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# CURRENT DEVELOPMENTS

**Bessner Gallay Kreisman** S.E.N.C.R.L. • L.L.P.



Comptables Agréés • Chartered Accountants

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## QUÉBEC BUDGET

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### INTRODUCTION

Finance Minister Michel Audet delivered the Québec government's 2005-2006 Budget before the National Assembly today. A summary of the more significant tax and related measures follows.

#### MEASURES CONCERNING INDIVIDUALS

##### NEW \$500 DEDUCTION FOR WORKERS

Starting in 2006 individuals will be able to deduct, in the calculation of their income for a given taxation year, an amount equal to 6% of their eligible earned income for the year, to a maximum of \$500.

##### ENHANCEMENT OF TAX ASSISTANCE FOR NATURAL CAREGIVERS

###### Supplement for handicapped children

The tax credit respecting a dependent child with an impairment will be replaced, as of the 2006 taxation year, by an improved supplement for handicapped children.

###### Refundable tax credit for natural caregivers of adults

The various measures for natural caregivers of adults will be replaced by a refundable tax credit, as of the 2006 taxation year. The new tax credit, for each eligible relative housed, will consist of a universal basic amount of \$550, plus a supplement of \$450 that may be reduced on the basis of the eligible relative's income for the year.

## TAX CREDITS FOR MEDICAL EXPENSES

### Tightening of the list of eligible medical expenses

The tax legislation will be amended to provide that expenses (including travel) incurred after April 21, 2005 to obtain medical, paramedical or dental services for purely cosmetic purposes (for example liposuction, facelifts and teeth whitening) will no longer be considered eligible expenses for the purposes of the tax credit for medical expenses. Also, the portion of all expenses incurred for eyeglass frames by a taxpayer or the taxpayer's spouse after April 21, 2005 will be limited to \$200 per person.

### Clarifications respecting certain eligible medical expenses

The tax legislation will be amended to provide that, as of the 2005 taxation year, health plans that provide moderate coverage of expenses ineligible for the tax credit for medical expenses can qualify as private health services plans if their main purpose is to cover eligible expenses, so that the premium will qualify as a medical expense.

The notion of "practitioner" will be clarified. Lists will be provided of recognized professions and of other professions in which only certain services will be eligible.

### Refundable tax credit for medical expenses

The maximum amount of \$543 will be raised to \$750 as of the 2005 taxation year.

## MEASURES CONCERNING BUSINESS

### REDUCTION OF THE TAX ON CAPITAL

The rate of the tax on capital of corporations that are not financial institutions, currently 0.6%, will be gradually reduced to 0.29%. These rate reductions will take effect on January 1 of each year.

#### RATE OF THE TAX ON CAPITAL

	Current	2006	2007	2008	2009
Per cent	0.6	0.525	0.49	0.36	0.29

The rate applicable for a taxation year that straddles two calendar years will be a weighted rate.

### Capital tax credit

A corporation other than a financial institution that makes an eligible investment in new manufacturing and processing equipment may claim a non-refundable capital tax credit, for such taxation year, equal to 5% of the amount of such eligible investment.

For each taxation year, the non-refundable portion of the capital tax credit that exceeds the tax on capital otherwise payable may be carried over to subsequent taxation years.

New manufacturing and processing equipment included in class 43, used within a period of at least 730 days, solely in Québec and mainly in the course of carrying on a business, will be considered eligible investments. These assets will have to be acquired after April 21, 2005 and before January 1, 2008.

A corporation will be allowed to apply this capital tax credit against its instalments.

### Technical change concerning the calculation of total assets

The tax legislation will be amended to stipulate that a corporation must neither include nor deduct, in calculating the corporation's assets, an amount shown in its financial statements resulting from an operation between it and a partnership or a joint venture of which it is a member. The application of this change will be declaratory.

**As always, readers are reminded that while budget proposals are customarily given the effect of law immediately, the amending legislation, when ultimately adopted by the National Assembly, may be altered to some degree.**

## Application of the minimum 120-day holding period rule to bonds issued by partnerships

The tax legislation will be amended to stipulate that bonds issued by a partnership will be subject to the minimum holding period of 120 days including the end of the taxation year. This change will apply to taxation years ending after April 21, 2005.

## CORPORATE INCOME TAX RATES

The tax rate applicable to active business income will be raised gradually, from 2006 to 2009, by 3 percentage points.

However, Canadian-controlled private corporations (CCPCs) will be entitled to a reduction in their tax rate. This reduction will apply only to the first \$400,000 of annual income from an eligible business carried on by a CCPC and must be shared among associated corporations.

The tax rate applicable for a taxation year that straddles two calendar years will be a weighted tax rate.

Corporations with paid-up capital greater than \$15 million will not be able to claim this reduction. The reduction will be phased out for paid-up capital between \$10 million and \$15 million. Paid-up capital for this purpose will include paid-up capital of associated corporations.

## TAX RATES FOR ACTIVE BUSINESS INCOME OF CCPCs

(Per cent)	Current	2006/ 2007	2008	2009
First \$400,000	8.9	8.5	8.5	8.5
Remainder	8.9	9.9	11.4	11.9

## TAX ASSISTANCE FOR RESEARCH AND DEVELOPMENT

The tax legislation will be amended so that the rate that a CCPC that qualifies as an SME (small business) can claim will vary from 17.5% to 37.5% on the first \$2 million of R&D spending.

This change will apply to R&D expenditures incurred after April 21, 2005 for R&D work done after that day.

## REFUNDABLE TAX CREDIT FOR DESIGN

The tax legislation will be standardized for the purposes of the two components of the design tax credit so that the gross income of the business that is carried on by a corporation will have to be at least \$150,000 for such corporation to be eligible.

The in-house component of this tax credit will be broadened to the entire industrial sector and the number of designers will no longer be limited.

In addition, the salary paid to an eligible patternmaker in the fashion sector will now be included in the base of the in-house component of the design tax credit, but will be capped at \$40,000.

The scope of the external component will be broadened.

These changes will apply to an eligible expenditure incurred by an eligible corporation after April 21, 2005 regarding work for an eligible design activity or an eligible pattern drawing activity done after that day.

To be eligible for the in-house component or the external component of the design tax credit concerning the fashion sector, a corporation must show that 20% of its total production (50% for the industrial sector) for the preceding fiscal year is attributable to goods that the corporation made itself in Québec.

## SME GROWTH STOCK PLAN

The Québec Stock Savings Plan will not be revived but will be wound down gradually and is replaced by the SME Growth Stock Plan. This new plan will end on December 31, 2009. A single deduction rate, 100% of the adjusted cost of eligible shares, will apply. The annual deduction cap of 10% of the individual's total income for a year that applied under the former QSSP will apply under the new plan.

## OTHER CHANGES

### INCREASE IN THE DEPRECIATION RATE OF WORKS OF ART BY A CANADIAN ARTIST

The depreciation rate of works of art by a Canadian artist will be raised from 20% to 33⅓%. This change will apply to works of art acquired after April 21, 2005.

### CAPITAL GAINS EXEMPTION FOR THE ESTABLISHMENT OF A SERVITUDE

The tax legislation will be amended to stipulate that the gain resulting from the establishment of a real servitude affecting an immovable may give rise to a capital gains exemption for qualified farm property or a capital gains exemption for a principal residence, where the immovable concerned satisfies the criteria for qualified farm property or a principal residence. This change will apply in respect of a real servitude established after April 21, 2005.

### FEDERAL BUDGET SPEECH OF FEBRUARY 23, 2005

Québec's tax legislation and regulations will be amended to incorporate most of the tax measures announced in the recent Federal Budget.

## DATES TO REMEMBER



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|----------------------|---|
| <b>May 2, 2005</b>   | 2004 Personal income tax returns filing due date.   |
| <b>June 15, 2005</b> | Second quarterly personal income tax instalment for 2005 due.   |
| <b>June 15, 2005</b> | 2004 Personal income tax returns filing due date for taxpayers (and their spouse) with income from self-employment. |

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215 avenue Redfern, Suite 300, Westmount, Québec H3Z 3L5  
Tel: 514-908-3600 Fax: 514-908-3630 Email: [admin@bgk.ca](mailto:admin@bgk.ca)  
600 Terry Fox Dr., Suite 210, Kanata, Ontario K2L 4B6  
Tel: 613-836-8228 Fax: 613-836-8338 Email: [ottawa@bgk.ca](mailto:ottawa@bgk.ca)

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