
Budget

in brief

November 16, 1978

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1978
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**Department of Finance
Canada**

**Ministère des Finances
Canada**



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*From the Budget speech
November 16, 1978*

"I believe that this budget will make a significant contribution to the containment of our domestic costs in the post-control era. This will enable us to take full advantage of the improvement in our competitive position that we have achieved.

"My budget measures will, of course, provide a more direct stimulus to growth. Investment will be stimulated by the enriched investment tax credit. Consumption will benefit from the increase in the real spending power of Canadians as a result of the income and sales tax cuts."

*Jean Chrétien
Minister of Finance*

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Economic Highlights

- The economy made much progress in 1978 but results fell short of earlier expectations. Growth in real output will likely be close to 4 per cent, with prices of the things we produce up about 6½ per cent.
- Slower than expected growth in real consumer spending was the main cause of the shortfall in growth. Real purchasing power grew more slowly due to higher food prices and the decline in the dollar which increased prices of imports. These factors offset the expansionary impact of strong gains in employment, a cut in personal income taxes and temporary reductions in provincial sales taxes.
- Since the introduction of the Anti-Inflation Program, Canada has made great progress in laying the basis for future sustained growth. Growth rate of the money supply has been gradually reduced, government expenditures put under tight control and average wage increases brought down from 15 per cent to 6 per cent in the last year of controls.
- The decline in the exchange rate has helped us regain competitiveness. Canadian firms are now in a good position to increase export sales and regain home markets from import competition.
- Performance to date indicates a record trade surplus this year of close to \$4 billion. A turnabout in manufacturing industry has brought strong gains in output and employment. Capacity utilization in

manufacturing is now above the long-term average.

- The outlook for self-reliance in energy is most encouraging, and oil and gas should contribute substantial improvement to our trade balance.

Economic Outlook

The Budget speech:

"Our most immediate challenge ... is to hold onto the gains we have been making in our competitive position as we come to the end of mandatory controls over prices and incomes."

- Strong expansionary forces are at work, from a better cost performance and a more competitive dollar. Planned increases in industrial capital spending are in evidence.
- Given steadier food prices and a steadier exchange rate, a lower rate of inflation should emerge so long as Canadians are reasonable in their income demands.
- Price increases, as measured by the Consumer Price Index, should be under 6 per cent by the fourth quarter of 1979. National output in real terms is forecast to rise next year by between 4 and 4½ per cent.

Fiscal Policy

- Federal spending cuts have produced some fiscal room. The budget shares these savings with the public.
- Budget proposals will cut income and sales taxes to increase the real spending power of Canadians, reduce pressures on prices and income demands, and stimulate investment.

The Budget speech:

“Action is needed now to encourage investment to respond to the needs of sectors and regions and to keep our costs competitive, while reducing our cash requirements from the present high level.”

Federal Sales Tax Reduction

- The federal sales tax is cut from 12 to 9 per cent, effective immediately, with tax savings of \$1 billion in a full year. Manufacturers and importers are expected to pass this through to consumers in the form of lower prices.

Commodity Tax Changes

- Special excise taxes on marine engines, private aircraft and motorcycles are not having an important effect on energy conservation and thus are being dropped. The special excise tax on gasoline of 7 cents a gallon is extended to non-commercial aviation fuel.
- Solar-powered water heaters are exempted from sales tax, and the exemption for insulation materials is being restricted to those with genuine insulating properties.
- The air transportation tax, earmarked for financing air transport services, will be increased after March 31, 1979.

Personal Income Tax

- The budget doubles to \$500 the maximum employment expense deduction that taxpayers can claim, effective for the 1979 tax year—a tax saving of \$270 million. Over 6,200,000 taxpayers will benefit.
- A further \$1.2 billion reduction in federal taxes next year will result from the indexing provision now in the Income Tax Act. This will come from a 9 per cent increase in personal exemptions and tax brackets, and in the child tax credit.
- A further \$400 million reduction in provincial income taxes will occur in those provinces with tax-collection agreements.

- Tax rules affecting registered retirement savings plans will provide relief in cases where both parents die leaving minor or disabled children.

Unemployment Insurance

- Unemployment insurance premiums in 1979 will be cut—a total \$300 million saving for workers and employers: For employees, the weekly rate will be reduced from \$1.50 to \$1.35 per \$100 of insurable earnings; the employer rate will decline from \$2.10 to \$1.89.

Canada-U.S. Tax Comparison

- A comprehensive comparison of Canadian and United States tax systems shows conclusively that the personal tax system in Canada compares most favourably with that of the U.S. Canadian taxes on business are fully competitive. Manufacturing in Canada enjoys effective income tax rates averaging some 10-12 percentage points lower.

Industrial Growth Incentives

- A series of proposed changes in corporate taxation flows from two major processes of policy consultation: the series of federal-provincial conferences on economic issues, and the work of 23 industrial sector Tax Forces that were set up following the First Ministers' Economic Conference last February. The measures are designed to improve efficiency, lower costs and promote a more balanced pattern of development across regions.

Sectoral and Regional Incentives

- The investment tax credit, which supports industrial expansion and modernization, will be extended indefinitely beyond its scheduled expiry date of June 30, 1980.
- The basic rate of tax credit will be raised from 5 to 7 per cent, with larger increases in designated areas of slower growth: to 10 per cent in most DREE-designated areas and to 20 per cent in the Atlantic Provinces and the Gaspé.
- The basic 7 per cent tax credit is being extended to investment in equipment for rail, air, water and long-haul road transport. This reflects the emphasis given to transportation at the First Ministers' Conference.
- Extension and improvements to the investment tax credit will mean benefits of about \$500 million in the first full year of application.

Resource Taxation

- In mining, the write-off for development expenditures is being raised from 30 to 100 per cent, and townsites and social assets required for new mines will qualify to earn depletion.
- The incentive for oil and gas drilling funds will be extended to December 31, 1981, from its scheduled expiry date on June 30, 1979.
- Provision for fast write-off of outlays for pollution control equipment, due to expire at the end of 1979, will be extended indefinitely. This will particularly benefit the mining and pulp and paper industries.

Research and Development

- The basic investment tax credit for R&D will be doubled from 5 to 10 per cent. It will be doubled to 20 per cent in the Atlantic Provinces and the Gaspé.
- A special R&D tax credit of 25 per cent will apply for small business corporations in all parts of Canada.
- These R&D incentives are in addition to substantial new measures announced earlier this year, and reflect a broad concern of the industry Task Forces.

Housing

- The tax incentive for multiple-unit residential buildings will be extended for one year, to the end of 1979.
- Developers will be allowed to deduct carrying charges incurred after tonight on their land inventory.

Other Tax Changes

- There will be a more precise definition of those businesses who may qualify for the very favourable small business tax rate. This will ensure that the incentives will serve their original purpose of promoting small business expansion and not be used as a tax shelter for personal, professional and investment income of individuals.
- The budget proposes to change the tax treatment of new issues of income debentures and term preferred shares. Income earned on such securities by financial institutions will in future be taxed in the same way as income on loans. This is because they are essentially debt obligations. The change will prevent a further erosion of some \$150 million in federal tax revenues in 1979-80.

Impact on the Economy

- The sales tax reduction will reduce the advance in the consumer price index by one-half of one per cent. This comes on top of the proposed postponement of the oil price increase, and last summer's reduction in the gasoline excise tax.
- The resulting lower rate of price increase, combined with the benefits to individuals from tax indexing, a higher tax deduction for employment expense and lower unemployment insurance premiums, should help to relieve pressures for large increases in incomes.
- Investment will be stimulated by the enriched investment tax credit and other changes in resource and R&D taxation.

Fiscal Position and Outlook

- Total financial requirements of the government in fiscal 1979-80, exclusive of foreign exchange transactions, are forecast at \$10,750 million. This would be down from the expected \$12,100 million this year. If account is taken of special factors relating to Canada Savings Bond interest, financial requirements would increase by about \$350 million.
- Budgetary and non-budgetary outlays in 1979-80 are forecast at \$52.6 billion, an increase of 8.9 per cent which would be well below the expected growth of GNP. Budgetary revenues are forecast at \$38.1 billion with a further \$3.7 billion available from non-budgetary transactions.

Effective Dates

Immediate

- Federal sales tax cut to 9 per cent from 12.
- Increased investment tax credit for qualifying property and R&D expenditures.
- Extension of investment tax credit to transportation equipment investments.
- Fast write-offs for costs incurred for the development of new mines.
- Depletion allowed for townsite and social asset investments for new mines.
- Amended treatment of income debentures and term preferred shares.

January 1, 1979

- Increase in the personal tax deduction for employment expense to a maximum \$500 from \$250.
- Indexing of personal income tax increases personal exemptions and widens tax brackets by 9 per cent.
- Reduction in unemployment insurance premiums.

Dates Extended

- Investment tax credit, due to expire June 30, 1980, extended indefinitely.
- Special incentive for multiple-unit residential buildings extended one year beyond January 1, 1979.
- Fast write-off for pollution control equipment, due to expire at the end of 1979, extended indefinitely.

For further information on the budget:
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