Amendments to the Income Tax Act

Explanatory Notes

Issued by
The Honourable Paul Martin, P.C., M.P.
Minister of Finance

February 1994

Canada

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Department of Finance Canada
Ministère des Finances Canada

These explanatory notes are provided to assist in an understanding of amendments to the *Income Tax Act.* These notes are intended for information purposes only and should not be construed as an official interpretation of the provisions they describe.

Cette publication est également offerte en français.

PREFACE

The legislation to which these explanatory notes relate contains amendments to the *Income Tax Act*. These amendments are designed to implement the income tax measures put forth in the Economic and Fiscal Statement of December 2, 1992 and the Budget of April 26, 1993.

These explanatory notes describe amendments, clause by clause, for the assistance of Members of Parliament, taxpayers and their professional advisors.

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Minister of Finance

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Clauses 1 and 2

Small Business Development Bonds and Small Business Bonds

ITA
15.1 and 15.2

Sections 15.1 and 15.2 of the Act set out rules defining and governing the treatment of small business development bonds (SBDBs) and small business bonds (SBBs). SBDBs and SBBs are debt obligations on which any interest payable is not deductible to the issuer but is instead treated as a taxable dividend to the recipient.

The Act provides that these instruments may be issued only until the end of 1992. The amendments to the definition of "qualifying debt obligation" in sections 15.1 and 15.2 extend the period during which SBDBs and SBBs may be issued to December 31, 1994.

These amendments apply to obligations issued after 1992. A special transitional rule provides that the joint election generally required to be filed within 90 days of the issuance of an SBDB or SBB will be considered to have been filed within that time period if it is actually filed no more than 90 days following the date on which these amendments are enacted.

Clause 3

Deductions in Computing Income From Business or Property

ITA
20(1)(hh)(ii)

Paragraph 20(1)(hh) of the Act provides a deduction for the repayment by a taxpayer of an amount included in the taxpayer's income under paragraph 12(1)(x) as an inducement or assistance. It also provides for a deduction of the repayment of certain other inducements or assistance not included in the taxpayer's income under paragraph 12(1)(x) that relate to outlays or expenses, unless the related outlays or expenses were deductible under any of sections 66 to 66.4 (or would have been so deductible if the income-based limits on deductions under those sections were not taken into account).

Subparagraph 20(1)(hh)(ii) is amended to replace a reference to subparagraph 66.1(2)(a)(ii) with a reference to subsection 66.1(2). This amendment is consequential on the amendment to subsection 66.1(2) described in subclause 6(1), under which the income-based limit for the deduction of Canadian exploration expenses by a principal-business corporation is now provided under paragraph 66.1(2)(b) rather than under subparagraph 66.1(2)(a)(ii).

This amendment applies to taxation years ending after December 2, 1992.

Clause 4

Scientific Research and Experimental Development

ITA
37

Section 37 of the Act sets out the rules for the deductibility of expenditures incurred by a taxpayer for scientific research and experimental development (SR&ED) both inside and outside Canada. Subsection 37(1) allows a taxpayer carrying on business in Canada to deduct certain current and capital expenditures incurred in respect of SR&ED carried on in Canada. Subsection 37(2), on the other hand, provides for the deduction only of current expenditures incurred in respect of SR&ED carried on outside Canada. SR&ED expenditures incurred in Canada are pooled under subsection 37(1) and may be deducted in the year incurred or carried forward indefinitely. Current SR&ED expenditures incurred outside Canada are not pooled, but rather must be deducted in the year they are incurred.

Subclause 4(1)

ITA
37(1)(e)

Subsection 37(1) of the Act provides for the pooling of certain SR&ED expenses incurred in Canada by a taxpayer carrying on business in Canada. The size of the pool changes in accordance with any annual additions to and deductions from the pool. New SR&ED expenditures are added to the pool while investment tax credits earned in respect of qualifying SR&ED expenditures, and claimed in earlier years, are subtracted from the pool. Paragraph 37(1)(e) provides for this reduction of the SR&ED pool by amounts claimed in respect of investment tax credits. Paragraph 37(1)(e) is amended as a consequence of the introduction of a "prescribed proxy amount" in the definition of "qualified expenditure" in subsection 127(9). This amendment, which applies to taxation years ending after December 2, 1992, ensures that the SR&ED pool is similarly reduced by investment tax credits claimed in respect of a prescribed proxy amount.

Subclause 4(2)

ITA
37(8)(a)(ii)

Paragraph 37(8)(a) of the Act provides the interpretation of the expression "expenditures on or in respect of scientific research and experimental development" which is used in subsections 37(1), (2) and (5). Subparagraph 37(8)(a)(i) applies to subsection 37(2) for SR&ED expenditures incurred outside Canada.
Subparagraph 37(8)(a)(ii) applies to subsection 37(1) for SR&ED expenditures incurred in Canada.

Subparagraph 37(8)(a)(ii) of the Act provides that an expenditure will qualify as an SR&ED expenditure incurred in Canada, and accordingly, be included in the SR&ED pool under subsection 37(1), if the expenditure is incurred for SR&ED carried on in Canada and if it is all or substantially all attributable to the prosecution or to the provision of premises, facilities or equipment for the prosecution of SR&ED in Canada. Furthermore, an expenditure will so qualify if it is of a current nature and is directly attributable to the prosecution or to the provision of the above property for the prosecution of SR&ED activities. Subsections 2900(2) and (3) of the *Income Tax Regulations* (as proposed in a release by the Minister of Finance in June 1993) further define what expenditures are directly attributable to the prosecution and to the provision of premises, facilities and equipment for the prosecution of SR&ED in Canada.

The amendment to subparagraph 37(8)(a)(ii) of the Act, which applies to taxation years ending after December 2, 1992, has two purposes. First, it clarifies the intent of the phrase "all or substantially all" in former clause 37(8)(a)(ii)(A), which is now provided for in new subclauses 37(8)(a)(ii)(A)(I) and (III). Second, it provides an alternative method for determining which expenditures incurred in Canada will qualify as SR&ED and will therefore be included in the SR&ED pool in subsection 37(1). This alternative method is provided for in new clause 37(8)(a)(ii)(B) of the Act.

New subclauses 37(8)(a)(ii)(A)(I) and (II) of the Act provide that an expenditure of a current nature will be considered to be an SR&ED expenditure if it is directly attributable to, or if it is for and all or substantially all attributable to, the prosecution of, or the provision of premises, facilities or equipment for the prosecution of, SR&ED in Canada. Subsections 2900(2) and (3) of the Regulations (with proposed revisions) set out, for the purposes of subclause 37(8)(a)(ii)(A)(II), the expenditures that are directly attributable to the prosecution of, or the provision of premises, facilities or equipment for the prosecution of, SR&ED in Canada.

New subclause 37(8)(a)(ii)(A)(III) of the Act provides that an expenditure of a capital nature in respect of premises, facilities or equipment will be considered to be an SR&ED expenditure if it was intended that the premises, facilities or equipment would be used during all or substantially all of its operating time on SR&ED in Canada or that all or substantially all the value of the property would be consumed in the carrying out of SR&ED in Canada.

New clause 37(8)(a)(ii)(B) of the Act contains the new alternative method for determining SR&ED expenditures. It is anticipated that in many cases the alternative method will be simpler for taxpayers. The taxpayer has a choice of using either the current method or the alternative method. The taxpayer must elect in prescribed form for each taxation year the alternative method is being used; otherwise the current method will apply automatically. If the taxpayer elects the alternative method, the following expenditures will be considered to be for SR&ED carried on in Canada and therefore included in the taxpayer's SR&ED pool under subsection 37(1) of the Act:

(1) an expenditure of a current nature (generally a lease expense) that was for and all or substantially all attributable to the use of premises, facilities or equipment for the prosecution of SR&ED in Canada, unless the expenditure was for general purpose office equipment or furniture. An expenditure for leasing general purpose office equipment or furniture used for the prosecution of SR&ED in Canada is not included in the subsection 37(1) SR&ED pool, but is accounted for in the prescribed proxy amount under the new definition of "qualified

expenditure" in subsection 127(9) of the Act. The prescribed proxy amount is eligible for investment tax credits;

(2) an expenditure in respect of SR&ED undertaken in Canada on behalf of the taxpayer;

(3) an expenditure of a capital nature that was for, and all or substantially all attributable to, the provision of premises, facilities or equipment (other than general purpose office equipment or furniture) where it was intended that the premises, facilities or equipment would be used during all or substantially all of its operating time on SR&ED in Canada;

(4) an expenditure of a capital nature that was for, and all or substantially all attributable to, the provision of premises, facilities or equipment (other than general purpose office equipment or furniture) where it was intended that all or substantially all of the value of the premises, facilities or equipment would be consumed in the prosecution of SR&ED in Canada;

(5) the portion of an expenditure incurred in respect of salary or wages of an employee directly engaged in SR&ED in Canada that can reasonably be considered to relate to such work having regard to the time spent by the employee in carrying out the SR&ED, and, for these purposes, in certain cases the time spent by an employee directly engaged in the management of scientific and technical aspects of SR&ED will be considered to be time spent by the employee directly engaged in SR&ED and the portion of the expenditure will be the whole amount of the expenditure if the time spent by the employee directly engaged in SR&ED is all or substantially all of the employee's working time;

(6) an expenditure made for materials consumed in the prosecution of SR&ED in Canada; and

(7) one-half of an expenditure of a current nature that was for the lease of equipment used primarily for SR&ED in Canada, other than an expenditure in respect of general purpose office furniture and equipment or an expenditure included in (1) above. An expenditure for leasing general purpose office equipment or furniture used for the prosecution of SR&ED in Canada is not included in the subsection 37(1) SR&ED pool,

but is accounted for in the prescribed proxy amount under the new definition of "qualified expenditure" in subsection 127(9) of the Act. The prescribed proxy amount is eligible for investment tax credits.

The elective method for determining SR&ED expenditures in new clause 37(8)(a)(ii)(B) does not account for expenditures of a general overhead nature even if they are directly attributable to the prosecution or the provision of premises for the prosecution of SR&ED in Canada. Tax recognition for expenditures of this type is provided by way of the "prescribed proxy amount" in the new definition of "qualified expenditure" in subsection 127(9) of the Act. Prescribed proxy amount is defined in proposed new subsection 2900(4) of the *Income Tax Regulations* (released by the Minister of Finance in June 1993).

The prescribed proxy amount is a substitute for the item-by-item accounting and apportioning of certain expenditures that could otherwise be considered directly attributable to SR&ED carried on in Canada. This elective method should be particularly attractive to taxpayers carrying on a diversified business including SR&ED. The proxy amount is relevant only for the purposes of calculating investment tax credits in respect of that amount. The proxy amount does not form part of the subsection 37(1) SR&ED expenditure pool nor do any of the expenditures for which it is a substitute form part of the pool. Investment tax credits earned in respect of the prescribed proxy amount and claimed by the taxpayer do, however, reduce the SR&ED expenditure pool. Prescribed proxy amount investment tax credits claimed in earlier years must be credited to the pool in the year under paragraph 37(1)(e) of the Act in the same manner as are other SR&ED investment tax credits. Those substituted expenditures, which would be included in the pool but for the proxy, need not be specifically identified as SR&ED expenditures, but rather will be treated as ordinary expenses and thus generally either deductible in the year incurred or eligible for capital cost allowance.

Proposed new subsection 2900(4) of the *Income Tax Regulations* establishes the proxy amount as 65% of that portion of salaries of employees directly engaged in SR&ED in Canada that relates to that work. In the case of a specified employee, proposed new subsection 2900(5) of the Regulations provides that the amount of salaries and wages of the employee taken into account in calculating the proxy amount shall not exceed the lesser of ¾ of the employee's full salary and 2.5 times the Year's Maximum Pensionable Earnings as defined in section 18 of the *Canada Pension Plan*. The Year's Maximum Pensionable Earnings for 1994 are $34,400. Subsection 248(1) of the Act is being amended in this Bill to define a "specified employee" of a person as an employee who is a specified shareholder of the person or who does not deal at arm's length with the person. A specified shareholder of a corporation is defined in subsection 248(1) as a person who owns 10% or more of any class of shares of the corporation.

In determining the portion of any employee's salary that relates to SR&ED, a reasonable allocation must be made of the time spent by the employee in the execution of SR&ED activities. The time spent by an employee, such as a supervisor or a manager, directing the course of ongoing SR&ED activities will generally be considered, for these purposes, to be time in which the employee was directly engaged in SR&ED. Consequently, this time may be included in determining the portion of the employee's salary to be taken into account in calculating the proxy amount. Where all or substantially all of an employee's time is spent on SR&ED in Canada, the whole amount of the employee's salary will be included in determining the base for the proxy amount.

The prescribed proxy amount for a taxation year cannot exceed the total amount that would otherwise be deductible by the taxpayer for the year in the absence of special rules.

For the purposes of the refundable investment tax credit in section 127.1 of the Act, credits earned in respect of the prescribed proxy amount will be treated in the same manner as credits earned in respect of expenditures of a current nature.

Subclause 4(3)

ITA
37(8)(d)(ii)

Paragraph 37(8)(d) of the Act sets out expenditures that do not qualify as expenditures incurred for scientific research and experimental development. For example, any capital expenditure or rental expenditure made for a building other than a prescribed special-purpose building will not qualify for SR&ED treatment. Subparagraph 37(8)(d)(ii) is amended, effective for taxation years ending after December 2, 1992, to clarify that any outlay or expense made or incurred for the use of, or the right to use, a building other than a prescribed special-purpose building does not qualify for SR&ED treatment.

Subclause 4(4)

ITA
37(9) and (10)

New subsection 37(9) of the Act provides that, for the purposes of new clauses 37(8)(a)(ii)(A) and (B) of the Act, salary or wages does not include remuneration based on profits nor a bonus, where the remuneration or bonus is for a specified employee of the taxpayer. Subsection 248(1) of the Act is amended to include a definition of the expression "specified employee" of a person. A specified employee of a person is an employee who does not deal at arm's length with the person or who is a specified shareholder of the person. In subsection 248(1), a specified shareholder of a corporation is generally defined as a person who owns 10% or more of any class of shares of the corporation.

Under new subsection 37(10), an election under clause 37(8)(a)(ii)(B) must be filed with the taxpayer's return of income for the year under Part I of the Act.

New subsections 37(9) and (10) apply to taxation years ending after December 2, 1992.

Clause 5

Resource Properties

ITA
66

Section 66 of the Act provides rules relating to Canadian and foreign resource properties.

Subclauses 5(1) and (2)

ITA
66(10.1)

Subsection 66(10.1) of the Act allows a joint exploration corporation to renounce a Canadian exploration expense in favour of a shareholder corporation. The amount that can be renounced in a taxation year excludes Canadian exploration expenses deductible in computing income for any preceding taxation year. The amount renounced by a joint exploration corporation is treated as if it were deducted or deductible by that corporation for the purposes of computing its cumulative Canadian exploration expense.

Paragraph 66(10.1)(a) is amended so that, for Canadian exploration expenses incurred in taxation years ending after December 2, 1992, the above exclusion applies only to expenses actually deducted under subsection 66.1(2).

Paragraph 66(10.1)(d) is amended to ensure that, for Canadian exploration expenses incurred in taxation years ending after December 2, 1992, the amount renounced by a joint exploration corporation under subsection 66(10.1) is treated by the corporation as if it were actually deducted by that corporation for the purposes of computing its cumulative Canadian exploration expense.

These amendments are strictly consequential on the amendment to subsection 66.1(2) which is described in subclause 6(1) of these notes.

Subclauses 5(3), (4), (6), (7), (8) and (9)

ITA
66(12.6), (12.62) and (12.64)

Subsections 66(12.6), (12.62) and (12.64) of the Act permit a principal-business corporation to renounce Canadian exploration expenses (CEE), Canadian development expenses (CDE) and Canadian oil and gas property expenses (COGPE) that it incurs to a person who acquires flow-through shares issued by it. Among the conditions which must be met under these provisions are:

- the CEE, CDE or COGPE must be incurred by the corporation on or after the day, and within 24 months from the end of the month that includes the day, the agreement to acquire the shares was entered into;

- the renunciation must be made no later than 30 days after the end of the 24-month period referred to above; and

- the total renounced amounts of CEE, CDE and COGPE in respect of a flow-through share cannot exceed the consideration for the share.

Subsections 66(12.6), (12.62) and (12.64) are amended to extend the time in which the renunciation must be made. The amendments allow a renouncing corporation to renounce expenses before March of the first calendar year commencing after the end of the 24-month period referred to above. They apply to expenses incurred after February 1986, at which time subsections 66(12.6), (12.62) and (12.64) became effective.

Paragraphs 66(12.6)(d), (12.62)(d) and (12.64)(c) are amended to make reference to new subsection 66(12.601), which permits the renunciation of a corporation's CDE. This ensures that the third condition described above applies to CDE renounced under the new subsection. These amendments apply in respect of expenses incurred after December 2, 1992.

Paragraph 66(12.62)(c) is amended to ensure that the same CDE cannot be renounced under both subsection 66(12.601) and 66(12.62). This amendment applies in respect of expenses incurred after December 2, 1992.

Subclause 5(5)

ITA
66(12.601), (12.602) and (12.61)

New subsections 66(12.601) and (12.602) of the Act permit a principal-business corporation to renounce specified CDE that it incurs to a person who acquires flow-through shares issued by the corporation. Where an amount is renounced by a corporation to a person under subsection 66(12.601), amended subsection 66(12.61) provides that the person is deemed, on the effective date of the renunciation, to have incurred CEE (rather than CDE) equal to the amount of specified CDE renounced. Except for the purposes of the renunciation, the corporation is deemed never to have incurred the specified CDE.

The conditions for renouncing specified CDE under subsection 66(12.601) are the same as renouncing CDE under amended subsection 66(12.62) with the following exceptions:

- the CDE must have been incurred by the renouncing corporation after December 2, 1992;

- the renouncing corporation (and corporations associated with the renouncing corporation) cannot collectively renounce under subsection 66(12.601) more than $2 million of CDE incurred in a calendar year; and

- there are new restrictions described in the commentary to subsections 66(12.67) and (12.671).

Specified CDE is CDE described in paragraph (a) or (b) of the definition of "Canadian development expense" in subsection 66.2(5), which relate to the development of oil and gas properties. Specified CDE also includes a corporation's share of such expenses incurred by a partnership and thereby included in the corporation's CDE under paragraph (f) of that definition.

With the exception of the amendments to subsections 66(12.66), (12.67) and (12.75) and the introduction of subsections 66(12.671) and (12.741), the changes described below are strictly consequential on the introduction of new subsection 66(12.601). In addition, it is intended to make any necessary consequential changes to the *Income Tax Regulations* to reflect the new renunciation mechanism. (In particular, it is intended to make references to new subsection 66(12.601) in section 228 and subsection 1206(4.2) of the Regulations.)

These subsections apply with respect to expenses incurred after December 2, 1992.

Subclause 5(10)

ITA
66(12.66)

Subsection 66(12.6) of the Act permits a principal-business corporation to renounce CEE to a flow-through shareholder. A corporation may only renounce CEE incurred by it on or before the effective date of the renunciation. For this purpose, where a number of stated conditions are met, subsection 66(12.66) deems specified CEE incurred in the first 60 days of a calendar year to have been incurred by the corporation at the end of the preceding calendar year.

Subsection 66(12.66) is amended so that the same rule applies, for the purposes of new subsection 66(12.601), with respect to specified CDE. For this purpose, specified CDE is CDE related to oil and gas development that is described in paragraph (a) or (b) of the definition of "Canadian development expense" in subsection 66.2(5).

This amendment applies with respect to expenses incurred after 1992.

Subclause 5(11)

ITA
66(12.67)

Subsection 66(12.67) of the Act is a rule that restricts the resource expenses that may be renounced under subsections 66(12.6), (12.62) and (12.64). The rule provides that a corporation may not, under those subsections, renounce resource expenses renounced to it under those subsections unless it was related to the corporation that renounced those expenses to it.

Subsection 66(12.67) is amended so that the existing rule also applies in respect of renunciations under new subsection 66(12.601). The amended version of the existing rule is contained in new paragraph 66(12.67)(a).

Paragraph 66(12.67)(b) is introduced so that a corporation cannot, under new subsection 66(12.601), renounce any amount to a trust, another corporation or a partnership if the renouncing corporation has a "prohibited relationship" with the trust, other corporation or partnership. "Prohibited relationships" are defined in new subsection 66(12.671), which is discussed below. An exception to this rule permits a renunciation under subsection 66(12.601) to a related corporation which renounces the same amount under subsection 66(12.6), in accordance with new paragraph 66(12.67)(d).

Paragraph 66(12.67)(c) is introduced so that a corporation cannot, under new subsection 66(12.601), renounce any CDE deemed to have been incurred by it because of a renunciation under subsection 66(12.62). This amendment is intended to ensure that the $2 million annual limit in respect of renunciations under subsection 66(12.601) is not avoided by virtue of renunciations between related corporations.

Paragraph 66(12.67)(d) is introduced so that a corporation cannot, under subsection 66(12.6), renounce any amount to a trust, another corporation or a partnership if the renouncing corporation has a "prohibited relationship" with the trust, other corporation or partnership. This paragraph applies only to CEE that is deemed to have been incurred by the renouncing corporation by virtue of a renunciation under new subsection 66(12.601) and that is not ultimately renounced by another corporation under subsection 66(12.6) to an individual or to a trust, corporation or partnership with which that other corporation does not have a prohibited relationship. The meaning of "prohibited relationship" is discussed below. This amendment is intended to ensure that the requirements under new paragraph 66(12.67)(b) cannot be avoided by virtue of renunciations between related corporations.

These amendments apply with respect to expenses incurred after December 2, 1992.

ITA
66(12.671)

New subsection 66(12.671) defines the expression "prohibited relationship" for the purposes of amended subsection 66(12.67). Subsection 66(12.67) applies where a trust, corporation or partnership has given consideration under an agreement for the issue of a flow-through share by a particular corporation.

In these circumstances, the particular corporation has a "prohibited relationship" with a shareholder trust if, at any time after the agreement was entered into and before the flow-through share was issued, the particular corporation (or a corporation related to the particular corporation) is beneficially interested in the shareholder trust. (Under subsection 248(25) of the Act, a person is "beneficially interested" in a trust if the person has any direct or indirect interest in the income or capital of the trust.)

The particular corporation has a "prohibited relationship" with the shareholder corporation if, immediately before the agreement was entered into, the shareholder corporation was related to the particular corporation.

The particular corporation has a prohibited relationship with the shareholder partnership if any part of the amount renounced is allocated through one or more tiers of partnership to the particular corporation or to another corporation in respect of which a specified condition is satisfied. This condition is that, at any time after the agreement was entered into and before the allocated amount would otherwise be considered to be incurred by it, the other corporation was (disregarding flow-though shares issued pursuant to the agreement and subsequent agreements) related to the particular corporation.

New subsection 66(12.671) applies in respect of expenses incurred after December 2, 1992.

Subclause 5(12)

ITA
66(12.69)

Subsection 66(12.69) of the Act requires that a partnership file an information return reporting allocations to its partners of amounts renounced to it under subsections 66(12.6), (12.62) and (12.64).

Subsection 66(12.69) is amended to apply the same rule with respect to renunciations under new subsection 66(12.601).

This amendment applies in respect of expenses incurred after December 2, 1992.

Subclause 5(13)

ITA
66(12.7)

Subsection 66(12.7) of the Act requires that a corporation file a prescribed form in respect of resource expenditures renounced by the corporation under subsections 66(12.6), (12.62) and (12.64). Subsection 66(12.7) is amended to apply the same rule with respect to renunciations under new subsection 66(12.601).

This amendment applies with respect to renunciations after December 2, 1992.

Subclause 5(14)

ITA
66(12.71)

Subsection 66(12.71) of the Act provides that a corporation may renounce an amount under subsection 66(12.6), (12.62) or (12.64) in respect of CEE, CDE or COGPE only to the extent that the corporation would otherwise have been able to claim a deduction in respect of the CEE, CDE or COGPE.

Subsection 66(12.71) is amended to apply the same rule with respect to renunciations under new subsection 66(12.601).

This amendment applies with respect to renunciations after December 2, 1992.

ITA
66(12.72)

Subsection 66(12.72) of the Act permits the Minister of National Revenue to verify or ascertain information pertaining to Canadian resource expenses renounced by a corporation under subsection 66(12.6), (12.62) and (12.64), as well as information pertaining to assistance in respect of such expenses.

Subsection 66(12.72) is amended to apply the same rule with respect to renunciations under new subsection 66(12.601).

This amendment applies after December 2, 1992.

ITA
66(12.73)

Subsection 66(12.73) of the Act provides that, where a corporation renounces amounts under subsection 66(12.6), (12.62) or (12.64) to one or more persons in excess of the amount the corporation was entitled to renounce, the corporation shall reduce the amount so renounced and shall file a statement with the Minister indicating the adjustments made.

Subsection 66(12.73) is amended to apply the same rule with respect to renunciations under new subsection 66(12.601).

This amendment applies with respect to renunciations made after December 2, 1992.

Subclauses 5(15), (16) and (17)

ITA
66(12.741) and (12.75)

Amended subsections 66(12.6), (12.62) and (12.64) (as well as new subsection 66(12.601)) generally provide for the renunciation, to a holder of a flow-through share, of resource expenditures incurred in the 24-month period following the first month ending after the date on which the agreement to issue the share is entered into. As discussed in the commentary above, the deadline for the renunciation is now the last day of February of the first calendar year commencing after the end of that period.

New subsection 66(12.741) allows a renouncing corporation to make a late renunciation, provided a penalty set out in amended subsection 66(12.75) is paid not more than 90 days following the late renunciation. The Minister of National Revenue must be satisfied that it is just and equitable to allow the late renunciation, unless the late renunciation is made not more than 90 days after the February deadline referred to above. Where a late renunciation is made, it is deemed for most purposes as having been made on the date of the February deadline. However, in order to avoid circularity and not provide an additional penalty for a corporation which files a prescribed form in respect of the late renunciation with the Minister before the end of the first month following the actual time of the late renunciation, the deeming rule does not apply for the purposes of subsections 66(12.7), (12.741) or (12.75).

Amended subsection 66(12.75) sets out the penalty in respect of a late renunciation under new subsection 66(12.741). The penalty in respect of a late renunciation is equal to the lesser of $15,000 and the greater of

- $100, and
- ¼ of 1% of the amount of the late renunciation.

This penalty is consistent with the penalties already provided in subsection 66(12.75) with respect to late filing of documents in connection with flow-through shares.

These amendments apply with respect to late renunciations made after February 1993.

Subclause 5(18)

ITA
66(15)

The definition of "flow-through share," for the purposes of sections 66 to 66.2, 66.4 and 66.7 of the Act, is provided in subsection 66(15). Expenses incurred pursuant to an agreement to issue flow-through shares are currently required to be renounced not more than 30 days after the 24-month period that commences at the beginning of the month following the date on which the agreement was entered into.

The definition is amended so that expenses may be renounced up to March of the first calendar year commencing after the 24-month period described above.

This amendment applies to shares issued pursuant to agreements entered into after February 1986.

Subclause 5(19)

ITA
66(19)

Subsection 66(19) of the Act is an "anti-warehousing" rule which applies for the purposes of renunciations under subsections 66(12.6), (12.62) and (12.64). In general terms, the rule requires a corporation which proposes to renounce an amount under those subsections to examine whether it would have been able to renounce the amount if amounts renounced to it by another corporation and its share of partnership expenses had been considered to have been incurred by it at the time the other corporation or the partnership incurred the renounced amount. This is intended to prevent a corporation from renouncing expenses that were originally incurred before the corporation had entered into a flow-through share agreement.

Subsection 66(19) is amended so that the same rule applies for the purposes of a renunciation under new subsection 66(12.601). This amendment applies to renunciations of outlays or expenses incurred after December 2, 1992.

Clause 6

Canadian Exploration Expenses

ITA
66.1

Section 66.1 of the Act provides rules relating to the deduction of Canadian exploration expenses.

Subclause 6(1)

ITA
66.1(2)

Subsection 66.1(2) of the Act provides a deduction with respect to Canadian exploration expenses incurred by a principal-business corporation. Under paragraph 66.1(2)(a), the amount required to be deducted by a corporation for a taxation year in this respect is equal to the lesser of the corporation's cumulative Canadian exploration expenses (CCEE) at the end of the year and the following amount:

- the corporation's income for the year, determined without reference to subsection 66.1(2) and depletion deductions (other than a depletion deduction claimed under section 1202 of the *Income Tax Regulations*) for the year,

- **minus** deductions allowed with respect to dividends under sections 112 and 113 of the Act to the corporation for the year.

Under paragraph 66.1(2)(b), a corporation may choose to deduct a further amount of its CCEE.

Subsection 66.1(2) is amended so that a corporation is no longer required to deduct any portion of its CCEE under subsection 66.1(2). However, the maximum CCEE that may be claimed by a corporation for a taxation year under subsection 66.1(2) is not affected by this amendment.

This amendment applies to taxation years ending after December 2, 1992.

Subclause 6(2)

ITA
66.1(6)

The description of F, in the formula in the definition of "cumulative Canadian exploration expense" in subsection 66.1(6) of the Act, provides that amounts deducted or deductible under subsection 66.1(2) by a taxpayer are deducted in computing a taxpayer's CCEE.

This description is amended so that, for expenses incurred in taxation years ending after December 2, 1992, only amounts actually deducted by a taxpayer are relevant for this purpose. This amendment is strictly consequential on the amendment to subsection 66.1(2) which is described above.

Subclause 6(3)

ITA
66.1(6)

Under subsection 66.1(9) of the Act, certain amounts of a taxpayer's CDE incurred in a taxation year may be re-classified as CEE in a subsequent taxation year. The subsection does not apply to "restricted expenses", as defined in subsection 66.1(6). "Restricted expenses" include CDE renounced by a taxpayer under subsection 66(12.62).

The definition is amended so that "restricted expenses" also include CDE renounced by a taxpayer under new subsection 66(12.601).

This amendment applies to expenses incurred after December 2, 1992.

Clause 7

Flow-Through Shares

ITA
66.3(4)(a)(ii)(B)

Subsection 66.3(4) of the Act provides rules for computing the paid-up capital of a corporation that issues flow-through shares. Paragraph 66.3(4)(a) requires a reduction in a corporation's paid-up capital in connection with the issue of a flow-through share equal to the amount, if any, by which

- the increase in the paid-up capital, otherwise determined, as a result of the issue of the share

exceeds

- the consideration received for the share **minus** 50% of amounts renounced under subsections 66(12.6), (12.62) or (12.64) in respect of the share.

Paragraph 66.3(4)(a) is amended so that amounts renounced under subsection 66(12.601) have the same effect on the computation of a corporation's paid-up capital.

This amendment applies after December 2, 1992.

Clause 8

Successor Rules

ITA
66.7

Section 66.7 of the Act provides rules relating to the deduction, by a "successor corporation", of unused resource expenses of another person in respect of resource properties acquired by the successor corporation.

Subclause 8(1)

ITA
66.7(3)(a)(iii)

Subsection 66.7(3) of the Act provides successor deductions for corporations in respect of Canadian exploration expenses (CEE) incurred by other taxpayers that were not deducted or deductible by those taxpayers.

Subparagraph 66.7(3)(a)(iii) is amended so that, for expenses incurred in taxation years ending after December 2, 1992, only amounts actually deducted by a taxpayer are relevant for this purpose. This amendment is strictly consequential on the amendment to subsection 66.1(2) which is described in subclause 6(1) of these notes.

Subclause 8(2)

ITA
66.7(10)

Subsection 66.7(10) of the Act provides a number of rules which generally apply when a corporation undergoes a change of control or ceases to be exempt from tax under Part I. Essentially, resource expenditures incurred by a corporation before that time are considered not to have been incurred by the corporation and instead are deemed, for the purposes of the successor rules, to have been incurred by an original owner. As a consequence, deductions by the corporation in respect of such expenditures may generally only be claimed against "streamed income" in connection with properties owned by the corporation before that time. Subsection 66.7(10) does not, however, apply for the purposes of determining a corporation's entitlement to renounce an amount under subsection 66(12.6), (12.62) or (12.64).

Subsection 66.7(10) is amended so that it also does not apply for the purposes of determining a corporation's entitlement to renounce an amount under new subsection 66(12.601).

This amendment applies to taxation years ending after December 2, 1992.

Subclause 8(3)

ITA
66.7(12)(b.1) and (b.2)

Paragraphs 66.7(12)(b.1) and (b.2) of the Act specify the amount of CEE incurred by an original owner that is available for deduction under subsection 66.7(3) by a successor. The amount excludes amounts deducted or deductible by an original owner.

The paragraphs are amended so that, for expenses incurred in taxation years ending after December 2, 1992, only amounts actually deducted by an original owner are relevant for this purpose. This amendment is strictly consequential on the amendment to subsection 66.1(2) which is described above.

Clause 9

Amalgamations

ITA
87

Section 87 of the Act provides rules that apply on the amalgamation of two or more taxable Canadian corporations.

Subclause 9(1)

ITA
87(2)

New paragraph 87(2)(mm) of the Act is consequential on the introduction of the UI premium tax credit contained in new subsection 126.1 of the Act. It will ensure that an amalgamated corporation will be treated as a continuation of, and the same corporation as, each of its predecessor corporations for the purposes of the provisions relating to the UI premium tax credit. Thus, for example, UI premiums payable by a predecessor corporation will be treated as if they were payable by the amalgamated corporation in determining that corporation's entitlement to the new credit. The provisions of paragraph 87(2)(mm) also apply, by virtue of paragraph 88(1)(e.2), to provide continuity where a corporation is wound up in a winding-up to which subsection 88(1) applies. New paragraph 87(2)(mm) applies to amalgamations occurring and windings-up commencing after 1991.

Subclause 9(2)

ITA
87(4.4)

Subsection 87(4.4) of the Act applies where a corporation that has entered into a flow-through share arrangement with a person amalgamates with another corporation. The rules in subsection 87(4.4) generally enable the corporation formed as a consequence of the amalgamation to renounce expenses incurred after the amalgamation to the person.

Subsection 87(4.4) of the Act is amended so that the same rules apply in respect of a renunciation under new subsection 66(12.601).

This amendment applies with respect to amalgamations occurring after December 2, 1992.

Clause 10

Windings-up

ITA
88(1)(e.3)

Paragraph 88(1)(e.3) of the Act provides for the flow-through of investment tax credits from a subsidiary corporation to a parent corporation on a winding-up of the subsidiary. Paragraph 88(1)(e.3) is amended to ensure that, for the purposes of the new definition of first term shared-use-equipment and second term shared-use-equipment in subsection 127(9) of the Act, the parent will be treated as the same corporation as the subsidiary. Consequently, the time periods stipulated in respect of first term shared-use-equipment and second term shared-use-equipment will not be severed as a result of a subsection 88(1) winding-up. Paragraph 87(2)(qq) of the Act addresses this issue in the case of a section 87 amalgamation.

Clause 11

Partnership Elections

ITA
96(3)

Subsection 96(3) of the Act provides rules that apply where a member of a partnership makes an election under certain provisions of the Act for a purpose that is relevant to the computation of the member's income from the partnership. In such a case, the election will be valid only if it is made on behalf of all of the members of the partnership and the member had authority to act for the partnership. This subsection is amended to include elections made under new clause 37(8)(a)(ii)(B) in respect of the new alternative method for determining scientific research and experimental development expenditures.

This amendment applies to fiscal periods that end after December 2, 1992.

Clause 12

Trusts and Their Beneficiaries

ITA
104(23)

Paragraph 104(23)(e) of the Act provides that instead of making quarterly instalment payments a testamentary trust must pay its tax owing for a taxation year within 90 days after the end of that year. Paragraph 104(23)(e) is amended, for the 1994 and subsequent taxation years, to exempt a testamentary trust, the chief source of income of which is farming or fishing, from the requirement to make a December instalment payment.

Clause 13

Capital Gains Exemption

ITA
110.6(1)

"investment expense"

The definition "investment expense" in subsection 110.6(1) of the Act applies for the purposes of determining an individual's "cumulative net investment loss". An increase in an individual's "investment expenses" can result in an increase in an individual's cumulative net investment loss and a consequential decrease in the individual's entitlement to the capital gains exemption under section 110.6. An individual's "investment expense" for a taxation year includes, under paragraph (d) of the definition, 50% of amounts deducted by the individual for the year in respect of resource expenses renounced to the individual under subsection 66(12.6), (12.62) or (12.64).

Paragraph (d) of the definition is amended so that the rule therein also applies in respect of resource expenses renounced under new subsection 66(12.601).

This amendment applies to the 1992 and subsequent taxation years.

Clause 14

UI Premium Tax Credit

ITA
126.1

New section 126.1 of the Act provides certain employers with a refundable tax credit of up to $30,000 to offset the increase in the employer's portion of 1993 unemployment insurance (UI) premiums. The tax credit (described in subsection 126.1(6) as an overpayment on account of an employer's liability under Part I of the Act equal to the employer's "UI premium tax credit") is based on the increase in the employer portion of the unemployment insurance premiums payable in respect of qualifying employees (referred to in the legislation as "qualifying employer premiums") for 1993 over the qualifying employer premiums for 1992.

Subject to certain limits and the rules pertaining to associated employers, where the total of the qualifying employer premiums of an employer for 1993 (the "1993 premium base") exceeds the total of the employer's qualifying employer premiums for 1992 (the "1992 premium base"), the employer will be eligible for a refundable tax credit equal to the excess.

The tax credit is intended to benefit primarily small businesses and is limited to a maximum credit of $30,000 per employer. Generally, the maximum potential tax credit of $30,000 is available to any employer or group of associated employers whose 1992 premium base does not exceed $30,000. Where the 1992 premium base exceeds $30,000, the maximum tax credit of $30,000 will be reduced by the amount of the excess. For example, if an employer's 1992 premium base is $42,000, the maximum potential tax credit of the employer will be $18,000.

In order to ensure that the tax credit benefits small businesses, where two or more employers are associated at the end of 1993, both the maximum tax credit and the increase in qualifying employer premiums of the members of the group will be calculated on a group basis. Thus, the maximum credit of $30,000 must be shared by members of an associated group and, where the combined 1992 premium base of the group exceeds $30,000, the maximum credit available to the group will be reduced by the amount of the excess. Associated employers will be required to file an agreement in prescribed form with Revenue Canada in order to allocate among them the tax credit available to them on a group basis. Reference may be made to the commentary on new subsections 126.1(9) to (11).

In determining whether employers are associated with each other at any time,

a) employers that are corporations that are associated with each other at that time for other income tax purposes will be considered to be associated at that time under the UI premium tax credit rules,

b) an employer who is an individual will be treated as a corporation all the voting shares of which are owned at that time by the individual, and

c) an employer that is a partnership will be treated as a corporation all the voting shares of which are owned at that time by the members of the partnership pro rata in the same proportion that the income or loss of the partnership is shared by them.

Reference may be made to the commentary on subsections 126.1(2) and (3).

The tax credit which, as indicated above, is generally based on the difference between the 1993 premium base and the 1992 premium base of an employer, arises on the earlier of March 1, 1994 and the day on which the employer files a prescribed form with Revenue Canada. It is contemplated that the prescribed form will be filed along with the employer's T4 Summary for 1993. Revenue Canada will be required by new subsection 164(1.6) to refund the tax credit with all due dispatch. However, an employer may obtain the benefit of the anticipated tax credit earlier by remitting from time to time in 1993 less than the full amount of the employer UI premiums then due. Where an employer does this, an amount will be deemed to be paid to the employer on account of the anticipated tax credit (referred to in these notes as a "prepayment" of the credit) and such amount will be treated as having been remitted by the employer to the Receiver General on account of the employer's UI premiums then due. Reference may be made to the commentary on subsections 126.1(12) and (13).

If an employer has received prepayments in excess of the tax credit to which the employer is ultimately entitled, the employer will be required to repay the excess on or before the employer's last UI premium remittance date for 1993. This might occur, for example, where an employer receives prepayments in early 1993 based on increased UI premiums and the 1993 UI premiums decrease below their 1992 levels during the latter part of 1993, such that the overall increase in UI premiums for the year is less than the prepayments received. Reference may be made to the commentary on subsections 126.1(14) and (15).

The new tax credit is available to both incorporated and unincorporated employers. Where the employer is a partnership, the credit (and any prepayments thereof) will be computed at the partnership level, and taxpayers holding interests in the partnership will be entitled to that portion of the credit (or prepayment) computed at the partnership level that can reasonably be considered to be their share thereof.

The rules for the UI premium tax credit in new section 126.1 do not affect, and are not affected by, the employee's portion of unemployment insurance premiums, which the employer is still required to withhold and remit.

Section 126.1 comes into force on January 1, 1993.

ITA
126.1(1)

New subsection 126.1(1) of the Act sets out a number of definitions that are relevant for the purposes of the rules relating the UI premium tax credit in section 126.1.

The "1992 cumulative premium base" and "1993 cumulative premium base" of an employer are relevant in determining whether on any UI premium remittance date for 1993 the employer is entitled to any prepayment under subsection 126.1(11) or (12) of the anticipated tax credit. The 1993 cumulative premium base of an employer on any day is the total of the employer's qualifying employer premiums payable on or before that day for the period beginning January 1, 1993 and ending on that day. The 1992 cumulative premium base of an employer on that day is the total of the employer's qualifying employer premiums for the corresponding period in 1992 that were payable on or before the last day of that period.

The "1992 premium base" of an employer is the total of the employer's qualifying employer premiums payable for 1992. This amount is relevant in determining the maximum prepayment of the UI premium tax credit to which an employer may be entitled under subsection 126.1(12) or (13) and in determining the UI premium tax credit of an employer under subsection 126.1(8) or, in the case of an associated employer, under subsections 126.1(9) to (11).

The "1993 premium base" of an employer is the total of the employer's qualifying employer premiums payable for 1993. This amount is relevant in determining the UI premium tax credit of an employer under subsection 126.1(8) or, in the case of an associated employer, under subsections 126.1(9) to (11).

The new tax credit is available only to a taxpayer who is an employer or a member of a partnership that is an employer. An "employer" is defined as a person or partnership (other than certain persons who are exempt under subsection 149(1) from tax under Part I of the Act) that has a qualifying employee in 1992 or 1993.

A "qualifying employee" of a tax-exempt employer is any employee of the employer. Where the employer is not tax-exempt, a qualifying employee is an employee whose remuneration is deductible in computing the employer's income from a business or property. As a result, a person whose only employee is hired for the personal benefit of the employer (e.g., a gardener or housekeeper) will not be an "employer" for the purposes of section 126.1. A "qualifying employee" of an employer also includes a person in respect of whom the employer is deemed for purposes of the *Unemployment Insurance Act* and regulations thereunder to be an employer.

A "qualifying employer premium" for a period of an employer is the portion of the employer's UI premium that is attributable to remuneration paid in the period to a qualifying employees of the employer. Only that portion of the employer's UI premium that relates to qualifying employees is relevant in determining an employer's UI premium tax credit. Thus the UI premiums payable in respect of employees hired for the personal benefit of the employer will not affect the employer's UI premium tax credit (or the prepayments thereof).

An employer's "remittance date" for 1993 is any date prescribed under the *Unemployment Insurance Act* on which a UI premium is payable by the employer in respect of remuneration paid in 1993. The remittance dates are the days on which prepayments are made under subsection 126.1(12) or (13) on account of the anticipated tax credit.

A "UI premium" of an employer is the employer's portion of the unemployment insurance premium payable in respect of the remuneration paid to employees. If the employer is a partnership, the UI premium of the employer is the employer portion payable by the members of the partnership in respect of the remuneration paid to employees of the partnership.

ITA
126.1(2) and (3)

New subsections 126.1(2) and (3) of the Act set out rules for determining whether two or more employers are associated with each other for the purposes of the rules relating to the UI premium tax credit.

The relevant time for determining whether employers are associated with each other is:

a) for the purpose of determining the UI premium tax credit of an employer under subsections 126.1(8) to (11), the end of 1993; and

b) for the purpose of determining the amount prepaid under subsection 126.1(12) or (13) to an employer or taxpayer on any remittance date, that remittance date.

Paragraph 126.1(2)(a) provides that two employers will be associated with each other at any particular time if they are corporations that are associated with each other at that time. The rules for determining whether corporations are associated are relevant for the purposes of the small business deduction and are set out in section 256 of the Act. Paragraph 126.1(2)(b) provides that where two employers are associated with the same corporation, they will be deemed to be associated with each other. This rule is necessary since for the purposes of the UI premium tax credit it is necessary to expand the concept of associated corporations to cover employers who are individuals or partnerships.

In determining whether two employers are associated with each other at any time, subsection 126.1(3) provides that

a) if an employer is an individual, the employer is to be regarded as a corporation all the shares of which, having full voting rights under all circumstances, are owned by the individual; and

b) if an employer is a partnership, the employer is to be regarded as a corporation having only one class of shares outstanding, all of the shares of which are owned by the partners *pro rata* in the same proportion that the income or loss of the partnership is shared by them.

Thus, for example, an employer who is an individual will be associated with a corporation controlled by the individual. Similarly, an employer that is a partnership will be associated with another employer that is a management corporation the shares of which are owned by the partnership. Further, an employer that is a partnership will also be associated with another employer that is a corporation the shares of which are held outside the partnership by members of the partnership.

ITA
126.1(4) and (5)

New subsection 126.1(4) of the Act deals with the situation in which an employer (the "successor") carries on a business that was previously carried on after 1991 by a "specified employer" in relation to the successor. A specified employer in relation to the successor at any time is defined in new subsection 126.1(5) of the Act as a former employer who does not deal at arm's length with the successor at that time or who would not be dealing at arm's length with the successor at that time if

a) where the former employer has ceased to exist, the former employer were in existence at that time, and

b) the former employer were controlled at that time by each person or group of persons who at any time in 1992 or 1993 controlled the former employer.

The rules in subsection 126.1(3), which treat an individual and a partnership as a corporation the shares of which are owned by the individual or the members of the partnership, apply in determining whether an employer is a specified employer in relation to the successor.

If subsection 126.1(4) applies, the UI premium tax credit of the successor and the former employer and the amount of any prepayment thereof to be made to the successor or the former employer after the successor commenced carrying on the business, will be determined as if the qualifying employer premiums of the former employer that can reasonably be considered to relate to the business were qualifying employer premiums of the successor and not of the former employer. This effectively transfers to the successor that part of the 1992 premium base, the 1992 cumulative premium base, the 1993 premium base and the 1993 cumulative premium base of the former employer that relates to the business carried on by the successor. For example, where an individual, wishing to pursue other business interests, transfers a business to the individual's spouse, the qualifying employer premiums of the transferor that relate to the transferred business will be treated as the qualifying employer premiums of the transferee, and not of the transferor, for the purposes of determining the UI premium tax credit of each of them and the prepayments of the credit available to each of them after the transferee starts carrying on the transferred business.

Subsection 126.1(4) will also apply, for example, where an employer in financial difficulty is dissolved, but the business or part of the business previously carried on by the former employer is later carried on by a new employer controlled by the same person or group of persons that at any time in 1992 or 1993 controlled the former employer.

ITA
126.1(6) and (7)

New subsection 126.1(6) of the Act provides an employer (other than a partnership) with a refundable tax credit equal to the employer's UI premium tax credit. The credit is treated as an overpayment on account of the employer's liability under Part I of the Act for the employer's last taxation year beginning before 1994. This overpayment, which is refundable under new subsection 164(1.6), arises only if the employer has filed a prescribed form with the Revenue Canada. Any such overpayment is treated as arising on the later of March 1, 1994 and the day on which the form is filed. In most circumstances, the overpayment will be delivered by Revenue Canada by way of a reduction of the taxpayer's remittance obligations under the *Unemployment Insurance Act.*

If the employer is a partnership, new subsection 126.1(7) of the Act provides a refundable tax credit to each taxpayer who holds, directly or indirectly through one or more partnerships, an interest in the partnership. As in subsection 126.1(6), the tax credit is provided to the taxpayer by way of a deemed overpayment on account of the taxpayer's liability under Part I of the Act for the taxpayer's last taxation year beginning before 1994. Each taxpayer's tax credit will be equal to the portion of the partnership's UI premium tax credit that can reasonably be considered to be the taxpayer's share thereof. As in the case of individuals and corporations, the credit will generally be delivered by way of a reduction in the remittance by the partnership of unemployment insurance premiums.

If a partnership is a member of another partnership that has a UI premium tax credit, the first partnership will not receive any tax credit. The tax credit is provided only to taxpayers. Thus, while the amount of the credit will be computed at the partnership level, the actual credit will be flowed through to the taxpayers who are members of the partnership or who, through one or more other partnerships, have an indirect interest in the partnership.

The UI premium tax credit of an employer for purposes of subsections 126.1(6) and (7) is determined under subsection 126.1(8) of the Act unless the employer is associated with another employer at the end of 1993. In that case, the employer's tax credit is determined under subsections 126.1(9) to (11) of the Act.

ITA
126.1(8)

New subsection 126.1(8) of the Act defines the "UI premium tax credit" of an employer. It is the lesser of two amounts. The first amount is the maximum credit, which is $30,000 unless the employer's 1992 premium base exceeds $30,000, in which case the maximum credit of $30,000 is reduced by the amount of the excess. This, together with the requirement for associated employers to compute their maximum credit on a group basis, effectively limits the UI premium tax credit to small businesses.

The second amount is the amount by which 1993 premium base of an employer exceeds the employer's 1992 premium base.

The UI premium tax credit of an employer who is associated at the end of 1993 with any other employer is nil unless an amount is allocated to the employer by the group of associated employers under subsection 126.1(9) of the Act or by Revenue Canada under subsection 126.1(10) of the Act.

The following table illustrates, in several different situations, the UI premium tax credit available to an employer who is not associated with any other employer at the end of 1993. In each situation, it is assumed that the 1993 premium base of the employer exceeds the employer's 1992 premium base by $25,000.

1992 premium base	1993 premium base	(A) 126.1(8)(*a*) amount	(B) 126.1(8)(*b*) amount	Tax credit (Lesser of (A) and (B))
$0	$25,000	$30,000	$25,000	$25,000
10,000	35,000	30,000	25,000	25,000
20,000	45,000	30,000	25,000	25,000
30,000	55,000	30,000	25,000	25,000
40,000	65,000	20,000	25,000	20,000
50,000	75,000	10,000[1]	25,000[2]	10,000
60,000	85,000	0	25,000	0

[1] Calculated as $30,000 - ($50,000 - $30,000) = $10,000
[2] Calculated as $75,000 - $50,000 = $25,000

ITA
126.1(9)

New subsection 126.1(9) of the Act provides a mechanism for employers who are associated with each other at the end of 1993 to allocate among themselves an amount that does not exceed the lesser of two amounts. The allocation is made by any member of the group filing with Revenue Canada an agreement in prescribed form. The least amount so allocated to any member of a group of associated employers will, by virtue of subsection 126.1(11) of the Act, be the UI premium tax credit of such member.

The first of the two amounts is the maximum potential credit available to the group, which is $30,000 unless the total of the 1992 premium bases of the associated employers exceeds $30,000, in which case the maximum credit of $30,000 is reduced by the amount of the excess. Thus, the maximum UI premium tax credit available to any member of the group is affected by the 1992 premium bases of all of the members of the group.

The second amount is the amount by which the total of the 1993 premium bases of associated employers exceeds the total of their 1992 premium bases. Thus, the UI premium tax credit available to the members of a group will be affected not only by any increases, but also by any decreases, in the qualifying employer premiums of its members.

The following table illustrates, in four different situations, the determination of the UI premium tax credit available on a group basis to two employers (Aco and Bco) that are associated with each other at the end of 1993. In each situation, the amount determined in Column (C), being the lesser of the amounts determined in columns (A) and (B), is the amount that will be available to be allocated between Aco and Bco as their respective UI premium tax credits.

Aco		Bco				
1992 premium base	**1993 premium base**	**1992 premium base**	**1993 premium base**	**(A) 126.1(9)(*a*) amount**	**(B) 126.1(9)(*b*) amount**	**(C) Lesser of (A)+(B)**
$10,000	$30,000	$10,000	$15,000	$30,000	$25,000	$25,000
10,000	30,000	10,000	5,000	30,000	15,000	15,000
20,000	40,000	10,000	20,000	30,000	30,000	30,000
20,000	40,000	30,000	50,000	10,000[1]	40,000[2]	10,000

[1] Calculated as $30,000 - ($20,000 + $30,000 - $30,000) = $10,000
[2] Calculated as ($40,000 + $50,000) - ($20,000 + $30,000) = $40,000

ITA
126.1(10)

New subsection 126.1(10) of the Act enables Revenue Canada to request any employer who is associated at the end of 1993 with any other employer to file an agreement in prescribed form as contemplated by subsection 126.1(9). If the employer fails to file such an agreement within 30 days after receiving such request, Revenue Canada may allocate among the associated employers an amount that does not exceed the amount that the associated employers could have allocated among themselves under subsection 126.1(9) if they had filed an agreement in prescribed form as contemplated by that subsection.

ITA
126.1(11)

New subsection 126.1(11) of the Act provides that the least amount allocated to an associated employer under any agreement described in subsection 126.1(9) or the amount allocated to an associated employer by Revenue Canada under subsection 126.1(10), as the case may be, is the employer's UI premium tax credit.

ITA
126.1(12) and (13)

The tax credit (deemed overpayment on account of a taxpayer's liability under Part I of the Act) arising under subsection 126.1(6) or (7) arises on the later of March 1, 1994 and the day on which the prescribed form is filed with Revenue Canada. Revenue Canada is required by new subsection 164(1.6) to refund such an overpayment with all due dispatch. New subsection 126.1(12) of the Act provides a mechanism for an employer who files the prescribed form with Revenue Canada before March 1994 to obtain the benefit of an anticipated tax credit earlier by remitting, on any remittance date for 1993 of the employer, less than the full amount of the employer's UI premium then due (referred to in these notes as "short-remitting").

Where an employer has short-remitted UI premiums on any remittance date, Revenue Canada will be treated as having paid to the employer, subject to certain limits, the amount short-remitted, and the employer will be considered to have remitted such amount to the Receiver General on account of the employer's UI premium then due. Where the employer has not short-remitted, or has short-remitted an amount less than the maximum then available to the employer as a prepayment of the UI premium tax credit, the unused portion of the prepayment will generally be available to reduce the employer's next remittance of 1993 UI premiums.

The amount of any such prepayment will be treated as government assistance received by the employer and, accordingly, will be included under paragraph 12(1)(x) in computing the income of the employer. As a result, only the employer's net remittance of the employer's UI premium will be deductible in calculating the employer's income.

Where the employer is a partnership, the amount that would be deemed by subsection 126.1(12) to be paid to the partnership will be deemed instead by subsection 126.1(13) of the Act to have been paid to the taxpayers who, directly or indirectly through one or more other partnerships, have an interest in the partnership. The portion of such amount that can reasonably be considered to be such a taxpayer's share thereof will be deemed by subsection 126.1(13) to be paid to the taxpayer.

Amounts deemed to be paid to an employer under subsection 126.1(12) or to a taxpayer under subsection 126.1(13) will be treated as having been paid on account of any overpayment arising in respect of the employer under subsection 126.1(6) or the taxpayer under subsection 126.1(7).

The manner of determining the amount of the prepayment on any remittance date of an employer will depend on whether the employer is associated with any other employer on that date. Where an employer is not associated on the remittance date with any other employer, the amount available to be prepaid to the employer, determined under subparagraph 126.1(12)(a)(i), will be the amount by which the lesser of the employer's maximum cumulative entitlement and the increase in the qualifying employer premiums on a cumulative basis for the year to date exceeds the total of all amounts prepaid to the employer before that remittance date. For this purpose, an employer's maximum cumulative entitlement is $30,000 unless the employer's 1992 premium base exceeds $30,000, in which case the $30,000 figure is reduced by the amount of the excess. The employer's increase in qualifying employer premiums determined on a cumulative basis on any remittance date is the amount by which the employer's 1993 cumulative premium base in relation to that date exceeds the employer's 1992 cumulative premium base in relation to that date.

Subparagraph 126.1(12)(a)(ii) provides that a prepayment does not arise on any remittance date on which the employer has not short-remitted UI premiums.

The following table illustrates the application of paragraph 126.1(12)(a) to an employer who has increased UI premiums and begins short-remitting on the employer's June 15, 1993 remittance date.

Remittance date	1992 cumulative premium base	1993 qualifying employer premium	1993 cumulative premium base	Amount actually remitted (A)	Amount deemed remitted (B)	Total remittance (A)+(B)
Feb 15/93	$2,000	$3,000	$3,000	$3,000	$ 0	$3,000
Mar 15/93	4,000	3,000	6,000	3,000	0	3,000
Apr 15/93	6,000	3,000	9,000	3,000	0	3,000
May 15/93	8,000	3,000	12,000	3,000	0	3,000
Jun 15/93	10,000	4,000	16,000	0	4,000[1]	4,000
Jul 15/93	12,000	4,000	20,000	0	4,000	4,000
Aug 15/93	15,000	4,000	24,000	3,000	1,000	4,000
Sep 15/93	18,000	4,000	28,000	3,000	1,000	4,000
Oct 15/93	21,000	4,000	32,000	3,000	1,000	4,000
Nov 15/93	24,000	4,000	36,000	3,000	1,000	4,000
Dec 15/93	27,000	4,000	40,000	3,000	1,000	4,000
Jan 15/93	30,000	4,000	44,000	3,000	1,000	4,000
Totals	**30,000**	**44,000**	**44,000**	**30,000**	**14,000**	**44,000**

[1] Calculated as the lesser of:

a) the increase in qualifying premiums for the year to date less any prepayments previously received, i.e., ($16,000 - $10,000) - $0 = $6,000; and

b) the amount short-remitted for the year to date less any prepayments previously received, i.e., ($16,000 - 12,000) - $0 = $4,000.

Where an employer is associated on a remittance date with any other employer, the amount available to be prepaid to the employer, determined under paragraph 126.1(12)(b), will be the lesser of:

a) the amount that would be available to be prepaid to the employer if the employer were not associated on that date with any other employer, and

b) the amount by which the lesser of the maximum entitlement of all the associated employers and the increase in the qualifying employer premiums of all the associated employers on a cumulative basis for the year to date exceeds the total of all amounts prepaid before that date to any of the associated employers and all amounts short-remitted by the associated employers (other than the employer whose prepayment entitlement is being determined).

For this purpose, the maximum entitlement of all of the associated employers is $30,000 unless the total of the 1992 premium bases of all the associated employers exceeds $30,000, in which case the maximum entitlement of $30,000 is reduced by the amount of the excess. The increase in qualifying employer premiums of all of the associated employers determined on a cumulative basis is the amount by which the total of the 1993 cumulative premium bases of all the associated employers on the particular remittance date exceeds the total of the 1992 cumulative premium bases of all the associated employers on that date.

Where two or more employers become associated during 1993, each of them might become disentitled to future prepayments for any of several reasons. First, whereas the maximum entitlement of each of the employers before their becoming associated might have been $30,000, the maximum entitlement of all of the associated employers cannot in the aggregate exceed $30,000. Second, where the total of their 1992 premium bases exceeds $30,000, their joint maximum entitlement of $30,000 will be reduced by the excess. Third, whereas one employer might have incurred increased UI premium liabilities, an associated employer might have incurred decreased UI premium liabilities, with the result that the increase is not reflected in an overall increase in the group's UI premium liabilities.

The following table illustrates the application of paragraph 126.1(12)(b) where two employers (Aco and Bco) become associated with each other at the end of June 1993 and each of them has taken advantage of the prepayments available under subsection 126.1(12) to the greatest extent possible.

	Aco				Bco			
Remittance date	1992 cumulative premium base	1993 cumulative premium base	Amount actually remitted	Amount deemed remitted	1992 cumulative premium base	1993 cumulative premium base	Amount actually remitted	Amount deemed remitted
			(in dollars)					
Feb 15/93	2,500	3,500	2,500	1,000	1,500	3,000	1,500	1,500
Mar 15/93	5,000	7,000	2,500	1,000	3,000	6,000	1,500	1,500
Apr 15/93	7,500	10,500	2,500	1,000	4,500	9,000	1,500	1,500
May 15/93	10,000	14,000	2,500	1,000	6,000	12,000	1,500	1,500
Jun 15/93	12,500	17,500	2,500	1,000	7,500	15,000	1,500	1,500
Jul 15/93	15,000	21,000	2,500	1,000	9,000	18,000	1,500	1,500
Aug 15/93	17,500	24,500	3,500	0	10,500	21,000	3,000	0
Sep 15/93	20,000	28,000	3,500	0	12,000	24,000	3,000	0
Oct 15/93	22,500	31,500	3,500	0	13,500	27,000	3,000	0
Nov 15/93	25,000	35,000	3,500	0	15,000	30,000	3,000	0
Dec 15/93	27,500	38,500	3,500	0	16,500	33,000	3,000	0
Jan 15/94	30,000	42,000	3,500	0	18,000	36,000	3,000	0
Totals	**30,000**	**42,000**	**36,000**	**6,000**	**18,000**	**36,000**	**27,000**	**9,000**

In this example, the maximum credit (and the maximum total prepayments) that can be enjoyed by Aco and Bco after they become associated is $12,000 (because the total of their 1992 premium bases exceeds $30,000 by $18,000). The total of the prepayments received by Aco and Bco by the time that they become associated is $15,000. Thus neither Aco nor Bco is entitled to any further prepayments after they become associated. Furthermore, one or both of Aco and Bco (depending on how they allocate the maximum tax credit of $12,000 between themselves under subsection 126.1(9)) will be required to repay the excess prepayments of $3,000 on or before January 15, 1994 (their last remittance date for 1993).

ITA
126.1(14) and (15)

New subsection 126.1(14) of the Act provides that where the total of the amounts prepaid to a taxpayer under subsection 126.1(12) exceeds the taxpayer's UI premium tax credit, the excess is deemed to have been refunded to the taxpayer on the taxpayer's last remittance date for 1993. This ensures such excess refund must be repaid and will be subject to interest after the last remittance date for 1993 of the taxpayer.

Since an employer's remittance date is the date by which a UI premium must be remitted under the *Unemployment Insurance Act,* where an employer has ceased to carry on business and does not start up the same or another business in 1993, the employer's last remittance date for 1993 will be seven days after the employer ceased to carry on the business.

New subsection 126.1(15) of the Act is similar to subsection 126.1(14) except that it applies to a taxpayer who, directly orr indirectly through one or more partnerships, has an interest in a partnership in respect of which amounts were deemed to be prepaid to the taxpayer under subsection 126.1(13). Where the total of the amounts so prepaid to a taxpayer exceeds that portion of the partnership's UI premium tax credit that can reasonably be considered to be the taxpayer's share thereof, the excess is deemed to have been refunded to the taxpayer on the partnership's last remittance date for 1993.

Clause 15

Investment Tax Credits

ITA
127

Section 127 of the Act permits deductions in computing tax payable in respect of logging taxes, political contributions and investment tax credits.

Subclause 15(1)

ITA
127(5)

Subsection 127(5) of the Act provides for the deduction of investment tax credits from a taxpayer's Part I tax otherwise payable for a taxation year. Under this subsection, the amount that may be deducted by a taxpayer for a year may not exceed the taxpayer's "annual investment tax credit limit" for the year (75% of tax otherwise payable, subject to a base amount for individuals and Canadian-controlled corporations). Subsection 127(5) is amended to remove this limitation for taxation years beginning after 1993, as announced in the budget of April 26, 1993.

Subclause 15(2)

ITA
127(9)

Subsection 127(9) of the Act provides definitions for certain terms used in sections 127 and 127.1 of the Act.

"annual investment tax credit limit"

The definition of "annual investment tax credit limit" is repealed, effective for taxation years beginning after 1993. This amendment is consequential on the amendment to subsection 127(5) of the Act, which provides that for those years a taxpayer's annual investment tax credit limit will no longer be used in determining the amount of credit that may be claimed by the taxpayer.

Subclauses 15(3), (4) and (5)

ITA
127(9)

"investment tax credit"

The definition of "investment tax credit" in subsection 127(9) of the Act provides for the calculation of a taxpayer's investment tax credit at the end of a taxation year and also ensures that a tax credit will not be generated in circumstances where the business income to which a cost or expenditure relates is not subject to income tax.

Subclauses 15(3) and (5) of this Bill amend the definition of "investment tax credit" to add references to the new definition of "qualified small-business property" in subsection 127(9). Qualified small-business property is property that is eligible for the new 10 per cent small business investment tax credit (SBITC). These amendments apply to such property acquired after December 2, 1992 and before 1994. Further discussion of the SBITC may be found in the commentary on subclause 15(9) in these notes.

Subclause 15(4) amends the definition of "investment tax credit" to make reference to new paragraphs 127(11.1)(e) and (f) of the Act. This amendment implements changes to the scientific research and experimental development (SR&ED) tax credit initially announced by the Minister of Finance on October 5, 1992. The effect of this amendment is to ensure that the calculation of a taxpayer's investment tax credit at the end of a taxation year provides for the appropriate additions and deductions. One such addition in paragraph (e.1) of the definition of "investment tax credit" is for the repayment by the taxpayer of assistance where that assistance previously reduced the amount on which a credit was earned. Paragraph (e.1) of this definition is amended as a consequence of the introduction of new paragraph 127(11.1)(f) of the Act. This ensures the addition of a repayment of assistance where that assistance previously reduced the prescribed proxy amount under paragraph 127(11.1)(f). New paragraph (e.2) of this definition similarly provides for the addition of ¼ of the repayment amount for assistance received in respect of first term shared-use-equipment or second term shared-use-equipment where that assistance previously reduced the cost of the equipment under new paragraph 127(11.1)(e) of the Act. These amendments apply to taxation years ending after December 2, 1992.

Subclause 15(6)

ITA
127(9)

"qualified expenditure"

The definition of "qualified expenditure" in subsection 127(9) defines the type of expenditures that are eligible to earn investment tax credits. Expenditures included in the SR&ED pool under paragraph 37(1)(a) and subparagraph 37(1)(b)(i) of the Act, other than prescribed expenditures, are eligible to earn investment tax credits. The rate at which the credits are earned may be 20%, 30% or 35% depending on where in Canada the expenditure was incurred and whether the taxpayer was an individual, public corporation or Canadian-controlled private corporation.

The definition of "qualified expenditure" is extended to include expenditures on first term shared-use-equipment and second term shared-use-equipment and a prescribed proxy amount. The term "prescribed proxy amount" is defined in proposed new subsection 2900(4) of the *Income Tax Regulations* (released by the Minister of Finance in June 1993). This amount is a substitute for certain expenditures which would otherwise have been claimable on an item-by-item portion-by-portion basis if the election under clause 37(8)(a)(ii)(B) of the Act were not made, and the alternative method of determining SR&ED expenditures were not used. Consequently, a prescribed proxy amount does not apply where the taxpayer uses the existing method for determining the SR&ED expenditures included in the SR&ED pool under subsection 37(1). For further discussion of the proxy amount, and its determination, reference may be made to the commentary on paragraph 37(8)(a) in subclause 4(2) of these notes.

Subclauses 15(7) and (8)

ITA
127(9)

"specified percentage"

The definition of "specified percentage" in subsection 127(9) sets out the relevant rates at which investment tax credits are earned in different circumstances.

Paragraph (f) of the definition of "specified percentage" permits an investment tax credit to be earned by the repayment of government assistance, non-government assistance or contract payments that reduced the cost of property or the amount of an expenditure under paragraphs 127(11.1)(b) or (c) of the Act. Subclause 15(7) of this Bill amends paragraph (f) as a consequence of the introduction of new paragraphs 127(11.1)(e) and (f) of the Act. New paragraph (f) of the definition of "specified percentage" ensures that amounts repaid in respect of assistance that previously reduced the amount of a qualified expenditure incurred in respect of first shared-use-equipment under new paragraph 127(11.1)(e) or the prescribed proxy amount under new paragraph 127(11.1)(f) will be eligible for investment tax credits. This amendment to the definition of "specified percentage" applies to taxation years ending after December 2, 1992.

The definition of "specified percentage" is also amended, by subclause 15(8) of this Bill, to add new paragraph (i), which provides that, for purposes of the SBITC, the rate applicable to acquisitions of qualified small-business property, is 10%. This amendment applies to property acquired after December 2, 1992.

Subclause 15(9)

ITA
127(9)

"eligible taxpayer"

The new expression "eligible taxpayer" in subsection 127(9) of the Act describes the entities eligible to earn the 10% SBITC. An eligible taxpayer is:

a) a corporation that is not a non-qualifying corporation,

b) an individual,

c) a trust all beneficiaries of which are themselves eligible taxpayers, or

d) a partnership all members of which are themselves eligible taxpayers.

A beneficiary of a trust is a person or partnership that is beneficially interested in the trust. Subsection 248(25) of the Act sets out the conditions under which a person or partnership will be considered to be beneficially interested in a trust.

"first term shared-use-equipment"

The new expression "first term shared-use-equipment" of a taxpayer is defined to mean depreciable property of the taxpayer (other than prescribed depreciable property) that is used by the taxpayer, during the period commencing with the time the property was acquired by the taxpayer and ending at the end of the first taxation year of the taxpayer ending at least 12 months after that time, primarily (more than 50%) for the prosecution of SR&ED in Canada. Given the interaction of this rule and the "available-for-use" rules, the time when a property is acquired for these purposes is considered to be the time when the property becomes available for use by the taxpayer.

First term shared-use-equipment does not, however, include general purpose office equipment or furniture.

It should be noted that the provisions relating to first term shared-use-equipment implement a test based on the actual use of the property and not its intended use.

"non-qualifying corporation"

The new expression "non-qualifying corporation" in subsection 127(9) of the Act describes corporations that are not eligible to acquire qualified small-business property and, therefore, are not eligible to earn the 10% SBITC. A non-qualifying corporation is:

a) any corporation, except a Canadian-controlled private corporation (CCPC),

b) a corporation that would be subject to the large corporations tax (LCT) under Part I.3 of the Act, if, in determining its LCT liability, no deduction were made in respect of the corporation's Canadian surtax and no account were taken of its debt or equity financing that was used to acquire qualified small-business property (this debt or equity financing exclusion allows a corporation to earn the SBITC in respect of property purchases even though the financing raised by the corporation to purchase the property would otherwise result in the corporation being liable to the LCT), or

c) a corporation that is related (for the purposes of the LCT) to a corporation described in (b) above. Subsection 181.5(7) of the Act provides that, for the purposes of the LCT, a CCPC will be considered to be related only to those corporations with which it is also associated.

"qualified small-business property"

The new expression "qualified small-business property" in subsection 127(9) of the Act describes the types of property that are eligible for the new SBITC. Qualified small-business property is defined as property acquired by a taxpayer after December 2, 1992 and before 1994 (regardless of the date the property becomes available for use), if:

a) the taxpayer is an eligible taxpayer at the time the property is acquired,

b) the property is new and unused,

c) the property is acquired to be used either by the taxpayer or, in the case of property other than certified property, by a person who does not deal at arm's length with the taxpayer, and

d) the property otherwise qualifies as "certified property", "qualified construction equipment", "qualified property" (other than a prescribed building) or "qualified transportation equipment", as those expressions are defined in subsection 127(9).

"second term shared-use-equipment"

The new expression "second term shared-use-equipment" of a taxpayer means property of the taxpayer that was first term shared-use-equipment of the taxpayer and that is used by the taxpayer, during the period commencing with the time the property was acquired by the taxpayer and ending at the end of the first taxation year of the taxpayer ending at least 24 months after that time, primarily (more than 50%) for the prosecution of scientific research and experimental development in Canada.

The provisions relating to second term shared-use-equipment, like those relating to first term shared-use-equipment, implement a test based upon the actual use of the property and not its intended use.

For property to qualify as second term shared-use-equipment of a taxpayer it must have first qualified as first term shared-use-equipment of the taxpayer. If property qualifies as first or second term shared-use-equipment, ¼th of its capital cost is a qualified expenditure eligible for an investment tax credit in the first taxation year ending after the first period or second period, as the case may be. The ¼ fraction reflects the fact that ½ of the capital cost of the property is eligible for an investment tax credit and that the credit in turn is earned over two periods resulting in ¼ thereof being earned in respect of each period. The capital cost of the first or second term shared-use-equipment of taxpayer for a particular taxation year is determined under new paragraph 127(11.1)(e) of the Act.

The new expressions added to subsection 127(9) of the Act apply to property acquired after December 2, 1992.

Subclause 15(10)

ITA
127(10.1) to (10.4)

Subsection 127(10.1) of the Act provides an additional investment tax credit for qualifying scientific research and experimental development (SR&ED) expenditures incurred by certain Canadian-controlled private corporations (CCPCs). To qualify for the additional credit, the corporation must be a CCPC throughout the taxation year in which the expenditures were incurred and its taxable income for its preceding taxation year, together with the taxable incomes for the preceding taxation years of all corporations with which it was associated, must not exceed the corporations' business limits for those years ($200,000). In addition, the total expenditures eligible for the additional credit cannot exceed the corporation's expenditure limit for the year.

Subsection 127(10.2) of the Act defines a corporation's expenditure limit for a year to be $2 million unless the corporation is associated with another corporation. Where this is the case the associated corporations must share the expenditure limit. Subsection 127(10.3) of the Act allows the associated corporations to allocate the $2 million expenditure limit among the members of the corporate group, while subsection 127(10.4) allows the Minister of National Revenue to allocate the limit where the associated corporations fail to do so.

Subsections 127(10.1) to (10.4) of the Act are amended to double the taxable income threshold to $400,000, and to provide an expenditure limit for taxable income in excess of $200,000. These amendments, which apply to taxation years that begin after 1993, implement the changes to investment tax credits for SR&ED expenditures announced in the budget of April 26, 1993.

Subsection 127(10.1) of the Act is amended to provide that a CCPC will be eligible for the additional investment tax credit in a taxation year if the corporation's taxable income for its immediately preceding taxation year, together with the taxable incomes for the preceding year of all corporations with which it was associated in the year, does not exceed twice the business limit of the corporations.

Subsection 127(10.2) of the Act is amended to provide a formula to determine a CCPC's expenditure limit for a taxation year for the purposes of determining SR&ED expenditures eligible for the additional credit under subsection 127(10.1). As taxable income of the corporation, or the corporate group, for the preceding year increases from $200,000 to $400,000, the expenditure limit decreases from $2,000,000 to zero. In other words, for every $1 that the previous year's taxable income exceeds $200,000 the expenditure limit is reduced by $10.

Subsections 127(10.3) and (10.4) of the Act, as amended, provide for the allocation of a corporation's expenditure limit for a taxation year, as determined under subsection 127(10.2), among the corporation and corporations associated with it. These amendments are consequential on the changes to the expenditure limit in subsection 127(10.2).

Subclause 15(11)

ITA
127(11.1)(b) and (c)

Subsection 127(11.1) of the Act sets out various rules for determining amounts to be included in the investment tax credit calculation in subsection 127(9). These rules provide for the reduction of capital cost and qualified expenditures by certain amounts that qualify as assistance or contract payments.

Paragraph 127(11.1)(b) of the Act provides that for investment tax credit purposes the capital cost of property is reduced by government and non-government assistance that the taxpayer has received, is expected to receive or may reasonably be expected to receive in respect thereof at the time the taxpayer's return of income is filed under section 150 for the year the property was so acquired. Paragraph 127(11.1)(b) is amended to clarify that the government or non-government assistance need only reasonably be considered to relate to the property to cause the capital cost of the property to be reduced by such assistance.

Paragraph 127(11.1)(c) of the Act provides that in determining the amount of a "qualified expenditure" for investment tax credit purposes, the expenditure will be reduced by the amount of government assistance, non-government assistance or contract payments that the taxpayer has received, is entitled to received or may reasonably be expected to receive in respect of the expenditure at the time of the filing of the return of income for the year the expenditures were incurred. Paragraph 127(11.1)(c) is amended to clarify that the reduction applies to the amount of assistance and contract payments that can reasonably be considered to be in respect of the expenditures. This paragraph is also amended to remove from the calculation qualified expenditure amounts in respect of a prescribed proxy amount and first term shared-use-equipment. The determination of these amounts is provided for in new paragraphs 127(11.1)(e) and (f) of the Act.

These amendments apply to taxation years ending after December 2, 1992.

Subclause 15(12)

ITA
127(11.1)(e) and (f)

New paragraph 127(11.1)(e) of the Act determines the portion of the capital cost of first term shared-use-equipment or second term shared-use-equipment that will be treated as a qualified expenditure for purposes of the investment tax credit. The portion of the capital cost included as a qualified expenditure of a taxpayer for the taxation year ending coincidentally with each of the first period or second period in respect of first or second term shared-use-property of the taxpayer is ¼ of the capital cost of the property, after accounting for related assistance and contract payments.

New paragraph 127(11.1)(f) of the Act provides that the prescribed proxy amount of a taxpayer for a taxation year must be reduced by the amount of related assistance and contract payments that can reasonably be considered to be in respect of an expenditure described in new subparagraph 37(8)(a)(ii) of the Act other than expenditures described in clause 37(8)(a)(ii)(B). This reduction is intended to ensure that the prescribed proxy amount, and therefore the amount eligible for investment tax credits, is reduced by assistance or contract payments received in respect of those expenditures of which the proxy is in lieu.

These amendments apply to taxation years ending after December 2, 1992.

Subclause 15(13)

ITA
127(17)

Subsection 127(17) of the Act defines the "tax otherwise payable" of a taxpayer for a taxation year for the purposes of the deductions under section 127. This subsection is repealed, effective for taxation years that begin after 1993, consequential on the amendment to subsection 127(5).

Clause 16

Refundable Investment Tax Credits

ITA
127.1

Section 127.1 of the Act provides for the refund of investment tax credits under certain circumstances.

Subclause 16(1)

ITA
127.1(2)

The definition of "refundable investment tax credit" in subsection 127.1(2) of the Act defines the portion of investment tax credits of a taxpayer that are refundable in a taxation year. Included in the definition are investment tax credits earned by the taxpayer in respect of qualified expenditures which are Canadian SR&ED expenditures, including amounts in respect of a prescribed proxy amount. The definition "refundable investment tax credit" is amended to delete a number of references that are no longer relevant and to refer to "qualified expenditures" in order to extend refundability to credits earned in respect of a prescribed proxy amount. This amendment applies to taxation years ending after December 2, 1992.

The definition of "refundable investment tax credit" is also amended, effective after December 2, 1992, to exclude the 10% small business investment tax credit, as the credit is not a refundable one.

Subclause 16(2)

ITA
127.1(2.01)

Under section 127.1 of the Act, refundable investment tax credits can be earned on qualifying SR&ED expenditures incurred in Canada, at the rate of 20%, 30% or 35% depending on the taxpayer and the province in which the expenditures are incurred.

Currently, investment tax credits are refundable only to qualifying corporations, individuals and certain trusts. The rate of refund is 40%, except in the case of certain expenditures of Canadian-controlled private corporations (CCPCs), for which the rate of refund is 100%. The full refund of investment tax credits applies in respect of the 35% investment tax credit for SR&ED expenditures of a current nature (up to $2 million annually) incurred by a qualifying corporation and its associated corporations. A corporation is a qualifying corporation for a particular taxation year if, throughout the particular year, it is a CCPC and the total of its taxable income, for its preceding taxation year, together with the taxable incomes for the preceding year of all corporations with which it was associated in the particular year, does not exceed their business limits for the preceding year ($200,000).

Under new subsection 127.1(2.01) of the Act, a CCPC (other than a qualifying corporation or an excluded corporation) will be eligible for a refund of its 35% investment tax credit. As in the case of qualifying corporations, the rate of refund of the 35% credit is 100% for SR&ED expenditures of a current nature and 40% for SR&ED expenditures of a capital nature. This amendment, which applies to taxation years beginning after 1993, is required to ensure refundability for a corporation earning the 35% SR&ED investment tax credit, the taxable income of which was between $200,000 and $400,000 for the preceding taxation year.

In the case of a qualifying corporation, the first $2 million of qualifying SR&ED expenditures is eligible for the 35% investment tax credit, with a full refund of the credit for expenditures of a current nature and a 40% refund for credits for expenditures of a capital nature. For example, a qualifying corporation incurring $2 million of current SR&ED expenditures in Canada, that is not associated with any other corporation, and has taxable income for the preceding taxation year under $200,000 would be eligible for a 35% investment tax credit on the $2 million of expenditures with eligibility for an investment tax credit refund of up to $700,000 (35% of $2 million).

In the case of a corporation that is neither a qualifying corporation nor an excluded corporation, a portion of the first $2 million of otherwise qualifying SR&ED expenditures may be eligible for the 35% investment tax credit. This portion is described in amended subsections 127(10.1) and (10.2) of the Act. For example, a corporation incurring $2 million of current SR&ED expenditures in Canada, that is not associated with any other corporation, and that has taxable income for its preceding taxation year of $300,000 would be eligible for a 35% investment tax credit on $1 million of expenditures and, generally, a 20% investment tax credit on the remaining $1 million of expenditures. The $350,000 investment tax credit earned on eligible expenditures under the expenditure limit (35% of $1 million) would be eligible for a full refund. (If the expenditures had been of a capital rather than a current nature, the $350,000 credit would be 40% refundable.) The $200,000 investment tax credit (20% of $1 million) would not be refundable. If the SR&ED expenditures had been carried out in either the Atlantic provinces or Gaspé Peninsula, the corporation would be eligible for a 30% rather than a 20% investment tax credit on the remaining $1 million of SR&ED expenditures.

The following table further illustrates the interaction of amended subsections 127(10.1) and (10.2), subsection 127.1(2) and new subsection 127.1(2.01).

TABLE

ITC rate is 35% for amounts less than or equal to limit;
20% for amounts above limit

ITCs earned on amounts in excess of the limit are not refundable

ITCs earned at the 35% rate are refundable at 100% for current expenditures – 40% for capital expenditures

EXAMPLE 1:

CURRENT SR&ED EXPENDITURES OF $2,000,000
CAPITAL SR&ED EXPENDITURES OF $0

Preceding Year Taxable Income	Expenditure Limit For Refund of 35% ITC	Amount of Refundable ITC	Amount of Non-refundable ITC	Total ITC Amount
		(in dollars)		
200,000	2,000,000	700,000	0	700,000
250,000	1,500,000	525,000	100,000	625,000
300,000	1,000,000	350,000	200,000	550,000
350,000	500,000	175,000	300,000	475,000
400,000	0	0	400,000	400,000

EXAMPLE 2:

CURRENT SR&ED EXPENDITURES OF $1,500,000
CAPITAL SR&ED EXPENDITURES OF $500,000

Preceding Year Taxable Income	Expenditure Limit For Refund of 35% ITC	Amount of Refundable ITC	Amount of Non-refundable ITC	Total ITC Amount
		(in dollars)		
200,000	2,000,000	595,000	105,000	700,000
250,000	1,500,000	525,000	100,000	625,000
300,000	1,000,000	350,000	200,000	550,000
350,000	500,000	175,000	300,000	475,000
400,000	0	0	400,000	400,000

EXAMPLE 3:

CURRENT SR&ED EXPENDITURES OF $3,000,000
CAPITAL SR&ED EXPENDITURES OF $0

Preceding Year Taxable Income	Expenditure Limit For Refund of 35% ITC	Amount of Refundable ITC	Amount of Non-refundable ITC	Total ITC Amount
		(in dollars)		
200,000	2,000,000	700,000	200,000	900,000
250,000	1,500,000	525,000	300,000	825,000
300,000	1,000,000	350,000	400,000	750,000
350,000	500,000	175,000	500,000	675,000
400,000	0	0	600,000	600,000

EXAMPLE 4:

CURRENT SR&ED EXPENDITURES OF $0
CAPITAL SR&ED EXPENDITURES OF $2,000,000

Preceding Year Taxable Income	Expenditure Limit For Refund of 35% ITC	Amount of Refundable ITC	Amount of Non-refundable ITC	Total ITC Amount
		(in dollars)		
200,000	2,000,000	280,000	420,000	700,000
250,000	1,500,000	210,000	415,000	625,000
300,000	1,000,000	140,000	410,000	550,000
350,000	500,000	70,000	405,000	475,000
400,000	0	0	400,000	400,000

Clause 17

Labour-Sponsored Funds Tax Credit

ITA
127.4

Section 127.4 of the Act provides a tax credit for individuals equal to 20% of the cost of "approved shares" of a prescribed labour-sponsored venture capital corporation. The credit cannot exceed $1,000 and is available to an individual only where that individual is the first purchaser of such shares.

Subsections 127.4(3) and (4) are amended so that the tax credit is provided to an individual where a trust governed by an RRSP (under which the individual or the individual's spouse is the annuitant) is the first purchaser of such shares and uses contributions made to the trust by the individual for the purchase. Such a trust is defined in amended subsection 127.4(1) as a "qualifying trust".

These amendments apply to the 1992 and subsequent taxation years.

Clause 18

Bankruptcies

ITA
128(2)(d)

Subsection 128(2) of the Act contains a number of special rules that apply in cases of personal bankruptcy. For most purposes, paragraph 128(2)(d) divides the calendar year in which an individual becomes bankrupt into two taxation years: one taxation year that runs from January 1 to the day before the bankruptcy and the other that commences on the day of the bankruptcy and runs to December 31. This rule does not apply for the purposes of subsection 146.01(9), which provides an income inclusion for the 1992 taxation year in certain cases where an individual (or the individual's spouse) withdraws RRSP funds under the Home Buyers' Plan and the individual also pays RRSP premiums within a specified period.

Paragraph 128(2)(d) is amended so that it also does not apply for the purposes of new subsection 146.01(10), which, for the 1993 taxation year, provides a rule similar to that in subsection 146.01(9). This amendment is strictly consequential on the proposed extension of the Home Buyers' Plan, as described in the commentary on the amendments to section 146.01.

This amendment applies to the 1993 and subsequent taxation years.

Clause 19

Home Buyers' Plan

ITA
146.01

The rules relating to the Home Buyers' Plan are set out in section 146.01 of the Act. Under the Home Buyers' Plan, a home buyer may withdraw amounts (referred to in the section as "eligible amounts") from one or more or his or her RRSPs on a tax-free basis after February 25, 1992 and repay the amounts on a non-deductible basis over 15 years from 1994 to 2008. The total of the eligible amounts withdrawn by an individual cannot exceed $20,000.

The Home Buyers' Plan is being amended to allow withdrawals after March 1, 1993 and before March 2, 1994. (In certain cases described in new paragraph 146.01(2)(e), withdrawals will also be permitted after March 1, 1994 and before April 1994.) Under the amendments, repayments may be made over the 15 year period from 1995 to 2009 irrespective of when the home buyer withdrew eligible amounts.

The amendments to this section apply to the 1992 and subsequent taxation years.

Subclause 19(1)

ITA
146.01(1)

"eligible amount"

An "eligible amount" received by an individual out of or under an RRSP under the Home Buyers' Plan is an "excluded withdrawal" and as such is not included in the individual's income by reason of subsection 146(8). Among the conditions that must presently be satisfied for an amount to qualify as an "eligible amount" in respect of a "qualifying home" are:

- the amount must be received before March 2, 1993, and

- the individual withdrawing the amount must acquire the home (or "replacement property" for it) before October 1993 (or, in certain cases referred to in paragraph 146.01(2)(c), before October 1994).

The definition of "eligible amount" is amended so that amounts may be received after March 1, 1993 and before March 2, 1994. (See, however, new paragraph 146.01(2)(e) which extends the March 1, 1994 deadline to the end of March 1994 in certain cases where an individual applies to receive an amount prior to March 2, 1994.)

The amendments to the definition of "eligible amount" also provide that where an individual receives an amount after March 1, 1993 and before March 2, 1994, the qualifying home must be acquired before October 1994 (or, in certain cases referred to in paragraph 146.01(2)(c), before October 1995.)

Paragraph (g) is added to the definition of "eligible amount" so that an amount received after March 1, 1993 does not qualify as an eligible amount for an individual if the individual (or a spouse of the individual) received an eligible amount before March 2, 1993. However, an exception to this rule is provided under new paragraph 146.01(2)(d) for certain amounts received in March 1993.

Subclause 19(2)

ITA
146.01(1)

"excluded withdrawal"

An "excluded withdrawal" is an amount received by an individual out of or under the individual's RRSP, pursuant to the Home Buyers' Plan. It is not included in computing the individual's income under subsection 146(8). An "excluded withdrawal" includes "eligible amounts" received by an individual, that is to say, those amounts that can be repaid by the individual over 15 years because the individual has acquired a qualifying home and satisfied other conditions set out in the definition of "eligible amount".

In addition, in two cases an amount can qualify as an "excluded withdrawal" if the conditions necessary for the amount to qualify as an "eligible amount" are ultimately not satisfied. The first case is where the individual dies before 1994 and had not ceased to be resident in Canada after the withdrawal and before death. The second case is where the individual repays all or part of the withdrawn amount to the RRSP issuer from which the amount was originally withdrawn before 1994 (or, in certain cases referred to in paragraph 146.01(2)(c), before 1995) and the individual notifies the RRSP issuer of the repayment on a prescribed form. If the individual is not resident in Canada at the time of filing a tax return for the year in which the amount was withdrawn from the RRSP, the repayment to the RRSP must also be made before the individual files that return.

The definition of "excluded withdrawal" is amended so that, where an amount in respect of a qualifying home is withdrawn after March 1, 1993, the times referred to above in respect of the death of an individual or repayments by the individual are extended by one year.

Subclause 19(3)

ITA
146.01(1)

"completion date"

The "completion date" generally is the date before which a qualifying home must be acquired. The completion date in respect of an RRSP withdrawal under the Home Buyers' Plan is October 1, 1994, except where the withdrawal was made before March 2, 1993, in which case it is October 1, 1993. Note that, for this purpose, certain amounts received in March 1993 are treated by new paragraph 146.01(2)(d) as having been received on March 1, 1993.

Subclause 19(4)

ITA
146.01(2)(c)

Paragraph 146.01(2)(c) applies where an individual has withdrawn an amount from an RRSP pursuant to the Home Buyers' Plan in respect of a qualifying home, but the individual has not acquired the qualifying home (or replacement property for the qualifying home) before October 1993. In these circumstances, the individual is deemed to acquire the qualifying home on September 30, 1993 where conditions set out in clause 146.01(2)(c)(ii)(A) or (B) are satisfied.

Paragraph 146.01(2)(c) is amended so that, where an individual withdraws an amount pursuant to the Home Buyers' Plan after March 1, 1993 and before March 2, 1994, the time references in paragraph 146.01(2)(c) are extended by one year.

ITA
146.01(2)(d) and (e)

New paragraph (g) of the definition "eligible amount" in subsection 146.01(1) of the Act provides that an amount received by an individual from an RRSP after March 1, 1993 does not qualify as an eligible amount where the individual (or a spouse of the individual) received an eligible amount before March 2, 1993. New paragraph 146.01(2)(d) treats an amount received from an RRSP by an individual which otherwise fails to qualify as an eligible amount for this reason to be an amount received on March 1, 1993, where the following conditions are satisfied:

- the request to receive the amount was made before March 2, 1993,
- the amount is received before April 1993, and
- the individual or the individual's spouse received another eligible amount before March 2, 1993.

In these circumstances, any RRSP premiums paid by the individual or the individual's spouse after March 1, 1993 and before the receipt of such an amount are generally treated, for the purposes of section 146.01, as having been paid on March 1, 1993. However, in determining whether an RRSP withdrawal is an "eligible amount", paragraph 146.01(2)(d) is relevant only for the purposes of paragraph (g) of the definition of "eligible amount".

Amended paragraph (a) of the definition "eligible amount" in subsection 146.01(1) of the Act provides that an amount received by an individual after March 1, 1994 does not qualify as an eligible amount. New paragraph 146.01(2)(e) treats an amount received by an individual which fails to qualify as an eligible amount for this reason to be an amount received on March 1, 1994, where

- the request to receive the amount was made before March 2, 1994, and
- the amount is received after March 1, 1994 and before April 1994.

In these circumstances, any RRSP premiums paid by the individual or the individual's spouse after March 1, 1994 and before the receipt of such an amount are generally treated, for the purposes of section 146.01, as having been paid on March 1, 1994. However, in determining whether an RRSP withdrawal is an "eligible amount", paragraph 146.01(2)(e) is relevant only for the purposes of paragraph (a) of the definition of "eligible amount".

New paragraphs 146.01(2)(d) and (e) affect the time at which an RRSP withdrawal is considered to have been made for the purposes of section 146.01. The paragraphs also affect the time at which certain RRSP premiums are considered to have been paid for the purposes of section 146.01. As a consequence, the paragraphs are relevant not only for the purposes of determining whether an RRSP withdrawal is an "eligible amount" but also for the purposes of amended subsection 146.01(9) and new subsection 146.01(10).

Subclause 19(5)

ITA
146.01(4)

Subsection 146.01(4) of the Act provides that, for the 1994 taxation year, an individual is required to include in income 1/15 of all eligible amounts received by the individual minus any repayments made under subsection 146.01(3) before the end of the year in respect of the eligible amounts. The repayment required to avoid an income inclusion for any subsequent taxation year is a fraction of the individual's "balance" under the Home Buyers' Plan at the beginning of the year. This balance, at the beginning of a particular year, is equal to the total of all eligible amounts received by the individual minus the sum of repayments made before that time and shortfalls included in the individual's income for previous years. The fraction is 1/14 for 1995, 1/13 for 1996, and so on until the fraction is 1 for 2008. Any balance remaining in 2008 must either be repaid to an RRSP or included in income for that year.

Subsection 146.01(4) is amended so that this repayment schedule starts in 1995 (i.e. with a repayment fraction of 1/15) and ends in 2009, regardless of when an individual withdrew an eligible amount.

Subclause 19(6)

ITA
146.01(7)

Subsection 146.01(7) of the Act provides an election that may be made where a deceased individual has a spouse who is resident in Canada immediately before the individual's death. Where the election is made, subsection 146.01(6) of the Act does not apply to the deceased spouse. Instead, the surviving spouse is treated as having received an eligible amount equal to the balance that would otherwise have been included in the deceased's income under subsection 146.01(6). This amount is added to the surviving spouse's own balance of eligible amounts that have not been repaid to RRSPs at that time. Paragraph 146.01(7)(b) is amended, effective for 1992 and subsequent years, so that the deemed receipt by the surviving spouse does not result in an income inclusion for the spouse under amended subsection 146.01(10) of the Act.

Subclause 19(7)

ITA
146.01(9) and (11)

Subsection 146.01(9) of the Act provides an income inclusion for the 1992 taxation year. It is amended so that the definition of "net premium balance" referred to therein is defined in respect of the 1992 taxation year. The existing definition of "net premium balance" in subsection 146.01(10) is renumbered as subsection 146.01(11) and amended so that it applies only for the 1992 taxation year. These amendments are strictly consequential on the introduction of subsection 146.01(10), which provides a rule similar to subsection 146.01(9) with respect to the 1993 taxation year.

The only change to the calculation of the income inclusion for the 1992 taxation year arises from the application of new paragraph 146.01(2)(d). Eligible amounts received by an individual or the individual's spouse before March 2, 1993 enter into the calculation of the income inclusion under subsection 146.01(9). For this purpose, new paragraph 146.01(2)(d) treats certain amounts received by an individual in March 1993 as having been received on March 1, 1993. In addition, new paragraph 146.01(2)(d) treats certain RRSP premiums paid after March 1, 1993 and before April 1993 as having been paid on March 1, 1993.

ITA
146.01(10) and (12)

New subsection 146.01(10) provides an income inclusion with respect to RRSP premiums paid after December 2, 1992 and before March 2, 1994 (referred to below as the "relevant period") by an individual who participates in the Home Buyers' Plan. It applies, for example, where RRSP premiums paid in the relevant period are withdrawn by the individual or the individual's spouse under the Home Buyers' Plan.

Subsection 146.01(10) of the Act applies only for the 1993 taxation year. An individual is generally required to include in computing income the lesser of two amounts.

The first amount is the "net premium balance" for the 1993 taxation year of the individual. As defined in new subsection 146.01(12), the net premium balance for that year of an individual is equal to the total premiums paid by the individual in the relevant period (other than "excluded premiums", defined in subsection 146.01(1)) **minus** RRSP withdrawals (other than amounts attributed to the individual's spouse or related to RRSP premiums paid after March 1, 1994) received by the individual or the individual's spouse after December 2, 1992 and before 1995.

The second amount is the sum of

- total eligible amounts withdrawn from an RRSP by the individual after March 1, 1993 and before March 2, 1994, and
- the lesser of
  - premiums (other than "excluded premiums") paid by the individual to a spousal RRSP in the relevant period, and
  - total eligible amounts withdrawn by the individual's spouse after March 1, 1993 and before March 2, 1994 minus the net premium balance for the 1993 taxation year of the individual's spouse.

Reference may be made to the explanatory notes on new paragraphs 146.01(2)(d) and (e), which contain rules affecting the time at which eligible amounts are treated as having been received for the purposes of new subsection 146.01(10) and the time at which certain RRSP premiums are considered to have been paid.

ITA
146.01(13)

Existing subsection 146.01(11) of the Act ensures that the Minister of National Revenue is able to assess or reassess the tax, interest and penalties of an individual outside the normal time limits in order to recognize the special income inclusion required under subsection 146.01(9).

The existing subsection is renumbered as subsection 146.01(13) and extended to apply in respect of income inclusions under subsection 146.01(10).

Clause 20

Assessments and Reassessments

ITA
152

Section 152 of the Act contains rules relating to assessments and reassessments of tax, interest and penalties payable by a taxpayer.

Subclause 20(1)

ITA
152(1.2)

Subsection 152(1.2) of the Act provides for the application of paragraphs 56(1)(1) and 60(o) and Divisions I and J of the Act relating to objections, assessments and appeals to various determinations and redeterminations made under Part I of the Act. This subsection is amended to ensure that such provisions also apply to determinations and redeterminations of amounts deemed to be overpayments under the child tax benefit provisions previously enacted and amounts deemed to be overpayments under the new UI premium tax credit provisions.

This amendment, which applies to determinations and redeterminations made after 1992, is consequential on the enactment of the child tax benefit provisions and the introduction of the new UI premium tax credit provisions in section 126.1.

Subclause 20(2)

ITA
152(3.4) and (3.5)

New subsection 152(3.4) of the Act enables a taxpayer to request the Minister of National Revenue to determine the amount deemed by subsection 126.1(6) or (7) to be an overpayment on account of the taxpayer's liability under Part I. New subsection 152(3.5) requires the Minister to respond to such a request with all due dispatch and determine the amount of such overpayment, or determine that there is no such amount, and to send a notice of such determination to the taxpayer. These new provisions are consequential on the enactment of section 126.1 and apply after 1992.

Subclause 20(3)

ITA
152(4.2)(d)

Subsection 152(4.2) of the Act gives the Minister of National Revenue discretion to make a reassessment or a redetermination beyond the normal reassessment period when so requested by a taxpayer who is an individual or a testamentary trust in order to give the taxpayer a refund or to reduce taxes payable. This amendment to paragraph 152(4.2)(d) adds a reference to subsections 126.1(6) and (7) to enable the Minister to make a redetermination of an amount deemed by either of those subsections to be an overpayment on account of the taxpayer's liability under Part I of the Act. This amendment is consequential on the enactment of section 126.1 and applies after 1992.

Clause 21

Payment of Tax

ITA
153(2)

Under subsection 153(2) of the Act, an individual is exempt from making instalment payments of income taxes for a year if at least ¾ of the individual's income for the year is subject to withholding of income tax at source. In this case the individual must pay any remainder of tax payable by the individual's balance-due day for the year (in most cases, April 30 of the following year).

As a consequence of the introduction of a new method of determining whether an individual is exempt from making instalment payments, announced in the budget of April 26, 1993 and contained in amended section 156.1 of the Act, subsection 153(2) is repealed as of 1995. Since the new exemption applies only to amounts that become payable after June 1994, subsection 153(2) remains in effect for the 1994 taxation year, subject to sections 155, 156 and 156.1 of the Act.

Clause 22

Instalment Payments – Farmers and Fishermen

ITA
155(1)

Subsection 155(1) of the Act provides that an individual whose chief source of income is farming or fishing may be required to make an instalment payment of income tax in December of a taxation year if less than ¾ of the individual's income for the year is subject to withholding of income tax at source. With the introduction of a new method of determining whether an individual must make instalment payments, contained in amended section 156.1 of the Act, the exclusion from the application of subsection 155(1) where subsection 153(2) applies is removed.

As well, as a consequence of the addition of a general provision in amended section 156.1 of the Act, requiring the payment of any remainder of tax owing by a taxpayer for a year by the taxpayer's balance-due day for the year, the similar provision in paragraph 155(1)(b) is repealed.

These amendments apply to the 1994 and subsequent taxation years.

Clause 23

Instalment Payments – Other Individuals

ITA
156(1)

Under subsection 156(1) of the Act an individual (other than a farmer or fisherman) may be required to pay quarterly tax instalments if less than ¾ of the individual's income for the year is subject to withholding at source. With the introduction of a new method of determining whether an individual must make instalment payments, contained in amended section 156.1 of the Act, the exclusion from the application of subsection 156(1) where subsection 153(2) applies is removed. This amendment applies to instalments that become payable after June 1994.

As a consequence of the addition of a general provision in amended section 156.1 of the Act, requiring the payment of any remainder of tax owing by a taxpayer for a year by the taxpayer's balance-due day for the year, a similar provision in the concluding words of subsection 156(1) is repealed. This amendment applies to the 1994 and subsequent taxation years.

Clause 24

Exemptions from Instalment Payments and Payment of Remainder

ITA
156.1

Section 156.1 of the Act relieves an individual from any obligation to pay instalments of tax if the individual's federal income tax payable for either the current or preceding taxation year is $1,000 or less ($1,000 test). Under subsection 153(2) of the Act an individual is also exempt from making instalments for a year if at least ¾ of the individual's income for the year is subject to withholding at source (the ¾ test).

Section 156.1 is amended to implement the new criteria for instalment remitters announced in the budget of April 26, 1993. This amendment, which applies to instalments payable after June 1994, replaces both the $1,000 test and the ¾ test with a new instalment threshold test based on an individual's net tax owing. The new test, which is provided in subsection 156.1(2) of the Act, varies with the individual's residency and chief source of income.

Generally, an individual resident in Quebec at the end of a taxation year will be required to pay quarterly tax instalments during the year if the individual's federal income tax payable after deducting federal income tax withheld at source (i.e., that individual's net tax owing) is more than $1,200 in both that year and either of the two preceding years.

Generally, an individual resident outside Quebec at the end of a taxation year will be required to pay quarterly tax instalments during the year if the individual's federal and provincial income taxes payable after deducting federal and provincial income taxes withheld at source (i.e., that individual's "net tax owing") is more than $2,000 in both that year and either of the two preceding years.

An exception to these general rules is provided for individuals whose chief source of income is farming or fishing. Farmers and fishermen are exempt from making the December instalment payment otherwise required under subsection 155(1) of the Act if the individual's net tax owing for the current year, the first preceding year, or the second preceding year does not exceed the individual's instalment threshold. In other words, if the individual's net tax owing is below the instalment threshold for any one of those three years, the individual is not required to make a December instalment payment for the current year.

New subsection 156.1(1) of the Act contains definitions of the terms "net tax owing" and "instalment threshold". An individual's net tax owing for a year is determined in the following manner. For a Quebec resident, net tax owing for a year is the total federal tax payable under Part I and Part I.1 of the Act for the year less the total of any federal tax withheld at source for the year and the Quebec tax abatement under subsection 120(2) of the Act for the year. For all other individuals, net tax owing for a year is the total federal and provincial income taxes payable for the year less the total of any federal and provincial taxes withheld at source for the year.

In addition, federal or provincial tax payable for the year is determined after deducting certain tax credits to which the individual is entitled for the year, and which become payable on or before the individual's balance-due day for the year. Amounts specified in subparagraphs 167(1)(a)(ii) to (v) of the Act, such as losses carried back from subsequent years, are not taken into account in determining net tax owing for a taxation year. Child tax credits and investment tax credits are deducted from an individual's federal tax otherwise payable in order to determine the individual's net tax owing for instalment purposes. The amount of any Canada Pension Plan overpayment, unemployment insurance overpayment, employee and partner GST rebate, child tax benefit, and GST credit is not taken into account in determining the individual's net tax owing. Similarly, for the purpose of calculating net tax owing, provincial income tax payable for a taxation year is net of provincial income tax credits for the year.

For any year, the instalment threshold is $1,200 for individuals who are residents of the province of Quebec at the end of the year, and $2,000 for all other individuals. The instalment threshold is lower for a Quebec resident because Quebec provincial income tax is not taken into account in determining a Quebec resident's net tax owing.

Individuals who have moved into or out of the province of Quebec will be required to use the applicable net tax owing formula and instalment threshold amount for each relevant year to determine whether they are exempt from making instalment payments. The following example illustrates this point.

Example:

- Marie was resident in Quebec at the end of 1992. At the end of 1993 and 1994 Marie was a resident of Nova Scotia. Her chief source of income in these years was not farming or fishing.

- To determine whether Marie is required to make instalment payments in 1994, she must calculate her net taxes owing for 1992, 1993 and 1994.

- For 1992 (the second preceding year), Marie would determine her net tax owing using the formula for Quebec residents. For the years 1993 (the first preceding year) and 1994 (the current year), Marie would determine her net tax owing using the formula for individuals residing outside the province of Quebec.

- Marie would be exempt from making quarterly instalment payments of income tax if:
    - her net federal and provincial income tax owing for 1994 did not exceed $2,000, or
    - her net federal and provincial income tax owing for 1993 did not exceed $2,000 and her net federal income tax owing for 1992 did not exceed $1,200.

New subsection 156.1(4)of the Act is a general provision requiring an individual to pay the remainder of any income tax payable on or before the individual's balance-due day for the year. This provision replaces existing subsection 153(2), paragraph 155(1)(b) and the concluding words of subsection 156(1) of the Act. New subsection 156.1(4) takes into account taxes already withheld at source, as well as other taxes paid or deemed paid, in determining the outstanding amount that must be paid by an individual's balance-due day.

Clause 25

Excess Refunds

ITA
160.1(2.2) and (3)

New subsection 160.1(2.2) of the Act makes members of a partnership jointly and severally liable to repay all amounts refunded to any member of the partnership in excess of the amounts to which such member is entitled under section 126.1. It applies only to amounts received under section 126.1 by a member of a partnership in the member's capacity as a member of the partnership, and not to amounts received in the member's capacity as an employer separate and apart from the partnership.

Subsection 160.1(3) of the Act enables the Minister of National Revenue to assess a taxpayer in respect of, among other things, excess funds referred to in subsection 160.1(1) and amounts for which the taxpayer is jointly and severally liable under subsection 160.1(2.1). The amendment to subsection 160.1(3), effective after 1992, adds a reference to new subsection 160.1(2.2).

Clause 26

Penalties

ITA
163

Section 163 of the Act imposes penalties in respect of serious failures to comply with the Act, such as making false statements or omitting to report income.

Subclause 26(1)

ITA
163(2)(c.2)

Subsection 163(2) of the Act imposes a penalty where a taxpayer, knowingly or in circumstances amounting to gross negligence, participates in or makes a false statement or omission in a return, form, certificate, statement or answer. New paragraph 163(2)(c.2), which is consequential on the introduction of the UI premium tax credit provided to employers under section 126.1, allows a penalty to be imposed where a false statement or omission is made in connection with that credit. This amendment applies after 1992.

Subclause 26(2)

ITA
163(2.2)

Subsection 163(2.2) of the Act provides a penalty where a taxpayer makes a false statement or omission in a renunciation of resource expenses under subsection 66(12.6), (12.62) or (12.64).

Subsection 163(2.2) is amended so that the same penalty apply in respect of a renunciation of resource expenses under new subsection 66(12.601).

This amendment applies on Royal Assent.

Clause 27

Refunds

ITA
164

Section 164 of the Act provides rules relating to income tax refunds.

Subclause 27(1)

ITA
164(1.6)

New subsection 164(1.6) of the Act requires Revenue Canada to refund to a taxpayer, with all due dispatch and without application therefor, any amount deemed by subsection 126.1(6) or (7) to be an overpayment on account of the taxpayer's liability under Part I of the Act. Although no application is required for the refund itself, the overpayment cannot arise under section 126.1 unless the employer or, in the case of a partnership, a member of the partnership acting on behalf of the partners, files with Revenue Canada a prescribed form on which the amount of the overpayment will be calculated. The amount refunded will be the amount of the deemed overpayment less any prepayments made under subsection 126.1(12) or (13) on account of the deemed overpayment. Subsection 164(1.6) is consequential on the introduction of UI premium tax credit under section 126.1 and applies after 1992.

ITA
164(1.7)

Subsection 164(1.1) of the Act provides that where 120 days have passed since the service of a notice of objection to an assessment in respect of a taxpayer and the Minister of National Revenue has not confirmed or varied the assessment or issued a reassessment in respect of the objection, or where the taxpayer has appealed from an assessment either to the Tax Court of Canada or directly to the Federal Court of Canada, the Minister must with all due dispatch refund the amount paid that is in dispute, or release the security obtained relevant to the amount in dispute, where the taxpayer so requests in writing.

Subsection 164.(1.7) is being added to the Act to provide that subsection 164(1.1) does not apply to non-resident persons in respect of security furnished or amounts paid pursuant to section 116 of the Act. Section 116 contains procedures for ensuring the collection of tax from non-residents on the disposition of particular types of taxable Canadian properties and Canadian resource properties. This amendment applies on Royal Assent.

Subclause 27(2)

ITA
164(3)

Subsection 164(3) of the Act provides for the payment of interest on tax refunds. This subsection is amended to provide that no interest is payable on any refund of any amount arising as a consequence of the operation of section 126.1. This amendment applies after 1992.

Clause 28

Individual Surtax

ITA
180.1(1.2) and (1.3)

Section 180.1 of the Act levies a general surtax on individuals at the rate of 3% of tax payable under Part I of the Act and also imposes an additional surtax of 5% on the portion of an individual's Part I tax in excess of $12,500.

Subsection 180.1(1.2) of the Act allows an individual to offset up to ¾ of the individual's surtax otherwise payable for a year, after deducting foreign tax credits for the year under subsection 180(1.1) of the Act, by claiming investment tax credits. Subsection 180.1(1.2) is amended, for taxation years that begin after 1993, to eliminate the ¾ restriction as a consequence of the elimination of the annual limit on the amount of investment tax credit that may be deducted by a taxpayer under subsection 127(5) of the Act.

Subsection 180.1(1.3) of the Act treats investment tax credits deducted for a year under subsection 180.1(1.2) as amounts deducted for the year under subsection 127(5) for purposes of the Act. Subsection 180.1(1.3) is amended, for taxation years that begin after 1993, consequential to the amendment to subsection 180.1(1.2) of the Act.

Clause 29

Labour-Sponsored Venture Capital Corporations

ITA
204.8

Section 204.8 of the Act sets out a number of definitions which apply for the purposes of Part X.3, relating to national labour-sponsored venture capital corporations (LSVCCs). A tax credit in respect of the acquisition of shares of LSVCCs registered under Part X.3 is provided under section 127.4.

Subclause 29(1)

"eligible investment"

An "eligible investment" for a national LSVCC includes common shares issued by qualifying small and medium-sized businesses and certain subordinated debt. A national LSVCC is ultimately required to invest at least 60% of its shareholder's equity in "eligible investments", pursuant to subsection 204.82(2).

The definition of "eligible investment" is amended so that preferred shares issued by qualifying small and medium-sized businesses are included therein.

Subclause 29(2)

"specified individual"

Section 204.8 is also amended to introduce the definition "specified individual". A "specified individual" in respect of a share in the capital stock of a national LSVCC is the individual whose labour-sponsored funds tax credit (as defined in subsection 127.4(3)) takes into account the consideration paid for the share, assuming the individual files the required form to claim the credit. This definition is consequential on the changes to sections 127.4 and 204.81 permitting the original purchaser of a share issued by LSVCCs to be made by a trust governed by an RRSP.

These amendments to section 204.8 apply after December 2, 1992.

Clause 30

Labour-Sponsored Venture Capital Corporations – Registration

ITA
204.81

Section 204.81 of the Act provides rules governing the registration of labour-sponsored venture capital corporations by the Minister of National Revenue.

Subclauses 30(1) and (5)

ITA
204.81(1)(c) and 204.81(6)

Subsection 204.81(1) of the Act permits the Minister of National Revenue to register a corporation as an LSVCC under Part X.3 if the corporation's articles of incorporation satisfy specified conditions and other requirements are met. Under paragraph 204.81(6)(a), the Minister may revoke the registration if the corporation fails to comply with such provisions.

The preamble to paragraph 204.81(1)(c) is amended so that the articles of a corporation, rather than its articles of incorporation are relevant for the purposes above. As defined in the *Canada Business Corporation Act*, the articles of a corporation include the original or restated articles of a corporation.

Subsection 204.81(6) is amended as a consequence of the above amendment. Amended paragraph 204.81(6)(a) allows for the revocation of the registration of a corporation where the articles of the corporation do not comply with the specified conditions. New paragraph 204.81(6)(a.1) allows for the revocation of the registration of a corporation where, at any time, it fails to comply with the specified conditions set out in its articles at that time.

These amendments apply after 1988.

Subclauses 30(2), (3) and (4)

ITA
204.81(1)(c)(ii) and (v) to (vii)

Paragraph 204.81(1)(c) of the Act sets outs the specified conditions that must be provided by the articles of a corporation, in order for the corporation to be registered as an LSVCC under Part X.3.

Subparagraph 204.81(1)(c)(ii) is amended to permit a trust governed by an RRSP to be the original purchaser of shares issued by a registered LSVCC. The restrictions on the redemption and transfer of LSVCC shares that currently apply where the original purchaser was an individual will apply in a substantially similar manner where the original purchaser is a trust governed by an RRSP.

Subparagraph 204.81(1)(c)(ii) is also amended to eliminate a reference to the restrictions on redemption and transfer of shares contained in subparagraphs 204.81(1)(c)(v) to (vii). This reference is no longer necessary because of amendments to subparagraphs 204.81(1)(c)(v) and (vii).

Subparagraphs 204.81(1)(c)(v) and (vii) are amended so that a share can be transferred or redeemed if consideration for the share would not be taken into account in computing any individual's labour-sponsored funds tax credit (within the meaning assigned by subsection 127.4(1)) if the required form to claim the credit were filed. These circumstances are anticipated to arise in very unusual situations. For example, a share could be issued to a trust governed by an RRSP that did not use contributions to the trust by any one individual to acquire the share.

Subparagraph 204.81(1)(c)(vii) is also amended to permit transfers of LSVCC shares to trusts governed by RRIFs to be made on the same basis as transfers to trusts governed by RRSPs.

Subparagraph 204.81(1)(c)(vii) is also amended to allow for the registration of a transfer of a Class A share, from (or to) an individual whose labour-sponsored funds tax credit takes into account the cost of the share, to (or from) that individual's spouse. This extends the existing provision in subparagraph 204.81(1)(c)(vii) which allows transfers to spousal RRSPs, but not to the annuitant of such an RRSP directly.

These amendments apply after December 2, 1992. However, where a corporation was registered under Part X.3 prior to December 3, 1992 the amendments apply on the earlier of

- the last day of the sixth month after the month in which Royal Assent occurs, and
- the first day after December 2, 1992 on which the articles of the corporation were amended.

Clause 31

Deferred Income Plans – Penalties

ITA
207.1(5)

Subsection 207.1(5) of the Act imposes a penalty tax on a trust governed by an RRSP or a RRIF with respect to "excessive" holdings in small business properties.

This subsection is repealed, retroactive to the date of its introduction.

Clause 32

Interpretation

ITA
248(1)

"specified employee"

Subsection 248(1) of the Act is amended to include the term specified employee which is used in new subsection 37(9) of the Act and proposed new subsection 2900(5) of the *Income Tax Regulations* (released by the Minister of Finance in June 1993). A "specified employee" of a person is an employee who is a specified shareholder of the person or who does not deal at arm's length with the person. Subsection 248(1) defines a specified shareholder of a corporation generally as a person who owns 10% or more of any class of shares of the corporation.

This amendment applies to taxation years that end after December 2, 1992.