

## Tax Highlights from the February 21, 2006 B.C. Budget

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### Introduction

On Tuesday, February 21, 2006, the British Columbia Minister of Finance, the Honourable Carole Taylor, introduced the province's 2006 budget. According to the Minister, the B.C. economy remains strong, with a low unemployment rate and strong business investment. As expected, the budget is balanced, with an estimated surplus of \$600 million for 2006/07, \$400 million for 2007/08 and \$150 million for 2008/09. These projected surpluses are based on an economic growth forecast of 3.3% for 2006 and 3.1% in each of the following two years. The budget includes a forecast allowance of \$850 million for 2006/07 to cushion the fiscal plan from contingencies, such as a sudden drop in commodity prices and other unexpected events. Total government expenditures are forecast to increase 6.9% over the next few years.

The budget does not change personal or corporate income tax rates, apart from enhancing B.C.'s dividend tax credit to parallel the proposed federal credit. However, the budget does contain a number of tax amendments, outlined below. For help determining how these changes affect you or your company, please contact your PricewaterhouseCoopers adviser, or:

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### Retail Sales Tax

#### Software

- The purchase of custom software or custom modified software is now exempt from tax when purchased as part of a business as a going concern. For the exemption to apply, the vendor cannot retain any rights or interests in the software being transferred. The exemption applies only when the entire business or business line is sold.
- Most services provided to software have been exempt from tax. Services such as installing, configuring, repairing or restoring were subject to tax. Now all such services provided to software are exempt. Tax continues to apply to the purchase of computer hardware and software, including software updates, unless the software qualifies as custom or custom-modified software.

#### Production Machinery and Equipment Exemption

- The exemption for production machinery and equipment (PM&E) is expanded to apply to businesses that use machinery and equipment more than 50% of the time to provide contract manufacturing services to a qualifying manufacturer.
- The exemption for pre-manufactured parts to repair and maintain exempt machinery and equipment is expanded to include parts purchased or leased by qualifying manufacturers to assemble qualifying machinery or equipment. Certain materials, such as lumber and sheet metal, remain subject to tax.

- The definition of “manufacture” is clarified to include:
  - fabrication or manufacture of tangible personal property to create a new product that is substantially different from the material or property from which it was made;
  - processing tangible personal property by performing a series of operations or a complex operation that results in a substantial change in the form or physical or chemical characteristics of the tangible personal property; and
  - extraction or processing of minerals, petroleum or natural gas.

Excluded from the definition of “manufacture” is the transformation of tangible personal property from gaseous, liquid or solid state to another one of these states by means of a change in temperature or pressure unless it is a step in a qualifying activity.

The new definition is considered a “clarification,” retroactive to July 31, 2001. Another clarification ensures that conventional office equipment does not qualify for the exemption.

#### **Vehicle Surtax Thresholds for Passenger Vehicles**

- The threshold for the surtax on passenger vehicles is increased to \$55,000 from \$49,000. The tax rates are graduated and reach 10% on passenger vehicles valued at \$57,000 or more. For leased passenger vehicles, the new vehicle surtax thresholds apply to the first lease payment due after February 22, 2006.

#### **Alternative Fuel Vehicles**

- A refund is provided for tax paid on parts and labour to convert shuttle buses and passenger buses to operate as hybrid vehicles. Shuttle and passenger buses are eligible for refunds of \$5,000 and \$10,000, respectively.

#### **Multi-jurisdictional Vehicles**

- A full tax refund of the B.C. portion of the annual multi-jurisdictional vehicle tax is available if the vehicle is primarily leased as a short-term rental vehicle to the public for the transportation of goods and if tax is paid on the vehicle rental by lessees.

#### **Application of Tax on Heat**

- Electricity, natural gas, manufactured gas, fuel oil and steam are exempt from tax when purchased for residential use. A clarification, effective February 21, 2000, is that heat is tangible personal property and qualifies for the residential-use exemption.

#### **Farmers’ Exemptions**

- Sand used for livestock bedding and heat are exempt from tax when purchased by a qualifying bona fide farmer. Hoop house frames are now specifically excluded from the exemption.

## **Income Tax**

#### **Enhanced Dividend Tax Credit**

- B.C. will introduce an enhanced dividend tax credit in conjunction with the proposed federal reduction in personal income taxes on certain dividends, announced November 23, 2005.

#### **Medical Expenses Tax Credit**

- For 2005 and subsequent years, the maximum annual amount of medical expenses that can be claimed on behalf of dependent relatives is increased from \$5,000 to \$10,000 per dependant.

#### **Mining Flow-through Share Tax Credit**

- The program allows individuals who invest in flow-through shares to claim a non-refundable tax credit equal to 20% of the B.C. flow-through mining expenditures renounced to them by the corporation issuing the flow-through shares. B.C. flow-through mining expenditures are specific exploration expenses incurred in the province in respect of qualifying grassroots surface exploration that is considered most likely to lead to the discovery of new mineral resources. The expiry date for the program, and for eligible expenditures for the credit, is extended by three years to December 31, 2008.

#### **Royalty and Deemed Income Rebate**

- B.C. will eliminate the royalty and deemed income rebate for tax years starting after 2006. The royalty and deemed income rebate is an income tax provision that the province implemented to differentiate B.C. income taxation from the federal resource allowance program and specifically allow for the deduction of taxes paid under the *Mineral Tax Act*. The federal government will phase out the resource allowance and provide for the full deductibility of provincial resource royalties and taxes by 2007. By eliminating the royalty and deemed income rebate, B.C.’s taxation of the resource sector will be harmonized with the federal system for 2007 and future years.

### Film and Television Tax Credits

- As announced on January 20, 2006, the enhanced tax credit rates for film and video productions are extended to 2008. The basic Film Incentive B.C. Tax Credit rate remains 30% for productions beginning before April 2008 and the basic Production Services Tax Credit remains 18% for productions that begin before June 2008.
- During 2007 the province will review the tax credit programs and make a decision whether to continue the tax credits beyond 2008 and if so at what rates.

### Tax Credit Filing Requirements

- Filing requirements, including deadlines for claiming various income tax credits, are clarified to be consistent with existing requirements under the B.C. *Income Tax Act* and with recent federal amendments.

## International Financial Activity Act

- The calculation of income used to determine the tax refund under the *International Financial Activity Act* is amended effective September 1, 2004 to remove the interest adjustment. The adjustment was designed to limit interest expenses in the calculation of revenue from international loans. The adjustment was considered too restrictive and is removed retroactive to the commencement of the Act.

## Property Tax

### Property Transfer Tax

- Under a clarified definition, a “family farm corporation” is a corporation of which the principal activity is farming farm land and no shareholder is a corporation.
- An exemption is provided for amalgamations under the *Society Act* similar to the existing exemption for amalgamations under the *Business Corporation Act* and similar federal and provincial statutes.
- The exemption for the transfer of a “family farm” and a “recreational residence” from the estate of a deceased to the Public Guardian on behalf of a minor is clarified.
- If both property transfer tax and Social Services Tax have been paid with respect to the same taxable transaction, a refund of property transfer tax is available.

### Home Owner Grant Act

- Starting with the 2006 taxation year:
  - the basic and additional home owner grants are increased by \$100, to \$570 and \$845, respectively.
  - the phase-out threshold of the home owner grant is increased from \$685,000 to \$780,000. Properties valued above the threshold will continue to have the grant reduced by \$5 for every \$1,000 of assessed value.
  - an additional \$275 grant is available under certain conditions for those with a disability or living with a relative or spouse with a permanent disability.

## Motor Fuel Tax

- Authorized uses of coloured fuel are expanded to include all unlicensed motor vehicles not used on a highway. This includes such vehicles as unlicensed dump trucks, all terrain vehicles and snowmobiles.
- The partial tax refund for tax paid on fuel used in stationary motor vehicles is expanded. The eligible purposes now include rotating the drum and pumping ready mixed concrete, operating mobile cranes and operating a hydraulic arm mounted on a logging truck.
- Biodiesel is now included in the definition of motive fuel and marine diesel fuel. The amendment ensures the tax is imposed at the appropriate clear or coloured fuel tax rate when biodiesel is not blended with diesel fuel.

## Hotel Room Tax

- Lodging let to the same person for a continuous period of more than one month is exempt. Previously, the exemption period required two continuous months.
- Lodging for which the charge is \$30 or less per day or \$210 per week is exempt from tax. Previously, the threshold was \$20 per day or \$140 per week.

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