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Explanatory Notes to Legislative Proposals Relating to Income Tax

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Preface

These explanatory notes are provided to assist in an understanding of legislative proposals relating to income tax. These explanatory notes describe these proposed amendments, clause by clause, for the assistance of Members of Parliament, taxpayers and their professional advisors.

The Honourable James M. Flaherty, P.C., M.P.,
Minister of Finance

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Income Tax Act

Clause 1

Dividends from Resident Corporations

ITA
12(1)(*j*)

Paragraph 12(1)(*j*) of the Income Tax Act (the Act) provides for the inclusion in computing a taxpayer's income in a taxation year of dividends required by Subdivision h of Division B of Part I to be included in the taxpayer's income for the year in respect of a dividend paid by a corporation resident in Canada on a share of its capital stock.

Paragraph 12(1)(*j*) is reworded to refer to any amount of a dividend in respect of a share of the capital stock of a corporation resident in Canada that is required by subdivision h to be included in computing the taxpayer's income for the year. This change makes the wording of paragraph 12(1)(*j*) consistent with the proposed wording of paragraph 12(1)(*k*), which applies to dividends required by subdivision i to be included in computing a taxpayer's income for a taxation year. The proposed change to paragraph 12(1)(*k*) was included in Bill C-10, which ceased to exist when Parliament was dissolved on September 7, 2008.

This amendment applies after Announcement Date.

Clause 2

Gains and Losses – General Rules

ITA
40

Section 40 of the Act provides rules for determining a taxpayer's gain or loss from the disposition of a capital property.

Deemed Gain for Certain Partners

ITA
40(3.11)

Subsection 40(3.11) of the Act provides a formula to determine the gain of a member of a partnership for the purposes of subsection 40(3.1). The amount determined by the formula equals any "negative" balance in the adjusted cost base of the member's interest in the partnership at the end of a fiscal period of the partnership.

The formula is amended to include in this calculation the income or loss, as the case may be, for the particular fiscal period, if the partnership is a "professional partnership" as defined in new subsection 40(3.111) of the Act.

New paragraph (*b*) of the description of variable A in subsection 40(3.11) provides that, if the partnership is a professional partnership, a taxpayer's share of any loss referred to in subparagraph 53(2)(*c*)(i) of the Act for the fiscal period will be added when calculating the amount under subsection 40(3.11).

New paragraph (*c*) of the description of variable B in subsection 40(3.11) provides that, if the partnership is a professional partnership, a taxpayer's share of any income referred to in subparagraph 53(1)(*e*)(i) of the Act for the fiscal period will be deducted when calculating the amount under subsection 40(3.11).

This amendment applies to fiscal periods that end after November 2001.

Professional Partnership

ITA
40(3.111)

New subsection 40(3.111) defines the term "professional partnership" for the purposes of the rules relating to deemed gains under subsection 40(3.1). "Professional partnership" means a partnership through which one or more persons carry on the practice of a profession that is governed or regulated under a law of Canada or a province.

This amendment applies to fiscal periods that end after November 2001.

Clause 3

Consideration for Warranties, Covenants or Other Obligations

ITA
42

Section 42 of the Act provides rules governing warranties, covenants, and other conditional or contingent obligations given by a taxpayer in respect of a disposition of property (the "subject property").

The provision provides generally that consideration for a warranty, covenant or other conditional or contingent obligation, given or incurred in respect of the disposition of the subject property, shall be treated as a gain from the disposition of a property, and not as consideration for the obligation.

The provision also provides generally that an outlay or expense under a warranty, covenant or other conditional or contingent obligation, given or incurred in respect of the disposition of the subject property, shall be treated as a loss from the disposition of a property, and not as an outlay or expense under the obligation.

Section 42 is amended to clarify the timing of the inclusion of gains and losses.

New paragraph 42(1)(*a*) provides generally that an amount received or receivable as consideration for an obligation is deemed to be a capital gain from the disposition of a property that occurs when the consideration is received or receivable. However, if the consideration is received or receivable on or before a "specified date", the amount is to be included in computing the proceeds of disposition of the subject property in the year in which the disposition occurred.

New subsection 42(2) of the Act defines "specified date" to mean generally the taxpayer's filing due-date for the taxation year in which the property was disposed of, except that, for partnerships, the specified date is the end of the partnership's fiscal period in which the subject property was disposed of.

New paragraph 42(1)(*b*) provides generally that an outlay or expense paid or payable under an obligation is deemed to be a capital loss from the disposition of a property that occurs when the outlay or expense is paid or payable. However, if the outlay or expense is paid or payable on or before the specified date, the amount is to be deducted in computing the proceeds of disposition of the subject property in the year in which the disposition occurred.

The amendment to section 42 generally applies to taxation years and fiscal periods that end on or after Announcement Date. For taxation years and fiscal periods that end after February 27, 2004 and before Announcement Date, section 42 of the Act will be read as proposed on February 27, 2004. The amendment applicable to taxation years and fiscal periods that end on or after Announcement Date is consistent with the amendment applicable to the earlier period but clarifies the timing of the inclusion of gains and losses in respect of partnerships.

Clause 4

Adjustments to Cost Base

ITA
53(1)

Subsection 53(1) of the Act sets out a number of amounts that are added, in computing a taxpayer's adjusted cost base of a property at a particular time, to the taxpayer's cost of the property. Subsection 53(2) of the Act sets out amounts that are similarly deducted.

Adjustments to Cost Base – Interest in a Partnership

ITA
53(1)(*e*)

Paragraph 53(1)(*e*) of the Act provides for additions to the adjusted cost base of a taxpayer's partnership interest.

Amounts Added to the Cost Base of a Partnership Interest

ITA
53(1)(*e*)(i)(A.1)

Paragraph 53(1)(*e*) of the Act provides for additions to the adjusted cost base of a taxpayer's partnership interest.

Existing clause 53(1)(*e*)(i)(A.1) of the Act is repealed consequential to the repeal of paragraph 18(1)(*l.1*) of the Act. This amendment applies to amounts that became payable after December 20, 2002.

New clause 53(1)(*e*)(i)(A.1) provides that a gain from a disposition of an object that is certified cultural property, by a partnership to a designated institution, will generally result in a corresponding adjustment to the adjusted cost base of the partners' interests in the partnership. That is, a partner's adjusted cost base will now be computed as if the Act were read without reference to subparagraph 39(1)(*a*)(i.1) of the Act, where the object referred to in that subparagraph is not the subject of a gifting arrangement, nor a property that is a tax shelter, for the purpose of section 237.1 of the Act.

New clause 53(1)(*e*)(i)(A.1) applies to the disposition of an object made after 2003.

Disposition of a Foreign Resource Property

ITA
53(1)(*e*)(viii.1)

New subparagraph 53(1)(*e*)(viii.1) provides for an addition in computing the adjusted cost base of a taxpayer's partnership interest, where the taxpayer is a member of the partnership, equal to the member's share of proceeds of disposition receivable by the member in respect of a disposition of a foreign resource property by the partnership. This amendment ensures that, on disposition of a foreign resource property by the partnership, the proceeds of the disposition that are deemed by subsection 59(1.1) of the Act to become receivable by a member of the partnership and that are excluded in computing the income of the partnership because of paragraph 96(1)(*d*) of the Act are added to the adjusted cost base of the member's partnership interest.

This amendment applies to fiscal periods of a partnership that begin after 2000.

Amounts Deducted from the Cost Base of a Partnership Interest

ITA
53(2)(*c*)(i)(A.1)

Paragraph 53(2)(*c*) of the Act provides for deductions to the adjusted cost base of a taxpayer's partnership interest.

Clause 53(2)(*c*)(i)(A.1) is repealed consequential to the repeal of paragraph 18(1)(*l.1*) of the Act.

This amendment applies to amounts that became payable after December 20, 2002.

Clause 5

Deduction – Pension Repayments

ITA
60(*n.1*)

Section 60 provides for various deductions in computing income, including deductions in respect of certain repayments. New paragraph 60(*n*.1) provides a deduction to an individual who repays to a registered pension plan (RPP) an overpayment of an amount received from the RPP that was included in the individual's income for the year or a preceding year. The repayment must relate to an amount that may reasonably be considered to have been paid from the RPP in error and not as an entitlement to benefits under the RPP. An individual cannot claim a deduction under new paragraph 60(*n*.1) if the individual is claiming a deduction for the amount under paragraph 8(1)(*m*) as a contribution to the RPP.

This amendment applies to the 2009 and subsequent taxation years.

Clause 6

Resource Expenses

ITA
66

Section 66 provides rules in respect of resource expenses.

Members of Partnerships

ITA
66(18)

Subsection 66(18) provides that, for the purposes of most of the resource taxation rules, a partner's share of resource expenditures incurred in a fiscal period is considered to have been incurred by the partner at the end of the fiscal period.

Subsection 66(18) is amended by adding a reference to the "pre-production mining expenditure", consequential to the introduction of subparagraph (*b*)(ii) in the definition in subsection 127(9) of the Act. A taxable Canadian corporation that is a member of a partnership could under certain circumstances earn investment tax credits in respect of the corporation's "pre-production mining expenditure." For more information, refer to commentary following the amendments to the definition of pre-production mining expenditure in subsection 127(9) of the Act.

This amendment applies to expenses incurred in fiscal periods that begin after 2001.

Clause 7

Canadian Exploration Expense

ITA
66.1

Section 66.1 provides the rules relating to the deduction of “Canadian exploration expense.”

Definitions

ITA
66.1(6)

Subsection 66.1(6) of the Act provides definitions for the purpose of section 66.1.

“Canadian exploration expense”

The definition “Canadian exploration expense” (CEE) defines oil, gas and mining expenses that qualify for treatment as CEE eligible for a 100% write-off.

Paragraph (*k.2*) of the definition provides that, for greater certainty, mining exploration expenses and pre-production expenses described in paragraph (*f*) or (*g*) of the definition (other than subparagraph (*f*)(ii)), do not include any portion of the expenses that may reasonably be considered to have resulted in revenue earned by the taxpayer before the mineral resource or mine referred to in those paragraphs come into production in reasonable commercial quantities.

This provision confirms that production revenue earned prior to the commencement of production in reasonable commercial quantities is to be netted out in computing CEE. Because paragraph (*k.2*) of the definition specifically refers to expenses described in paragraphs (*f*) and (*g*), paragraph (*k.2*) of the definition CEE is repealed and paragraphs (*f*) and (*g*) are reworded to accomplish the same result.

These amendments apply in respect of expenses incurred after Announcement Date.

“cumulative Canadian exploration expense”

A taxpayer's “cumulative Canadian exploration expense” (CCCE) includes the taxpayer's undeducted pool of Canadian exploration expenses. A taxpayer is permitted a deduction under either subsection 66.1(2) or (3) with respect to a positive CCEE. A “negative” CCEE is included in a taxpayer's income under subsection 66.2(1).

The description of B, in the formula in the definition of CCEE, adds negative CCEE amounts that are required to be included in a taxpayer’s income during previous taxation years. The description of B is amended to ensure that only amounts that were included in a taxpayer’s income during previous taxation years are added to the taxpayer’s CCEE pool.

Clause 8

Canadian Development Expense

ITA
66.2

Section 66.1 provides the rules relating to the deduction of “Canadian development expense.”

Definitions

ITA
66.2(5)

Subsection 66.2(5) contains the definitions “Canadian development expense” and “cumulative Canadian development expense” of a taxpayer.

“cumulative Canadian development expense”

A taxpayer's “cumulative Canadian development expense” (CCDE) includes the taxpayer's undeducted pool of Canadian development expenses. A taxpayer is permitted a deduction under subsection 66.2(2) with respect to a positive CCDE. A “negative” CCDE is included in a taxpayer's income under subsection 66.2(1).

The description of B, in the formula in the definition of CCDE, adds negative CCDE amounts that are required to be included in a taxpayer’s income during previous taxation years. The description of B is amended to ensure that only amounts that were included in a taxpayer’s income during previous taxation years are added to the taxpayer’s CCDE pool.

This amendment applies to taxation years ending after Announcement Date.

Clause 9

Foreign Resource Expense

ITA
66.21

Section 66.21 sets out the rules governing foreign resource expenses.

Definitions

ITA
66.21(1)

Subsection 66.21(1) of the Act provides several definitions for the purpose of section 66.21.

“cumulative foreign resource expense”

A taxpayer's “cumulative foreign resource expense” (CFRE) in respect of a country includes the taxpayer's undeducted pool of foreign resource expenses in respect of the country. A taxpayer is generally permitted a deduction under subsection 66.21(4) with respect to a positive CFRE on a country-by-country basis. A “negative” CFRE is included in a taxpayer's income under subsection 66.21(3).

The description of B, in the formula in the definition of CFRE, adds negative CFRE amounts that are required to be included in a taxpayer’s income during previous taxation years. The description of B is amended to ensure that only amounts that were included in a taxpayer’s income during previous taxation years are added to the taxpayer’s CFRE pool.

This amendment applies to taxation years ending after Announcement Date.

Clause 10

Successor Rules – Resource Expenses

ITA
66.7

Section 66.7 provides rules (commonly known as the “successor rules”) in respect of foreign exploration and development expenses, foreign resource expenses, Canadian exploration expenses, Canadian development expenses and Canadian oil and gas property expenses. The successor rules establish the parameters within which unused resource expenses of an "original owner" may be deducted by a corporation ("successor corporation") following an acquisition of resource properties by the successor corporation in certain circumstances.

Non-successor Acquisitions

ITA
66.7(16)

Subsection 66.7(16) provides that where a particular Canadian resource property or foreign resource property is acquired by a person in circumstances in which the successor rules do not apply, every person who was an original owner or predecessor owner of the property by reason of having previously disposed of the property shall, for the purposes of applying the successor rules to future owners of the property, be treated as never having been an original owner or predecessor owner of the property. Thus, the income from such properties thereafter will not qualify any expenses of a predecessor or original owner for a deduction in the hands of a successor.

The subsection is amended by removing the phrase "by reason of having previously disposed of the property," to ensure that the rule applies to all dispositions of resource properties. As well, the reference to "shall be deemed" is replaced by "is deemed" to reflect the current drafting style.

This amendment applies to property acquired after Announcement Date.

Clause 11

Limited Partners – Resource Expenses

ITA
66.8

Section 66.8 provides for the rules regarding the deduction of a taxpayer's share of a partnership's resource expenditures incurred in a fiscal period in certain cases where the taxpayer's share of such resource expenditures exceeds the taxpayer's "at-risk amount" at the end of the fiscal period in respect of the partnership.

Interpretation

ITA
66.8(3)(*a*) and (*a.1*)

Paragraph 66.8(3)(*a*) currently provides the meaning for two expressions for the purpose of section 66.8. The expression "at-risk amount" of a taxpayer in respect of a partnership, has the meaning assigned by subsection 96(2.2), and the expression "limited partner" of a partnership (subject to certain date references in the definition of "exempt interest" in subsection 96(2.5)) has the meaning assigned by subsection 96(2.4).

Paragraph 66.8(3)(*a*) is amended so that it no longer provides the meaning of the expression "at-risk amount" – now in new paragraph 66.8(3)(*a.1*). It continues to provide for the meaning of the expression "limited partner," which meaning remains unchanged.

New paragraph 66.8(3)(*a.1*), which provides for the meaning of the expression "at-risk amount", is amended to provide that, for the purposes of deducting resource expenses of a limited partner under section 66.8, the "at-risk amount" of a taxpayer will not be adjusted for any amount owing by the taxpayer to a person in respect of which the taxpayer is a wholly-owned subsidiary or, if the taxpayer is a trust, to a person that is the sole beneficiary of the taxpayer.

These amendments apply to fiscal periods ending after 2003.

Clause 12

Expenses for Food, etc.

ITA
67.1

Section 67.1 provides a general limitation on the amount that may be deducted in respect of the human consumption of food or beverages or the enjoyment of entertainment, limiting an otherwise deductible amount to 50% of the expense.

Expenses for food and beverage of long-haul truck drivers

ITA
67.1(1.1)

Subsection 67.1(1.1) provides that the amount paid or payable by a long-haul truck driver during an eligible travel period is deemed to be a specified percentage of the amount instead of the 50% of the amount otherwise deemed in subsection 67.1(1). The specified percentage is 70% in 2009, 75% in 2010 and 80% after 2010.

The preamble to subsection 67.1(1.1) is amended to ensure that the subsection applies to expenses in respect of the consumption of food or beverages by a long-haul truck driver, whether or not the expenses are paid or payable by the driver. This ensures that the subsection applies in respect of deductibility of such expenses by an employer who may have paid the expenses.

This amendment applies to amounts that are paid, or become payable after March 18, 2007.

Clause 13

***Inter Vivos* Transfer of Farm or Fishing Property to a Child**

ITA
73(3)

Subsection 73(3) provides a tax-deferral for an *inter vivos* transfer of farm or fishing property by a taxpayer to a child of the taxpayer. Paragraph 73(3)(*a*) is amended to remove the word "immediately", such that the property need not be used in the farming or fishing business immediately before the transfer in order to qualify for this rollover.

This amendment applies to transfers of property that occur after May 1, 2006, other than a transfer in respect of which a taxpayer has made a valid election under subsection 11(5) of *Budget Implementation Act, 2006, No. 2*.

Clause 14

Exempt Amounts – Leave of Absence Plans

ITA
81(1)(*s*)

Subsection 81(1) lists various amounts that are not included in computing income.

New paragraph 81(1)(*s*) provides a tax exemption in respect of already-taxed amounts received from a leave of absence plan if that plan is excepted from the salary deferral arrangement rules by reason of paragraph 6801(a) of the *Income Tax Regulations*.

Paragraph 6801(*a*) of the *Income Tax Regulations* requires, in subparagraph (iv), that income accruing to the benefit of an employee in the year under the plan be paid to the employee in that year. Some plans are structured so that the employee recognizes the income in the year for tax purposes, but then immediately recontributes that income to the plan. New paragraph 81(1)(*s*) provides that a subsequent distribution of a re-contributed amount that was taxed in an earlier year is not included in income.

This amendment applies to the 2000 and subsequent taxation years.

Clause 15

When Dividend Payable

ITA
84(7)

Subsection 84(7) of the Act provides that a dividend deemed under sections 84, 128.1 or 212.1 to have been paid at a particular time as a dividend is also regarded, for the purposes of Subdivision h of Division B in Part I and sections 131 and 133, to have become payable at that time. Subsection 84(7) is amended to replace the reference to subsection 84(7) with a reference to section 84.

This amendment applies to dividends deemed to have been paid after February 23, 1998.

Clause 16

Share for Share Exchange

ITA
85.1

Section 85.1 permits a tax-deferred rollover for shareholders who exchange shares of a corporation for shares of a purchaser corporation in the course of an arm's length sale of the acquired corporation's shares. Under this rule, the exchanged shares must both be shares of a taxable Canadian corporation, or both be shares of a foreign corporation. In either case, the purchaser corporation is required to "issue" its shares on the exchange.

Deemed Issuance

ITA
85.1(2.2)

New subsection 85.1(2.2) of the Act provides a deeming rule for the purpose of subsection 85.1(1) under which certain share issues made by a taxable Canadian corporation (the purchaser corporation) to a trust under a court-approved plan of arrangement are deemed to be issued to a person (the vendor) who exchanges the vendor's shares of a taxable Canadian corporation for the shares issued by the purchaser corporation. For this deeming rule to apply, the vendor must dispose of the vendor's shares to the purchaser corporation solely for the shares issued by the purchaser corporation. As well, the vendor's shares must trade on a designated stock exchange and be disposed of for shares of the purchaser corporation that are widely traded on a designated stock exchange immediately after and as part of completion of the plan of arrangement.

Generally, this amendment applies to share exchanges made after June 2005.

Deemed Issuance

ITA
85.1(6.1)

New subsection 85.1(6.1) of the Act provides a deeming rule for the purpose of subsection 85.1(5) under which certain share issues made by a foreign corporation (the foreign purchaser corporation) to a trust under a court-approved plan of arrangement are deemed to be issued to a person (the vendor) who exchanges the vendor's shares of a foreign corporation for the shares issued by the foreign purchaser corporation. For this deeming rule to apply, the vendor must dispose of the vendor's shares to the foreign purchaser corporation solely for the shares issued by the foreign purchaser corporation. As well, the vendor's shares must trade on a designated stock exchange and be disposed of for shares of the foreign purchaser corporation that are widely traded on a designated stock exchange immediately after and as part of completion of the plan of arrangement.

Generally, this amendment applies to share exchanges made after June 2005.

Clause 17

Capital Gains Exemption

ITA
110.6

Section 110.6 of the Act sets out the rules for calculating the entitlement of an individual to the lifetime capital gains exemption.

Definitions

ITA
110.6(1)

The definitions in subsection 110.6(1) of the Act apply for the purposes of rules in section 110.6 for the capital gains exemption.

"qualified farm property"

Subsection 110.6(2) of the Act provides to individuals an exemption of up to $750,000 for capital gains realized on the disposition of "qualified farm property". Qualified farm property generally includes real property owned by an individual, the individual's spouse or a family farm partnership in which the individual or spouse has an interest. In general, in order to qualify, paragraph (*a*) of that definition requires that the property have been used principally in a farming business operated by the individual, the individual's spouse or any of their children (including, in general terms, when such business is operated through a family farm corporation or partnership or a personal trust).

Paragraph (*a*) of that definition is amended to remove the word "principally". This amendment applies to dispositions made after May 1, 2006.

"qualified fishing property"

Subsection 110.6(2.2) of the Act provides to individuals an exemption of up to $750,000 for capital gains realized on the disposition of "qualified fishing property". Qualified fishing property generally includes real property owned by an individual, the individual's spouse or a family fishing partnership in which the individual or spouse has an interest. In general, in order to qualify, paragraph (*a*) of that definition requires the real property have been used principally in a fishing business operated by the individual, the individual's spouse or any of their children (including, in general terms, when such business is operated through a family fishing corporation or partnership or a personal trust).

Paragraph (*a*) of that definition is amended to remove the word "principally". This amendment applies to dispositions made after May 1, 2006.

Property Used in a Farming Business

ITA
110.6(1.3)

Subsection 110.6(1.3) of the Act provides that, for the purposes of the definition of "qualified farm property" in subsection 110.6(1) of the Act, a property will not be considered to have been used in the course of carrying on the business of farming in Canada except in certain circumstances.

In this regard, existing paragraphs 110.6(1.3)(*a*) and (*b*) describe conditions of ownership for property that was acquired, generally, after June 17, 1987 and not acquired under an agreement in writing entered into before June 18, 1987. These paragraphs are amended to combine them as new paragraph (*a*), clarifying that the conditions in both of new paragraphs 110.6(1.3)(*a*)(i) and (ii) must be met in order for the property to be considered to be used in the business of farming in Canada.

Subsection 110.6(1.3) is also consequentially amended by renumbering paragraph (*c*) as paragraph (*b*).

These amendments apply to dispositions made after Announcement Date.

Clause 18

Deductions of Taxable Dividends Received by Corporation Resident in Canada

ITA
112

Section 112 is one of the principal provisions dealing with the treatment of dividends received by a corporation resident in Canada from another corporation. Subsection 112(1) permits a corporation to deduct, subject to certain exceptions, taxable dividends in computing its taxable income.

Where No Dividend Deduction Permitted

ITA
112(2.1)

Subsection 112(2.1) prevents a specified financial institution from deducting taxable dividends received on most term preferred shares in computing its taxable income. This subsection is amended to replace the first reference to the term "paid" with the word "received" and to remove the second reference to the term "paid".

This amendment applies to dividends received on or after Announcement Date.

Guaranteed Shares

ITA
112(2.2)

Subsection 112(2.2) denies the intercorporate dividend deduction for dividends on certain shares that are guaranteed by a specified financial institution. Paragraph 112(2.2)(*a*) is amended to replace the reference to the term "paid" with the word "received".

This amendment applies to dividends received on or after Announcement Date.

Clause 19

Public Transit Pass Credit

ITA

118.02

Section 118.02 of the Act provides to an individual a non-refundable tax credit in respect of the cost of eligible public transit passes attributable to the use, by the individual or a qualifying relation in respect of the individual, of public transit in a taxation year.

The definition of "qualified Canadian transit organization" in subsection 118.02(1) is amended to clarify that the definition "permanent establishment" in section 8201 of the Regulations applies for these purposes.

This amendment applies to the 2009 and subsequent taxation years.

Clause 20

Medical Expenses

ITA
118.2(2)(*i*)

Section 118.2 of the Act provides rules for determining the amount which may be claimed, as a tax credit, in respect of an individual's medical expenses. Subsection 118.2(2) of the Act contains a list of expenditures that qualify as eligible medical expenses. Paragraph 118.2(2)(*i*) is amended to correct the spelling of ileostomy.

This amendment applies on Royal Assent.

Clause 21

Credit for Mental or Physical Impairment

ITA
118.3(4)

Section 118.3 of the Act provides a tax credit, generally referred to as the Disability Tax Credit (DTC), for individuals who have a severe and prolonged mental or physical impairment. Paragraph 118.3(4)(*a*) of the Act provides a requirement for certain persons to provide, upon request of the Minister of National Revenue, additional information with respect to an individual's impairment. If this information is provided by a medical practitioner referred to in paragraph 118.3(1)(*a.2*) of the Act, paragraph 118.3(4)(*b*) of the Act provides that the information is considered to be in the form of a certificate required for the purpose of claiming the DTC.

Paragraph 118.3(4)(*b*) is amended to add a similar reference to a medical practitioner referred to in paragraph 118.3(1)(*a.3*) of the Act, which was added by the 2006 budget.

This amendment applies to the 2005 and subsequent taxation years.

Clause 22

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 (ITCs).

Definitions

ITA
127(9)

Subsection 127(9) provides various definitions relevant for the purpose of calculating the investment tax credits (ITCs) of a taxpayer.

"eligible salary and wages"

"Eligible salary and wages" payable by a taxpayer to an eligible apprentice means the amount, if any, that is the salary and wages payable by the taxpayer to the eligible apprentice in respect of the first 24 months of the apprenticeship. The definition does not include remuneration that is based on profits, bonuses, and amounts described in section 6 or 7 of the Act, and amounts deemed to be incurred by subsection 78(4) of the Act.

The definition is amended to ensure that the definition does not include a qualified expenditure incurred by the taxpayer in a taxation year. Where an amount paid to an eligible apprentice is eligible to be included in both the eligible salary and wages and the qualified expenditures of a taxpayer, the taxpayer can include that amount only in one of the definitions and not both.

This amendment applies to taxation years ending after Announcement Date.

“pre-production mining expenditure”

A “pre-production mining expenditure” qualifies for the 10% investment tax credit, available to a taxpayer that is a taxable Canadian corporation, as provided for in paragraph (*a.3*) of the definition “investment tax credit.”

Generally, a pre-production mining expenditure is a grass roots exploration and pre-production development expenditure in Canada for qualifying minerals. These expenses are described in paragraphs (*f*) and (*g*) of the definition of “Canadian exploration expense” in subsection 66.1(6). Those paragraphs require that the expenses be incurred before a new mine comes into production in reasonable commercial quantities. Qualifying minerals for the credit are diamonds, base or precious metals and industrial minerals that become base or precious metals through refining.

A taxable Canadian corporation which claims an investment tax credit in respect of a pre-production mining expenditure generally must actually incur the expense, in order for the expense to qualify as a pre-production mining expenditure. Specifically, an expense which has been renounced to the taxable Canadian corporation under subsection 66(12.6) does not qualify as a pre-production mining expenditure. The credit is also not allocable by a trust. As well, a member’s share of expenses incurred by a partnership does not qualify as a pre-production mining expenditure.

Paragraph (*b*) of the definition “pre-production mining expenditure” (PPME) in subsection 127(9) is amended to allow for the flow-through of PPME in limited circumstances. In particular:

- new subparagraph (*b*)(i) allows for the renunciation of PPME by a wholly owned subsidiary to its parent, and
- new subparagraph (*b*)(ii) provides that a corporation’s share of pre-production mining expenditures is deemed by subsection 66(18) to be made, or have been incurred, by the corporation at the end of the fiscal period of a partnership only if,
    - the corporation is an actively engaged member of the partnership, and
    - the corporation is a principal-business corporation engaged in mining activities.

This amendment applies to the 2003 and subsequent taxation years.

Clause 23

Labour-sponsored Funds Tax Credit

ITA
127.4(6)

Subsection 127.4(6) of the Act sets out the calculation of an individual’s “labour-sponsored funds tax credit” for a taxation year in respect of an “original acquisition” of an approved share of a labour-sponsored venture capital corporation (LSVCC). Except as provided by paragraphs 127.4(6)(*b*), (*c*) and (*d*), this tax credit is generally equal to 15% of the net cost to the individual (or to an RRSP trust funded by the individual) in respect of the original acquisition of the share by the individual or trust.

New paragraph 127.4(6)(*e*) is added concurrently with the amendment of sections 211.7 and 211.8 of the Act that allow for the issuance of exchangeable shares by LSVCCs. New paragraph 127.4(6)(*e*) is added to ensure that a tax credit is not provided if a new share of the LSVCC is acquired in exchange for another share of the LSVCC.

This amendment applies to the 2004 and subsequent taxation years.

Clause 24

Adjusted Taxable Income Determined

ITA
127.52(1)(*h*)(i)

Section 127.52 of the Act defines the “adjusted taxable income” of an individual for a taxation year for the purpose of determining the individual’s minimum tax liability under Part I of the Act.

Paragraph 127.52(1)(*h*) provides that in computing an individual’s adjusted taxable income, only certain of the deductions under sections 110 to 110.7 may be taken into account. Paragraph 127.52(1)(*h*) is amended to eliminate the reference to subsection 110.6(3), which was repealed by S.C. 1995, c. 3.

This amendment applies upon Royal Assent.

Clause 25

Basic Minimum Tax Credit Determined

ITA
127.531

Section 127.531 of the Act permits an individual to claim deductions, in computing minimum tax, for most non-refundable personal tax credits.

Paragraph 127.531(*a*) is amended so that the tax credit provided under section 119 of the Act, which is a credit regarding certain dispositions of taxable Canadian property, is included among those taken into account in computing minimum tax.

This amendment applies to dispositions made after December 23, 1998 for individuals who ceased to be resident in Canada after October 1, 1996.

Paragraph 127.531(*a*) is also amended to add a reference to subsection 127(1) of the Act, so that the logging tax credit is also taken into account in computing minimum tax.

This amendment applies to the 2009 and subsequent taxation years.

Clause 26

Personal Bankruptcy

ITA

128(2)(*g*)(iii)

Subsection 128(2) of the Act contains a number of special rules that apply in cases of personal bankruptcy. Paragraph 128(2)(*g*) prohibits an individual who is discharged absolutely from bankruptcy from claiming certain non-refundable tax credits, particularly those credits computed by reference to expenditures made before the individual became bankrupt. Subparagraph 128(2)(*g*)(iii) is amended consequential to the introduction of the textbook tax credit in the 2006 Budget, to make reference to unused tuition, textbook and education tax credits.

This amendment applies to the 2006 and subsequent taxation years.

Clause 27

Tax-Free Savings Accounts

ITA
146.2(1)

“holder”

Subsection 146.2(1) of the Act provides a number of definitions for the purposes of the rules applicable in respect of Tax-Free Savings Accounts (TFSAs). Under the current definition “holder” in subsection 146.2(1), only a “survivor” (defined in subsection 146.2(1) as the individual who was, immediately before the death of the individual who opened the TFSA, the spouse or common-law partner of that individual) can be a successor holder. The legislation does not allow the survivor to designate a subsequent successor holder (e.g. a new spouse of the survivor in case of remarriage of the survivor) in respect of the TFSA. On the other hand, the TFSA rules do permit the survivor to transfer the funds out of the existing TFSA to a new TFSA in respect of which he or she can designate a successor holder, thereby achieving the same result indirectly.

The definition “holder” is amended to simplify the TFSA rules regarding successor holder designations by allowing the survivor (and subsequent survivors) to designate a subsequent successor holder. Note that the same conditions apply to the designation of a successor holder to a survivor as to the designation of a survivor to the initial holder of the TFSA: that is, the successor holder has to acquire, as part of the survivor’s rights as holder or in addition to those rights, the unconditional right to revoke any beneficiary designation made by the survivor in relation to the TFSA.

This amendment applies to the 2009 and subsequent taxation years.

Clause 28

Registered Pension Plans – *Foreign Missions and International Organizations Act*

ITA
147.1(1) “compensation”

Subsection 147.1(1) of the Act provides a number of definitions relating to registered pension plans, including the definition “compensation”. As currently defined, “compensation” includes amounts that, but for paragraph 81(1)(*a*) as it applies with respect to the *Indian Act*, would be required by section 5 or 6 to be included in computing an individual’s income. In other words, the existing definition includes as compensation amounts that are exempt from income tax under paragraph 81(1)(*a*) only as it applies with respect to the *Indian Act*.

The amended definition “compensation” extends the meaning of the term to also include amounts exempt from income tax under paragraph 81(1)(*a*) as it applies with respect to the *Foreign Missions and International Organizations Act*. This will accommodate participation in registered pension plans by employees whose compensation is tax-exempt because of that Act and ensure that the remuneration of these employees can be taken into account for the purposes of the pension adjustment limits in subsection 147.1(8) and any other applicable pension tax rules.

This amendment applies after 1990.

Clause 29

Registered Pension Plans

ITA
147.2(7)

Subsection 147.2 provides rules that govern the deductibility of contributions to registered pension plans (RPPs). Subsection 147.2(7) applies where, as a result of a default or failure under the terms of a letter of credit, the issuer of the letter of credit pays an amount to a registered pension plan. Subsection 147.2(7) generally treats the payment as if it had been an employer contribution and entitles the employer to a deduction for the amount of the payment.

Subsection 147.2(7) is amended, consequential on the introduction of new subsection 147.2(8), to ensure that the wording of those two subsections is consistent.

This amendment applies after Announcement Date.

Registered Pension Plans – Purchase of a Business

ITA
147.2(8)

New subsection 147.2(8) allows the deductibility of eligible contributions made to RPPs under subsections 147.2(1) and (2) and 147.1(18), and under related regulations, to apply appropriately in certain circumstances relating to the purchase of a business. The amendment ensures that contributions made by a participating employer to fund benefits in respect of former employees of a predecessor employer (referred to as the "vendor") are deductible. For example, the amendment is relevant to a situation where the purchase transaction involves the assignment of a defined benefit plan by the vendor to the participating employer (being the purchaser of the vendor's business) and the participating employer takes over the responsibility of funding benefits provided under the plan to the former employees of the vendor. By deeming the former employees of the vendor to be former employees of the participating employer, the amendment allows the participating employer to deduct eligible contributions made to the plan to fund benefits provided to these employees.

Under subsection 147.2(8), a former employee of the vendor is deemed to be a former employee of the participating employer if

- the former employee would not otherwise be an employee or a former employee of the participating employer; and
- benefits are provided to the former employee under a defined benefit provision of the plan in respect of periods of employment with the vendor.

This amendment applies to employer contributions made after 1990.

Clause 30

Registered Pension Plans - Transfers

ITA
147.3(6)(*b*)

Subsection 147.3 provides rules governing the transfer of funds from a registered pension plan (RPP) to another RPP, an RRSP or a RRIF. Subsection 147.3(6) provides rules applicable to the transfer of member contributions under a defined benefit provision of an RPP. Theses rules contemplate only contributions that were actually made to the plan in question. This can create difficulties where member contributions are transferred from one plan to another as a result of a plan reorganization (for example, the splitting of one plan into two or more plans, the transfer of a group of members from one plan to another or the amalgamation of two or more plans). Paragraph 147.3(6)(*b*) is amended to ensure that subsection 147.3(6) and related provisions apply appropriately where member contributions are transferred from one plan to another. With the amendment, member contributions that were made to the former plan will be treated as having been made to the replacement plan for the purpose of permissible transfers and refunds.

For more information, see the commentary to the amendments to subsection 8500(9) of the *Income Tax Regulations*.

This amendment applies to transfers out of registered pension plans that occur after 1999.

Clause 31

Pension Investment Corporations

ITA
149(1)(*o.2*)(iii)(B)

Subsection 248(26) identifies circumstances in which an obligation of a person (referred to as the "debtor") will be regarded as having been issued as a debt obligation of the debtor. This provision applies where a debtor becomes liable to repay borrowed money, or becomes liable to pay an amount (other than interest) as consideration for any property acquired by the debtor or services rendered to the debtor or an amount that is deductible in computing the debtor's income. Although introduced principally for the purposes of the debt forgiveness rules in section 80 and for certain other purposes, this rule has general application for the purposes of the Act.

Under clause 149(1)(*o.2*)(iii)(B), a tax-exempt pension investment corporation cannot issue debt obligations. The amendment to clause 149(1)(*o.2*)(iii)(B) ensures that a pension investment corporation does not lose its tax-exempt status solely by the operation of subsection 248(26).

This amendment applies to taxation years that end after February 21, 1994.

Clause 32

Assessment

ITA

152

Section 152 of the *Income Tax Act* contains rules relating to assessments (including reassessments) of tax, interest and penalties payable by a taxpayer.

Consequential Assessment

ITA

152(4.3)

Where it is necessary, as a result of an assessment or an appeal of a taxpayer for a taxation year, to adjust an amount deducted or included in computing a "balance" that is relevant for another taxation year, subsection 152(4.3) of the Act allows the Minister of National Revenue to reassess the other taxation year beyond its normal reassessment period, as well as to redetermine an amount deemed to have been paid or to have been an overpayment on account of tax in respect of that other year. Subsection 152(4.3) is amended to also allow, under the same conditions, the modification of a refund or other amount payable by a taxpayer for the other year.

This amendment applies to reassessments, redeterminations and modifications in respect of taxation years that relate to changes in balances for other taxation years as a result of an assessment made, or a decision on appeal rendered, after Announcement Date.

Reassessment for Section 119 Credit

ITA
152(6.3)

Section 119 of the Act provides a tax credit in certain circumstances where the “stop- loss” rule in subsection 40(3.7) applies to an individual who ceased to be resident in Canada in a prior year.

Currently, paragraph 152(6)(c.1) provides that assessments to take into account section 119 credits are permitted only where they are made within 3 years after the normal reassessment period, as subsection 152(6) of the Act is to be read together with paragraph 152(4)(b).

New subsection 152(6.3) of the Act is being introduced to ensure that credits under section 119 are available to emigrant taxpayers without regard to the normal or extended reassessment periods. Specifically, new subsection 152(6.3) requires that the Minister of National Revenue reassess a taxpayer's tax for the departure year (and any relevant subsequent year) in order to take into account a deduction claimed under section 119 in respect of a disposition in a post-departure year if

- the taxpayer has filed for the departure year the return of income required by section 150,
- an amount is subsequently claimed by the taxpayer, or on the taxpayer’s behalf, for the departure year as a deduction under section 119, and
- the taxpayer files with the Minister, on or before the filing-due date of the taxpayer for the post-departure year, a prescribed form amending the return.

Existing paragraph 152(6)(c.1) is being repealed as it is no longer necessary.

These amendments generally apply to taxation years that end after October 1, 1996. However, for taxation years that end before Royal Assent, the filing deadline, under new subsection 152(6.3), for the prescribed form amending the departure year return is the filing-due date for the year that includes the day of Royal Assent.

Clause 33

Instalments

ITA
157

Section 157 sets out the required payment dates for corporate income tax instalments and for any balance of corporate income tax payable.

Small Canadian-controlled Private Corporation

ITA
157(1.2)

Subsection 157(1.2) sets out the conditions that a corporation must meet in order to be a small Canadian-controlled Private Corporation and then to be eligible to pay its annual tax liability by quarterly instalments, instead of monthly.

Paragraph 157(1.2)(b) requires that the corporation's taxable capital employed in Canada, determined under subsection 157(1.4) which includes the taxable capital employed in Canada of associated corporations, cannot be more than $10 million, either in the preceding taxation year or in the current taxation year.

Taxable Capital – Small Canadian-controlled Private Corporation

ITA
157(1.4)

Subsection 157(1.4) provides that the reference to the amount in paragraph 157(1.2)(b) is, if a corporation is associated with other corporations, a reference to the sum of taxable capital employed in Canada by each corporation in the group of associated corporations. For this purpose, the taxable capital employed in Canada by the corporation has the meaning assigned by section 181.2 of the Act and includes the taxable capital employed in Canada in the year of any associated corporation.

Paragraphs (*a*) and (*b*) of subsection 157(1.4) are amended to add a reference to section 181.3. If a corporation is a financial institution, its taxable capital employed in Canada is described in subsection 181.3. This amendment ensures the correct measurement, for the purposes of determining the eligibility for payment of quarterly instalments, of the taxable capital employed in Canada by a Canadian-controlled Private Corporation that is a financial institution.

These amendments apply to taxation years that begin after 2007.

Clause 34

Election to Treat Excessive Eligible Dividend Designation as an Ordinary Dividend

ITA
185.1(2)

A corporation that would otherwise be subject to tax under Part III.1 of the Act in respect of an excessive eligible dividend designation can, provided that certain conditions are met, undo all or part of the excessive designation through a mechanism provided in subsections 185.1(2) to (4) of the Act. If these conditions are met, the excessive amount may be deemed to be an ordinary, non-eligible dividend.

The French version of subsection 185.1(2) is amended to provide that this election can be made in prescribed manner ("*selon les modalités réglementaires*") instead of on a prescribed form ("*formulaire prescrit*").

This amendment applies to the 2006 and subsequent taxation years.

Clause 35

Definitions

ITA
204.8(1)

The definitions in subsection 204.8(1) of the Act apply for the purposes of penalties and taxes and other provisions under Part X.3 of the Act that govern labour-sponsored venture capital corporations.

"reserve"

Federally registered labour-sponsored venture capital corporations (LSVCCs) are generally required to invest at least 60 percent of their assets in eligible small businesses. Any amount not invested in eligible small businesses must be held in investments that meet the definition "reserve" in subsection 204.8(1) of the Act. "Reserve" is defined as property described in any of paragraphs (*a*), (*b*), (*c*), (*f*) and (*g*) of the definition "qualified investment" in section 204 of the Act. The definition "reserve" in subsection 204.8(1) is amended to include deposits with credit unions that are "member institutions", as that term is defined in subsection 137.1(5) of the Act.

This amendment applies to taxation years ending after 2006.

“terminating corporation”

Paragraph 204.8(2)(*a*) of the Act, in conjunction with section 204.841 of the Act, imposes a tax on an LSVCC if its articles cease to comply with the requirements in paragraph 204.81(1)(*c*). Some LSVCCs may be required to amend their articles of incorporation in order to complete a merger with another LSVCC. In these cases, the predecessor LSVCCs will terminate and continue as a new fund. The successor LSVCC will purchase, at fair market value, all the assets of each terminating LSVCC. The terminating LSVCCs will redeem the shares of the individual investors, providing, as payment for the redemption, Class A shares of the continuing LSVCC.

Such a transaction may qualify as a "merger" under subsection 204.85(3) of the Act, providing relief from some provisions of the Act that might otherwise apply upon the redemption of shares of an LSVCC. For example, a redemption arising on a merger will generally not result in recovery of the labour-sponsored funds tax credit from the shareholders of the terminating LSVCCs.

The new definition “terminating corporation” applies to an LSVCC (the “predecessor LSVCC”) that undertakes a merger to which subsection 204.85(3) applies with another LSVCC if Class A shares of the continuing LSVCC have been issued to the predecessor LSVCC in exchange for property of the predecessor LSVCC and, within a reasonable period of time after the exchange, the Class A shareholders of the predecessor LSVCC will receive all of those Class A shares of the continuing LSVCC in the course of a wind-up of the predecessor LSVCC.

This amendment is made concurrently with the amendment of clause 204.81(1)(*c*)(ii)(A) of the Act and applies after 2004.

Clause 36

Conditions for Registration

ITA
204.81(1)

Section 204.81 sets out the conditions for the registration of labour-sponsored venture capital corporations (LSVCCs). Subsection 204.81(1) permits the Minister of National Revenue to register a corporation as an LSVCC under Part X.3 if its articles satisfy specified conditions, and other requirements are met.

Subparagraph 204.81(1)(*c*)(ii) sets out the conditions that relate to the authorized capital of an LSVCC. Clause 204.81(1)(*c*)(ii)(A) sets out that the Class A shares of the LSVCC may be issuable only to individuals (other than trusts), trusts governed by registered retirement savings plans, and trusts governed by Tax-Free Savings Accounts.

Clause 204.81(1)(*c*)(ii)(A) is amended to also permit the issuance of Class A shares to a terminating corporation that is being merged with the LSVCC. This amendment is made concurrently with the addition of the definition “terminating corporation” in subsection 204.8(1) of the Act and applies after 2004.

Clause 37

Taxes in respect of Registered Education Savings Plans

ITA
204.94(2)

Tax on Accumulated Income Payments

Part X.5 of the Act imposes a special 20% tax on “accumulated income payments” from registered education savings plans (RESPs). This special tax generally applies where an RESP is terminated because the beneficiary does not pursue post-secondary education and the plan’s accumulated investment income is paid out to the subscriber. The tax is intended to discourage the use of RESPs strictly for tax deferral purposes and is in addition to regular income tax. Subsection 204.94(2) of the Act sets out the charging provision for the tax.

Under section 146.1 of the Act, an RESP may be established on behalf of a child in care by the child's “public primary caregiver”, which is defined in subsection 146.1(1) as the department, agency or institution that maintains the child or the public trustee or curator of the province in which the child resides. Child welfare services are generally administered by a provincial government department. However, some jurisdictions, including Ontario and Nova Scotia, have created independent non-profit organizations to provide these services. While paragraph 149(1)(*l*) of the Act will provide an exemption from regular income tax with respect to any accumulated income payments made to child welfare agencies in these provinces, there is no comparable exemption from Part X.5 tax. Child welfare agencies in Ontario and Nova Scotia may thus be liable for Part X.5 tax on accumulated income payments from RESPs set up on behalf of children under their care.

Subsection 204.94(2) is amended so that it does not apply to a public primary caregiver as defined in subsection 146.1(1) of the Act. This will ensure that all child welfare organizations – regardless of legal structure – are able to reallocate the full amount of any investment income from an RESP that is not used for the beneficiary's post-secondary education to other RESPs established for other children under the organization's care. The amendment is consistent with the fact that non-profit child welfare organizations are already exempt from regular income tax on accumulated income payments and will provide comparable tax treatment for all RESPs established by child welfare organizations.

This amendment applies to the 2007 and subsequent taxation years.

Clause 38

Qualifying Exchange

ITA
211.7(1)

Part XII.5 of the Act imposes a tax on certain dispositions of “approved shares” of a labour-sponsored venture capital corporation (LSVCC). This tax is designed to recover federal tax credits that may have been available to a taxpayer under section 127.4 of the Act upon the original acquisition of the shares.

“qualifying exchange”

The new definition “qualifying exchange” means an exchange by a taxpayer of an approved share, that is part of a series of Class A shares of the capital stock of an LSVCC, for another approved share of the LSVCC, where the only consideration received by the taxpayer on the exchange is the other share, and the rights in respect of the series of shares are identical except for the portion of the reserve (within the meaning assigned by the definition in subsection 204.8(1) of the Act) of the corporation that is attributable to each series.

The definition “qualifying exchange” is added concurrently with amendments to sections 127.4 and 211.8 of the Act to allow for the issuance of exchangeable shares by LSVCCs. This amendment applies after 2003.

For more information regarding the definition “reserve”, refer to the commentary for subsection 204.8(1).

Deemed Issuance Date Qualifying Exchange

ITA
211.7(3)

Section 211.8 of the Act provides a mechanism for the recovery of the federal tax credit under section 127.4 of the Act with respect to the original acquisition of a share issued by a labour-sponsored venture capital corporation (LSVCC). The special tax payable under section 211.8 is generally charged where the share of a federally-registered LSVCC or a revoked corporation is redeemed, acquired or cancelled less than eight years after the share was issued.

New subsection 211.7(3) of the Act is added consequential to the amendment of sections 127.4 and 211.8 to allow for the issuance of exchangeable shares by LSVCCs. New subsection 211.7(3) is added to ensure that a share issued in a qualifying exchange is considered to have been issued on the same date as the share for which it was exchanged. This amendment ensures that the date a share is issued on an exchange, for a qualifying exchange, is not taken into account in determining whether the share has been redeemed, revoked or cancelled within eight years of the date the share was issued.

This amendment also ensures that the date of issuance on an exchange, for a qualifying exchange, is ignored for the purposes of determining the corporation's obligations under Part X.3 of the Act, such as for the purposes of determining penalties, if any, for investment shortfalls under section 204.82 of the Act.

This amendment applies in respect of shares issued after 2003.

Clause 39

Disposition of Approved Share

ITA
211.8(1)

Subsection 211.8(1) of the Act imposes a special tax under Part XII.5, generally if Class A shares of the capital stock of a federally-registered labour sponsored venture capital corporation (LSVCC), that qualify for the federal LSVCC tax credit under section 127.4 of the Act, are redeemed prior to the expiry of a minimum period.

Subsection 211.8(1) is amended, concurrently with amendments to sections 127.4 and 211.7 of the Act, to allow for the issuance by LSVCCs of Class A shares that are exchangeable shares in certain circumstances. In particular, where the new share is issued by an LSVCC as part of a "qualifying exchange" (as defined in subsection 211.7(1) of the Act) and is another Class A share of the LSVCC, the disposition of the original share by the shareholder will not result in the application of the special Part XII.5 tax.

This amendment applies in respect of shares redeemed, assigned or cancelled after 2003.

Income Tax Regulations

Clause 40

Retirement Compensation Arrangements - Exceptions

ITR
6802(*h*)

A retirement compensation arrangement (RCA) is defined in subsection 248(1) of the Act as a plan or arrangement under which an employer makes payments to another person, called a custodian, in order that benefits may be paid to an employee or any other person after the employee retires or otherwise ceases employment with the employer. RCAs are subject to a special tax regime under section 207.5 of the Act which generally removes the tax deferral advantages that were associated with the plans before the introduction of the RCA rules. The RCA definition is subject to a number of exclusions including, at paragraph (*n*) of the definition, a "prescribed plan or arrangement". For this purpose, the list of prescribed plans or arrangements is contained in section 6802 of the *Income Tax Regulations*.

Regulation 6802 is amended to add a new trust that was established in 2009 by Air Canada in relation to pension funding. On June 14, 2009, Air Canada signed a memorandum of understanding (MOU) with the five unions that represent its workers to address pension funding requirements. Pursuant to this MOU, the unions agreed that certain payments required to fully fund Air Canada's pensions could be deferred. Regulatory changes to the *Pension Benefits Standards Regulations, 1985* were made to accommodate this arrangement, which was determined to be important to the financial viability of Air Canada.

As part of this MOU, the parties agreed to establish a trust. Shares of Air Canada would be issued to the trust, which would hold the shares on behalf of the unions. The unions could then direct that the shares be sold at a later time. Under the MOU and the terms of the trust, the proceeds would then be contributed to the Air Canada pension plans in accordance with a formula agreed to by the parties.

Applying the RCA rules to a trust of this nature would not be consistent with the objectives of the RCA rules, which are in general terms to prevent tax deferral in relation to employee retirement savings beyond the registered pension plan and registered retirement savings plan limits.

This amendment applies after 2008.

Clause 41

Permanent Establishment

ITR
8201

Section 8201 of the Regulations defines the meaning of "permanent establishment" for the purposes of various provisions of the Act. This section is amended to add a reference to the definition "qualified Canadian transit organization" in subsection 118.02(1) of the Act. This section is also amended to remove the reference to subsection 34.2(6) of the Act, which does not have application for the 2009 and subsequent taxation years.

This amendment applies to the 2009 and subsequent taxation years.

Clause 42

Registered Pension Plans – Definitions

ITR
8500(1)

"predecessor employer"

Subsection 8500 of the Regulations provides a number of definitions relating to registered pension plans (RPPs). The definition of "predecessor employer" is amended so that provisions pertaining to RPPs apply appropriately in the context of certain purchases of businesses. In particular, with this amendment an employer will be a "predecessor employer" in relation to a particular employer (or to another employer who subsequently becomes the predecessor employer of the particular employer) if the employer has disposed of all or part of its business or assets to the particular employer and all or a significant number of its employees have become employees of the particular employer.

This amendment applies after Announcement Date, except that it does not apply to benefits that were provided before that date.

ITR
8500(1.2)

Under new subsection 147.2(8), a former employee of a predecessor employer in relation to a participating employer is deemed to be a former employee of the participating employer in certain circumstances. New subsection 8500(1.2) of the Regulations provides that the amended definition of "predecessor employer" in subsection 8500(1) of the Regulations applies for the purpose of subsection 147.2(8).

For more information, see the commentary to new subsection 147.2(8).

This amendment applies to employer contributions made after 1990.

Registered Pension Plans – Business Re-organizations

ITR
8500(9)

New subsection 8500(9) will accommodate certain transfers and refunds from registered pension plans that occur after business re-organizations. The new subsection will ensure that, for the purposes of specified transfers or refunds of a member's contributions made to a registered pension plan, the member's contributions will include amounts contributed to a former defined benefit provision of a registered pension plan if his or her benefits under the former provision have been replaced by benefits under the current defined benefit provision.

This new rule will deem member contributions under the former provision to be contributions under the current provision if

- assets have been transferred from the former provision to the current provision under section 147.3(3) of the Act; and
- the current provision replaces the benefits of all or a significant number of the members of the former provision.

For more information, see the related commentary to paragraph 147.3(6)(b) of the Act.

This amendment applies after 1999.

Clause 43

Registered Pension Plans – Permitted Contributions

ITR
8502(*b*)

Paragraph 8502(*b*) of the Regulations lists the contributions that are permitted to be made to a registered pension plan. Paragraph 8502(*b*) is amended to add a reference to the Air Canada trust described in paragraph 6802(*h*) of the Regulations. This will allow pension contributions made by the trust to Air Canada pension plans to be accepted without jeopardizing the registration of the Air Canada pension plans. For more information, please refer to the commentary on new paragraph 6802(*h*) of the Regulations.

This amendment applies after 2008.

Clause 44

Registered Pension Plans – Previous Employment

ITR
8504(2.1)

Subsection 8504(2) of the Regulations specifies how to compute the highest average indexed compensation of a plan member for the purpose of a defined benefit provision of a registered pension plan. The highest average indexed compensation is relevant in determining, under subsection 8504(1), the maximum lifetime retirement benefits that may be paid to the member.

New subsection 8504(2.1) accommodates situations where part or all of an employee's highest compensation was earned with a predecessor employer. Under new subsection 8504(2.1), where the pensionable service of a plan member includes a period of employment with a predecessor employer (see also new subsection 147.2(8)), the predecessor employer is deemed to have participated under the defined benefit provision for the benefit of the member. These amendments ensure that compensation received by the plan member for periods of employment with the predecessor employer is taken into account for purposes of computing the highest average compensation, and hence for purposes of the maximum lifetime retirement benefits payable to the member.

This amendment applies after 1990.