budget 2011: accelerated capital cost allowance for the M&P and clean energy sectors

Budget 2011 builds on prior federal Government initiatives that have provided tax incentives to the manufacturing and processing and clean energy sectors in the form of accelerated capital cost allowance ("**CCA**") rates.

Taxpayers may generally claim CCA in respect of a broad range of capital assets at prescribed rates that are typically based on the useful life of the assets. Accelerated rates of CCA provide a financial benefit to taxpayers by permitting a greater percentage of the cost of eligible capital assets to be deducted in the years immediately following the acquisition of the assets when computing taxable income.

manufacturing and processing

Initially introduced as a temporary incentive in the 2007 Budget, Budget 2011 proposes to extend by 2 years the accelerated rate of CCA that may be claimed in respect of machinery and equipment acquired by a taxpayer primarily for use in Canada for the manufacturing and processing of goods for sale or lease. Under Class 29 of Schedule II of the *Income Tax Regulations* (the "**Regulations**"), such machinery and equipment is eligible for an accelerated CCA rate of 50 percent on a straight line basis (subject to the application of the "half-year rule"). Budget 2011 proposes that the accelerated CCA rate will be available in respect of such machinery and equipment acquired by a taxpayer after March 18, 2007 and before 2014.

clean energy generation

Class 43.2 of Schedule II of the Regulations provides for an accelerated CCA rate of 50 percent, on a declining balance basis, in respect of specified clean energy generation and conservation equipment that was acquired by a taxpayer after February 22, 2005 and before 2020.

In an attempt to encourage the productive use of thermal energy that would otherwise be wasted to generate electricity, Budget 2011 proposes to expand the list of assets that fall within Class 43.2 of Schedule II of the Regulations to include certain equipment that is used by a taxpayer, or by a lessee of a taxpayer, to generate electrical energy in a process in which all or substantially all of the energy input is from waste heat ("**Eligible Equipment**").

Budget 2011 proposes that Eligible Equipment will include electrical generating equipment, control, feedwater and condensate systems, and other ancillary equipment. Buildings or other structures, heat rejection equipment (*e.g.*, condensers and cooling water systems), transmission equipment, distribution equipment and systems that use chlorofluorocarbons (CFCs) or hydrochlorofluorocarbons (HCFCs) will not be eligible for inclusion in amended Class 43.2. Also excluded from the proposed expansion of Class 43.2 is equipment that uses heat from a gas turbine in the first stage of a combined cycle system because, subject to certain energy efficiency thresholds, such equipment already qualifies for inclusion in Class 43.2.

The Government is of the view that this tax incentive will increase investment in equipment that uses thermal energy to generate electricity, which, in turn, can displace the consumption of energy from other power generating sources such as fossil fuels and thereby assist Canada in meeting its target, set out in the Federal Sustainable Development Strategy, of reducing greenhouse gas emissions levels by 17 percent by 2020.

The proposals regarding the accelerated rate of CCA in respect of clean energy generation equipment will apply to Eligible Equipment acquired on or after March 22, 2011.

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For additional information on the proposals announced in the 2010 Budget that expanded Class 43.2 to include: (i) heat recovery equipment used in a broader range of applications; and (ii) distribution equipment used in district energy systems that rely primarily on ground source heat pumps, active solar systems or heat recovery equipment, please see our March 2010 bulletin entitled "budget 2010: significant tax changes announced affecting the development of district energy systems".

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a cautionary note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.