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2006 BUDGET TAX NOTES

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FEDERAL AND PROVINCIAL BUDGET UPDATE

Now that the cycle of federal and provincial budgets has been completed for 2006, this issue of *Tax Notes* is devoted to providing a brief summary of the various federal and provincial 2006 budgets.

FEDERAL BUDGET

REDUCTION IN THE RATE OF GST/HST

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As most taxpayers are aware, the federal Government made a significant change to the Goods and Services Tax (GST) in the May budget. Effective July 1, 2006, the rates of GST (and the corresponding rate of HST - Harmonized Sales Tax applicable in the Atlantic Provinces) have been reduced. GST has been reduced from 7% to 6% and, correspondingly, the HST has been reduced from 15% to 14%. Legislative amendments have been introduced to implement these changes (the recently enacted Bill C-13).

This obviously has a significant impact on suppliers who must change point of sale equipment as well as invoicing systems to reflect this fact. The most significant impact will be on taxpayers who do not obtain full input tax credits (a refund of a tax is available through the ITC (input tax credit) mechanism to most commercial businesses other than financial service businesses, and those in the public sector such as healthcare, educational institutions, and charities and non-profits). Public sector taxpayers obtain a partial rebate of GST paid (municipalities have recently been granted a 100% rebate) but do not receive a full input tax credit as they are not considered to be engaged in a commercial activity.

Clearly, the rate reduction is beneficial to individual consumers (the political target of the relieving "measure") and particularly financial institutions, who pay the bulk of the GST (and are the biggest beneficiary), as well as to public sector or non-profit entities who receive a partial rebate. However, most business will not receive any benefit (as they receive credit for GST paid through the ITC mechanism) and will have significant expenses and administrative costs in dealing with the transitional rules and to change point of sale equipment and automated billing software. The transitional rules for supplies straddling the start up date are complex.

General Transitional Rule

The general rule is that if the GST/HST becomes "payable" or is paid without becoming payable after June 30, 2006, the lower rate applies. In other words, if the GST is paid after June 30 without having become "payable" (the earlier of the invoice date or the date specified in the contract) before then, the lower rate applies. However, there are very specific transitional rules for real property sales, as well as a new real property transitional rebate available where the Agreement was entered into before May 3, 2006 with closing taking place after June 30, 2006, in addition to other special situations such as leases or employee reimbursements. As can be expected, anti-avoidance rules (both existing and new) will be applied where taxpayers try to delay transactions or change agreements to take advantage of the new rule.

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Anti-avoidance Rules/Completed Supplies

If there is an undue delay in issuing an invoice, the consideration is "payable" on the day the invoice would have been issued without that undue delay. In other words, if the invoice would normally be or should have been issued prior to July 1, 2006 tax would be applied at the rate of 7%.

There are specific rules to deal with delayed payments for supplies that are completed or take place over a period of time as follows:

- In the case of the sale of goods for which the consideration is not payable on the last day of the calendar month after the calendar month in which the sale takes place, tax becomes "payable" on the earlier of the day the buyer acquires ownership or possession of the property.
- In the case of sale of goods on approval or consignment, tax is payable on the day the buyer acquires ownership of the property or re-supplies it to someone else.
- In the case of construction contracts for real property or marine vessels where the work is expected to last more than 3 months, the tax is "payable" on the date work is substantially completed.

New anti-avoidance rules are also enacted to deal with amendments to existing agreements primarily to take advantage of the lower (6%) rate or, in the case of related parties, where any transaction is entered into to obtain the benefit of the lower rate.

Transitional Rules for Real Estate

1. Real Estate Transitional Rule - 6% Rate

The lower rate of GST/HST will apply only where the agreement of purchase and sale is entered into after May 2, 2006 and both ownership and possession are transferred after June 30, 2006. The GST new housing rebate is, accordingly, adjusted for sales of housing subject to the new lower rate to a maximum of $7,560 (36% of 6%). This rebate is commonly assigned to the builder who can credit an amount to the purchaser and build it into the selling price.

2. 7% Rate Where Agreement of Purchase and Sale Entered Into Before May 3, 2006

The new lower rate of tax will not apply to purchasers of new housing who contract before May 3, 2006, even if ownership and possession are transferred after June 30, 2006. However, a new temporary 1% GST/HST "transitional rebate" will be available if both ownership and possession are transferred after June 30, 2006 in this circumstance. This rebate can only be claimed by the purchaser, but not if the purchaser claims input tax credits (for example, if the unit is purchased for commercial purposes). It is noted that this transitional rebate is available even if the purchase price is over $450,000 (the new housing rebate is phased out for housing priced between $350,000 and $450,000 and is not available where the consideration exceeds $450,000). Clearly, the intention of this transitional rebate is to give the purchaser the benefit of the 1% reduction in tax but to prevent the builder/Vendor from benefiting in situations where the price is GST included.

3. 7% Where Agreement of Purchase and Sale after May 2, 2006 But Closing Before July 1

The new lower rate only applies where ownership and possession are transferred after June 30, 2006. If either ownership or possession is transferred before July 1st, the 7% (15%) rate will apply. However, the transitional rebate is not available. In situations where a building is not sold out and an agreement is entered into after May 2, 2006 for a unit that is completed or almost completed, closing or possession should take place prior to July 1st, if possible, to enable the purchasers to apply for the transitional rebate.

Leases

For supplies of property by way of a lease or license, the tax becomes payable the earlier the day payment is made and the date it is required to be made under the agreement for the supply. The lease agreement will specify the date the consideration is payable and this is normally the date to look to for the transitional rule to see if it is before or after June 30. However, there are potential issues where the payment is made in arrears and where the lease interval straddles July 1. The transitional rule needs to be applied carefully.

Expense reimbursements and taxable benefits.

These are very specific issues that have complex transitional rules. In the case of benefits, a tax credit or rebate is based on the employees as shareholders. Employee expense reimbursements made using the 7% rate (the employee paid 7%) will attract an ITC at 7% for all payments made to employees on or before June 30, 2006. Thereafter, expense reimbursement payments will result in employer ITCs at 6% even if reimbursed to the employee at 7%.

GST Web Registry

An important administrative change has been made to the CRA website following up on the 2005 federal budget commitment to provide an online registry for checking GST numbers. This was implemented in April of this year. Purchasers who want to confirm that the suppliers are GST registered, and remain so on the date of the supply, can do so by going to the web registry on the CRA website (www.cra-arc.gc.ca) and fill in the supplier's name in the first box and the nine-digit GST number in the second box. The web registry will confirm registration on the effective date of choice if **both** pieces of information are correct. This will enable the purchaser to confirm that the person is indeed registered by printing off the confirmation and keeping it on file. This will provide proof to auditors of the registration status on a certain date. This is important because the ITC (input tax credit) to obtain the refund of the tax is not available unless the vendor is GST registered and remains so as of the date of the supply. This is required according to the GST *Input Tax Credit Information Regulations*.

The GST Web Registry should also be used by a vendor of real property for confirming the GST status of the beneficial purchaser of the real property if the GST is to be not collected pursuant to Section 221 of the *Excise Tax Act*, as the vendor will otherwise be liable for the GST not remitted.

PERSONAL TAX

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The 2006 Federal Budget contains a number of changes that will affect personal taxes - notably, the reduction in GST. Also of significance, as discussed elsewhere in this Newsletter, the Budget exempts from tax the capital gain realized on gifts of publicly-listed securities to charitable organizations and public foundations made after May 2, 2006, as discussed in Robert Hayhoe's article below.

The Budget lowers the lowest personal income tax rate (from 16% to 15% for 2005, 15.25% for 2006 and 15.5% for 2007) and increases the basic personal amount slightly. The Budget also introduces a number of tax credits to assist taxpayers. The "Canada Employment Credit" will be available to employees and is designed to take into account the cost of working, and somewhat narrow the inequity between employees and the self-employed who are able to deduct many of the costs associated with working. Other tax credits will assist families with children, students and the disabled: the "fitness tax credit" for children (of up to $500), a textbook tax credit ($65 for each month of qualifying full-time attendance and $20 for each month of qualifying part-time attendance), and a transit pass tax credit (calculated by reference to the lowest personal income tax rate) will be incorporated into tax planning for families. Student scholarship, bursary and fellowship income will be exempt from taxation. The Child Disability Benefit and the Refundable Medical Expense Supplement will be increased.

The Budget proposes amendments to the tax treatment of dividends which will increase the gross-up and dividend tax credit for eligible dividends. Eligible dividends will generally include dividends paid after 2005 by public corporations (and other corporations that are not CCPCs) that are resident in Canada and subject to the general corporate income tax rate. CCPCs will be able to pay eligible dividends to the extent that their income (other than investment income) is subject to tax at the general corporate rate. Eligible dividends will be grossed up by 145% (instead of 125%) and the tax credit increased to approximately 19%. The result of this measure is essentially to eliminate the current tax preference in the rates on realization of capital gains. For planning purposes, depending on whether the provinces follow suit, Canadians should be somewhat indifferent between realizing capital gains or dividend income.

Canadians in the fishing industry will be able to access the $500,000 lifetime capital gains exemption which is currently available to family farming businesses and private corporations when they transfer property used in a fishing business. Qualified fishing property will include real property, fishing vessels and eligible capital property used principally in a fishing business carried on in Canada in which the individual, or the individual's spouse or common-law partner, parent, child or grandchild, was actively engaged on a regular and continuous basis. As well, an individual's fishing property will be eligible for an inter-generational rollover in certain circumstances. These new rules will provide greater inter-generational planning opportunities for Canadians in this industry.

Of note is the fact that one of the Conservative election promises was not pursued in this Budget. The Conservatives had proposed to eliminate the capital gains tax on the sale of investment assets if the proceeds of the sale were reinvested in other investment assets within a certain period of time. While it is unfortunate that this measure was not introduced, it is perhaps not surprising given the legislative complexity such a measure would entail.

CORPORATE TAX

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Reduction in Corporate Tax Rates

The federal budget proposes to reduce the general corporate income tax rate from 21% to 20.5% effective January 1, 2008, 20% effective January 1, 2009, and 19% effective January 1, 2010. These new income tax rates will be pro-rated for non-calendar taxation years.The rate reduction will apply only to income that is taxed at the general, including manufacturing and processing, corporate income tax rate.

As well, the corporate surtax of 4% of federal tax will be eliminated for all corporations effective January 1, 2008. Again, this change will be pro-rated for non-calendar taxation years. The elimination of the corporate surtax is equivalent to a 1.12% decrease in corporate income tax rates.

Small Business Rates and Thresholds

The federal budget enhances tax relief to Canadian controlled private corporations ("CCPC's") by increasing the annual amount of active business income of a CCPC eligible for the reduced income tax rate from $300,000.00 to $400,000.00 effective January 1, 2007. As well, the budget proposes to reduce the small business income tax rate from 12% to 11.5% effective January 1, 2008, and to 11% effective January 1, 2009. These changes are pro-rated for non-calendar years.

Investment Tax Credit Expenditure Limit

Refundable investment tax credits are available to CCPC's at an enhanced rate of 35% on up to $2,000,000.00 of scientific and experimental development expenditures annually. This $2,000,000.00 expenditure limit begins to be reduced as the taxable income of a CCPC for the previous taxation year reaches $300,000.00 and is completely eliminated when the prior year's taxable income reaches $500,000.00. As a consequence of the increase in the annual small business limit to $400,000.00, for taxation years ending after 2006, the $2,000,000.00 expenditure limit will be reduced when taxable income in the previous year is between $400,000.00 and $600,000.00.

Federal Capital Tax

The Federal Capital Tax which is currently 0.125% of taxable capital, will be eliminated as of January 1, 2006, which is two years earlier than originally scheduled for this elimination. The Federal Capital Tax will be pro-rated for non-calendar taxation years.

Carry-Forward Period for Losses and Investment Tax Credits

The Carry-Forward Period for Losses and Investment Tax Credits incurred or earned in taxation years ending after 2005 will be extended from 10 years to 20 years.

Capital Cost Allowance for Tools, Utensils and Instruments

Currently, tools, certain kitchen utensils and medical and dental instruments costing less than $200.00 are eligible for a 100% Capital Cost Allowance ("CCA") rate. The budget proposes to increase the cost limit for the 100% CCA rate from $200.00 to $500.00 for such items acquired after May 2, 2006. Items costing more than $500.00 are generally eligible for a 20% CCA rate.

Apprenticeship Job Creation Tax Credit

The federal budget proposes to introduce an Apprenticeship Job Creation Tax Credit, which provides businesses (eligible employers) with a non-refundable tax credit equal to 10% of salaries and wages paid to qualifying apprentices on or after May 2, 2006, to a maximum credit of $2,000.00 per year, per apprentice.

BUDGET CHANGES FOR CHARITIES

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The 2006 Federal Budget, released on May 2, includes complete capital gains relief for gifts of publicly listed securities to charitable organizations and public foundations. A similar measure was also included to provide complete capital gains relief for gifts of ecologically sensitive land to approved conservation charities.

Beginning in 1997, when a Canadian individual or corporate donor made a gift of publicly listed securities (defined broadly to include such investment products as mutual funds) to a charitable organization or a public foundation (but not to a private foundation), the capital gain that is deemed to have been realized as a result of the gift was only taxed at 50% of the usual capital gains inclusion rate. Immediately before the 2006 Budget, the usual capital gains inclusion rate was 50% with the result that the capital gains inclusion rate for gifts of publicly listed securities to charitable organizations or public foundations was 25%.

In recent years, the charitable sector has engaged in a concerted effort to educate the government about the potential benefits of reducing the effective capital gains inclusion rate for gifts of publicly listed securities from 25% to 0%. Some, but not all, segments of the charitable sector also sought to have the class of eligible recipient charities expanded to include private foundations. The charitable sector was therefore pleased when, in the course of the last federal election campaign, Stephen Harper proposed to eliminate capital gains on gifts of publicly listed securities. The 2006 Budget implements this election promise effective for gifts made on or after May 2, 2006.

Although the Conservative election promise (supported after announcement by the other major parties) was unclear on whether the elimination of capital gains tax on gifts of publicly listed securities would be extended to gifts to private foundations, the Budget announcement has confirmed that the tax benefit is not proposed to be extended immediately to private foundations. However, the Budget confirms the government's intent to enact a similar regime for private foundations if a suitable regime can be developed to prevent inappropriate self-dealing transactions involving individuals who control public corporations and who exercise influence over private foundations to which the corporation's shares are donated.

Ecologically Sensitive Land
Beginning in 2000, donations of ecologically sensitive land (or easements protecting ecologically sensitive land) to approved conservation charities had only been taxed on the deemed capital gain at 50% of the usual rate. As has been described above in the context of publicly listed securities, the 2006 Budget announces that the capital gains inclusion rate for these donations will be reduced to zero effective May 2, 2006.

Investment Asset Rollover Delayed?
Another Conservative election promise was that sales of investment assets would be treated on a rollover basis if the proceeds of the sale were reinvested in other investment assets. A concern has been raised by the charitable sector that this new rollover would reduce the incentive for donors to make gifts of publicly listed securities. However, the 2006 Budget does not include any provisions to implement this proposal.

PROVINCIAL BUDGETS

BRITISH COLUMBIA

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On February 21, 2006, the British Columbia Minister of Finance, Carole Taylor, delivered the 2006 BC Budget. According to the Minister, the BC economy remains strong, with a low unemployment rate and strong business investment. The budget announced significant new funding for children and family services, job skills and training, and higher education. $421 million is allocated toward programs for children in need, while $400 million is allocated to increase training and skills development and to expand post-secondary education. No changes were announced with respect to personal or corporate income tax rates. However, the budget did include a number of tax relief measures that benefit both individuals and businesses. Some of the highlights of these proposed amendments are outlined below.

Enhanced Dividend Tax Credit
BC will introduce an enhanced dividend tax credit to harmonize with the federal government's proposal to reduce the tax rate on dividends from Canadian corporations. Under the federal government proposal, which was announced November 23, 2005, an increase in the gross-up factor for dividends from 25% to 45% is planned, together with a corresponding increase in the federal dividend tax credit. Specific changes will be announced once the details on the federal proposals become available.

Medical Expenses Tax Credit
For 2005 and subsequent years, the maximum amount of medical expenses that may be claimed on behalf of dependent relatives will be increased from $5,000 to $10,000 per dependent.

Mining Tax Credits
The BC mining flow-through share tax credit program allows individuals who invest in flow-through shares to claim a non-refundable tax credit equal to 20% of the BC flow-through mining expenditures renounced to them by the corporation issuing the shares. The program is designed to provide incentive for raising venture capital mineral exploration in British Columbia. The expiry date for the program, and for eligible expenditures for the credit, will be extended by three years to the end of 2008.

Film and Television Tax Credits
As announced on January 20, 2006, the enhanced film and video production tax credit rates introduced in last year's budget will be extended to 2008. The rates remain at 30% for the basic Film Incentive BC Tax Credit and 18% for the Production Services Tax Credit.

Royalty and Deemed Income Rebate
BC will eliminate the royalty and deemed income rebate and harmonize with the federal resource sector rules effective for tax years after 2006.

Retail Sales Tax / Software
Social Service Tax (SST) on the installation, modification and repair and maintenance of computer software is eliminated effective February 22, 2006. SST continues to apply to purchases of computer hardware and software unless the software qualifies as custom software or custom modified software. The purchase of custom software or custom modified software will be exempt from SST when purchased as part of a business or as a going concern.

Retail Sales Tax / Production Machinery and Equipment

Effective February 22, 2006, the SST exemption for production machinery and equipment was expanded to include businesses providing manufacturing services to qualifying manufacturers. Additionally, the exemption for pre-manufactured parts to repair and maintain exempt equipment was expanded to include parts purchased or leased by qualifying manufacturers to assemble qualifying machinery or equipment.

Retail Sales Tax / Increased Vehicle Surtax Thresholds

The threshold for the surtax on passenger vehicles is increased from $49,000 to $55,000, effective for vehicles purchased after February 22, 2006. For leased passenger vehicles, the new vehicle surtax thresholds will apply to lease payments due after February 22, 2006.

Homeowner Grant

Starting in 2006, the basic and additional homeowner grants will be increased by $100. The upper threshold for claiming the full grant will also be increased from $685,000 to $780,000. For properties valued above this threshold, the grant will continue to be reduced by $5 for every $1,000 of assessed value. Eligibility for the supplementary grant for people with disabilities will also be expanded for those who meet certain conditions.

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On March 22, 2006 the Alberta Government tabled its 2006 Budget, forecasting a surplus of over $4 billion for the coming year. The government considers the tax system to be working well, and as a result the budget makes very few changes. For the time being, policymakers seem content to remind us of the personal and corporate tax rate reductions implemented over the past decade, and the recent distribution to Albertans of over $1.3 billion through the Resource Rebate program.

Highlights of tax changes for 2006 are:

Corporate Tax Rate Reduction

Effective April 1, 2006, Alberta's general corporate tax rate will decrease to 10% from 11.5%. The small business tax rate remains at 3% with a $400,000 threshold.

Personal Tax Credits

Tax credit amounts will increase by 1.9% in 2006 to offset inflation. The basic, spousal and eligible dependant amounts are increased by an additional $100 to $14,899 for 2006. Indexing of the Alberta Family Employment Tax Credit begins in July 2006. Families will now receive $560 for the first child, $510 for the second child, $306 for the third child and $102 for the fourth child. This credit begins to be phased out for incomes over $25,475.

School Property Tax Rate Reduction

The province collects a portion of property taxes to fund education. These taxes are being reduced by about 7.1%. Residential and farm property rates are set at $4.80 per $1,000 of equalized assessment (down from $5.17). Commercial property will be taxed at $7.05 per $1,000 (down from $7.59).

Health Care Premium Subsidy Threshold

As of April 1st, 2006, income levels at which Albertans qualify for full and partial premium subsidies are rising by $5,000. Full subsidies are now available to individuals under age 65 with income below $17,450, couples with income below $26,200, and families with income below $32,210. Partial subsidies are phased out when incomes reach $20,970, $33,240 and $39,250 respectively. All seniors continue to receive a full subsidy.

Wait and See

Budget documents indicate that the province is still examining the effect of the federal government's two-tiered dividend tax credit, announced in November 2005. The province will decide whether to adopt similar treatment once more details are available. Similarly, the government is watching the effect of income trusts on provincial tax revenues. Due to residency rules, the shift from corporate to personal taxation under these structures is estimated to result in a net tax loss to Alberta of about $400 million per year.

SASKATCHEWAN

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On April 6, 2006, the Government of Saskatchewan tabled its budget for the 2006/2007 fiscal year. There were few income tax measures; however, there were some tax bracket changes, business tax rate changes and personal tax credit amendments.

Tax bracket thresholds and personal amounts are to increase by 2.2% in 2006, and the Province has introduced an employee's tool tax credit to assist in defraying the cost of tools purchased as a condition of employment. The credit consists of a one time trade entry tool amount and an annual maintenance amount which, together, will be calculated as 11% of a specified credit for each of four specific trade groups.

For businesses, the budget announced a reduction in the corporate income tax rate from 17% to 12% by July 1, 2008 (being cut from 17% to 14% on July 1, 2006), and announced the increase of the small business threshold from $300,000.00 to $500,000.00, also by July 1, 2008 (increasing from $300,000.00 to $400,000.00 July 1, 2006). Also, the corporate capital tax surcharge rate will be decreased to 3.3% of resource sales from 3.6% on July 1, 2006, falling to 3% over the next two years, and the corporation capital tax rate will fall from 0.6% to 0.3% on July 1, 2006, and to 0.15% again in July 2007 and be eliminated by July 1, 2008.

In conjunction with the province's sales tax, the budget made note that there was widespread support for harmonization of the 7% provincial sales tax with the federal GST to streamline sales tax administration. However, the Province has deferred a decision on harmonization to future budgets.

MANITOBA

The Government of Manitoba tabled its 2006/2007 budget on March 7, 2006, with some rate tinkering similar to that in Saskatchewan. In particular, the middle income tax rate will be reduced to 13% on January 1, 2007, down from the 13.5% rate that was slated for 2006 in the 2005 budget. The individual basic personal amount has also been increased $100.00 to $7,834.00. Also, the provincial budget will track the federal budget provisions for the dividend tax credit for dividends received from Canadian corporations and for the children's physical activity tax credit. For businesses, the small business tax rate will be reduced to 3% effective January 1, 2007, with the general corporate tax rate being reduced to 14% effective July 1, 2007, and to 13% on July 1, 2008. The corporate capital tax will be phased out, commencing with a 20% reduction on July 1, 2008.

ONTARIO

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The 2006 Ontario budget was tabled on May 23rd, 2006. A deficit of $1.4 billion was recorded for 2005-2006 fiscal year. For the fiscal year 2006-2007, the Ministry of Finance estimated a deficit of $2.4 billion.

In summary, the Ontario budget cut corporate capital tax, gave tax incentives for the entertainment industry and for renewable energy use and production and also signaled that Ontario would follow the federal government's implementation of certain taxation measures.

The Ontario budget proposed an accelerated capital tax rate reduction. Effective January 1, 2007 corporations paying capital tax will have their rates reduced by 5%. This rate reduction is two years in advance of the rate reduction anticipated in the 2004 budget. Ontario has planned to eliminate corporate capital tax by 2010. This will benefit all corporations with capital in excess of $12.5 million.

The budget also proposes several tax incentives designed to develop Ontario's entertainment industry.

Generally, Ontario's regime of tax credits for the entertainment industry equates to a $120 million annual investment in the industry. To attract Ontario film production from foreign sources, the Ontario Production Services Tax Credit (OPSTC) rate was increased to 18% from 11%, effective January 1, 2005 to March 31, 2006. The Ontario budget extended the credit increase to March 31, 2007. The OPTSC is available to Ontario-based corporations for foreign-based and domestic productions not claimed under the Ontario Film and Television Tax Credit (which is available to Ontario-based Canadian controlled corporations for eligible film and television productions).

The tax credit rate for the Ontario Interactive Digital Media Tax Credit (OIDMTC) is proposed to be raised to 30% (from 20%) for corporations qualifying under the existing OIDMTC provisions. However, corporations with annual gross revenues over $20 million and total assets over $10 million, the OIDMTC rate is extended to 20%. The budget also proposed to extend the 20% OIDMTC rate to fee for service work done in Ontario.

Also for the entertainment industry, the exemption from provincial sales tax under the *Retail Sales Tax Act* ("RSTA") on donated complimentary admission tickets is proposed to be expanded to include such tickets donated to community colleges, schools, universities and certain not-for-profit organizations. This proposal would be effective for donations made after March 23, 2006.

Other proposed amendments to the RSTA concern extending the provincial sales tax exemption on destination marketing fees charged by hotels. For example, hotels that are organizations that are members of the Greater Toronto Hotel Association charge a voluntary fee to fund tourism in Ontario. Under the proposed measure this charge would not be subject provincial sales tax for one year ending June 30, 2007.

Adding a "green" tinge to the 2006 budget, Ontario proposed to double the retail sales tax rebate for hybrid electric vehicles from $1,000 to $2,000. This means that all the provincial sales tax paid on a hybrid electric vehicle priced $25,000 (or less) would be eligible for a full rebate.

Other "green" tax measures proposed in the Ontario budget addressed the renewable energy sector. The increased capital cost allowance rate introduced in the 2005 Federal budget targeting assets used for renewable energy production would be adopted under the Ontario *Corporations Tax Act* in respect of systems that use "black liquor" for energy production. Black liquor is a by-product of paper making process (and probably does not go down smoothly).

Also, to coincide with the requirement that by January 1, 2007 the content of gasoline sold in the province will have minimum 5% ethanol content, the *Gasoline Tax Act* exemption on ethanol is proposed to be removed. This measure appears to be the sole tax increase (or expansion) in the budget and is proposed to pay for the proposed 12-year $520 million Ontario Ethanol Growth Fund.

The Ontario budget also proposed to parallel certain taxation initiatives introduced by the Federal government upon their implementation, including:

- permitting a tax deferral on the payment of certain patronage dividends paid by agriculture cooperative corporations; and
- extending the non-capital loss carry forward period from 10 years to 20 years.

Notably, the Ontario budget also signaled that it would "respond" to the federal government's implementation of a new dividend tax credit designed to place the taxation of dividends from a large corporation to be on par with income received through an income.

QUÉBEC

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Finance Minister Michel Audet tabled the Québec government's 2006-2007 Budget before the National Assembly on March 23, 2006. It is "a responsible budget, a budget with a vision", said the Minister, built on four main objectives:

- ongoing improvement of health and social services system and education system;
- wealth creation in a sustainable development context;
- infrastructure development and repair;
- debt burden reduction to ensure greater inter generational equity;

The following is a summary of some of the measures he announced.

Measures Concerning Individuals

- The maximum amount of the deduction for workers will be doubled, from $500 to $1,000 as of the 2007 taxation year;
- There will be changes as of the 2007 taxation year, to the parameters of the refundable tax credit for home support for elderly persons;
- Tax treatment of donations and gifts: the tax legislation will be amended as of the 2006 taxation year, to reduce the threshold of $2,000 to $200 above which the tax credit applies to a rate of 24%;
- The tax legislation will be amended to extend the carry-forward period for donations made by corporations during a taxation year ending after March 23, 2006 from five to twenty years;

- Opportunity for artists to defer taxation of their income: the excluded amount will be reduced from $50,000 to $25,000 beginning in the 2006 taxation year for the purposes of determining the maximum amount that can be used to acquire an eligible income-averaging annuity.

Measures Concerning Business

- the small tax rate applicable to the business ceiling of corporations will be reduced from 8.5% to 8% as of March 24, 2006;
- adjustments to refundable tax credits for R&D: the tax legislation will be amended so that an R&D project will no longer be eligible for the tax credit for university R&D; and R&D project carried out as part of a public-private partnership will no longer be eligible for the tax credit for pre-competitive R&D;

The tax credit for pre-competitive R&D will be replaced with the refundable tax credit for pre-competitive private partnership research that will apply to R&D projects that exclusively involve a private-private partnership.

Measures concerning culture

Changes will be made to the types of production eligible for the tax credit for the production of sound recording and adjustments, to the refundable tax credit for Quebec film and television program, for book publishing and for the production of multimedia titles.

Tax treatment applicable to taxable dividends

The Quebec legislation will be amended to increase the gross-up of dividend income from 25% to 45% for dividend income consisting of eligible dividends.

The Quebec dividend tax credit will be increased for dividend income consisting of eligible dividends to equal 11.9% of the grossed-up dividend.

The Quebec dividend tax credit applicable to non eligible dividend income will be reduced to equal 8% of the grossed-up dividend.

Consequently, the maximum combined Federal/Quebec tax rate applicable to dividends will decrease from 32.82% to 29.65% for an eligible dividend and increase to 36.36% for other dividends.

These changes will apply to dividends that are paid or are deemed to have been paid after March 23, 2006.

Federal Legislation

Quebec's tax legislation will be amended to incorporate with adaptations based on their general principles various legislative amendments announced by the Federal.

NEW BRUNSWICK

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The New Brunswick budget for 2006-2007, tabled on March 28, 2006, estimates a surplus of $116.8 million for 2005-2006 and forecasts a surplus of $22.2 million for 2006-2007.

Provincial income tax credit amounts and tax brackets will continue to be indexed and, effective for the 2007 tax year, single tax filers with incomes up to $13,750 and families with incomes up to $22 000 will pay no provincial personal income tax. As in Nova Scotia, residential customers in New Brunswick will receive a rebate of the 8% provincial portion of the Harmonized Sales Tax on home energy costs.

The small business tax rate will drop to 1.5% effective July 1, 2006 and will be further reduced to 1% in 2007. The small business tax threshold will be increased to $475,000 on July 1, 2006, and further increased to $500,000 on July 1, 2007. General corporate income tax will be lowered from 13% to 12% effective January 1, 2007. The Large Corporation Capital Tax will be eliminated by the end of 2008. Currently the rate is 0.3% of the federal capital tax base, with a $5 million exemption. The rate will be reduced to 0.25% in 2006, 0.2% in 2007, 0.1% in 2008 and nil in 2009. Qualifying forestry industries investing in the Province after March 31, 2006 and before December 31, 2007 will receive a rebate of 50% of their investments in manufacturing and processing equipment, up to a maximum of 50% of the provincial property tax paid that year.

NOVA SCOTIA

The Nova Scotia budget for 2006-2007, tabled on May 9, 2006, projected a surplus of $71.9 million for 2006-2007 and reported a surplus of $151 million for 2005-2006.

Effective January 1, 2007, the basic personal exemption will be raised by $250 over each of the next four years. Non-refundable tax credits will increase proportionately by same increase over this period. Starting in 2011, full indexation will be implemented. Effective January 1, 2007, a new household energy rebate of 8% for every household on the total provincial portion of the Harmonized Sales Tax will apply to all forms of home heating costs (including natural gas, home heating fuel, wood, and other fuel sources) and basic electricity.

The small business tax threshold was increased to $400,000 from $350,000. The Large Corporations Capital Tax rate was proposed to be decreased from 0.275 to 0.25% resulting in the complete elimination of the tax by July 1, 2012. A new Energy Efficiency Tax credit, equal to 25% of a company's capital investment in renewable energy sources or energy efficiency (up to a maximum of 50% of the Large Corporations Capital Tax payable in the year) will come into effect on purchases made after July 1, 2006.

Additional measures include an increase in the Healthy Living Tax incentive from $150 to $500 per child and a $1000 non-refundable provincial tax credit on earnings within three years of graduation.

PRINCE EDWARD ISLAND

The Prince Edward Island budget for 2006-2007 was tabled on March 30, 2006, and forecast a deficit for 2005-2006 of $18 million, down $4 million from the $22 million projected in the 2005 budget. The deficit for 2007 is projected to further decrease to $12.5 million.

Over the next five years, the Province will continue to reduce its small business rate annually on April 1 from 6.5% to 5.4% in 2006, 4.3% in 2007, 3.2% in 2008, 2.1% in 2009, and 1% in 2010. The Province also proposes to adjust the dividend tax credit to preserve integration between the corporate and personal tax systems.

NEWFOUNDLAND

The Newfoundland budget for 2006-2007, tabled on March 30, 2006, reported a $76.5 million surplus in 2005 versus the budget target deficit of $492.5 million, and forecasted a $6.2 million surplus for 2006. The Province plans to focus investment in education, infrastructure, development and innovation.

There are no new taxes and only one tax increase. The tobacco tax rate on cigarettes will increase by one percent per cigarette and by five cents per gram of fine-cut tobacco, effective March 31, 2006 at 12:01 a.m.

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