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Canadian Tax and Legal alert

2022 Fall Economic Statement tax highlights

November 4, 2022

Deputy Prime Minister and Minister of Finance, the Honourable Chrystia Freeland, presented the 2022 Fall Economic Statement in the House of Commons on November 3, 2022. Draft legislation was also released to advance certain measures from Budget 2022, in addition to select measures from the Fall Economic Statement.

A summary of the tax highlights contained in the Fall Economic Statement is provided below.

What wasn't there

- There were no broad increases to personal or corporate tax rates, no increases in goods and services tax (GST), or harmonized sales tax (HST), and no new taxes on wealth, inheritance or capital. The capital gains inclusion rate remains at 50%.

- Several details on Budget 2022 initiatives, expected for fall 2022, have been deferred until Budget 2023. These include updates on the review of the Scientific Research and Experimental Development (SR&ED) program (including work on a potential patent box regime) and the individual Alternative Minimum Tax. No timelines were provided on broader tax consultations on topics such as the general anti-avoidance rule or transfer pricing.

- No draft legislation or detailed rules were announced on broader international tax measures, including hybrid mismatch arrangements or Canada's implementation of initiatives from the Organization for Economic Co-operation and Development's (OECD) concerning the reallocation of taxing rights (Pillar One) and a global minimum tax (Pillar Two). However, the government reiterated its support for a multilateral coordinated approach for the implementation of these initiatives.

New taxes on share buybacks by public corporations coming in 2024

A new tax equal to 2% of the net value of all types of share buybacks by public corporations was announced, effective January 1, 2024. The measure is expected to raise $2.1 billion over the next five years.

The government will release details in Budget 2023. The measures are intended to be similar to a recent US measure, as introduced in the Inflation Reduction Act. The US measure is applicable for repurchases made after December 31, 2022, at a rate of 1% of the fair market value of the repurchases.

More funding for the green economy

Building on Budget 2022, additional measures were announced to encourage investment in technologies to help achieve the government's goal of net zero emissions by 2050.

- A new refundable investment tax credit of up to 30% to encourage investment in clean technologies, including electricity generation systems, electricity storage systems, low-carbon heat equipment and certain industrial zero-emission vehicles. This measure was previously announced, without details, in Budget 2022.

- A new refundable investment tax credit of up to 40% for clean hydrogen investments. The tax credit appears to be based on recent measures in the US Inflation Reduction Act, with a forthcoming public consultation being launched to determine the implementation.

- Details were released on the operation of a $15 billion Canada Growth Fund, first announced in Budget 2022. The fund intends to invest alongside private sector capital on scale-up projects through a flexible range of instruments, including debt, equity, price assurance contracts and offtake contracts. The fund will be operated independently from government. Budget 2022 suggested that for every dollar of investment it will aim to attract at least three dollars of private capital – a target which was not reiterated in the technical background document.

For both new investment tax credits, they will be applicable as of the day of Budget 2023 and subject to phase outs starting in 2030 (clean hydrogen) and 2032 (clean technologies). In addition, consultations with unions and other stakeholders will be undertaken to inform required labour conditions. Failure to achieve labour conditions will result in claiming a lower investment tax credit by 10%.

Updated draft legislation on interest deductibility limits

Budget 2021 first announced the Excessive Interest and Financing Expenses Limitations (EIFEL), with draft legislation released in February 2022 for public comment. Generally, the rules are intended to limit deductible net interest and financing expenses to 30% of a corporation's adjusted taxable income (ATI) – which is essentially a version of earnings before interest, taxes, depreciation and amortization (EBITDA) determined using tax principles – in a detailed and complex framework, as outlined in our tax alert of March 15, 2022.[1] Concurrent with the Economic Statement, revised draft legislation was released deferring the introduction of the EIFEL measures until taxation years commencing on or after October 1, 2023 (originally January 1, 2023). Additionally, the previously proposed transitional measure, which provided for an increased deduction limit based on 40% of ATI for the first taxation year in which the rules apply, has been eliminated for a large subset of taxpayers, most notably those with calendar year ends. A second public consultation period is open until January 6, 2023.

Key highlights in the revised draft legislation include:

- An expansion of safe harbour rules to exclude i) Canadian groups with net interest expense not in excess of $1 million (previously $250,000), ii) associated CCPC groups with taxable capital not in excess of $50 million (previously $15 million), and iii) certain groups that carry on substantially all of their business in Canada and, among other things, do not hold shares in material foreign affiliates.
- The new rules expand the potential relief for highly leveraged groups under the GAAP-based group ratio rules.
- The revised draft legislation permits taxpayers to carry forward any restricted interest and financing expense indefinitely (previously limited to 20 years).
- An exemption in respect of certain public-private partnership infrastructure projects.
- The computation of ATI has been amended to require a taxpayer to reflect adjustments for terminal losses and recapture income under the capital cost allowance (CCA) system.
- The computation of ATI has been amended to permit a taxpayer to add back certain resource expenses including Canadian exploration expense, Canadian development expense and Canadian oil and gas property expense, etc.
- The rules have been expanded to incorporate various elements of foreign accrual property income and losses in the EIFEL computations and restrictions.
- The rules have been amended to provide an expansion of circumstances in which related financial institutions can share capacity.
- The rules provide the Canada Revenue Agency (CRA) with discretion to accept late or amended elections concerning the transfer of capacity within eligible groups.
- The government amended various anti-avoidance rules to make them more narrowly targeted.

A separate tax alert will follow with additional technical details in due course.

Expanded tax disclosure reporting rules delayed

Budget 2021 proposed expanded mandatory reporting of certain tax transactions by taxpayers and advisors. The proposals, as detailed through draft legislation released in February 2022 and August 2022, were broadly drafted in favour of disclosure. These proposals, which created numerous challenges for taxpayers and their advisors, were scheduled to take effect on January 1, 2023.

The Department of Finance announced that, in order to fully assess consultation feedback, the reporting requirements for reportable transactions and notifiable transactions would be deferred until legislation is introduced and receives Royal

[1] Canadian Tax & Legal Alert - Finance releases long-awaited draft proposals limiting deductibility of interest and financing expenses (deloitte.com)

Assent. New disclosure rules for large corporations on uncertain tax treatments remains scheduled for taxation years beginning after 2022, with financial penalties only applying after Royal Assent.

How can Deloitte help you?

Deloitte professionals can help you understand how these measures may impact your business. If you have any questions, please reach out to your Deloitte advisor or any of the individuals noted in this alert.

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