most-Favoured-Nation Tariff	General Tariff	B.P. Tariff	M.F.N. Tariff	General Tariff
44503-1	*Parts of electric light fixtures and appliances which would otherwise be classified under tariff item 44500-1, but not including electric cords, plugs, sockets, switches, connectors, high intensity discharge ballasts, or assemblies incorporating any of the foregoing*	15 p.c.	15 p.c.	30 p.c.	17 1/2 p.c.	20 p.c.	30 p.c.
44533-1	Radio and television apparatus and parts thereof, n.o.p.	Free	15 p.c.	25 p.c.	Free	15 p.c.	25 p.c.
	Except that in the case of colour television receiving sets having an overall diagonal measurement across the picture tube of sixteen inches or more that are the manufacture of any country, colony, protectorate or territory to which the benefits of the British Preferential Tariff have been extended, the Most-Favoured-Nation Tariff applies until December 31, 1979.						
	Except that in the case of television apparatus and parts thereof, for use in community antenna television transmission lines, that are the manufacture of the United Kingdom of Great Britain and Northern Ireland, the Channel Islands, the Isle of Man, or Eire, the Most-Favoured-Nation Tariff applies.						
44540-1	Loudspeakers; audio-frequency electric amplifiers; parts thereof, n.o.p.	Free	15 p.c.	25 p.c.	Free	15 p.c.	25 p.c.
	Except that in the case of audio-frequency electric amplifiers and parts thereof, for use in community antenna television transmission lines, that are the manufacture of the United Kingdom of Great Britain and Northern Ireland, the Channel Islands, the Isle of Man, or Eire, the Most-Favoured-Nation Tariff applies.						

Tariff Item	Description	British Prefer-ential Tariff	Most-Favoured-Nation Tariff	General Tariff	Rates in Effect Prior to Rates Proposed in this Budget: B.P. Tariff	M.F.N. Tariff	General Tariff
56805-1	Knitted garments, knitted fabrics and knitted goods, n.o.p.	20 p.c.	27 1/2 p.c.	55 p.c.	20 p.c. or 25 p.c.	27 1/2 p.c.	55 p.c.
	Except that in the case of any such goods that are the manufacture of the United Kingdom of Great Britain and Northern Ireland, the Channel Islands, the Isle of Man, *or Eire, the Most-Favoured-Nation Tariff applies.*						
61810-1	Tires and tubes, wholly or in part of rubber, for equipment of the agricultural implements and agricultural machinery specified in tariff items 40904-1, 40906-1, 40908-1, 40910-1, 40912-1, 40914-1, 40916-1, 40918-1, 40920-1, 40924-1, 40928-1, 40932-1, 40936-1 and the tractors provided for in tariff items 40938-1 and 40940-1 *when such tractors are used for farm purposes only*	Free	Free	Free	Free	Free	Free
68205-1	*Articles and* materials for use in the manufacture or repair of the goods specified in tariff item 68200-1	Free	Free	Free	Free Various	Free Various	Free Various
68705-1	*Catgut, n.o.p.*	Free	Free	Free	15 p.c.	17 1/2 p.c.	25 p.c.
	Materials of all kinds for use in producing or manufacturing the products of heading 93811, when imported exclusively for such use, whether or not otherwise enumerated in Schedule A, subject to such regulations as the Minister may prescribe:						
85001-1	*Other than the following*	Free	Free	Free	Free	Free	Free

Tariff Item	Description	British Preferential Tariff	Most-Favoured-Nation Tariff	General Tariff	Rates in Effect Prior to Rates Proposed in this Budget		
					B.P. Tariff	M.F.N. Tariff	General Tariff
85002-1	*2,4 dichlorophenoxyacetic acid, 2 methyl — 4 chlorophenoxyacetic acid, and their esters and amine salts*	10 p.c.	15 p.c.	25 p.c.	Free	Free	Free
	91510 — Industrial mixtures, including reaction blends, of fatty acids not containing 90 per cent or more by weight of any one acid; acid oils from refining, n.o.p.; industrial mixtures, including reaction blends, of fatty alcohols not containing 90 per cent or more by weight of any one alcohol:						
91510-4	Higher fatty alcohols, unsulphated, for use in the manufacture of *the goods enumerated in tariff item 93402-1*	Free	Free	25 p.c.	Free Free	Free 15 p.c.	25 p.c. 25 p.c.
	93811 — Chemicals for use exclusively as, and preparations compounded exclusively for use as disinfectants, insecticides, fungicides, herbicides, anti-sprouting products, rodenticides, or otherwise in combatting pests of a plant or animal nature; all the foregoing subject to such regulations as the Minister may prescribe:						
93811-3	*2,4 dichlorophenoxyacetic acid, 2 methyl — 4 chlorophenoxyacetic acid, and their esters and amine salts, when in packages exceeding 3 pounds each gross weight*	10 p.c.	15 p.c.	25 p.c.	Free	Free	Free

3. That the Schedule to subsection 3.1(3) of the *Customs Tariff* be amended by striking out tariff item 52306-1 and the enumeration of goods and the rate of duty set opposite that item, and by inserting in the Schedule to the said subsection the following item, enumeration of goods and rate of duty:

Tariff Item	Description	General Preferential Tariff	Rates in Effect Prior to Rates Proposed in this Budget			
			British Preferential Tariff	Most-Favoured-Nation Tariff	General Tariff	General Preferential Tariff
52306-1	Industrial shop towels, hemmed but not bleached or dyed except for identification markings, not less than 17 inches nor more than 22 inches in width and not less than 17 inches nor more than 24 inches in length, made from woven fabrics wholly of cotton or of cotton and man-made fibres in yarn counts from 6 to 14, either single-ply or double-ply, and having not less than 20 yarns nor more than *32* yarns per inch in the warp and not less than 20 yarns nor more than 22 yarns per inch in the weft and weighing not less than 4 ounces nor more than 6 ounces per square yard	Free	22 1/2 p.c.	22 1/2 p.c.	35 p.c.	Free
			22 1/2 p.c.	22 1/2 p.c.	35 p.c.	—

4. That Schedule B to the *Customs Tariff* be amended by striking out item 97056-1 and the enumeration of goods and the rate of drawback of duty set opposite that item, and by inserting therein the following items, enumerations of goods, and rates of drawback of duty.

Item	Goods	When Subject to Drawback	Portion of Duty Payable as Drawback
97012-1	*Costumes or parts thereof, designed or decorated in a manner reflecting a specific ethno-cultural heritage.*	*When for the use of bona fide ethno-cultural groups, who are recognized as such pursuant to regulations established by order of the Governor in Council, and who require such costumes for the public manifestation of their ethno-cultural heritage, under such regulations as the Minister may prescribe* . . . . *Any goods which are sold or otherwise disposed of within twelve months after drawback has been claimed under this item are subject to the duties otherwise prescribed.*	*99 p.c.*
97056-1	Materials, including all parts, wholly or in chief part of metal, of a class or kind not made in Canada.	When used in the manufacture of goods entitled to entry under tariff items 41100-1, 41105-1, 41110-1, 42723-1, 42726-1, 42729-1, 42732-1, 42733-1, 42741-1, 42805-1, 42815-1, *42816-1,* 42817-1, 44037-1, 44040-1 and 44705-1	99 p.c.

5. That any enactment founded upon subparagraph 1(2) of this motion shall be deemed to have come into force on the 1st day of July 1978, and to have applied to all goods mentioned in the said paragraph imported or taken out of warehouse for consumption on or after that day, and to have applied to goods previously imported for which no entry for consumption was made before that day.

6. That any enactment founded upon subparagraph 1(1) and paragraphs 2, 3 and 4 of this motion shall be deemed to have come into force on the 11th day of April, 1978, and to have applied to all goods mentioned in the said paragraphs imported or taken out of warehouse for consumption on or after that day, and to have applied to goods previously imported for which no entry for consumption was made before that day.

7. That any enactment founded upon subparagraph 1(2) of this motion shall expire on the 30th day of June, 1979, and all rates of customs duty established by such enactment shall be deemed to be restored on the expiration thereof to the rates that were in effect immediately prior to the 20th day of February, 1973, and such restored rates shall thereupon, subject to the *Customs Tariff,* apply after the 30th day of June, 1979, as they applied immediately before the 20th day of February, 1973.

8. That where, as a result of an amendment made to Schedule A to the *Customs Tariff* by an enactment founded upon subparagraph 1(2) of this motion, a rate of duty on any goods is reduced from the rate applicable thereto immediately prior to the 20th day of February, 1973, the Governor in Council, at any time during the period commencing with the coming into force of the enactment and ending on the 30th day of June, 1979, may by order restore the rate applicable in the case of the goods to the rate that was in effect immediately prior to the 20th day of February, 1973, and such restored rate shall thereupon, subject to the *Customs Tariff,* apply thereafter as it applied immediately before the 20th day of February, 1973.

Supplementary Information

Research and Development Costs

There has been growing concern in recent months about the adequacy of scientific research and development activity in the Canadian industrial sector, given the importance of R&D as a contributor to long-run economic performance.

At the conclusion of the federal-provincial Conference of First Ministers in February a statement was issued announcing, among other things, that joint steps would be taken to improve the tax incentives or credits to private industry for R&D activities.

Since 1961, the Income Tax Act has allowed a 100 per cent write-off of current and capital R&D expenditures in the year they are made. This fast write-off was supplemented last year by an investment tax credit on current and capital R&D outlays varying by region from 5 to 10 per cent.

As an added stimulus, it is now proposed to introduce for a 10-year period beginning in 1978 a special allowance of 50 per cent of the increase in R&D activity. The allowance, which is deductible in computing income, would apply to the amount by which a company's R&D expenditures in a year exceed the company's average R&D expenditures over the previous three-year period. The effect would be to reduce a company's after-tax cost of each additional dollar spent on R&D to as low as 20 cents.

Because of the incremental nature of the new incentive, its impact on tax revenues will depend upon the extent to which industry responds. However, it is estimated that in the initial years the reduction in federal revenue will be about $50 million a year. Provincial tax revenue would also be reduced in those provinces that have tax collection agreements with Ottawa and those outside the collection agreement who decide to adopt these new provisions.

Energy

Additional tax incentives are being introduced to stimulate the production of energy, in the immediate as well as long term, particularly by new methods that increase the rate of recovery from known oil deposits. Two changes are made in the depletion allowance.

First, the cost of machinery, equipment and other facilities acquired after tonight for use in an enhanced or "tertiary" recovery system will be eligible to earn a depletion allowance of $1 for each $2 of expenditure as compared to the normal depletion allowance earning rate of $1 for $3. An enhanced recovery system is one that uses new technology to recover additional marketable oil from either conventional or heavy oil fields. Depletion is a special allowance, deductible from taxable income, based on the eligible costs of recovering minerals and petroleum.

Second, the amount of the depletion allowance that may be claimed each year will be increased for depletion earned on certain investments in non-conventional oil. At present the maximum deduction for depletion is limited to 25 per cent of resource profits. This limit will be increased, effective this year, for depletion earned on certain eligible expenditures to 50 per cent of total taxable income — that is, resource profits and any other profits of the corporation. For this purpose eligible expenditures will include investments in machinery and equipment forming part of an enhanced recovery project and depreciable property in class 28 that is acquired for a bituminous sands mining project.

For tax purposes, plants established to upgrade heavy oil, other than those established in connection with a bituminous sands mining project, will be treated as manufacturing and processing facilities. This will place them on the same tax footing as oil refineries and other manufacturers. These plants process the heavy, thick types of oil that cannot be sold now in volume, and turn them into a marketable form.

Rail Transportation

Major investments are needed in the railway transportation system to improve efficiency and restrain cost increases. More modern equipment is required in many areas of railway operations including signalling, track and equipment maintenance, motive power and rolling stock.

An additional straight line capital cost allowance of 6 per cent will be provided on all railway system assets (other than certain non-rail automotive assets) acquired after April 10, 1978 and before 1983. This additional allowance will be available in the year of investment and in each of the four subsequent years.

For example, signalling equipment now qualifies for an allowance at a rate of 4 per cent a year on the reducing balance. The special depreciation will permit a further deduction of 6 per cent of the original cost of the equipment in the year in which it is purchased and the following four years.

New investment stimulated by this measure will benefit suppliers of railway equipment, including Canadian producers of rail locomotives and cars, strengthening output and employment in this important manufacturing sector.

Certified Canadian Films

To assist the financing and development of the Canadian film industry, the tax law provides a special write-off for investment in certain Canadian motion picture films or video tapes certified by the Secretary of State. The budget proposes a number of changes to this incentive designed both to improve the quality of Canadian film production and to eliminate abuses.

Under the present capital cost allowance system, the incentive is technically available for a taxation year only if the film or tape is brought into existence by the end of the year. This has tended to rush the completion of the photography, at a sacrifice of quality in many cases. To allow for a more orderly pace of production, a change will be made to permit the deduction to be taken under certain circumstances even though principal photography was not commenced until after the end of the year. This special rule, applicable to the 1978 and subsequent taxation years, will allow the incentive claim provided principal photography of the film is completed within 60 days after the end of the year.

Changes are also necessary to curtail the use of this incentive provision as a device for the undue deferral or avoidance of tax. The principal area of abuse involves a special guarantee arrangement the purpose of which is to increase the amount that an investor may deduct beyond his investment in the film. To curtail abuse, the amount deductible by an investor will be limited to the amount he has at risk. Effective for the 1978 and subsequent taxation years, the amount deductible will be reduced by any revenues or repayments that have been guaranteed.

The Registered Retirement Savings Plan

The Income Tax Act now requires a taxpayer, prior to reaching age 71, to use the funds accumulated in a Registered Retirement Savings Plan (RRSP) to purchase a life annuity from an insurance company. The annuity benefits are then taxable as they are received. The only alternative now available is to withdraw the full amount of the RRSP and become liable to pay income tax on it in the same year.

There have been many complaints that this compels holders to buy a life annuity and denies the holders any control over the investment of funds from RRSPs.

The budget of March 31, 1977 referred to this situation and reported that the government was examining the matter. As a result of that examination, it has been decided to add two alternatives for providing retirement income from RRSP funds:

1. A fixed-term annuity may be purchased to provide benefits to age 90.
2. The savings may be transferred into a new kind of investment vehicle — a Registered Retirement Income Fund (RRIF).

Financial and other institutions that are now eligible to issue RRSPs will be permitted to offer the new options. At present, these are mainly life insurance and trust companies. Under the second, or RRIF, option, a specific fraction of the total assets in the fund — capital plus accumulated earnings — would be withdrawn each year by the holder to provide annual income to age 90. The fraction will be related to the age of the taxpayer in the year and will simply be equal to one divided by the number of years remaining to age 90.

As an example, for a purchaser aged 70 an RRIF would run for 20 years. In the first year, with 20 years remaining, the holder would be required to take into income 1/20th of the total value of the plan at the beginning of the year. After another year 1/19th would be withdrawn, a year later 1/18th, and so on until the final year, when the taxpayer reaches age 90, withdrawal would exhaust the fund. A table at the end of this section shows the results for each $1,000 of investment in a typical RRIF.

The essential purpose of the RRSP, with its exceedingly generous tax treatment, is to provide income in retirement. Since more than 40 per cent of men and more than 50 per cent of women at age 70 would, for example, live longer than to age 85, retirement income must be assured well beyond that age. The new alternatives assure retirement income to age 90 which covers the retirement span of most Canadians.

A taxpayer will be limited to ownership of one RRIF. But he may, if he chooses, allot only a portion of his RRSP accumulations to the establishment of an RRIF and invest the remainder in any number of fixed-term or life annuities.

A taxpayer may base the term of an annuity or RRIF on the age of a spouse, if the spouse is younger, thus securing benefits to age 90 for the spouse. Should a person die before age 90, the benefits under the new options, as well as life annuities with a guaranteed term, could be transferred to the spouse. Otherwise, the value of any remaining benefits must be included in the person's income in the year in which he dies.

The current requirement that an RRSP be matured before attaining age 71 will be modified to require that it be matured during the calendar year in which the holder reaches age 71. This will allow the taxpayer more time to choose the combination of options best suited to his retirement income needs. A new provision will stipulate that a taxpayer may transfer an RRSP into any of the retirement income options, including a life annuity, only after reaching the age of 60.

An RRIF owner will be allowed to manage his own investments through directions to the trust company holding his funds, similar to the existing provision for a self-administered RRSP. There will be a wide variety of qualified investments available, matching those allowed under RRSP investment rules. These include stocks, bonds, bank certificates, savings bonds and mutual funds.

The changes proposed will be effective from the date of Royal Assent. There will, however, be a special provision for taxpayers who reach age 71 between the date of the budget, April 10, 1978, and 60 days following the date on which the enabling legislation receives Royal Assent. If such taxpayers choose to withdraw funds from their RRSPs prior to attaining age 71, they may do so without incurring a tax liability to the extent the amount withdrawn is invested in any of the permissible retirement income options within 120 days of the legislation receiving Royal Assent.

The following table illustrates the characteristics of the RRIF and how it would operate. It shows the annual payments that would be received on a $1,000 investment in an RRIF assuming 5 per cent and 8 per cent rates of interest. Payments under an RRIF grow from year to year at the rate of return on investments in the fund. To the extent that the rates of return reflect price increases, this will tend to protect the real value of the benefits over time. Indeed, if the rates of return exceed the rate of inflation, this will enable the pensioner to improve his real standard of living along with other Canadians.

Payments Under a Registered Retirement Income Fund for Each $1,000 Investment by a Taxpayer at Age 70

Taxpayer's age on Jan. 1	Fraction of plan assets to be paid	5% Interest: Balance at start of year	5% Interest: Payments during the year	8% Interest: Balance at start of year	8% Interest: Payments during the year
70	1/20	$1,000.00	$50.00	$1,000.00	$50.00
71	1/19	997.50	52.50	1,026.00	54.00
72	1/18	992.25	55.12	1,049.76	58.32
73	1/17	983.98	57.88	1,070.76	62.99
74	1/16	972.40	60.78	1,088.39	68.02
75	1/15	957.21	63.81	1,102.00	73.47
76	1/14	938.07	67.00	1,110.81	79.34
77	1/13	914.62	70.36	1,113.99	85.69
78	1/12	886.47	73.87	1,110.56	92.55
79	1/11	853.23	77.57	1,099.45	99.95
80	1/10	814.45	81.44	1,079.46	107.95
81	1/9	769.65	85.52	1,049.24	116.58
82	1/8	718.34	89.79	1,007.27	125.91
83	1/7	659.98	94.28	951.87	135.98
84	1/6	593.98	99.00	881.16	146.86
85	1/5	519.73	103.95	793.04	158.61
86	1/4	436.57	109.14	685.19	171.30
87	1/3	343.80	114.60	555.00	185.00
88	1/2	240.66	120.33	399.60	199.80
89	1	126.35	126.35	215.79	215.79

Note: It is assumed that the required withdrawals from the Fund are made at the beginning of the year, that simple interest is credited at year end, and that no change occurs in the market value of the investments.

Family Farms

Changes are proposed to broaden the special rules that permit the tax to be deferred on a transfer of farm property by a farmer to his children. This is generally referred to as a tax-free rollover and now applies only to the transfer of farmland and depreciable farm property owned by a farmer. It will be made to apply to an incorporated family farm effective immediately.

The rollover will cover transfers to children of shares in qualifying farm corporations and of interests in qualifying farm partnerships. To qualify, the farm corporation or partnership must be carrying on a farming business in Canada, substantially all of its assets must be used in the business and one or more members of the farmer's family must be actively engaged in running the farm. The rollover will also be extended to cover transfers of agricultural quotas.

Family Law Reform

Several provinces are enacting important basic changes in their laws relating to the division of certain properties between parties to a marriage. In some provinces the new laws for the division of property will apply to all married couples, while in others they will relate to property division only in the case of a marriage breakdown.

Although property law is a field entirely within provincial jurisdiction, these changes affecting marital properties give rise to a problem in the application of federal Income Tax Act provisions relating to capital gains.

Technical changes will be made to the Income Tax Act to facilitate the division of property between spouses without incurring a capital gains tax liability. No tax would arise on the original transfer. On a subsequent sale of the property, each spouse would report an equal share of any capital gain.

An example would be a cottage (other than a principal residence) originally bought by a husband in Ontario for $10,000 and valued at $25,000 at the time of a divorce or legal separation. Under the existing Income Tax Act, the husband would be deemed to have disposed of a one-half interest in the property. The difference between the fair market value of his half-interest ($12,500) and his cost thereof ($5,000) would represent a capital gain of $7,500 and the husband would be liable to tax on half of that amount. Since the taxpayer's wife would not have paid anything for her interest in the property, she would have no cost. This means that on a later sale of the property, she would be required to treat her full share of the proceeds as a capital gain and would be required to bring one-half the proceeds into her income.

The change proposed ensures that a capital gain will not arise on the division of the property. The husband will be deemed to transfer his half-interest in the cottage for $5,000. On any subsequent sale of the property, both the husband and wife would include one-half the gain in income.

Federal Compensation for Provincial Retail Sales Tax Reductions

The federal government has offered to compensate provinces to effect a temporary reduction in their general retail sales tax rates.

This offer to finance the provincial reductions takes the form of full compensation for a reduction of three percentage points for six months in the Atlantic Provinces. In all other provinces except Alberta where no retail sales tax is imposed, the federal government will compensate for the revenue forgone arising out of a two-point reduction for a period of six months, provided that these provinces agree to effect a further cut of one point. However, these provinces will have the option of reducing their sales taxes by three points for six months or by two points for nine months. In either event, the federal government will compensate these provinces to the extent of a two-point reduction for six months.

The federal share of the provincial sales tax reductions will be provided to the provinces in the form of a transfer of personal income tax room and, where necessary, by an additional cash payment. This transfer will be made through a temporary abatement of federal personal income tax which will reduce every taxpayer's federal tax liability by $100 or net federal tax otherwise payable, whichever is less. Provinces accepting the offer will increase their income tax on each individual by exactly the amount of the federal abatement. In this way there will be no change in a taxpayer's total tax liability. Taxpayers will not be burdened by any extra calculation when they file their returns since the necessary adjustments will be made by Revenue Canada. In provinces where the amount of the federal reduction of income taxes is not sufficient to fully compensate the province for the agreed level of sales tax revenue forgone, the federal government will make a supplementary cash payment. Similarly, where the federal transfer results in over-compensation, a recovery will be made from the province.

The federal abatement and provincial income tax increase will not apply to residents of the Yukon and Northwest Territories since, like Alberta, these jurisdictions do not levy a retail sales tax.

The accompanying table shows the forecast values of the provinces' retail sales tax reduction and associated federal-provincial financing arrangements.

Estimated Federal Compensation for Provincial Retail Sales Tax Reductions

Province	Present provincial retail sales tax rates	Reduced provincial retail sales tax rates	Value of sales tax reduction
	(%)	(%)	($ millions)
Newfoundland	11	8	24
Prince Edward Island	8	5	5
Nova Scotia	8	5	28
New Brunswick	8	5	27
Quebec	8	6 or 5*	340
Ontario	7	5 or 4*	433
Manitoba	5	3 or 2*	62
Saskatchewan	5	3 or 2*	53
British Columbia	7	5 or 4*	176
Total			1,147

(*) These provinces have the option of reducing their sales tax rates by 3 points for 6 months or 2 points for 9 months.

Proposed Method of Financing Sales Tax Reductions

Province	Federal share			Provincial share	Total
	Tax abatement	Cash payment	Total		
			($ millions)		
Newfoundland	15	9	24	–	24
Prince Edward Island	3	2	5	–	5
Nova Scotia	27	1	28	–	28
New Brunswick	22	5	27	–	27
Quebec	222	5	226	113	340
Ontario	346	-57	289	144	433
Manitoba	37	4	41	21	62
Saskatchewan	28	7	35	18	53
British Columbia	102	16	117	59	176
Total	801	-8	793	354	1,147

Note: Totals may not add due to rounding.

Employees at Remote Work Sites

The Income Tax Act specifies that free board and lodging provided to an employee is a benefit subject to tax. However, it allows an exemption for persons working at remote locations far from their homes who have married or equivalent status. Single persons in similar circumstances are deemed to have a taxable benefit. Typical remote work sites are logging camps, construction projects and drilling locations.

It is now proposed to apply the exemption to all workers at remote sites.

Part IV Tax

Another budget measure concerns the special Part IV tax — that is, the tax of 25 per cent on intercorporate dividends. To assist small business financing and joint venture operations, the 1977 budget removed this tax from dividends received on any shareholding that represented an interest of more than 10 per cent in a corporation provided that the investor corporation's cumulative deduction account did not exceed $750,000. A change is proposed to eliminate the Part IV tax on all dividends received by a private corporation from another corporation in which it has an interest in excess of 10 per cent.

The change described above would by itself permit an inappropriate increase in the amount of business income that qualifies for the special low rates of corporate tax. To prevent such an unintended increase, a consequential change is proposed that will prevent the deduction by a payor corporation in determining its cumulative deduction account of dividends paid by it to any other corporation (other than an associated corporation) that owns more than 10 per cent of its shares.

Deferred Profit-Sharing Plans

The Income Tax Act imposes a special refundable tax on the acquisition by a deferred profit-sharing plan of certain non-qualified investments. Interest is charged where the tax is not paid at the time the investment is made. A change will ensure that interest on any such unpaid taxes ceases to accrue on the refundable portion of the tax as of the date the non-qualified property is disposed of.

Employee Loans

Rules were introduced in 1977 to treat as taxable the benefit an employee enjoys on loans that do not require him to pay a reasonable rate of interest. Certain housing loans and loans to enable an employee to purchase shares were exempted from these new rules. However, the exemption for such loans was available only if the loan was made by the employer. A change will ensure that the exemption will apply on loans made by a person other than the employer. This is needed because in some provinces companies are prohibited from making such loans directly and must do so through a financial institution. Another change will exclude any benefit on housing loans made to persons moving from a location outside Canada.

Surplus Stripping

The Income Tax Act contains special provisions designed to prevent surplus stripping — that is, the tax-free distribution of corporate earnings through a series of transactions involving the sale of shares. One of the rules applies on the sale of shares of one corporation to another by shareholders who act in concert to control the purchasing corporation. The rule presents a number of problems from the point of view of administration and compliance. A change is proposed to eliminate the "acting in concert" rule. The existing provisions relating to surplus stripping will be extended to those situations in which, immediately following a non-arm's length sale of shares, the purchasing corporation owns more than a 10 per cent interest in the corporation whose shares it acquired.

Reduction of Capital

To prevent the possibility of an unintended tax deferral on distributions by public corporations, a change is proposed to treat as a dividend a payment made to a shareholder as a reduction of capital except where the capital reduction takes place on the redemption or cancellation of the share, on the reorganization of the capital, or the winding-up of the corporation.

Insurers Branch Tax

A special 25 per cent branch tax applies to non-resident insurance companies carrying on business in Canada. To implement a change announced in the March 31, 1977 budget, the branch tax provisions are amended to limit the amount by which an insurer can reduce its Canadian investment fund — that is, the assets producing income subject to Canadian corporate tax. Thus an insurer will only be able to reduce his Canadian investment fund to the extent his surplus exceeds a level to be prescribed by regulation. This change is designed to bring the tax treatment of non-resident insurers into agreement with that accorded resident insurers.

Life Insurance Company Losses

A change is proposed to deal with losses of certain life insurance companies. The existing provisions in the Income Tax Act deny the carryforward into 1978 of losses and deductions from prior years to the extent that they arose as a result of the deduction of certain reserves in those years. The technical formula by which this is achieved produced a harsh result for certain small insurance companies that have suffered losses. The proposed change provides relief for losses in those cases where the losses and deductions of prior years exceeded a company's reserves.

Insurance Policy Loan Interest

Loan Interest Paid in 1978 and Subsequent Years

Two changes are proposed relating to life insurance policy loans. The first relates to the deductibility of interest. A policy holder who uses the proceeds of a policy loan to earn income can deduct the interest he pays from his income for tax purposes. However, he must have the insurance company verify that such interest has not been added to the cost of the policy. A change is needed to ensure that such verification is made for loans taken before April 1, 1977 as well as after.

Loan Interest Paid Prior to 1978

The Income Tax Act also provides that all interest paid prior to 1978 is included in the cost basis of an insurance policy. Because the records needed to establish amounts paid in previous years frequently do not exist, a change is required to ignore this interest paid before 1978.

Loans to Shareholders

Amendments were made in 1977 to broaden the rules relating to the inclusion in income of certain loans by corporations to shareholders. An exception was provided for loans to an employee of a corporation where the funds were to be used to acquire shares of the corporation. A further technical amendment is to be made to provide a similar exception for loans made after March 31, 1977 to an employee to assist him in acquiring shares of a related corporation.

Northwest Territories

Effective in 1978, the Northwest Territories introduced its own income tax. Consequential changes are introduced in this budget to provide for a corresponding reduction of the federal tax. The changes ensure that the Northwest Territories is treated on the same basis as the provinces, which already impose their own taxes. This does not result in any change in the level of tax paid by individuals or corporations in the Northwest Territories.

Penalties

The Act will be changed to correct a technical deficiency in the wording of Section 163 that leaves some categories of unreported income outside the calculation of the penalty that applies when a taxpayer has made a false statement on his income tax return.

Customs Tariff Reductions

Temporary tariff reductions on a wide range of goods, initially introduced as an anti-inflationary measure in the 1973 budget and scheduled to expire June 30, 1978, are being extended to June 30, 1979. Exceptions to this extension are canned and frozen asparagus and frozen Brussels sprouts for which the Tariff Board has recommended increased protection, glass tableware which a Canadian manufacturer intends producing in increased quantities if the pre-1973 rate is restored, and surface-active agents or synthetic detergents which are now being imported in such increased quantities as to threaten continued expansion of production in Canada. The temporary rate of 10 per cent on certain canned meats will also expire at the end of June; it will be replaced by a 15 per cent rate, which is more in line with the rates on other meat products and the needs of the industry but still substantially lower than the pre-1973 rates.

Importations of the products on which tariff reductions are being continued were valued at about $1.5 billion in 1977. The main trade items are raw sugar, motor vehicle parts, cameras and films, vacuum cleaners, pharmaceuticals, chinaware, bottles and hand tools. It is again proposed to have Order in Council authority to withdraw any reduced rates that adversely affect employment or production.

The temporary duty-free provisions covering aircraft and aircraft engines of types or sizes not made in Canada initially established in 1952 and scheduled to expire on June 30, 1978, are to be continued for another year. Free entry is also being proposed for markers used in the aerial spraying or dusting of crops and for catgut used mainly for stringing sports racquets. An existing free-entry provision for fatty alcohols for synthetic detergents is being extended to cover fatty alcohols used to make all kinds of surface-active agents.

A reduction from 20 per cent to 15 per cent is proposed for certain parts for electric light fixtures to help Canadian manufacturers compete with imports.

A few amendments of a more technical nature are being introduced as a consequence of those outlined above or to broaden the coverage of existing duty-free provisions (e.g., for gladiolus corms, and certain periodical publications).

Customs Tariff Increases

It is proposed to withdraw the benefits of the British Preferential Tariff from certain goods imported into Canada from the United Kingdom and Ireland. These goods include confectionery, cranes for mounting on trucks, certain diesel engines, certain apparatus used in community antenna television transmission lines, and knitted garments. The main reason for this action is to assist Canadian manufacturers who are operating at below capacity or who have lost significant business to imports from the United Kingdom and Ireland. These imports will now be dutiable at Most-Favoured-Nation rates of duty. Since Britain and Ireland ended Canada's preferential access by joining the European Economic Community, Canada no longer has an obligation to extend preferential tariff treatment to British and Irish goods. Many of the remaining margins of preference will disappear as a result of tariff reductions made in the multilateral trade negotiations.

An amendment is being introduced to exclude tires for non-agricultural tractors from duty-free entry. This change is to assist Canadian manufacturers of industrial tractor tires and to correct an anomaly whereby tires used on the tractor portion of some equipment are free of duty while the same tires used on the non-tractor portion are subject to duty.

An amendment is also being proposed to impose a tariff on two basic chemicals used in the manufacture of pesticides. This action will result in substantial investments being made in expanded production of these chemicals and will help ensure a reliable Canadian source of supply. Formulated pesticides used in agricultural and other applications are now free of duty and will continue to be so.

Effective Dates of Budget Measures

Jan. 1, 1978 — Special allowance to permit deduction from taxable income of 50 per cent of the costs of increases in research and development activity.

Jan. 1, 1978 — Rules on tax incentives for Canadian films certified by the Secretary of State modified to allow additional time for completion of photographic work.

Jan. 1, 1978 — Federal income tax rates reduction in the Northwest Territories to facilitate introduction of a territorial income tax with no tax increase for individuals or corporations.

April 10, 1978 — Costs of machinery, equipment and other facilities for enhanced oil recovery systems become eligible to earn depletion allowances of $1 for each $2.

April 10, 1978 — Limit on the deduction of depletion earned on certain expenditures on non-conventional oil projects increased to 50 per cent of total profit.

April 10, 1978 — Tax-free rollover provisions apply to incorporated family farms.

April 10, 1978 — Plants established to upgrade heavy oil deemed to be manufacturing and processing facilities.

April 10, 1978 — Additional capital cost allowance provided on depreciable railway system assets acquired by railways before 1983.

April 11, 1978 — Tariff changes.

July 1, 1978 — Tariff reductions on a wide range of consumer goods, due to expire, renewed for one year. Duty-free entry of aircraft and aircraft engines of types not made in Canada, also due for expiry, continues for another year. Other tariff changes take effect April 11, 1978.

Upon Royal Assent — Changes relating to retirement income options for owners of Registered Retirement Savings Plans. A special provision will allow RRSP owners reaching age 71 after April 10, 1978 to make use of the new options proposed.