Federal Budget 2018 – A Continued Focus on Fairness and the Middle Class

February 27, 2018

The Honourable William Morneau, Minister of Finance, tabled the government's 2018 federal budget ("Budget 2018") on February 27, 2018 ("Budget Day"). Budget 2018 predicts slowly decreasing deficits and announces spending increases focused on increasing benefits to families, opportunities and equality for women, and funding for science and Indigenous services. Budget 2018 includes little detail addressing the aggressive stances taken on trade negotiations and tax reform by the United States — Canada's largest trading partner and competitor for business and investment.

The tax measures included in Budget 2018 focus on three themes: shifting the tax burden to wealthier Canadians, reducing tax avoidance opportunities, and promoting compliance. These tax measures include a new iteration of the July 2017 proposals regarding the taxation of passive investment income in private corporations as well as related changes to the refundable dividend tax on hand ("RDTOH") regime. Budget 2018 also includes various tax measures that propose to limit what the government views as avoidance opportunities, including in respect of equity-based financial arrangements, tiered partnerships and cross-border surplus stripping. As the government seeks to increase compliance, Budget 2018 also proposes changes to reassessment periods and enhanced information sharing.

Business Income Tax Measures

Passive Investment Income

Budget 2018 proposes two measures, and introduces companion draft legislation, to limit tax deferral advantages on passive investment income earned inside private corporations. The government anticipates that these measures, together with the previously announced changes to the income sprinkling rules, will raise $925 million annually by 2022-2023.

These measures will apply to taxation years that begin after 2018.

Business Limit Reduction

Budget 2018 proposes to reduce the business limit for Canadian-controlled private corporations ("CCPCs") that have significant income from passive investments. Under this measure, the business limit will be reduced on a straight-line basis for CCPCs having between $50,000 and $150,000 in investment income.

The measure will affect CCPCs only to the extent that their business income exceeds the reduced business limit. For example, a CCPC with $100,000 of investment income would have its business limit reduced to $250,000. As long as the reduced business limit remains above the active business income of the CCPC, all of that income would continue to be taxed at the small business tax rate. A CCPC with $75,000 of business income would have to earn more than $135,000 in passive income before its business limit is reduced below its business income. This feature of the proposed rules recognizes that CCPCs with lower amounts of business income generate less retained earnings that can later be used for reinvestment in the business, and may have more difficulty accessing capital. CCPCs with business income above the reduced business limit will be taxed on income above the business limit at the general corporate tax rate.

For the purpose of determining the reduction of the business limit of a CCPC, investment income will be measured by "adjusted aggregate investment income" which will be based on "aggregate investment income" (a concept that is currently used in computing refundable tax in respect of a CCPC's investment income) with certain adjustments. Adjusted aggregate investment income will exclude taxable capital gains from the disposition of "active assets" (which are assets used in an active business in Canada), qualified small business corporation shares of a connected corporation, or a 10% or greater interest in a partnership that meets certain active business tests. Adjusted aggregate investment income will also exclude investment income that is incidental to an active business.

The business limit reduction under this measure will operate alongside the existing business limit reduction that applies in respect of taxable capital in excess of $10 million. The reduction in a corporation's business limit will be the greater of the two reductions.

Refundability of Taxes on Investment Income

Budget 2018 proposes that a refund of RDTOH be available only in cases where a private corporation pays non-eligible dividends. An exception will be provided in respect of RDTOH that arises from eligible portfolio dividends received by a corporation, in which case the corporation will still be able to obtain a refund of RDTOH upon the payment of eligible dividends. As such, CCPCs will no longer be able to obtain refunds of tax paid on investment income while distributing dividends from active business income taxed at the general corporate rate. Refunds will continue to be available when investment income is paid out. This measure will apply to taxation years that begin after 2018.

The proposed measures will necessitate the addition of a new RDTOH account. The current RDTOH account (which will be referred to as non-eligible RDTOH) will include the refundable portion of Part I tax, refundable Part IV tax on non-eligible portfolio dividends (*i.e.* non-eligible dividends that are paid by non-connected corporations) and refundable Part IV tax to the extent dividends from a connected corporation resulted in a dividend refund from the non-eligible RDTOH account of that connected corporation. A

new RDTOH account (eligible RDTOH) will track refundable taxes paid under Part IV on eligible portfolio dividends received from non-connected Canadian corporations and refundable Part IV tax in respect of eligible dividends from a connected Canadian corporation where the dividend resulted in a dividend refund from the eligible RDTOH account of that connected corporation.

Upon the payment of a non-eligible dividend, a private corporation will be required to obtain a refund from its non-eligible RDTOH account before it obtains a refund from its eligible RDTOH account.

An anti-avoidance rule will apply to prevent the deferral of the application of this measure through the creation of a short taxation year.

A corporation's existing RDTOH balance will be allocated as follows:

- For a CCPC, the lesser of its existing RDTOH balance and an amount equal to 38⅓% of the balance of its general rate income pool, if any, will be allocated to its eligible RDTOH account. Any remaining balance will be allocated to its non-eligible RDTOH account.
- For any other corporation, all of the corporation's existing RDTOH balance will be allocated to its eligible RDTOH account.

Tax Support for Clean Energy

Under the capital cost allowance regime, Class 43.2 of Schedule II to the *Income Tax Regulations* provides an accelerated capital cost allowance rate (50% on a declining-balance basis) for investments in specified clean energy generation and conservation equipment in respect of property acquired before 2020. Budget 2018 proposes to extend eligibility for Class 43.2 by five years so that it is available in respect of property acquired before 2025 to continue to encourage investment in technologies that can contribute to a reduction in emissions of greenhouse gases and air pollutants.

Artificial Losses Using Equity-Based Financial Arrangements

Previous amendments to the dividend rental arrangement rules essentially denied the inter-corporate dividend deduction on dividends received by a taxpayer on a Canadian share in respect of which there is a synthetic equity arrangement. To address perceived continued abuses, Budget 2018 introduces amendments (described as clarifying) to certain aspects of the synthetic equity arrangement rules and the securities lending arrangement rules to prevent taxpayers from realizing artificial tax losses through the use of equity based financial arrangements.

Synthetic Equity Arrangements

Budget 2018 proposes an amendment to the "no tax-indifferent investor" exception to the synthetic equity arrangement rules that will clarify that the exception cannot be met when a tax-indifferent investor obtains all, or substantially all, of the risk of loss and opportunity for gain or profit in respect of the Canadian share in any way, including where the tax-indifferent investor has not entered into a synthetic equity arrangement or a specified synthetic equity arrangement in respect of the share.

This measure will apply to dividends that are paid, or become payable, on or after Budget Day.

Securities Lending Arrangements

Budget 2018 proposes an amendment to broaden the "securities lending arrangement" definition in the *Income Tax Act* to ensure that taxpayers that enter into arrangements that are substantially similar to those that fall within that definition are subject to several provisions normally applicable to "securities lending arrangements". As a result of this amendment, when a taxpayer receives dividends on a Canadian share acquired under a substantially similar arrangement, the dividend rental arrangement rules will generally apply. Therefore, the inter-corporate dividend deduction will be denied, resulting in a dividend income inclusion that will appropriately offset the available deduction for the amount of the corresponding dividend compensation payments made to the counterparty under the arrangement.

Budget 2018 also proposes an amendment to clarify the interaction of two rules governing the deductibility of dividend compensation payments made by a taxpayer under a securities lending arrangement. Under the first rule, a taxpayer that is a registered securities dealer is permitted to deduct up to two-thirds of a dividend compensation payment to a counterparty. The second rule applies when a securities lending arrangement is a dividend rental arrangement. In these circumstances, the second rule generally permits the taxpayer, whether or not it is a registered securities dealer, to fully deduct any dividend compensation payment made to the counterparty. The proposed amendment will clarify that this first rule does not apply when the second rule applies.

This measure will apply to dividend compensation payments that are made on or after Budget Day, unless the securities lending or repurchase arrangement was in place before Budget Day, in which case this measure will apply to dividend compensation payments that are made after September 2018.

Stop-Loss Rule on Repurchase of Mark-to-Market Shares

Previous amendments extended the dividend stop-loss rules to shares held as mark-to-market property in all cases where the taxpayer is deemed to have received a dividend on a share repurchase. Under the current rules, the dividend stop-loss rule only denies a portion of the tax loss realized on a share repurchase equal to the excess of the original cost of the shares over their paid-up capital. The portion of the tax loss equal to the mark-to-market income previously realized on the shares is allowed on the premise that the Canadian financial institution already paid tax on that income. However, if the repurchased shares are fully hedged (which the government considers to be the typical case) any mark-to-market income is fully offset under the hedge, and the Canadian financial institution would realize an artificial tax loss on the share repurchase.

In order to combat transactions that the government perceives as taking advantage of the unintended tax benefits of the current rules, Budget 2018 proposes to amend the provisions of the *Income Tax Act* pertaining to shares held as mark-to-market property so that the tax loss otherwise realized on a share repurchase is generally decreased by the dividend deemed to be received on that repurchase when that dividend is eligible for the inter-corporate dividend deduction.

This measure will apply in respect of share repurchases that occur on or after Budget Day.

At-Risk Rules for Tiered Partnerships

A recent Federal Court of Appeal decision (*The Queen v. Green et al,* 2017 FCA 107) permitted an expanded use of limited partnership losses in the context of so-called "tiered" partnership structures (*i.e.* a partnership that is itself a partner in another partnership).

Budget 2018 proposes to clarify how the "at-risk" rules apply to a tiered partnership. In this case, the at-risk amount of a limited partner generally represents the partner's invested capital that is at risk in the partnership. Budget 2018 proposes a measure to restrict the losses from the lower-tier partnership that can be allocated to the top-tier partnership that is a limited partner to that upper-tier partnership's at-risk amount in respect of the lower-tier partnership. Any such losses in excess of the at-risk amount of the upper-tier limited partnership cannot be immediately deducted by the upper-tier partnership and will not be eligible for an indefinite carry-forward. Rather, such losses will be reflected in the adjusted cost base of the upper-tier partnership's interest in the lower-tier partnership.

This measure will apply in respect of taxation years that end on or after Budget Day. Losses from a partnership incurred in a taxation year that ended prior to Budget Day will not be available to be carried forward to a taxation year that ends on or after Budget Day if the losses were allocated — for the year in which the losses were incurred — to a limited partner that is another partnership.

Health and Welfare Trusts

For many years, health and welfare trusts ("HWTs") have been used as a means of providing health benefits to employees pursuant to administrative requirements established by the CRA. In 2010, provisions were added to the *Income Tax Act* to regulate employee life and health trusts ("ELHTs"), which provide designated employee benefits (*i.e.* group sickness or accident insurance, group term life insurance or benefits provided under a private health services plan) for employees and certain related persons. Budget 2018 proposes to consolidate the rules applicable to HWTs and ELHTs and require HWTs to convert into ELHTs. As a result, the CRA will no longer apply its administrative positions with respect to HWTs after the end of 2020, and will not apply its administrative positions with respect to HWTs established after Budget Day.

To facilitate the conversion of existing HWTs to ELHTs, transitional rules will be introduced to the *Income Tax Act*. The CRA will announce transitional administrative guidance relating to winding-up existing HWTs. HWTs that do not convert to ELHTs (or wind-up) will be subject to the normal income tax rules for *inter vivos* trusts.

The government has invited stakeholders to submit comments by June 29, 2018 on transitional issues, both administrative and legislative, to facilitate the discontinuation of the HWT regime. Following the consultation, the government intends to release draft legislative proposals and transitional administrative guidance.

International Tax Measures

Budget 2018 reflects continued tightening around the edges of the elements of Canada's tax system dealing with international transactions to address perceived tax avoidance, as well as administrative amendments designed to make audits of such transactions easier for the CRA. In particular, Budget 2018:

- reiterates Canada's commitment to work collectively with other countries on various information sharing and anti-avoidance initiatives contained in the OECD's Base Erosion and Profit Shifting ("BEPS") project, including the enactment and ratification of the Multilateral Instrument later in 2018;
- moves up the deadline for T1134 information returns in respect of foreign affiliates of a taxpayer to the taxpayer's income tax return deadline; and
- extends the statutory limitation period for the CRA to re-assess taxpayers (1) in respect of income arising in connection with a foreign affiliate of a taxpayer, or (2) where certain losses arising from transactions with non-arm's-length non-residents have been carried back to a prior year.

The expansion of the CRA's ability to gather information and re-assess taxpayers in respect of international transactions continues to be a priority for the government.

Cross-Border Surplus Stripping Using Partnerships and Trusts

Paid-up capital ("PUC") generally reflects amounts received by a Canadian corporation on the issuance of its shares from treasury, subject to various adjustments in the *Income Tax Act*. PUC constitutes an important tax attribute, in particular for non-resident shareholders. This is because (1) a Canadian corporation can generally choose to distribute property to shareholders as a non-dividend return of capital up to the amount of its PUC (*i.e.*, without incurring non-resident dividend withholding tax otherwise applicable to non-resident shareholders); and (2) the PUC of such shares held by significant non-resident shareholders forms part of the corporation's "equity" supporting the deductibility of interest for tax purposes under Canada's "thin capitalization" rules.

The *Income Tax Act* contains various rules designed to prevent the inappropriate extraction of property out of a Canadian corporation in excess of the PUC of its shares ("surplus stripping") without tax being paid, as well as the undue creation or duplication of PUC that would enable future surplus stripping. These rules either deem the Canadian corporation to have paid a dividend (triggering dividend withholding tax for non-resident shareholders) or suppress the corporation's PUC below what it would otherwise be. In particular, the rules dealing with cross-border anti-surplus stripping prevent non-residents from achieving these tax benefits through a transfer of the shares of one corporation resident in Canada (the "Canadian subject corporation"), to another such corporation (the "Canadian purchaser corporation") with which the non-resident does not deal at arm's length.

These rules (which were amended in the 2017 federal budget to address perceived avoidance techniques) are being further tightened in Budget 2018. The 2018 measures (which are not yet the subject of specific draft legislation) propose to prevent the circumvention of the main cross-border anti-stripping rule through the transfer of an interest in a partnership or trust that owns shares of a Canadian corporation, instead of

direct transfers of those shares to which the main rule applies. This will be accomplished via an anti-avoidance “look-through” rule that will allocate the assets, liabilities and transactions of a partnership or trust to its members or beneficiaries, *pro rata* to the fair market value of their respective interests in the partnership or trust. Budget 2018 expressly states (1) the government’s intention to challenge pre-Budget Day transactions of this nature under the general anti-avoidance rule ("GAAR") in the *Income Tax Act*, and (2) that planning devices indirectly achieving what would otherwise be caught under these rules will be considered inconsistent with their policy intent and therefore open to challenge under the GAAR. This measure will apply to transactions occurring on or after Budget Day.

Foreign Affiliates

Budget 2018 proposes modifications to the rules applicable to the taxation of Canadian resident shareholders with interests in non-resident corporations that qualify as foreign affiliates. In general terms, Canada’s foreign affiliate rules differentiate between certain active business income and other income referred to as "foreign accrual property income" ("FAPI") earned by foreign affiliates of Canadian taxpayers. FAPI of a controlled foreign affiliate of a Canadian taxpayer may be taxable in the hands of the taxpayer in the year in which the FAPI is earned. Budget 2018 proposes two important administrative changes and introduces a number of targeted avoidance rules regarding foreign affiliates.

T1134 Information Returns

Taxpayers (and certain partnerships) are required to file a T1134 information return each year in respect of each of their foreign affiliates in the year. These returns contain, among other things, information about amounts included in, and excluded from FAPI.

Budget 2018 proposes to bring the T1134 information return deadline in line with the taxpayer’s income tax return deadline by requiring the information returns to be filed within six months after the end of the taxpayer’s taxation year. This means that for a corporate taxpayer, any T1134 information return for a particular taxation year will be due at the same time as its T2 income tax return and any T106 information returns, rather than 15 months after the end of its taxation year.

To give taxpayers time to adjust, this measure will apply to taxation years of a taxpayer that begin after 2019.

Reassessment Period Extended by Three Years

Budget 2018 proposes to extend the reassessment period for a taxpayer by three years in respect of income arising in connection with a foreign affiliate of the taxpayer (this is separate from the three-year extended reassessment period that currently exists in respect of transactions with non-arm’s length non-residents). This means that for most taxpayers with foreign affiliates, the CRA will generally have seven years after its initial assessment in which to audit and reassess the taxpayer’s tax liability in respect of foreign affiliates.

This measure will apply to taxation years of a taxpayer that begin on or after Budget Day.

Trading or Dealing in Indebtedness

Budget 2018 proposes to add a minimum capital requirement to the regulated foreign financial institutions exception found in the rules applicable to foreign affiliates that are trading or dealing in indebtedness; the capital requirement will be similar to that in the foreign financial institutions exception found in the “investment business” rules.

This measure will apply to taxation years of a taxpayer’s foreign affiliate that begin on or after Budget Day.

Investment Business Tracking Arrangements

Budget 2018 proposes anti-avoidance rules aimed at certain "tracking arrangements" used by Canadian taxpayers. The first measure targets certain tracking arrangements used by taxpayers engaged in planning with other taxpayers seeking to cause a foreign affiliate to meet the beneficial "more than five full-time employees" condition (sometimes referred to as the "six employees test") in the investment business exception, such that the foreign affiliate’s income from its foreign investment activities would not be included in FAPI. This planning involves grouping their financial assets together in a common foreign affiliate in order to carry on investment activities outside of Canada through the affiliate that, if undertaken separately, would require five or fewer full-time employees.

Budget 2018 proposes to introduce a rule which, generally summarized, would deem income attributable to specific activities carried out by the common foreign affiliate which accrues to the benefit of a specific taxpayer under a tracking arrangement to be a separate business and that separate business itself would need to satisfy each relevant condition in the investment business exception, including the six employees test. Budget 2018 suggests that some tracking arrangements may give rise to separate businesses irrespective of whether this proposed deeming rule applies, and indicates that the CRA may challenge such arrangements on the basis of the proposed deeming rule as well as existing anti-avoidance rules where appropriate.

This measure will apply to taxation years of a taxpayer’s foreign affiliate that begin on or after Budget Day.

Controlled Foreign Affiliate Status Tracking Arrangements

FAPI earned by a controlled foreign affiliate of a Canadian taxpayer is attributed to, and taxed in the hands of, the Canadian taxpayer. Budget 2018 also proposes a second tracking arrangement measure to target arrangements used by Canadian taxpayers to avoid controlled foreign affiliate status (*i.e.* the group of taxpayers is sufficiently large that they take the position that they do not have, and do not participate in, a controlling interest in the affiliate). Under the tracking arrangement, each taxpayer retains control over its contributed assets and any returns from those assets accrue to its benefit.

Budget 2018 proposes an anti-avoidance rule to target these types of tracking arrangements by deeming a foreign affiliate of a taxpayer to be a controlled foreign affiliate of the taxpayer if FAPI attributable to activities of the foreign affiliate accrues to the benefit of the taxpayer under a tracking arrangement. This measure is intended to ensure that each taxpayer involved in such a tracking arrangement — no matter how

large the group — is subject to accrual taxation in respect of FAPI attributable to that taxpayer.

This measure will apply to taxation years of a taxpayer's foreign affiliate that begin on or after Budget Day.

Reassessment Period — Requirements for Information and Compliance Orders

Budget 2018 proposes to amend the *Income Tax Act* to introduce a "stop-the-clock" rule where a taxpayer contests a requirement for information or compliance order issued by the CRA. This rule, which currently applies to requirements for foreign-based information, will extend the reassessment period of a taxpayer by the period of time during which the requirement or compliance order is contested. The period will generally start at the time the taxpayer makes an application for judicial review of the requirement or opposes (generally by way of notice of appearance) the CRA's application for a compliance order. The period will end upon the final disposition of the application (including any appeals). Related amendments will also be made to conform the rules with respect to requirements for foreign-based information. These measures will prevent taxpayers from shortening the period during which the CRA can issue a reassessment by contesting a requirement for information or compliance order.

This measure will apply in respect of challenges instituted after Royal Assent to the enacting legislation.

Reassessment Period — Non-Resident Non-Arm's Length Persons

If a taxpayer incurs a loss in a taxation year and carries the loss back to deduct against the taxpayer's income in a prior taxation year, the CRA has an additional three years to reassess that prior year. The loss carry-back reassessment period does not take into account the fact that an extended three-year reassessment period exists in respect of reassessments made as a consequence of a transaction involving a taxpayer and a non-resident person with whom the taxpayer does not deal at arm's length.

Budget 2018 proposes to provide the CRA with an additional three years to reassess a prior taxation year of a taxpayer where the reassessment relates to the adjustment of the loss carryback, resulting from the reassessment of a taxation year as a consequence of a transaction involving a taxpayer and a non-resident person with whom the taxpayer does not deal at arm's length. The additional three-year period will be available where the reassessment reduces the taxpayer's loss for the taxation year that is available for carryback, and all or any portion of that loss had in fact been carried back to the prior taxation year.

This measure will apply in respect of taxation years in which a carried back loss is claimed, where that loss is carried back from a taxation year that ends on or after Budget Day.

Sharing Information for Criminal Matters

Budget 2018 proposes to enhance information sharing as part of the government's commitment to address global tax evasion and promote fairness of the tax system through the following measures:

- allow existing legal tools available under the *Mutual Legal Assistance in Criminal Matters Act* ("MLACMA") (which is administered by the Department of Justice) to be used with respect to the sharing of criminal tax information under Canada's tax treaties and tax information exchange agreements ("TIEAs"), and the *Convention on Mutual Administrative Assistance in Tax Matters*.
- Enable confidential information under Part IX of the *Excise Tax Act* and the *Excise Act, 2001* to be disclosed to Canadian police officers in respect of offences where such disclosure is currently permitted in respect of taxpayer information under the *Income Tax Act*.

These measures may require amendments to a number of statutes and should come into force upon Royal Assent to the enacting legislation.

Other International Tax Matters

- *Adoption of the MLI*: In 2017, Canada, along with 71 other jurisdictions, became signatories to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (known as the Multilateral Instrument or MLI). The MLI is intended to allow participating jurisdictions to modify their existing tax treaties to include measures developed under the OECD/G20 BEPS project without having to individually renegotiate those treaties. Steps will be taken in 2018 to enact the MLI into Canadian law and ratify it as needed to bring it into force.
- *Anti-treaty Abuse Provisions*: Budget 2018 announced that the government intends to adopt new anti-treaty abuse provisions in Canada's tax treaties either through the MLI or by renegotiating existing tax treaties.
- *Transfer Pricing*: Canada has adopted the revised OECD Transfer Pricing Guidelines and has assisted in developing additional guidance on issues identified in the course of the BEPS project, including the attribution of profits to permanent establishments, the use of the profit split method, and the treatment of hard-to-value intangibles. Additional guidance regarding these issues is due to be published in 2018.

Personal Income Tax Measures

Reporting Requirements for Trusts

The Government takes the view that more comprehensive information with respect to trusts will help authorities to effectively counter aggressive tax avoidance, tax evasion, money laundering and other criminal activities.

To improve collection of information about the beneficial owners of trusts in Canada, Budget 2018 proposes to require that express trusts resident in Canada and non-resident trusts currently required to file a T3 return provide additional information on an annual basis. The new reporting requirements will impose an obligation on certain trusts to file a T3 return where one does not currently exist.

Exceptions to the additional reporting requirements are proposed for the following types of trusts:

- mutual fund trusts, segregated funds and master trusts;
- trusts governed by registered plans;
- lawyers' general trust accounts;
- graduated rate estates and qualified disability trusts;
- trusts that qualify as non-profit organizations or registered charities; and
- trusts that have been in existence for less than three months or that hold less than $50,000 in assets throughout the taxation year (provided, in the latter case, that their holdings are confined to deposits, government debt obligations and listed securities).

It will be important for investment funds and other collective investment vehicles that are structured as trusts which do not qualify as mutual fund trusts, segregated funds or master trusts, to consider how compliance with these new rules can be achieved. This may be particularly difficult for trusts with regularly changing ownership.

Trusts will be required to disclose the identity of:

- settlors
- trustees
- beneficiaries
- any person who can exert control over trustee decisions regarding the appointment of income or capital (*e.g.* a protector)

To support these new reporting requirements, Budget 2018 proposes to introduce a new penalty of $25 per day of delinquency up to a maximum of $2,500, for a failure to file a T3 return, including the new required information. If a failure to file the return was made knowingly, or due to gross negligence, an additional penalty of 5% of the fair market value held by the trust in the year will apply in addition to existing penalties.

These proposed new reporting requirements and penalties will apply to returns required to be filed for the 2021 and subsequent taxation years.

Consistent with the above changes to information reporting requirements for trusts, in December 2017, federal, provincial and territorial finance ministers agreed to pursue amendments to corporate statutes to require corporations to improve their beneficial ownership information.

Other Charity and Personal Income Tax Measures

- *Municipalities as Eligible Donees:* Allow transfers of property to municipalities to be considered qualifying expenditures for the purposes of reducing the revocation tax payable by a charity whose registration has been revoked by CRA, subject to the approval of the Minister of National Revenue on a case-by-case basis. This measure will apply to transfers made on or after Budget Day.
- *Universities Outside Canada:* To simplify the administration of the donation rules and the registration process applicable to certain universities outside Canada by removing the requirement that universities outside Canada be prescribed in the *Income Tax Regulations*. This measure will apply as of Budget Day.
- *Registered Disability Savings Plan ("RDSP") — Qualifying Plan Holders:* The current temporary measure allowing a qualifying family member (*i.e.* a parent, spouse or common-law partner) to act as a holder of an RDSP on behalf of an

incapable adult beneficiary of an RDSP has been extended by five additional years, to the end of 2023. All such arrangements then in place may continue.
- *Deductibility of Employee Contributions to the Enhanced Portion of the Québec Pension Plan ("QPP"):* Provide a deduction for employee contributions (as well as the "employee" share of contributions made by self-employed persons) to the enhanced portion of the QPP for the 2019 and subsequent taxation years to provide consistent income tax treatment of CPP and QPP contributions.

Changes to Tax Credits

- *Medical Expense Tax Credit — Eligible Expenditures:* Expand the medical expense tax credit to recognize expenses incurred after 2017 in respect of an animal specially trained to perform tasks for a patient with a severe mental impairment in order to assist them in coping with their impairment.
- *Mineral Exploration Tax Credit for Flow-Through Share Investors*:Extend eligibility for the mineral exploration tax credit for an additional year, to flow-through share agreements entered into on or before March 31, 2019.
- *Child Benefits — Provincial/Territorial Access to Taxpayer Information*: Provide legislative authority for the government to share with the provinces and territories taxpayer information related to the Canada Child Benefit (introduced in Budget 2016), as of July 1, 2018, solely for the purpose of administering their social assistance payment regimes.
- *Child Benefits — Retroactive Eligibility of Foreign-Born Status Indians*: Foreign-born status Indians residing legally in Canada who are neither Canadian citizens nor permanent residents (currently eligible for the Canada Child Benefit) be made retroactively eligible for the Canada Child Tax Benefit, the National Child Benefit supplement and the Universal Child Care Benefit, where all other eligibility requirements are met, from the 2005 taxation year to June 30, 2016.
- *Canada Workers Benefit:* Rename the Working Income Tax Benefit as the “Canada Workers Benefit”, enhance the benefits by an additional $500 million per year starting in 2019 and certain other administrative and reporting amendments.

Sales and Excise Tax Measures

GST/HST Measures

GST/HST and Investment Limited Partnerships

On September 8, 2017, the government released draft legislative and regulatory proposals relating to the application of the Goods and Services Tax/Harmonized Sales Tax ("GST/HST") to investment limited partnerships ("ILPs").

Budget 2018 confirms the intention to proceed with previous proposals for ILPs, with the following changes:

- Modify the September 8, 2017 proposal so that the GST/HST applies to management and administrative services rendered by the general partner on or after September 8, 2017, and not to management and administrative services rendered by the general partner before September 8, 2017 unless the general

partner charged GST/HST in respect of such services before that date. GST/HST will generally be payable on the fair market value of management and administrative services, and will be payable in the period in which these services are rendered.
- Allow ILPs to make an election to advance the application of the special HST rules as of January 1, 2018.

The updated legislation does not address concerns surrounding GST/HST valuation and timing issues, particularly as general partner management and administrative services may be rendered to a partnership well in advance of the date the general partner receives payment. The updated legislation also provides no further guidance on the seemingly overly broad definition of ILPs. That said, these changes appear to address investment fund industry concerns relating to management and administrative services rendered prior to September 8, 2017 which would have been caught under the draft legislation.

Consultations on the GST/HST Holding Corporation Rules

The GST/HST Holding Corporation rules allow a parent corporation to claim input tax credits to recover GST/HST paid in respect of expenses that relate to a related operating corporation. It has been questioned why these rules apply only to corporations. Disputes have also arisen as to which expenses of the parent corporation are in respect of shares or indebtedness of a related corporation and qualify for input tax credits. The government intends to consult on both of these aspects. Consultation documents and draft legislative proposals are to be released for public comment in the near future.

Other Excise Tax Measures

Tobacco Taxation

Budget 2018 proposes to advance the existing inflationary adjustments for tobacco excise duty rates to occur on an annual basis (April 1) rather than every five years. Budget 2018 also includes further excise duty rate increases on various tobacco products. Inventories of cigarettes held by manufacturers, importers, wholesalers and retailers at the end of Budget Day will be subject to an inventory tax.

Cannabis Taxation

Budget 2018 confirms the government's intention to implement proposed amendments to the *Excise Act, 2001* regarding the federal excise duty framework for cannabis products. The duty will generally apply to all products available for legal purchase, whether for medical purposes through the *Access to Cannabis for Medical Purposes Regulations* or for adult use purposes through applicable commercial channels.

Notably, the government reversed its plan to tax all cannabis products equally. Products with low amounts of THC will generally not be subject to the excise duty. Pharmaceutical products derived from or including cannabis will also be exempt provided that the product has a Drug Identification Number (DIN) and can only be acquired through a prescription. The government is also considering a rebate program to retroactively reimburse consumers for the federal portion of the excise duty on

purchases of cannabis products that are subsequently assigned a DIN and sold as prescription drugs.

Previously Announced Measures

Budget 2018 confirms the government's intention to proceed with the following previously announced tax and related measures, as modified to take into account consultations and deliberations since their release:

- Measures confirmed in Budget 2016 relating to the GST/HST joint venture election;
- Income tax measures announced in Budget 2016 expanding tax support for electrical vehicle charging stations and electrical energy storage equipment;
- The income tax measure announced in Budget 2016 on information reporting requirements for certain dispositions of an interest in a life insurance policy;
- Technical income tax legislative amendments released on September 16, 2016, relating to a division of a corporation under foreign laws, and to the requirements to qualify as a prescribed share;
- The income tax measure announced in Budget 2017 to support the establishment of a tax-exempt Memorial Grant for First Responders (the Community Heroes benefit);
- The income tax measure announced on May 18, 2017 for additional tax relief for Canadian armed forces personnel and police officers;
- Remaining legislative and regulatory proposals released September 8, 2017 relating to GST/HST;
- The income tax measure announced on October 16, 2017 to lower the small business tax rate from 10.5% to 10%, effective January 1, 2018, and to 9%, effective January 1, 2019, along with related amendments to the gross-up amount and dividend tax credit for taxable dividends;
- The income tax measure announced on October 24, 2017 to provide for the indexing of the Canada Child Benefit amounts as of July 1, 2018 instead of July 1, 2020; and
- Income tax measures released on December 13, 2017 to address income sprinkling.

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