

2023 Issue No. 42
21 November 2023

Tax Alert – Canada

Federal Fall Economic Statement 2023

EY Tax Alerts cover significant tax news, developments and changes in legislation that affect Canadian businesses. They act as technical summaries to keep you on top of the latest tax issues. For more information, please contact your EY advisor or EY Law advisor.

“Built upon our responsible fiscal plan, our Fall Economic Statement has two objectives. The first is to continue to support the middle class at a time when some prices are still high and mortgage renewals are looming... Our second objective is equally urgent. For generations, Canada has been a place where if you worked hard – if you went to school, found a good job, and squirreled some money away, there would be a home that you could afford. For generations, that promise was kept... Keeping that promise demands a great national effort – and it is an effort that our government is stepping up to lead.”

*Deputy Prime Minister and Finance Minister Chrystia Freeland
Fall Economic Statement 2023*

On 21 November 2023, federal Deputy Prime Minister and Finance Minister Chrystia Freeland tabled the federal government's *Fall Economic Statement 2023*. The *Fall Economic Statement 2023* (FES) contains several tax measures affecting individuals and corporations. As set out in Table A, the minister anticipates a deficit of \$40.1b for 2023-24 and projects declining deficits for each of the next five years.

On the same day, draft legislative proposals were released with respect to the proposed new GST/HST joint venture election rules, which are summarized below. Comments on these proposals are sought by 15 March 2024.

Also on 21 November 2023, draft legislative and regulatory proposals were released, with accompanying explanatory notes, with respect to proposed changes to the underused housing tax (UHT), which are noted below in more detail. Interested parties are invited to send comments by 3 January 2024.

Table A: Projections of federal budgetary deficit*

	2022-23 \$b	2023-24 \$b
Federal budget 2023 (Budget 2023) balance	(43.0)	(40.1)
Economic and other fiscal developments	7.7	2.7
Budgetary balance before policy actions and measures	(35.3)	(37.4)
Policy actions since Budget 2023 and measures in this FES	–	(2.7)
Final budgetary balance (i.e., deficit)	(35.3)	(40.0)
Budgetary balance (percent of GDP)	(1.3%)	(1.4%)
Federal debt (percent of GDP)	41.7%	42.4%

*Numbers represent the government's baseline scenario and may not add due to rounding.

Business income tax measures

The following is a summary of the business support measures announced:

Corporate tax rates

No changes are proposed to the corporate income tax rates or to the \$500,000 small-business income limit of a Canadian-controlled private corporation. The enacted Canadian federal corporate income tax rates are summarized in Table B.

Table B: Federal corporate income tax rates*

	2023	2024
General corporate rate**	15.0%	15.0%
Small-business rate	9.0%	9.0%

*The corporate income tax rate for zero-emission technology manufacturers is reduced to 7.5% for eligible income otherwise subject to the 15% general corporate income tax rate, or 4.5% for eligible income otherwise subject to the 9% small-business corporate income tax rate, applicable for taxation years beginning after 2021. Under proposed legislation, the reduced tax rates are scheduled to be gradually phased out beginning in 2032 and fully phased out for taxation years beginning after 2034. This proposal is not yet substantively enacted.

**An additional tax on banks and life insurers at a rate of 1.5% on taxable income (subject to a \$100 million exemption to be shared by group members) applies for taxation years ending after 7 April 2022 (prorated for taxation years straddling this effective date). These rates are not reflected in the rates shown in the table above.

Other business tax measures

The minister also proposed the following business income tax measures:

Investment tax credit for clean hydrogen - additional design details - This credit, first announced in the 2022 FES and for which details were included in Budget 2023, includes a 15% tax credit on eligible equipment that converts clean hydrogen to ammonia and a tax credit between 15% and 40% of eligible project costs, with the rate dependent on the carbon intensity (CI) of the hydrogen produced.

Additional design details are included in the FES, as follows:

- ▶ Eligible clean ammonia production equipment - For purposes of this 15% tax credit, various specific conditions are introduced, including:
 - ▶ The taxpayer that is producing the ammonia must use their own hydrogen feedstock in the ammonia production (the feedstock must come from a clean hydrogen project eligible for the clean hydrogen investment tax credit).
 - ▶ The clean hydrogen project must have sufficient production capacity to satisfy the taxpayer's ammonia production facility.
 - ▶ The taxpayer demonstrates the feasibility of transporting the hydrogen from the hydrogen production facilities to the ammonia production facility (if they are not co-located).
- ▶ Power purchase agreements - Introduction of specific conditions that allow for the use of power purchase agreements and other similar instruments to enable project owners to purchase clean electricity from the electricity grid for the purpose of calculating a project's CI.

- ▶ Renewable natural gas - Allowing for the use of renewable natural gas for purposes of calculating a project's CI, subject to several conditions, as some hydrogen production projects may use renewable natural gas to reduce the CI of their hydrogen production.
- ▶ Initial project CI assessment and validation - Clarifying details included (e.g., the initial project CI assessment will need to be validated by a third party).
- ▶ Compliance - Projects will be subject to a one-time verification based on a five-year compliance period. Over the course of the period, projects will compute and report annually on the effective CI of the hydrogen produced, and at the end of the period, compliance would be determined based on the weighted-average CI over the entire period. Taxpayers will be required to submit third-party verification reports, including any required documentation, of the CI of a project's hydrogen.
- ▶ Recovery - Provision of an exception from recovery of the credit with respect to projects with a verified CI of no more than 0.25 kilograms of carbon dioxide equivalent per kilogram of hydrogen above their original validated CI, even if the verified CI exceeds the upper bound of the originally assessed CI tier (however, full recovery of the credit will be required in respect of ammonia production equipment, if the hydrogen production project supplying the hydrogen used in ammonia production has a verified CI of 4 kilograms or more of carbon dioxide equivalent per kilogram of hydrogen). The clean hydrogen credit, in general, may be subject to recovery if a project fails to achieve a CI of produced hydrogen in the same CI tier that the project was assessed at.

Expansion of investment tax credits for clean technology and clean electricity - Expansion of the 30% clean technology investment tax credit and the 15% clean electricity investment tax credit to include systems that generate electricity, heat, or both electricity and heat from waste biomass. The FES includes details on eligible property and eligible systems. For these purposes, eligible waste biomass will include only specified waste materials, as defined for purposes of capital cost allowance Classes 43.1 and 43.2. Eligible electricity and cogeneration systems will generally include those that use feedstock, all or substantially all of the energy content of which is from specified waste materials, as determined on an annual basis, and that do not exceed a heat rate threshold of 11,000 British thermal units per kilowatt-hour. Eligible heat generation systems will generally include those that use feedstock, all or substantially all of the energy content of which is from specified waste materials (other than spent pulping liquor), as determined on an annual basis. The expansion of eligibility for the clean technology investment tax credit will be effective in respect of property that is acquired and becomes available for use on or after 21 November 2023, provided it has not been used for any purpose before its acquisition. The expansion of eligibility for the clean electricity investment tax credit will be effective as of the day of the 2024 federal budget, and for projects that did not begin construction before 28 March 2023.

Rental expense deduction for non-compliant short-term rentals - Introduction of a new rule preventing short-term rental operators from claiming an income tax deduction for expenses incurred to earn short-term rental income in any province or municipality that has prohibited short-term rentals. The rule will apply to interest expenses as well as other types of rental expenses. An operator will also be unable to claim income tax deductions for a short-term rental if they had failed to comply with provincial or municipal licensing, permitting or registration requirements. These new restrictions will apply to all rental expenses incurred on or after 1 January 2024.

Canadian journalism labour tax credit - Increase in the cap on labour expenditures per eligible newsroom employee from \$55,000 to \$85,000, as well as a temporary increase in the tax credit rate from 25% to 35% for a period of four years. These changes will apply to qualifying labour expenditures incurred on or after 1 January 2023; the changes will be prorated where a qualifying journalism organization's taxation year does not follow a calendar year.

Dividend received deduction by financial institutions - Introduction of an exception to the Budget 2023 proposal to deny the deduction in respect of dividends received on shares of other corporations resident in Canada by financial institutions on shares that are mark-to-market property. Specifically, the FES proposes to exclude dividends received on taxable preferred shares from the application of this measure. As a result, financial institutions may continue to claim a deduction for dividends received on taxable preferred shares. This exception, along with the original proposed measure, will apply to dividends received after 2023.

Concessional loans and government assistance - The FES proposes a relieving rule to counteract the effect of a recent court decision on the treatment of "concessional loans," which are loans from public authorities that are either non-interest bearing or are granted at below-market interest rates. The court decision determined that the principal amount of a concessional loan constituted government assistance for purposes of the *Income Tax Act* (the Act). The FES proposes that, effective 21 November 2023, a bona fide concessional loan with reasonable repayment terms from a public authority will generally not be treated as government assistance.

International tax measures

The following is a summary of the international tax measures announced:

International tax reform - Confirmation of Canada's intention to move ahead with enacting its proposed legislation to implement the OECD/G20 Pillar Two global minimum tax in Canada (i.e., the *Global Minimum Tax Act*), as well as its interim proposed *Digital Services Tax Act*, while continuing to work with its international partners to bring the new multilateral system under Pillar One into effect as soon as a critical mass of countries is willing. Forthcoming legislation will allow the government to determine the entry-into-force date of the new digital services tax, as Canada continues conversations with its international partners. For more information, see EY Tax Alert 2023 Issues No. 35, [Global Minimum Tax Act released for public comment](#), and No. 36, [Canada moving ahead with its own digital services tax: revised draft legislation released](#).

International shipping - Introduction of a measure to make the exemption for international shipping income in the Act generally available to Canadian resident companies. This measure will allow shipping companies with management in Canada to continue their operations in line with both the Pillar Two international shipping exclusion, which is proposed to be implemented in Canada's *Global Minimum Tax Act*, and the exemption in the Act. The measure will apply to taxation years that begin on or after 31 December 2023.

Tax measures for individuals and trusts

Personal income tax rates

There are no individual income tax rate or tax bracket changes in this FES. The brackets will continue to be indexed for inflation.

See Table C for the 2023 federal rates.

Table C: Federal personal income tax rates

	2023
Up to \$53,359	15.0%
\$53,360 to \$106,717	20.5%
\$106,718 to \$165,430	26.0%
\$165,431 to \$235,675	29.0%
Over \$235,675	33.0%

Other personal and trust tax measures

The FES includes the following personal and trust tax measures:

Taxpayer information sharing for the Canadian Dental Care Plan - Budget 2023 proposed amendments to the Act (as well as to the *Excise Tax Act* and *Excise Act, 2001*) to allow the Canada Revenue Agency (CRA) to share taxpayer information with Health Canada and Employment and Social Development Canada for the purpose of delivering the Canadian Dental Care Plan. The relevant amendment to the Act was enacted on 22 June 2023. The FES proposes to amend the Act to allow the CRA to also share taxpayer information with Public Services and Procurement Canada for the purpose of delivering the Canadian Dental Care Plan. Similar amendments are proposed to the *Excise Tax Act* and the *Excise Act, 2001*. These amendments will take effect when the enacting legislation receives Royal Assent.

Employee ownership trusts - Budget 2023 introduced new rules to facilitate the use of employee ownership trusts (EOTs) to acquire and hold shares of a Canadian-controlled private corporation for the benefit of the corporation's employees. These rules will apply as of 1 January 2024. The FES proposes to temporarily exempt the first \$10 million in capital gains realized on the sale of a business to an EOT from taxation, subject to certain conditions (that were not provided in the FES), with the stated intention of encouraging more business owners to sell to an EOT. This incentive would be in effect for the 2024, 2025 and 2026 taxation years. Further details are to be provided in the coming months.

Sales and excise tax

Also, the FES includes the following indirect tax measures:

GST/HST relief for psychotherapists' and counselling therapists' services

The FES proposes to remove the GST/HST from psychotherapists' and counselling therapists' services. Specifically, these practitioners would be added to the list of health care practitioners whose professional services are exempt from GST/HST when rendered to individuals. This measure will take effect when the enacting legislation receives Royal Assent.

Joint venture election

By way of background, a joint venture is a commercial arrangement under which each participant contributes resources to the venture and obtains a right of mutual control or management, a joint interest in assets or property that are the subject matter of the venture, a liability for expenses, and a right to revenues.

A joint venture is not considered to be a person for GST/HST purposes and is therefore not entitled to register and account for the tax. Without special rules, each participant would be required to register separately and account for their proportionate share of tax and input tax credits. To provide flexibility, participants may make an election that makes one of the participants (the operator) responsible for accounting for GST/HST on all purchases and sales made by the participants through the operator. This election is available if the activities are eligible activities set out in subsection 273(1) of the *Excise Tax Act* or prescribed activities under the *Joint Venture (GST/HST) Regulations*.

The Department of Finance has highlighted aspects of the current rules that could be improved. For example, the requirement that joint venture activities must be eligible activities as set out in the *Excise Tax Act* or the regulations means that the simplification benefits of the election may not be available for some commercial joint ventures. To make the election more widely available and improve other aspects of the rules, the proposed new joint venture election rules would:

- ▶ Replace the condition that all activities must be eligible activities under the *Excise Tax Act* or the regulations with a requirement that all or substantially all of the joint venture activities described in the joint venture agreement be commercial activities;
- ▶ Require all electing participants to be GST/HST registrants; and
- ▶ Replace existing deeming measures with revised measures that focus more precisely on tax accounting.

The proposed rules would allow a qualifying operator and a qualifying participant in a qualifying joint venture to jointly make or revoke a joint venture election. A number of measures would generally apply if an election were in effect. For example, if an operator made a supply (other than a supply described in Subdivision C or D of Division II of the *Excise Tax Act*) on behalf of the participant in the course of joint venture activities, the tax collectible for the supply would be deemed to be collectible by the operator and not by the participant for the purpose of determining their respective net tax obligations. The proposals also set out new rules with respect to accounting for GST/HST in relation to various tax adjustment measures, as well as for determining input tax credits within a joint venture context.

The Department of Finance has released draft legislative proposals for public consultation. Currently, it is proposed that the new rules take effect on the day the enacting legislation receives Royal Assent. The government is also asking interested parties to provide feedback on coming-into-force considerations, as well as transitional considerations. Canadians and stakeholders are invited to provide their views and comments by 15 March 2024.

Other measures

Underused housing tax - Introduction of various changes to the UHT rules, which first took effect on 1 January 2022, to relieve some of the compliance burden while also ensuring the UHT continues to apply as intended. The proposed changes include:

- ▶ **Excluded owners** - Expansion of the base of owners of residential property in Canada that are exempt from the UHT and the annual reporting obligations by making specified Canadian corporations, partners of a specified Canadian partnership, and trustees of a specified Canadian trust excluded owners, as well as by expanding the definitions of “excluded owner”, “specified Canadian partnership” and “specified Canadian trust” to include a broader range of Canadian ownership structures, effective for 2023 and subsequent calendar years.
- ▶ **Penalties** - Reduction of the minimum failure to file penalties to \$1,000 (from \$5,000) per failure for individuals and to \$2,000 (from \$10,000) per failure for corporations, effective for 2022 and subsequent calendar years.
- ▶ **Employee accommodations** - Introduction of a new UHT exemption for residential properties held as a place of residence or lodging for employees, effective for 2023 and subsequent calendar years. This exemption would apply for residential properties located anywhere in Canada other than in a population centre within either a census metropolitan area or a census agglomeration having 30,000 or more residents.
- ▶ **Technical changes** - Introduction of additional technical changes to ensure the UHT applies in accordance with its policy intent and to ensure uniformity of tax statutes. These changes would include, for example, providing that unitized apartment buildings are not “residential property,” for UHT purposes, effective for 2022 and subsequent calendar years, and ensuring that the vacation property UHT exemption can be claimed by an individual or a spousal unit for only one residential property for a calendar year, effective for 2024 and subsequent calendar years.

Draft legislative and regulatory proposals relating to these changes have been released for consultation. Interested parties are invited to provide feedback on the proposals by 3 January 2024.

Pension fund investment – The FES announced the government’s intention to explore removing the “30 per cent rule” from pension fund investments in Canada. The 30 per cent rule is a requirement under the federal *Pension Benefits Standards Regulations* that restricts Canadian pension funds from holding more than 30% of the voting shares of most corporations. The stated intention of this measure is to enable pension funds to more fully participate in Canada’s economic growth. The government also proposes to require large federally regulated pension plans to disclose the distribution of their investments to the Office of the Superintendent of Financial Institutions.

Learn more

For more information, please contact your EY or EY Law advisor.

EY | Building a better working world

EY exists to build a better working world, helping to create long-term value for clients, people and society and build trust in the capital markets.

Enabled by data and technology, diverse EY teams in over 150 countries provide trust through assurance and help clients grow, transform and operate.

Working across assurance, consulting, law, strategy, tax and transactions, EY teams ask better questions to find new answers for the complex issues facing our world today.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. Information about how EY collects and uses personal data and a description of the rights individuals have under data protection legislation is available via ey.com/privacy. For more information about our organization, please visit ey.com.

About EY's Tax Services

EY's tax professionals across Canada provide you with deep technical knowledge, both global and local, combined with practical, commercial and industry experience. We offer a range of tax-saving services backed by in-depth industry knowledge. Our talented people, consistent methodologies and unwavering commitment to quality service help you build the strong compliance and reporting foundations and sustainable tax strategies that help your business achieve its potential. It's how we make a difference.

For more information, visit ey.com/ca/tax.

About EY Law LLP

EY Law LLP is a national law firm affiliated with EY in Canada, specializing in tax law services, business immigration services and business law services.

For more information, visit eylaw.ca.

About EY Law's Tax Law Services

EY Law has one of the largest practices dedicated to tax planning and tax controversy in the country. EY Law has experience in all areas of tax, including corporate tax, human capital, international tax, transaction tax, sales tax, customs and excise.

For more information, visit <http://www.eylaw.ca/taxlaw>

© 2023 Ernst & Young LLP. All Rights Reserved.

A member firm of Ernst & Young Global Limited.

This publication contains information in summary form, current as of the date of publication, and is intended for general guidance only. It should not be regarded as comprehensive or a substitute for professional advice. Before taking any particular course of action, contact EY or another professional advisor to discuss these matters in the context of your particular circumstances. We accept no responsibility for any loss or damage occasioned by your reliance on information contained in this publication.

ey.com/ca