Cassels

Budget 2024: Did the Federal Government Get the Balance Right?

April 17, 2024

Introduction

On April 16, 2024 (Budget Day), the Honourable Chrystia Freeland, Deputy Prime Minister and Finance Minister, delivered the 2024 federal budget titled, “Fairness for Every Generation” (Budget 2024).

Although Budget 2024 did not increase federal corporate or personal tax rates under the *Income Tax Act* (Canada) (Tax Act), significant tax measures were announced in Budget 2024 aimed at addressing the federal government's (Government's) theme of tax fairness, notably:

- increasing the capital gains inclusion rate to two-thirds, subject to certain thresholds for individuals;
- boosting the lifetime capital gains exemption (LCGE) to $1.25 million;
- introducing a new Canadian Entrepreneurs' Incentive (Entrepreneurs’ Incentive);
- revising certain alternative minimum tax (AMT) proposals previously announced in Budget 2023;
- providing details on the conditions necessary to qualify for the $10 million capital gains exemption on the sale of Canadian businesses to Employee Ownership Trusts (EOTs);
- outlining the design and implementation of various clean energy measures, including the Clean Electricity Investment Tax Credit (Clean Electricity ITC);
- bolstering various anti-avoidance rules; and
- implementing the Crypto-Asset Reporting Framework (CARF) developed by the Organisation for Economic Co-operation and Development (OECD) in Canada to facilitate the international exchange of tax information relating to crypto-assets.

The following is a summary of select income tax measures announced in Budget 2024 that are most relevant to taxpayers, including:

- Personal Tax Measures;
- Business Income Measures;
- International Tax Measures;
- Administrative Tax Measures; and
- Previously Announced Income Tax Measures

Cassels

Personal Tax Measures

Capital Gains Inclusion Rate

Currently, the inclusion rate for capital gains is 50% (and has been since 2000), such that generally a taxpayer is only taxed on half of any capital gain realized. The same applies to capital losses.

Budget 2024 proposes to increase the capital gains inclusion rate from 50% to two-thirds for (a) corporations and trusts, and (b) individuals on the portion of capital gains realized in the year that exceed $250,000. Capital gains realized on the disposition of a principal residence remain unaffected by this proposed measure. The increased inclusion rate would apply to capital gains realized on or after June 25, 2024.

The $250,000 threshold would apply to capital gains realized by an individual, either directly or indirectly via a partnership or trust, net of any:

- current-year capital losses;
- capital losses of other years carried back or forward to reduce current-year capital gains; and
- capital gains in respect of which the LCGE, the proposed EOT Exemption, or the proposed Entrepreneurs' Incentive is claimed.

Employees that claim the stock option deduction would be provided a one-third deduction of the taxable benefit to reflect the increased capital gains inclusion rate but would be entitled to a deduction of 50% of the taxable benefit up to a *combined* limit of $250,000 per taxation year for both employee stock options and capital gains.

Net capital losses of prior years would continue to be deductible against taxable capital gains in the current year by adjusting their value to reflect the new inclusion rate of the capital gains being offset. In other words, capital losses realized prior to the rate change would fully offset an equivalent capital gain realized after the rate change.

For tax years that begin before and end on or after June 25, 2024, which will be the case for all individuals (other than certain trusts), two different inclusion rates would apply. As a result, transitional rules will be required to separately identify capital gains and losses realized before June 25, 2024 (Period 1) and those realized on or after June 25, 2024 (Period 2).

The annual $250,000 threshold would be fully available in 2024 (i.e., not prorated) and would apply only in respect of net capital gains realized in Period 2.

The Government will release design details with respect to the increased inclusion rate in the coming months.

Over the last few years, there has been speculation about whether the Government would increase the capital gains inclusion rate in order to manage the huge deficit coming out of the pandemic. But after the comprehensive draft legislation that came out in 2023, including the new general anti-avoidance rule (GAAR), the Budget 2024 proposals seem to have taken the tax community by surprise, perhaps since some of the more recent tax changes in the last year were already aimed at replenishing the Government's coffers.

The fact that the new inclusion rate does not come into effect until June 25, 2024, leads many to wonder whether taxpayers who may be sitting on large unrealized gains should crystallize prior to that date. The ability to lock in at lower capital gains rates (currently 26.8% for individuals, versus 35.7% as of June 25, 2024, for Ontario residents taxed at the highest marginal rate), will need to be measured against paying capital gains tax earlier than one might have otherwise done. Of the estimated $19.3 billion in tax revenue over the next five years as a result of this tax measure, $6.9 billion is estimated to be earned in 2024, leading one to infer that the Government is anticipating that many taxpayers will choose to trigger their capital gains prior to June 25, 2024.

However, it is important not to lose sight of the new GAAR, the legislative proposals for which are currently before Parliament in Bill C-59, (specifically in relation to the new economic substance test) when considering any planning to trigger a capital gain in the near future. Moreover, the enhanced AMT rules, which are intended to be effective as of January 1, 2024, should also be considered when triggering a large amount of capital gains at the current 50% inclusion rate.

Lifetime Capital Gains Exemption

The LCGE generally provides individuals with an exemption on capital gains realized on the disposition of "qualified small business corporation shares" or "qualified farm or fishing property" (eligible capital gains). The amount of the LCGE is $1,016,836 in 2024 and indexed to inflation.

Budget 2024 proposes to increase the LCGE to up to $1.25 million of eligible capital gains. This measure would apply to dispositions that occur on or after June 25, 2024 and be indexed to inflation starting in 2026.

While the proposed amendments to the LCGE appear to provide some additional shelter for taxpayers, the overall tax relief (which Budget 2024 expects will result in a decrease in tax revenue of $1 billion over the next five years) may not appear to be that substantive, especially when taking into account the proposed increase to the capital gains inclusion rate.

Canadian Entrepreneurs’ Incentive

Budget 2024 proposes the new Entrepreneurs' Incentive, intended to encourage entrepreneurship by reducing the tax rate on capital gains on the disposition of qualifying shares by eligible individuals. The Entrepreneurs' Incentive would provide for a capital gains inclusion rate of one-third on up to $2 million of capital gains per eligible individual over their lifetime. The limit would begin at $200,000 starting on January 1, 2025 and be phased in annually by increments of $200,000 to ultimately reach a value of $2 million by January 1, 2034. This measure is intended to apply in addition to the existing LCGE regime and for dispositions that occur on or after January 1, 2025. For greater certainty, an eligible individual would first benefit from the existing LCGE on a disposition of qualifying shares and then rely on the Entrepreneurs' Incentive to have a portion of the remaining gain taxed at a capital gain inclusion rate of one-third.

A qualifying share is a share of a corporation that satisfies all of the following conditions:

- at the time of disposition, it was a share of a "small business corporation" owned directly by the claimant of the Entrepreneurs' Incentive;
- throughout the 24-month period immediately prior to the disposition, it was a share of a Canadian-controlled private corporation (CCPC) and more than 50% of the fair market value of the assets were:
    - used principally in an active business carried on primarily in Canada by the CCPC or a related corporation;
    - certain shares or debts of connected corporations; or
    - a combination of the above;
- the claimant was a founding investor at the time the corporation was initially capitalized and held the share for at least five years prior to disposition;
- at all times since the initial share subscription until immediately prior to disposition, the claimant directly owned shares amounting to more than 10% of the fair market value of all of the shares of the corporation, giving the claimant more than 10% of the votes that could be cast at an annual shareholders' meeting;
- throughout the five-year period immediately prior to disposition, the claimant was actively engaged on a regular, continuous, and substantial basis in the activities of the business;
- the share does not represent a direct or indirect interest in a professional corporation, a corporation whose principal asset is the reputation or skill of one or more employees, or a corporation that carries on certain types of business (including operating in the financial, insurance, real estate, food and accommodation, arts, recreation, or entertainment sector or providing consulting or personal care services); and
- the share must have been obtained for fair market value consideration.

While it may appear that the Entrepreneurs' Incentive could potentially create some tax savings to business

owners, only those who are founding investors of a corporation will be eligible, thereby excluding anyone who becomes a shareholder after the corporation has been initially capitalized (such as investors who come in at additional rounds of funding). This will also prove problematic for family-owned businesses who may introduce the next generation as shareholders at a later date as part of a business succession plan. When taking the foregoing into consideration, combined with the significant number of carve-outs to the types of business eligible for the Entrepreneurs' Incentive, the number of individuals who may be able to benefit from this measure will be limited, which may explain Budget 2024’s modest decrease of proposed Government revenue in 2024-25 of $35 million in implementing this tax measure (and only $625 million over the next five years) from this measure.

Alternative Minimum Tax

Considering the proposed increased capital gain inclusion rate that will be effective as of June 25, 2024, some Canadians may consider triggering capital gains and paying capital gains tax now to take advantage of the current rate. That said, high-income Canadians must be mindful of the amendments to the AMT that are intended to be effective as of January 1, 2024.

Budget 2023 announced significant amendments to the AMT, a parallel tax calculation that allows fewer tax credits, deductions, and exemptions than under the ordinary personal income tax rules. A taxpayer will be liable for AMT if the computed net AMT is greater than the taxpayer’s federal income tax for the taxation year. The goal of the AMT is to ensure high-income Canadians do not disproportionately lower their tax bill.

In response to feedback received during a consultation period relating to the AMT proposals in Budget 2023, Budget 2024 proposes to amend the AMT proposals further in the following ways (all proposed amendments will apply to taxation years that begin on or after January 1, 2024):

- allow individuals to claim 80% (rather than 50%, as previously proposed) of a Charitable Donation Tax Credit when calculating AMT (prior to the proposed amendments in Budget 2023, individuals could claim 100% of a Charitable Donation Tax Credit when calculating AMT);
- allow individuals to claim 100% of Guaranteed Income Supplement, social assistance, and workers' compensation payments when calculating AMT;
- allow individuals to fully claim the federal logging tax credit when calculating AMT;
- fully exempt EOTs from AMT;
- allow individuals to carry forward disallowed credits under the AMT (i.e., the federal political contribution tax credit, investment tax credits, and labour-sponsored funds tax credit).

Proposed Exemption for Certain Trusts for the Benefit of Indigenous Groups

Generally, trusts are also subject to the AMT rules. Budget 2024 proposes to provide an exemption from the

AMT for trusts established under:

- a law of Canada or a province if the trust is for the benefit of an Indigenous group, community, or people that holds rights recognized and affirmed by section 35 of the *Constitution Act, 1982*; or
- a treaty or a settlement agreement between His Majesty in right of Canada or His Majesty in right of a province and an Indigenous group, community, or people recognized and affirmed by section 35 of the *Constitution Act, 1982*,

provided that all or substantially all of the contributions to the trust before the end of the year are amounts paid under the law, treaty, or settlement agreement described above or are reasonably traceable to those amounts.

An exemption from the AMT will also be provided for trusts where the beneficiaries are any combination of the following persons or entities:

(a) all of the members of a recognized Indigenous group, community, or people that holds rights recognized and affirmed by section 35 of the *Constitution Act, 1982*;

(b) a public body performing a function of government in Canada (within the meaning of the Tax Act) in relation to an Indigenous group, community, or people that holds rights recognized and affirmed by section 35 of the *Constitution Act, 1982*;

(c) a registered charity or a non-profit organization that is organized and operated primarily for health, education, social welfare, or community improvement for the benefit of the members of an Indigenous group, community, or people that holds rights recognized and affirmed by section 35 of the *Constitution Act, 1982*;

(d) a corporation, all of the shares of which are owned by any combination of persons or entities described in (b) or (c) above, a Settlement Trust, or another corporation meeting this definition;

(e) a Settlement Trust (which is a trust that establishes a relationship between an Indigenous group and the trustee of the trust property with the goal of having specific capital invested and preserved for future generations of an Indigenous group).

The Government is seeking feedback on these proposed exemptions for Indigenous settlement and community trusts until June 28, 2024.

Mineral Exploration Tax Credit (METC)

As previously announced by the Department of Finance (Finance) on March 28, 2024, the Government proposes to extend the eligibility for the METC for one year to flow-through share agreements entered into on or before March 31, 2025. The METC was originally set to expire on March 31, 2024. For more details, please see our Comment.

Employee Ownership Trust Tax Exemption

EOTs were introduced in Budget 2023 as a vehicle to facilitate the tax-efficient sale of Canadian businesses to employees. Legislative proposals are currently before Parliament in Bill C-59. The 2023 Fall Economic Statement proposed to temporarily exempt the first $10 million in capital gains realized on the sale to an EOT, subject to certain conditions (EOT Exemption). Budget 2024 provides further details on the proposed EOT Exemption and conditions. The EOT Exemption would apply to qualifying dispositions of shares that occur between January 1, 2024 and December 31, 2026.

Qualifying Conditions

The EOT Exemption would be available to an individual (other than a trust) on the sale of shares to an EOT where the following conditions are satisfied:

- the individual, a personal trust of which the individual is a beneficiary, or a partnership in which the individual is a member, disposes of shares of a corporation that is not a professional corporation;
- the transaction is a "qualifying business transfer" (as defined in Bill C-59) in which the trust acquiring the shares is not already an EOT or a similar trust with employee beneficiaries;
- throughout the 24 months immediately preceding the qualifying business transfer, (a) the transferred shares were exclusively owned by the individual claiming the exemption, a related person, or a partnership in which the individual is a member, and (b) over 50% of the fair market value of the corporation's assets were used principally in an active business;
- at any time prior to the qualifying business transfer, the individual (or their spouse or common-law partner) has been actively engaged in the qualifying business on a regular and continuous basis for a minimum of 24 months; and
- immediately after the qualifying business transfer, at least 90% of the beneficiaries of the EOT must be Canadian residents.

If multiple individuals disposed of shares to an EOT as part of a qualifying business transfer and satisfied the conditions above, they may each claim the exemption but the total exemption in respect of the qualifying business transfer cannot exceed $10 million. The individuals would be required to agree on the allocation of the $10 million exemption.

Disqualifying Events

If a disqualifying event occurs within 36 months of the qualifying business transfer, the EOT Exemption would not be available. A disqualifying event occurs where an EOT loses its status as an EOT or if less than 50% of the fair market value of the qualifying business' shares is attributable to assets used principally in an active business at the beginning of two consecutive taxation years of the corporation. If an individual has already claimed the exemption, it would be retroactively denied.

If a disqualifying event occurs more than 36 months after a qualifying business transfer, the EOT would be deemed to realize a capital gain equal to the total amount of exempt capital gains.

Alternative Minimum Tax

Capital gains exempted on a qualifying business transfer to an EOT would be subject to an inclusion rate of 30% for the purposes of AMT, similar to the LCGE.

Administration

The EOT Exemption will be elective. The EOT (and any corporation owned by the EOT that acquired the transferred shares) and the individual would need to elect to be jointly and severally, or solidarily, liable for any tax payable by the individual as a result of the exemption being denied due to a disqualifying event within the first 36 months after a qualifying business transfer.

The normal reassessment period of an individual for a taxation year in respect of this exemption is proposed to be extended by three years, matching the 36-month period during which a disqualifying event cannot occur.

Worker Cooperatives

Budget 2024 proposes to expand qualifying business transfers to include the sale of shares to a worker cooperative corporation as defined in the *Canada Cooperatives Act*. If the relevant requirements are satisfied, an individual could claim an exemption on selling a business to a worker cooperative. Such a sale would also be eligible for the 10-year capital gains reserve and the 15-year exception to the shareholder loan and interest benefit rules contained in Bill C-59 and previously announced in Budget 2023.

Finance will release further details on this aspect of the exemption in the coming months.

Qualified Investments for Registered Plans

Budget 2024 invites stakeholders to provide suggestions on how the qualified investment rules could be modernized on a prospective basis to improve the clarity and coherence of the registered plans regime (i.e.,

Registered Retirement Saving Plans, Registered Retirement Income Funds, Tax-Free Savings Accounts, Registered Education Savings Plans, Registered Disability Savings Plans, First Home Savings Accounts, and Deferred Profit Sharing Plans). Stakeholders are invited to submit comments by July 15, 2024.

Indigenous Child and Family Services Settlement

Budget 2024 proposes to exclude the income of the trusts established under the First Nations Child and Family Services, Jordan's Principle, and Trout Class Settlement Agreement from taxation. This would also ensure that payments received by class members as beneficiaries of the trusts would not be included in their income for federal income tax purposes. This settlement was approved by the Federal Court on October 24, 2023 and this measure would apply as of the 2024 taxation year and onwards.

Business Income Measures

Clean Electricity Investment Tax Credit

Budget 2024 sets forth the design and implementation of the Clean Electricity ITC previously announced in Budget 2023, as supplemented by additional changes in the 2023 Fall Economic Statement. The Clean Electricity ITC is a refundable tax credit equal to 15% of the capital cost of eligible property acquired by eligible Canadian corporations that meet the labour requirements for prevailing wages and apprenticeships currently before Parliament in Bill C-59 (Labour Requirements). If the Labour Requirements are not met, the Clean Electricity ITC is reduced to 5%.

The Clean Electricity ITC would be available in respect of eligible property that (i) becomes available for use on or after Budget Day and before 2035, and (ii) is not part of a project that began construction (which does not include permitting or preliminary studies) before March 28, 2023.

If a particular expenditure is eligible for more than one of the Clean Electricity ITC, the Clean Technology investment tax credit (Clean Technology ITC), the Carbon, Capture, Utilization and Storage investment tax credit (CCUS Tax Credit), the Clean Hydrogen investment tax credit (Clean Hydrogen ITC), the Clean Technology Manufacturing investment tax credit (Clean Technology Manufacturing ITC), and the Electric Vehicle Supply Chain Investment tax credit, an eligible corporation (described below) would only be able to claim one credit. However, multiple credits may be available for the same project, to the extent the project includes expenditures eligible for different investment tax credits.

Eligible Corporations

The Clean Electricity ITC is available to taxable Canadian corporations as well as certain corporations that are exempt from income tax (e.g., provincial and territorial Crown corporations, municipal corporations, corporations owned by Indigenous communities, and pension investment corporations). To receive the credit, these tax-exempt corporations must agree to be bound by the compliance provisions of the Tax Act, including the provisions related to audit, penalties, and collections.

Where eligible property is owned by a partnership, any partners that are corporations eligible for the credit would be allowed to claim their share of the partnership's Clean Electricity ITC, subject to partnership rules generally consistent with those proposed for the Clean Technology ITC currently before Parliament in Bill C-59. Where a property is eligible for both the Clean Electricity ITC and the Clean Technology ITC, a partner could claim either credit (but could not claim both credits in respect of the same property) to the extent of their reasonable share as determined for partnership income tax purposes.

Eligible Property

Eligible property is depreciable property that has not been used for any other purpose before its acquisition and that is:

- **Solar, wind, or hydro**: equipment used to generate electricity from solar, wind, or water energy that is described under specific provisions of capital cost allowance (CCA) Class 43.1 (Class 43.1);
- **Concentrated solar**: concentrated solar energy equipment, as defined for the purposes of the Clean Technology ITC, but limited to equipment used to generate electricity;
- **Nuclear**: equipment used to generate electricity, or both electricity and heat, from nuclear fission as defined for the purposes of the Clean Technology ITC, but without generating capacity limits or requirements to be small modular reactors;
- **Geothermal**: equipment used exclusively for the purpose of generating electricity, or both electricity and heat, solely from geothermal energy, as described in Class 43.1, but excluding any equipment that is part of a system that extracts fossil fuel for sale;
- **Biomass**: equipment that is part of a system used to generate electricity, or both electricity and heat, from specified waste materials, as described in the 2023 Fall Economic Statement;
- **Energy Storage**: stationary electricity storage or pumped hydroelectric energy storage equipment that is described in Class 43.1 (e.g., BESS systems), but excluding equipment that uses any fossil fuel in operation;
- **Natural Gas**: equipment that is part of an eligible natural gas energy system (described below); and
- **Transmission**: equipment and structures used for the transmission of electricity between provinces and territories.

Qualifying expenditures could include capital expenditures that are additions or alterations to existing facilities (e.g., certain hydro-electric facilities).

Eligible property must meet the conditions for qualification on an annual basis. Where property ceases to qualify because it has been converted to an ineligible use, exported from Canada, or disposed of, the Clean Electricity ITC will be subject to potential repayment obligations (Recapture) similar to those applicable to the proposed Clean Technology ITC currently before Parliament in Bill C-59.

Eligible Natural Gas Energy Systems

Eligible property for natural gas energy systems includes equipment used to generate electricity, heat, or both, as well as carbon capture equipment that stores the captured carbon appropriately and prepares or compresses it for transportation, provided that the system attains an emissions intensity of no greater than 65 tonnes of carbon dioxide per gigawatt hour of energy produced. Certain modifications are made to the emissions calculation to (i) include certain emissions attributable to combustion of biomass as defined by regulation and (ii) exclude certain emissions that are captured and stored in dedicated geological storage that meets requirements that align with those in the proposed CCUS Tax Credit currently before Parliament in Bill C-59.

Natural Resources Canada would review project plans to determine equipment and system eligibility before a Clean Electricity ITC claim could be made. Project plans would be required to reflect a front-end engineering design study and other information required by the Minister of Energy and Natural Resources.

Verification of emissions intensity will be required. During the first 5-year compliance period, a third-party engineering firm will need to report the emissions intensity produced annually by the system and submit reports to Natural Resources Canada. At the end of the period, compliance will be assessed based on the weighted average (by electricity and useful heat produced) emissions intensity over the entire compliance period. An average emissions intensity more than 5% above the limit of 65 tonnes of carbon dioxide per gigawatt hour of energy produced would lead to full Recapture of the Clean Electricity ITC. After the initial five-year compliance period there will be a requirement to continue producing emissions intensity reports annually for an additional 15 years. During this 15-year period an annual emissions intensity above the limit would be considered a conversion to an ineligible use and trigger the associated Recapture provisions.

Crown Corporations

The Clean Electricity ITC would be available to provincial and territorial Crown corporations only for investments made in jurisdictions designated by the Minister of Finance (Minister). The Minister will designate a province or territory where the Minister is satisfied that the provincial or territorial government has:

- publicly committed to (a) work towards a net-zero electricity grid by 2035, and (b) Crown corporations passing the value of the Clean Electricity ITC to electricity ratepayers in the province or territory to reduce electricity bills; and

- directed Crown corporations claiming the credit to provide annual reports to the public on how the tax credit has improved ratepayers' bills.

Polymetallic Extraction and Processing

Budget 2023 proposed a refundable Clean Technology Manufacturing ITC equal to 30% of the cost of eligible property used all or substantially all for eligible activities, which would include "qualifying mineral activities" that produce all or substantially all "qualifying materials" (i.e., copper, nickel, cobalt, lithium, graphite, and rare earth elements). "Qualifying mineral activities" would consist of extraction; certain processing activities at mine or well sites, tailing ponds, mills, smelters, or refineries; certain recycling activities; and certain graphite activities. Draft legislative proposals were released in December 2023.

Budget 2024 acknowledges that production of qualifying material(s) may occur at projects engaged in the production of multiple minerals (polymetallic projects) and proposes adjustments to the Clean Technology Manufacturing ITC to clarify that the value of qualifying material shall be used as the output metric when assessing whether property is used for qualifying mineral activities.

In addition, Budget 2024 proposes to include as qualifying expenditures, investments in eligible property used in qualifying mineral activities that are expected to produce "primarily" qualifying materials at mine or well sites (including tailing ponds and mills located at these sites). The use of the term primarily as the threshold for qualification would generally mean that, at mine or well sites, eligible property must be used or be expected to be used for activities in which 50% or more of the financial value of the output comes from qualifying materials, rather than 90% as previously proposed. The proposed amendments are applicable to property that becomes available for use after January 1, 2024.

The December 2023 draft legislative proposals for the Clean Technology Manufacturing ITC provide that the credit could be subject to Recapture if eligible property is converted to a use that is a non-qualifying activity (which could occur if the actual financial value of the materials extracted from a mine site is less than 50% from qualifying materials).

In an acknowledgment that mineral prices can be volatile, Budget 2024 proposes a safe-harbour rule that will limit Recapture if, when claiming the Clean Technology Manufacturing ITC, the claimant calculates the value of expected production from the eligible property using specified five-year historical average mineral prices. The claimant would then be permitted to use those same mineral prices to calculate the ratio of qualifying materials produced from the property over the 10-year Recapture period.

Accelerated Capital Cost Allowance

Purpose-Built Rental Housing

Budget 2024 proposes an accelerated CCA of 10% (increased from 4%) for new eligible purpose-built rental projects that (a) begin construction on or after Budget Day and before January 1, 2031, and (b) are available for use before January 1, 2036. Eligible property would be new purpose-built rental housing that is a residential complex with at least four private apartment units (or 10 private rooms or suites) in which at least 90% of residential units are held for long-term rental. Projects that convert existing non-residential buildings and the cost of additions to an existing structure would be eligible so long as they create new purpose-built rental housing. Renovations to existing residential complexes would not be eligible.

Productivity-Enhancing Assets

Budget 2024 proposes immediate expensing (i.e., a 100% first-year deduction) for property that is: (a) a patent or a right to use patented information for a limited or unlimited period described in CCA Class 44; (b) data network infrastructure equipment and related systems software described in CCA Class 46; or (c) general purpose electronic data processing equipment and systems software described in CCA Class 50, so long as the property is acquired after Budget Day and becomes available for use before January 1, 2027.

The properties described above will continue to be eligible for the accelerated investment incentive introduced with Federal Budget 2018. This incentive suspends the application of the “half-year rule”, which would generally limit the capital cost allowance deduction in the year the property is available for use to one-half of the deduction otherwise available, for property that is available for use before 2028.

Canada Carbon Rebate for Small Businesses

Budget 2024 proposes to return a portion of fuel charge proceeds collected in a province subject to the federal backstop pollution pricing fuel charge (Federal Carbon Tax) via the new Canada Carbon Rebate for Small Businesses, an automatic refundable tax credit directly issued to eligible businesses and sized in proportion to the number of persons they employ in the province. The government expects to return $2.5 billion annually through this measure, reflecting Federal Carbon Tax proceeds from 2019-20 through 2023-24.

Currently, the Federal Carbon Tax applies in Alberta, Saskatchewan, Manitoba, Ontario, New Brunswick, Nova Scotia, Prince Edward Island, and Newfoundland and Labrador. Although Budget 2024 specifically refers to the 2019-20 to 2023-24 Federal Carbon Tax years, the government's intention is to return proceeds for future Federal Carbon Tax years as well.

Eligible Businesses

The Canada Carbon Rebate for Small Businesses will be available to a CCPC that files a tax return for its 2023 taxation year by July 15, 2024. Additionally, to be eligible for a credit in respect of an applicable Federal Carbon Tax year, the corporation must have had no more than 499 employees throughout Canada in the calendar year in which the Federal Carbon Tax year begins. For example, eligibility for receiving a payment in respect of the 2022-23 Federal Carbon Tax year would be based on the number of persons employed in the 2022 calendar year.

Automatic Payments

Corporations do not have to apply to receive the tax credit. The Canada Revenue Agency (CRA) will automatically determine the tax credit amount for an eligible corporation and pay the amount to the eligible corporation through the new Canada Carbon Rebate for Small Businesses.

Credit Determination

The amount of the tax credit for an applicable Federal Carbon Tax year will be determined for each applicable province in which the eligible corporation had employees in the calendar year in which the Federal Carbon Tax year begins. The amount of the tax credit would be equal to

$$A \times B$$

where

A = the number of persons employed by the eligible corporation in the province in that calendar year, and

B = a payment rate specified by the Minister for the province for the corresponding Federal Carbon Tax year.

Interest Deductibility Limits – Purpose-Built Rental Housing

The excessive interest and financing expenses limitation (EIFEL) rules in Bill C-59, currently before Parliament, were developed in response to the recommendations under Action 4 of the OECD/G20 Base Erosion and Profit Shifting Project. These rules create an earnings stripping measure that limits the amount of net interest and financing expenses that may be deducted by certain taxpayers in computing taxable income.

Interest and financing expenses incurred in respect of arm's length financing for public-private partnership infrastructure projects are exempt from the EIFEL rules. Budget 2024 proposes to expand this exemption to also include an elective exemption for certain interest and financing expenses incurred before January 1,

2036 in respect of arm's length financing used to build or acquire eligible purpose-built rental housing in Canada. Eligible purpose-built rental housing would be the same residential complexes that are eligible for accelerated CCA treatment – i.e., a residential complex with at least four private apartment units (or 10 private rooms or suites) and in which at least 90% of residential units are held for long-term rental. This change would apply to taxation years that begin on or after October 1, 2023 (i.e., consistent with the intended effective rate of the broader EIFEL regime).

Mutual Fund Corporations

Budget 2024 proposes to deem a corporation not to be a "mutual fund corporation" after a particular time if, at that time (a) a person or partnership, or any combination of persons or partnerships that do not deal with each other at arm's length (specified persons) own, in the aggregate, shares of the corporation having a fair market value of more than 10% of the fair market value of all of the issued and outstanding shares of the corporation; and (b) the corporation is controlled by or for the benefit of one or more specified persons. This rule will not apply if the corporation was incorporated not more than two years before the particular time and the aggregate fair market value of the shares of the corporation owned by specified persons at the particular time does not exceed $5 million.

A mutual fund corporation benefits from special rules that generally allow capital gains realized by the mutual fund corporation to be treated as capital gains realized by its investors. This measure is intended to prevent a corporate group from using a mutual fund corporation to benefit from the special rules available to these corporations in an unintended manner (e.g., where a corporation controlled by a corporate group qualifies as a mutual fund trust, even though it is not widely held, because it lists a class of its shares on a designated stock exchange).

This measure would apply to taxation years that begin after 2024.

Synthetic Equity Arrangements

Generally, a corporation may deduct any dividends received on a share of a corporation resident in Canada, subject to certain limitations, including an anti-avoidance rule that denies the dividend received deduction in respect of synthetic equity arrangements. Synthetic equity arrangements include agreements that provide all or substantially all of the risk of loss and opportunity for gain or profit (economic exposure) in respect of a share to another person.

The anti-avoidance rule does not apply where a taxpayer establishes that no tax-indifferent investor has all or substantially all of the economic exposure in respect of the share. An associated exception to the anti-avoidance rule is also available for synthetic equity arrangements traded on a derivatives exchange.

Budget 2024 proposes to remove the tax-indifferent investor exception (including the exchange traded exception) to this anti-avoidance rule. This measure would apply to dividends received on or after January 1, 2025.

Manipulation of Bankrupt Status

Bankrupt taxpayers are generally excluded from the debt forgiveness rules. Instead, a separate loss restriction rule applies to extinguish losses of bankrupt corporations that have received an absolute order of discharge.

Budget 2024 proposes to repeal this exception and the loss restriction rule applicable to bankrupt corporations in an attempt to target a perceived manipulation of the bankrupt status of insolvent corporations. Accordingly, under this proposal, bankrupt corporations would be subject to the general debt forgiveness rules applicable to corporations whose commercial debts are forgiven. Bankrupt individuals will continue to be exempt from the debt forgiveness rules. Bankrupt corporations would be subject to the reduction of their tax attributes upon debt forgiveness; however, as insolvent corporations, they may qualify for relief from the debt forgiveness income inclusion rule under the existing deduction for insolvent corporations.

These proposals would apply to bankruptcy proceedings commenced on or after Budget Day.

INTERNATIONAL TAX MEASURES

Crypto-Asset Reporting Framework and the Common Reporting Standard

Budget 2024 proposes to implement the CARF in Canada and to implement amendments to the Common Reporting Standard (CRS) endorsed by the OECD in connection with the CARF. These measures will apply to the 2026 and subsequent calendar years, allowing the first reporting and exchange of information under the CARF and amended CRS to take place in 2027 with respect to the 2026 calendar year.

The CRS is the global standard developed and endorsed by the OECD for the automatic exchange of financial information for tax purposes. Canada's implementation of the CRS requires Canadian financial institutions to report to the CRA information on financial accounts held in Canada by non-residents. The CRA shares this information with foreign tax authorities and, in exchange, receives information on financial accounts held by Canadian residents outside of Canada.

Crypto-Asset Reporting Framework

Currently, crypto-assets (including stablecoins, derivatives issued in the form of a crypto-asset, and certain non-fungible tokens), which can be transferred or held without interacting with traditional financial intermediaries, do not need to be reported under the CRS. Canada's implementation of the CARF would impose a new annual reporting requirement in the Tax Act on entities and individuals (crypto-asset service providers) that are resident in Canada, or that carry on business in Canada, and that provide business services effectuating exchange transactions in crypto-assets. This would include crypto exchanges, crypto-asset brokers and dealers, and operators of crypto-asset automated teller machines.

Crypto-asset service providers will be required to report to the CRA certain information in respect of each customer and crypto-asset transaction. Unlike the CRS, as proposed in Budget 2024, crypto-asset service providers will be required to report information on Canadian resident and non-resident customers.

Common Reporting Standard

The amendments to the CRS, as endorsed by the OECD in connection with the CARF, will broaden the scope of the CRS to include specified electronic money products and central bank digital currencies which are not covered by the CARF. Other changes would require additional information to be reported in respect of financial accounts and account holders and will strengthen the due diligence procedures financial institutions are required to follow.

Withholding for Non-Resident Service Providers

Under the Tax Act, a person who pays a non-resident for services rendered in Canada is required to withhold 15% of the payment and remit it to the CRA. These rules are intended to act as a prepayment of taxes that such non-resident may ultimately owe. Generally, a non-resident person is subject to Canadian tax on income from carrying on business in Canada. However, many non-resident service providers do not ultimately owe Canadian taxes because they do not have a permanent establishment in Canada under an applicable tax treaty or because the service is international shipping or operating an aircraft in international traffic, both of which are generally exempt from Canadian tax.

Currently, a non-resident person may apply to the CRA for an advance waiver from the withholding requirement for a specific planned transaction or the non-resident person may subsequently apply for a refund of the withheld amounts.

Budget 2024 proposes to provide the CRA with the legislative authority to waive the withholding requirement (on multiple transactions on a single waiver), over a specified period, for payments to a non-resident service provider if:

- the non-resident would not be subject to Canadian income tax in respect of the payment because of

- a tax treaty between their country of residence and Canada; or
- the income from providing the services is exempt income from international shipping or from operating an aircraft in international traffic.

This measure will come into force upon royal assent of the enacting legislation.

Administrative Tax Measures

Non-Compliance with Information Requests

Budget 2024 proposes several amendments to the information gathering provisions in the Tax Act. These amendments would come into force on royal assent of the enacting legislation.

Notice of Non-Compliance

Budget 2024 proposes to amend the Tax Act to allow the CRA to issue a new type of notice (notice of non-compliance) to a person that has not complied with a requirement or notice to provide assistance or information issued by the CRA. A person who is sent or served with a notice of non-compliance may, within 90 days, request that the notice of non-compliance be reviewed. Within 180 days of receiving the request to review the notice of non-compliance, the CRA must confirm, vary, or vacate the notice of non-compliance. The notice of non-compliance would be vacated if the CRA determines it was unreasonable to issue the notice of non-compliance or the person had reasonably complied, at the time the notice of non-compliance was issued, with the initial requirement or notice. After the person receives notification of the CRA's decision, the person may, within 90 days, apply to the Federal Court to review the decision.

Where a notice of non-compliance related to a taxpayer has been issued to the taxpayer or a person that does not deal at arm's length with the taxpayer, the normal reassessment period for any taxation year of the taxpayer to which the notice of non-compliance relates would be extended by the period of time the notice of non-compliance is outstanding.

A person issued a notice of non-compliance is liable to a penalty of $50 per day that the notice is outstanding, to a maximum of $25,000. The penalty will not apply if a notice of non-compliance is ultimately vacated by the CRA or a court.

Questioning Under Oath

Budget 2024 proposes to amend the Tax Act to allow the CRA to include in a requirement or notice that any required information, whether oral or written, or documents be provided under oath or affirmation. There was

previously a concern around the CRA's ability to request information from a person orally, which was introduced in Budget 2021, without the ability to reflect on the information being requested and to consult with an advisor. This proposal goes beyond the CRA's power to compel oral interviews by requiring that such oral interviews take place under oath.

Compliance Orders

Budget 2024 proposes to impose a penalty when the CRA obtains a compliance order against a taxpayer. The penalty would be equal to 10% of the aggregate tax payable by the taxpayer in respect of the taxation year(s) to which the compliance order relates. The penalty will only be applied if the tax owing in respect of one of the taxation years to which the compliance order relates exceeds $50,000.

Budget 2024 also proposes an amendment to the Tax Act to allow the CRA to seek a compliance order when a person has failed to comply with a requirement to provide foreign-based information or documents.

Prior to Budget 2024, the CRA could obtain a compliance order from a court directing a non-compliant taxpayer to comply with the CRA's information requests. However, the Government's position is that the use of compliance orders has generally not been effective in compelling compliance, because the primary consequence for not complying is a contempt order (which is time consuming to obtain and does not generally impose a material financial cost on the taxpayer).

Stopping the Reassessment Limitation Clock

Prior to Budget 2024, a taxpayer could seek judicial review of a requirement or notice issued to the taxpayer by the CRA, which would extend the reassessment period by the amount of time it takes to dispose of the judicial review. An analogous rule applied in respect of a compliance order. However, these “stop the clock” rules did not apply to all situations where a taxpayer does not comply with a requirement or notice issued by the CRA.

Budget 2024 proposes to amend the “stop the clock” rules so that these rules apply when a taxpayer seeks judicial review of any requirement or notice issued to the taxpayer by the CRA in relation to the audit and enforcement process or during any period that a notice of non-compliance is outstanding. Analogous rules will apply where a requirement or notice has been issued to a person that does not deal at arm's length with the taxpayer.

Other Tax Statutes Administered by the CRA

Budget 2024 proposes that other tax statutes administered by the CRA which have similar provisions to the Tax Act also be amended appropriately, including the *Excise Tax Act*, *Air Travellers Security Charge Act*, *Excise Act, 2001*, *Underused Housing Tax Act*, *Select Luxury Items Tax Act*.

Avoidance of Tax Debts

Budget 2024 proposes to introduce a supplementary rule to strengthen the existing tax debt anti-avoidance rules which prevent taxpayers from avoiding paying their tax liabilities by transferring their assets to non-arm's length persons.

The current rules make the transferee jointly and severally, or solidarily, liable with the transferor for the transferor's tax debts, to the extent that the value of the property transferred exceeds the amount of consideration given by the transferee for the property. The Government is of the view that taxpayers are continuing to engage in planning that is intended to circumvent the tax debt avoidance rule, often with a tax planner who receives a significant fee that is effectively funded by a portion of the avoided tax debt. Accordingly, this supplementary rule would apply in the following circumstances:

- there has been a transfer of property from a tax debtor to another person;
- as part of the same transaction or series of transactions, there has been a separate transfer of property from a person, other than the tax debtor, to a transferee that does not deal at arm's length with the tax debtor; and
- one of the purposes of the transaction or series is to avoid joint and several, or solidary, liability.

Where these conditions are met, the property transferred by the tax debtor would be deemed to have been transferred to the transferee for the purposes of the tax debt avoidance rule. The Government's position is that this would ensure that the tax debt avoidance rule applies in situations where property has been transferred from a tax debtor to a person and, as part of the same transaction or series, property has been received by a non-arm's length person.

Penalty

Additionally, Budget 2024 proposes to extend the penalty to tax debt avoidance planning that is subject to the proposed supplementary rule.

The penalty is equal to the lesser of:

- 50% of the tax that is attempted to be avoided; and
- $100,000 plus any amount the person, or a related person, is entitled to receive or obtain in respect of the planning activity.

Expanded Joint and Several, or Solidary, Liability

Budget 2024 also proposes that taxpayers who participate in tax debt avoidance planning be jointly and

severally, or solidarily, liable for the full amount of the avoided tax debt, including any portion that has been effectively retained by a planner as a fee.

Similar Statutes

Similar amendments will be made to comparable provisions in other federal statutes (e.g., the *Excise Tax Act*, the *Excise Act, 2001*, the *Select Luxury Items Tax Act*, and the *Underused Housing Tax Act*).

Coming into Force

These measures would apply to transactions or series of transactions that occur on or after Budget Day.

Reportable and Notifiable Transactions Penalty

The Tax Act contains a general penalty provision which provides that a person who fails to file or make a return is guilty of an offence and liable to penalties up to $25,000 and imprisonment up to a year.

The mandatory disclosure rules also contain specific penalty provisions that apply for failing to file an information return with respect to a reportable transaction or a notifiable transaction.

Budget 2024 announces the Government's intention to remove from the scope of the general penalty provision the failure to file an information return in respect of a reportable or notifiable transaction under the mandatory disclosure rules.

This amendment will be deemed to have come into force on June 22, 2023 (i.e., the date the mandatory disclosure rules came into effect).

Previously Announced Income Tax Measures

In addition to the measures described above, Budget 2024 confirms the Government's intention to proceed with the following previously announced measures:

- Legislative proposals released on December 20, 2023, including with respect to:
    - the Clean Hydrogen ITC;
    - the Clean Technology Manufacturing ITC;
    - Concessional Loans;
    - Short-Term Rentals;
    - Vaping Excise Duties; and

  - International Shipping.
- Legislative proposals announced in the 2023 Fall Economic Statement, including with respect to the proposed expansion of eligibility for the Clean Technology ITC and Clean Electricity ITC to support generation of electricity and heat from waste biomass.
- Legislative proposals released on August 4, 2023, including with respect to:
  - the CCUS Tax Credit;
  - the Clean Technology ITC;
  - labour requirements related to certain investment tax credits;
  - enhancing the reduced tax rates for zero-emission technology manufacturers;
  - flow-through shares and the critical mineral exploration tax credit for lithium from brines;
  - EOTs;
  - retirement compensation arrangements;
  - strengthening the intergenerational business transfer framework;
  - the AMT;
  - a tax on repurchases of equity;
  - modernizing the GAAR;
  - Global Minimum Tax (Pillar Two);
  - Digital Services Tax;
  - EIFEL;
  - revised luxury tax draft regulations to provide greater clarity on the tax treatment of luxury items; and
  - technical amendments to the Tax Act and the *Income Tax Regulations* (Canada) (Regulations).
- Legislative amendments to implement changes discussed in the transfer pricing consultation paper released on June 6, 2023.
- Tax measures announced in Budget 2023, including the Dividend Received Deduction by Financial Institutions.
- Legislative proposals released on August 9, 2022, including with respect to:
  - Substantive CCPCs; and
  - technical amendments to the Tax Act and the Regulations.
- Legislative amendments to implement the Hybrid Mismatch Arrangements rules announced in Budget 2021.

Budget 2024 also reaffirms the Government's commitment to move forward as required with other technical amendments to improve the certainty and integrity of the tax system.

If you have any questions about Budget 2024, please contact any member of the Cassels Tax Group.

This publication is a general summary of the law. It does not replace legal advice tailored to your specific circumstances.