CANADA

Department of Finance
Ministère des Finances

HIGHLIGHTS
OF
THE BUDGET MEASURES
and
TAX REFORM LEGISLATION

June 18, 1971

TAX REFORM HIGHLIGHTS

Highlights of the tax reform legislation intended to come into effect in 1972:

Personal Income

* Basic exemptions increased: single, to $1,500 from $1,000; married, to $2,850 from $2,000.

* On wage or salary income, all married-status taxpayers pay less in 1972 than at present; single-status taxpayers pay less on employment income below $8,000.

* Initial 17-per-cent rate of federal tax will be reduced progressively to 6 per cent by 1976.

* Child care expenses deductible up to $500 per child under 14, maximum of $2,000 per family.

* Special exemption of $650 for individuals age 65 and over. Replaces exemption of $500 at age 70.

* Employment expenses deductible: 3 per cent of employment income up to $150 a year.

* Moving expenses deductible for taxpayers changing jobs.

* Employer-paid living expenses at distant work sites made tax-free.

* More items included in income.

* Calculation of tax simplified.

* Limits raised on contributions to pension plans and other retirement plans.
  Limit on total charitable donations raised to 20 per cent of income from 10 per cent.

* Two income-averaging plans available.

Capital Gains

* Half of capital gain taxable at taxpayer's personal rate.
  Half of capital loss deductible.

* Five-year revaluation dropped. Accrued capital gains taxed at death.

* Federal gift and estate taxes abolished on December 31, 1971.

* Taxpayer's home and one acre of land completely exempt from capital gains tax.

* Personal-use property exempt unless selling price is more than $1,000.

* Special rules for corporate reorganizations.

Corporations and Shareholders

* General tax rate for corporations is 50 per cent in 1972, declining one percentage point annually to 46 per cent in 1976.

* Tax rate of 25 per cent on first $50,000 of business income available to Canadian-controlled private corporations to assist growth.

* Dividend tax credit increased to 33 1/3 per cent and included in income.

* Dividends received by corporations generally tax-exempt. Refund of taxes available on investment income and taxable dividends of private corporations.

Mining and Petroleum

* Automatic percentage depletion continues to 1976, then replaced by earned depletion.

* Three-year tax exemption for new mines to be withdrawn after 1973, replaced by fast write-off.

* Federal tax on mining profits to be reduced to 25 per cent from 40 per cent in 1977 to allow for provincial mining taxes.

Business and Property Income

* Interest paid by corporations on money borrowed to buy shares in other corporations made deductible.

* Reasonable entertainment and convention expenses continue to be deductible, with geographical limitation on conventions.
  Club fees, costs of yachts, camps, lodges not deductible.

* Taxpayers in the professions will bring amounts into income as fees are billed.

International Income

* Tax treaty expansion to seek competitive tax treatment for Canadians investing abroad.

* Witholding tax on investment income paid to non-residents remains at 15 per cent until end of 1975, then increased to 25 per cent in non-treaty countries. Pensions subject to withholding tax after January 1, 1972 but all Old Age Security pensions and $1,290 of Canada and Quebec Pension Plan benefits exempt.

* Tax imposed on income diverted to tax havens.

Tax Reform Count

If the present system and rates of tax remained in effect in 1972, Canada would have about 9,000,000 taxpayers. Tax reform will give these results for them:

All personal income taxes eliminated for	1,000,000
Taxes reduced for	4,700,000
Taxes changed by less than 1 per cent for	2,000,000
Taxes increased for	1,300,000

1971 BUDGET MEASURES AND ECONOMIC REVIEW

To reinforce the expansion of the economy now underway, the budget proposes the following 1971 tax and tariff changes:

* Removal of the 3-per-cent surtax on personal and corporate income taxes effective July 1, 1971, at a cost of $130 million for the balance of the calendar year.

* Changes effective July 1 in lowest tax brackets to exempt taxpayers with less than $500 of taxable income.

* Exemption of Guaranteed Income Supplement from taxation retroactive to January 1, 1971.

* Low-bracket changes and GIS exemption end income taxes for more than 750,000 effective July 1.

* Removal of 12-per-cent sales tax on margarine, effective immediately, at a cost of $7 million in a full year.

* Removal of 12-per-cent sales tax on all anti-pollution equipment used in production, effective immediately, at a cost of around $8 million in a full year.

* Abolition immediately of 15-per-cent excise tax on television, radio and hi-fi sets, their components and other electronic equipment, at a full-year cost of about $40 million.

* Duty on petroleum feedstocks of 3/4 cent per gallon under British Preferential Tariff and 1 cent per gallon under Most-Favoured-Nation Tariff reduced to 1/3 cent per gallon to aid Canadian petrochemical industry.

* Increase in tariff on polyethylene resins from 7 1/2 to 10 per cent, with corresponding increases for further processed forms of these resins, to assist Canadian plastics industry.

* Duty-free entry of production machinery not available in Canada and considered to be in the public interest extended to cover sawmill and logging machinery for the benefit of the Canadian forest industry.

* Suspension for two-year period of 1/3 cent per gallon duty on heavy fuel oils to help offset recent substantial price increases incurred by pulp and paper producers and power utilities, the saving for the pulp and paper industry alone amounting to over $3.5 million.

Revenues, Expenditures and Cash Requirements

The budget deficit for 1970-71 was just under $420 million, representing a swing of $810 million from the surplus of approximately $390 million in 1969-70. Non-budgetary cash requirements rose by $550 million, with the result that total cash requirements for 1970-71 increased by $1,360 million over the previous year, not including funds required to finance foreign exchange transactions.

For 1971-72, budgetary revenues after tax changes are estimated at approximately $13,660 million and expenditures at $14,410 million, leaving a budget deficit of $750 million.

Net non-budgetary requirements are forecast at $1,680 million not including foreign exchange transactions, and total cash requirements for 1971-72 are estimated to be $2,430 million.

Economic Background to Budget

The Minister said his view of the advance of the economy in the second half of 1971 is even stronger than it was at the time of his budget last December. He said he expects that the gross national product for the balance of this year will be 9 per cent or more above the same period last year.

"The Canadian economy last autumn marked a turning point from declining to expanding rates of growth in demand, output and employment. I am confident that as we move on through the second half of 1971 and into 1972, the performance of the economy will be strong and gaining momentum."

Total domestic demand increased in the first quarter of 1971 at the very high annual rate of 8 per cent, boosted particularly by high levels of expenditures for housing and consumer durables and by all levels of government.

Business capital investment continued to be the weakest element in the economy. But the stage has been set for an upturn by the expansion underway in demand for goods and services, the removal of uncertainty associated with tax reform, and the improvement in profits during the first quarter of 1971.

Consumer spending on goods and services other than durables has been relatively sluggish to date in 1971. But high rates of personal savings, the ready availability of consumer credit and the growth of income produced by an expanding economy will all help to generate accelerating consumer expenditures.

More recent statistics confirm the accelerating expandion of the economy. Retail sales increased substantially in April. New orders received by manufacturers and shipments moved ahead vigorously in April following some hesitation in March. The value of non-residential building permits issued for the first four months of 1971 was up 5 1/2 per cent over the total for the same period last year. On a seasonally-adjusted basis, exports in May were up to 5 per cent over the previous month and 4.7 per cent over the very high level in May, 1970.

Canada had a record merchandise trade surplus of $3 billion during 1970 and this strong merchandise trade position was maintained during the first quarter of 1971 despite a rise in imports. The budget expressed concern about the appreciation of the value of the Canadian dollar that resulted from Canada's strong balance of payments position and welcomed the recent decline in the exchange rate.

Employment, which grew by 140,000 jobs last spring and summer, grew by 180,000 in the fall and winter. This increase was not sufficient to bring the unemployment rate down far enough.

Canada had a better price performance record than any other industrial nation in 1970. While the decline in food prices that occurred last year was partially reversed in the early months of 1971, the rate of increase in other consumer goods and services continued to moderate.

There has been some slowing down in the high rate of cost increases, which have also been offset to some extent by rising productivity.

Federal Financial Assistance to the Provinces

More than $4 billion of funds raised by the federal government during the current fiscal year will be made available to the provinces and municipalities to support their services. This represents 31 per cent of total federal budgetary resources, compared to less than 23 per cent five years ago. Over $1 billion will be paid to the provinces in the form of equalization grants during the current fiscal year, compared to the total of $370 million five years ago.

1971 Changes in Income Taxes

Withdrawal of surtaxes

The surtaxes of 3 per cent on personal and corporation income taxes will end July 1, 1971, six months ahead of their scheduled expiry. The revenue loss will total $90 million for the surtax on individuals and $40 million for the surtax on corporations.

The surtax on individuals is 3 per cent of basic tax in excess of $200. The surtax otherwise payable in 1971 will be cut in half by its withdrawal at mid-year.

GIS exemption

Payments under the Guaranteed Income Supplement may total up to $55 per month for single pensioners and up to $95 per month for husband and wife, depending on other income.

They are subject to tax if the total income of a pensioner including the GIS payments exceeds his exemptions and standard deductions.

Effective January 1, 1971, the payments will not be included in the taxable income of recipients. They will, however, be taken into account in determining the pensioner's income if he is claimed as a dependant and supported by another taxpayer.

Cost of the change is estimated at $10 million in 1971.

Low-bracket changes

Taxpayers with less than $500 of taxable income will be taken off the rolls effective July 1. This will be accomplished by reducing the 11-per-cent federal rate of tax on taxable income between $0 and $500. Rates on taxable income between $500 and

$3,000 will be adjusted so that the benefits of changes are effectively directed only to taxpayers with taxable incomes below $3,000.

In terms of deductions at source, these are the effects:

Taxable Income	Tax for First Half 1971	Tax for Second Half 1971
$ 500	$ 37	$ 0
$1,000	$ 75	$ 45
$1,500	$ 125	$105
$2,000	$ 175	$165
$3,000	$ 290	$290

These changes also required offsetting adjustments affecting two other provisions--the special $20 abatement and the social development tax.

The tax saving for the remainder of 1971 is estimated at $35 million.

1971 Sales and Excise Tax Changes

Margarine

The federal sales tax of 12 per cent will be removed from margarine effective budget night. Similar spreads sold under brand names will also become exempt. The tax represents an amount per pound of two to four cents, depending on the cost of the product. The removal reduces federal revenues by about $7 million on the basis of a full year. Canadians consumers buy about 180 million pounds of margarine a year. Industry submissions estimate that the average retail price of 39 cents a pound in Canada would be reduced to 35 cents as a result of removing the sales tax.

Pollution Equipment

The 12-per-cent sales tax will be removed effective budget night at an estimated cost of $8 million a year. Qualifying equipment will be all machinery and apparatus acquired by manufacturers or producers for use in the detection, prevention, removal or reduction of pollutants to water, soil or air. The amount spent by manufacturers and producers for pollution equipment is estimated at about $65 million and is increasing annually.

This change brings the treatment of such equipment into line with the exemption for machinery and equipment used directly in manufacture and production of goods.

Radios, record players, television sets, other electronic equipment

These household durables account for retail sales of several hundred million dollars annually in Canada. Whether Canadian-produced or imported, they are subject to a special excise tax of 15 per cent.

Elimination of the tax effective budget night is expected to provide a significant stimulus for sales. The prospects for consumers are considerably lower prices on many big-ticket purchases for their homes. The estimated saving is at least $40 million annually.

1971 Tariff Changes

The budget proposes changes in 45 tariff items, effective June 19, 1971. The most important changes set aside the duty on certain heavy fuel oils for a two-year period, establish a program for the duty-free entry of logging and sawmill machinery, and implement the recommendations of Tariff Board Report No. 141 on petroleum fractions for petrochemical manufacturing and Report No. 143 on polyethylene.

The net loss of tariff revenue from the changes is estimated at $5 million a year. Of this, about $4 million represents the abolition of the duty on heavy fuel oils.

Petroleum Fractions

Existing duties on petroleum fractions such as naphtha are 3/4 cent per gallon under the British Preferential Tariff and 1 cent per gallon under the Most-Favoured-Nation Tariff. Both are reduced to 1/3 cent per gallon.

These fractions are used as petrochemical feedstocks and represent an important cost in the manufacture of petrochemicals such as ethylene and methanol.

Canadian oil refiners produce most of the fractions used in Canada and the reduced duty will maintain adequate tariff protection for them while setting an upper limit on their prices. It should enable Canadian petrochemical producers to obtain supplies at prices more closely comparable to prices paid by their foreign competitors.

Polyethylene

The Tariff Board recommended that duties on polyethylene resin be increased to 10 per cent from 7 1/2 per cent with corresponding increases on moulding compounds to 12 1/2 per cent from 10 per cent and film and sheet to 17 1/2 per cent from 15 per cent, bringing the rates into line with duties on most other Canadian-made plastics and to the rates established in the Kennedy Round.

The changes will assist Canadian polyethylene producers to meet import competition. As noted by the board, Canadian polyethylene producers have been faced with declining prices, raw material costs which are higher than those for producers in other countries, and a significant change in the balance of trade on polyethylene resin.

Heavy Fuel Oils

The duty of 1/3-cent per gallon on heavy fuel oils is equivalent to 11.7 cents per barrel. Domestic production has not satisfied Canadian market requirements. Last year the output of Canadian refiners totalled about 85 million barrels and about 34 million barrels were imported. Prices have increased.

The pulp and paper industry, a large consumer, is alone expected to realize savings of over $3.5 million annually. The specified period for the change will permit the government to reassess the situation in light of developments.

Logging and Sawmill Machinery

The existing duty on this machinery is 12 1/2 per cent Most-Favoured-Nation. This rate applies to about $20 million of imports of logging and sawmill machinery. Such machinery will now be eligible for free entry when not available from production in Canada.

Other Changes

Most other amendments are of a clarifying or relieving nature. They provide for reductions on products such as a packaging material for fresh fruit, machines of a class or kind not made in Canada for tanning or embossing leather, machine card clothing for the textile industry, patterning devices or exercisers used to treat children suffering from cerebral palsy, certain musical instruments, and films, video tapes and sound recordings imported on a temporary basis for dubbing into another language. The provisions for free entry for works of art are broadened.

1971 Change in Withholding Tax on Short -Term Securities

The Income Tax Act imposes a 15-per-cent withholding tax on interest payments to non-residents. However, a non-resident can avoid payment if he sells a security before the date on which interest is actually payable, at a price that includes the interest accrued to the time of sale. An amendment to the act will require a resident purchasing a short-term security from a non-resident to withhold tax on such accrued interest.

In the case of short-term securities issued or sold to non-residents at a discount, the resident issuer or seller will be required to deduct withholding tax calculated on the difference between the sale or issue price and the amount payable for the security when it matures.

This change will apply only to securities issued after budget night. It will not apply to securities with maturities of five or more years, to securities prescribed as "public issue securities", or to securities now exempt from withholding tax.