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"The purpose of my budget tonight is to take positive and responsible action to deal with the problems which face the Canadian economy in a very troubled world."–Jean Chrétien.

Federal compensation for cuts in provincial sales tax – budget

Finance Minister Jean Chrétien, presenting his budget to the House of Commons on April 10, announced the Federal Government's offer to compensate provinces to effect a six-month reduction in their retail sales tax rates. As a result, Newfoundland has reduced its taxes from 11 to 8 per cent; New Brunswick, Nova Scotia and Prince Edward Island from 8 to 5 per cent; Ontario from 7 to 4 per cent; British Columbia from 7 to 5 per cent; Manitoba from 5 to 2 per cent; and Saskatchewan from 5 to 3 per cent. At press time, Quebec was still considering the federal offer. Alberta, the Yukon and the Northwest Territories are not affected since their jurisdictions do not levy a sales tax.

Mr. Chrétien announced that the federal deficit this fiscal year would rise to \$11.5 billion from \$8.5 billion in the 1977-78 fiscal year.

Some of the other proposed changes are in the following areas:

Research and development

Since 1961, the Income Tax Act has allowed a 100 percent write-off of current and capital research and development (R & D) expenditures in the year they are made. This fast write-off was supplemented last year by an investment tax credit on current and capital R & D outlays varying by region from 5 to 10 per cent.

As an added stimulus, it is now proposed to introduce for a ten-year period beginning in 1978 a special allowance of 50 per cent of the increase in R & D activity. The allowance, which is deductible in computing income, would apply to the amount by which a company's R & D expenditures in a year exceed the company's average R & D expenditures over the previous three-year period. The effect would be to reduce a company's after-tax cost of each additional dollar spent on R & D to as low as 20 cents.

Because of the incremental nature of the new incentive, its impact on tax revenues will depend upon the extent to which industry responds. However, it is estimated that in the initial years the reduction in federal revenue will be about \$50 million a year. Provincial tax revenue would also be reduced in those provinces that have tax collection agreements with Ottawa and those outside the collection agreement which decide to adopt these new provisions.

Energy

Additional tax incentives are being introduced to stimulate the production of energy, in the immediate as well as long term, particularly by new methods that increase the rate of recovery from known oil deposits. Two changes are made in the depletion allowance.

First, the cost of machinery, equipment and other facilities acquired after April 10 for use in an enhanced or "tertiary" recovery system will be eligible to earn a depletion allowance of \$1 for each \$2 of expenditure as compared to the normal depletion allowance earning rate of \$1 for \$3. (An enhanced recovery system is one that uses new technology to recover additional marketable oil from either conventional or heavy oil fields.)

Second, the amount of the depletion allowance that may be claimed each year will be increased for depletion earned on certain investments in non-conventional oil. At present the maximum deduction for depletion is limited to 25 per cent of resource profits. This limit will be increased, effective this year, for depletion earned on certain eligible expenditures to 50 per cent of total taxable income – that is, resource profits and any other profits of the corporation.

Rail transportation

Major investments are needed in the railway transportation system to improve efficiency and restrain cost increases. Therefore an additional straight line

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