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## Tax Alert – Canada

### Finance releases draft legislation for 2018 budget and other measures for comment

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.

On 27 July 2018, the Department of Finance released for consultation a package of draft legislative proposals and explanatory notes relating to a number of measures announced in the 2018 federal budget, together with a revised version of an income tax measure originally announced on 16 September 2016, as well as some other indirect tax measures. The government also released a consultation paper on proposed changes to the GST/HST holding corporation rules.

Interested parties are invited to provide comments on the legislative proposals by 10 September 2018, and on the consultation paper by 28 September 2018.

### 2018 federal budget measures

The package includes a number of income tax measures, as well as certain GST/HST and excise duty-related measures, that were announced in the 2018-19 federal budget, but not included in the first budget implementation bill enacted in June (Bill C-74).

#### *Business income and international tax measures*

- ▶ **At-risk rules for tiered partnerships** – Amendments to ensure that the at-risk rules apply at each level of a tiered partnership structure. (Applicable to taxation years ending on or after 27 February 2018, including in respect of partnership losses incurred in a taxation year ending before 27 February 2018 that would otherwise have been carried forward to a taxation year ending on or after that date).

- ▶ **Synthetic equity arrangements** – Amendments to the “no tax-indifferent investor” exception to the synthetic equity arrangement rules to ensure that the exception cannot be satisfied when a tax-indifferent investor obtains all or substantially all of the risk of loss and opportunity for gain or profit in respect of a Canadian share in any way. (Applicable to dividends that are paid, or become payable, on or after 27 February 2018).
- ▶ **Securities lending arrangements** – Broadening of the securities lending arrangement (SLA) rules to target certain securities lending or repurchase arrangements designed to fail the requirements of the current SLA definition, although they are substantially similar to an SLA. Amendments to clarify the interaction of two rules governing the deductibility of dividend compensation payments made by a taxpayer under an SLA. (Applicable to dividend compensation payments that are made on or after 27 February 2018 or, for written securities lending or repurchase arrangements in place before this date, to dividend compensation payments that are made after September 2018).
- ▶ **Stop-loss rule on share repurchase transactions** – Amendments to the dividend stop-loss rule 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 the repurchase (under subsection 84(3) of the *Income Tax Act*) when the dividend is eligible for the intercorporate dividend deduction. (Applicable in respect of share repurchases that occur on or after 27 February 2018).
- ▶ **Cross-border surplus stripping using partnerships and trusts** – Amendments to the cross-border anti-surplus stripping rule, and the corresponding corporate immigration rule, to address situations where a partnership or trust is inserted into a corporate reorganization for the purpose of achieving a tax benefit that is intended to be denied by the anti-surplus stripping rule. (Applicable to transactions or events that occur on or after 27 February 2018).
- ▶ **Foreign affiliates** – Amendments to the foreign affiliate rules, including the following:
  - ▶ **Controlled foreign affiliate status** – Amendments to deem 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.” Under a tracking arrangement, each taxpayer purportedly retains control over its contributed assets and any returns from those assets accrue to its benefit, but ownership of the nonresident entity is spread among many unrelated investors such that no single group can be said to control the affiliate. (Applicable to taxation years of a taxpayer’s foreign affiliate that begin on or after 27 February 2018).
  - ▶ **Investment business** – Amendments to the investment business exception (that treats investment income of a foreign affiliate as active business income in certain circumstances and not FAPI) to address situations where a taxpayer engages in tracking arrangements with other taxpayers in order to meet the exception. (Applicable to taxation years of a taxpayer’s foreign affiliate that begin on or after 27 February 2018).

- ▶ **Trading or dealing in indebtedness** – Amendments to add a minimum capital requirement, as well as a requirement to conduct the foreign affiliate’s relevant business principally with arm’s length persons, to the regulated foreign financial institutions exception under the trading or dealing in indebtedness rules (similar to that under the investment business rules). (Applicable to taxation years of a taxpayer’s foreign affiliate that begin on or after 27 February 2018).
- ▶ **T1134 information returns** – Amendment to bring the filing deadline for information returns in respect of a taxpayer’s foreign affiliates (Form T1134, Information Return Relating to Controlled and Not-Controlled Foreign Affiliates) in line with the taxpayer’s income tax return filing deadline of six months after the end of its taxation year (or fiscal period, if the reporting entity is a partnership). (Applicable to taxation years of a taxpayer, or fiscal periods of a partnership, that begin after 2019).
- ▶ **Passive investment income and loss allocation** – Measures to allocate losses between a corporation’s non-eligible refundable dividend tax on hand (NERDTH) and eligible refundable dividend tax on hand (ERDTH) accounts where the corporation is claiming the losses in order to partly reduce its Part IV taxes otherwise payable and those taxes would have otherwise been added to these accounts. (Applicable to taxation years beginning after 2018).
- ▶ **Reassessment periods** – Amendments to extend the reassessment period in specified circumstances, including the following:
  - ▶ **Transactions with non-arm’s-length nonresident persons** – Amendments to extend the reassessment period for a loss carried back to a prior taxation year from a subsequent taxation year by an additional three years, in circumstances where the subsequent taxation year has been reassessed (or a notification that no tax is payable has been issued for it) in respect of a transaction involving a nonresident non-arm’s-length person and the loss available for carryback is reduced by the reassessment or the notification. (Applicable to taxation years in which a carried-back loss is claimed, if that loss is carried back from a taxation year that ends on or after 27 February 2018).
  - ▶ **Requirements for information or compliance orders** – Introduction of a “stop-the-clock” rule to extend the reassessment period of a taxpayer by the period of time during which the taxpayer contests a requirement for information issued by the CRA (that does not involve foreign-based information) or compliance order issued by a court. (Applicable to challenges instituted by a taxpayer after royal assent of the enacting legislation).
  - ▶ **Income in connection with foreign affiliates** – Amendments to extend the reassessment period for a taxpayer by three years in respect of income, loss, or other amount in connection with a foreign affiliate of the taxpayer. (Applicable to taxation years of a taxpayer that begin on or after 27 February 2018).

### *Personal and other income tax measures*

- ▶ **Canada Workers Benefit** – Amendments to make optional, in the calculation of the Canada Workers Benefit, the tax-exempt part of working income earned on a reserve or an allowance received as an emergency volunteer. (Applicable as of 1 January 2019)  
Requirement for designated educational institutions in Canada to report to the CRA prescribed information regarding students' enrolment. (Applicable as of 1 January 2019).
- ▶ **Contributions to enhanced portion of the Quebec Pension Plan (QPP)** – Amendments to specifically permit the deduction for employee contributions, and the "employee" share of contributions made by self-employed persons, to the enhanced portion of the QPP. (Applicable as of 1 January 2019).
- ▶ **Reporting requirements for trusts** – Measures to require the filing of a trust return as well as the provision of additional beneficial ownership information for express trusts, with some exceptions, and to impose new penalties for failing to file a trust return (including any required beneficial ownership information) in these circumstances or making a false statement or omission in a return. (Applicable to taxation years ending after 30 December 2021).

### *GST/HST and excise duty measures*

- ▶ **Holding corporations** – Amendments to the GST/HST holding corporation rules, which generally allow a registrant corporation (the parent corporation) to claim input tax credits (ITCs) for expenses relating to the shares or indebtedness of a related corporation that is engaged in commercial activities (the operating corporation).
  - ▶ Broadening of the "commercial operating corporation property test" that the operating corporation must meet for the parent to benefit from the holding corporation rules, to include property that was last manufactured or produced by the operating corporation. Similar amendments are also made to the commercial operating corporation property test found in the takeover fees rule of subsection 186(2) of the *Excise Tax Act*, the interpretative rule of subsection 186(3) of the *Act*, and the optional GST/HST registration rule in paragraph 240(3)(d) of the *Act*. (These amendments, which address the issue raised in a 22 January 2018 comfort letter, are generally applicable to any acquisition, importation, or bringing into a participating province of property or a service after 27 July 2018).
  - ▶ Clarifications on to what extent the parent corporation can claim an ITC under the holding corporation rules for the expenses it incurred, and under which circumstances. (Applicable to any acquisition, importation, or bringing into a participating province of property or a service after 27 July 2018).

In addition to the draft legislative proposals, the government is initiating consultations, with the release of a consultation paper, on two other aspects of the GST/HST holding corporation rules, namely:

- ▶ replacing the requirement that the parent corporation and the commercial operating corporation be related (i.e., generally, one corporation controls the other corporation) with a requirement that they be closely related, meaning there is, generally, at least 90% common ownership among the corporations; and
  - ▶ expanding the holding corporation rules to include partnerships and trusts.
- ▶ **Requirements for information or compliance orders** – Amendments to the *Excise Tax Act*, and the *Excise Act, 2001* to introduce a “stop-the-clock” rule similar to the income tax one mentioned above, to extend the reassessment period of a taxpayer by the period of time during which the taxpayer contests a requirement for information issued by the CRA (that does not involve foreign-based information) or compliance order issued by a court. (Applicable to challenges instituted by a taxpayer after royal assent of the enacting legislation).

For more information on the 2018 federal budget measures, refer to EY Tax Alert 2018 Issue No. 7, Federal budget 2018-19: Equality + Growth - A Strong Middle [Class](#).

### **Previously announced income tax measures**

The package also includes a revised version of measures concerning foreign spinoffs and shareholder benefit rules, applicable to divisions of nonresident corporations that occur after 23 October 2012. The revised measures include consequential changes to the foreign affiliate surplus rules, which are generally applicable in respect of dispositions that occur after 23 October 2012. These measures were originally announced on 16 September 2016. For more information on the original measures refer to EY Tax Alert 2016 Issue No. 41, *Finance releases draft income tax technical [amendments](#)*.

### **Other GST/HST and excise tax measures**

The package also includes certain other GST/HST and excise tax measures.

- ▶ **Rebate for printed books** – Amendments to clarify that a specified person, such as a public library or educational institution, may generally not claim the GST/HST rebate in respect of acquisitions or importations of printed books and other specified property, where the person acquires or imports specified property for the purpose of making a supply by way of sale of the property, or transfers ownership of the property in the course of supplying another property or service. (Applicable to any acquisition or importation of property for which GST/HST becomes payable after 27 July 2018 without having been paid on or before that day, or is paid after 27 July 2018 without having become payable on or before that day).
- ▶ **Diesel fuel** – Amendments to allow vendors of diesel fuel to apply, under certain conditions, for an excise tax refund where a purchaser will use excise tax-paid diesel fuel to generate electricity, other than to generate electricity in or by a vehicle, including a conveyance attached to a vehicle. Currently, either the vendor or the purchaser may claim a refund for excise tax-paid diesel fuel used exclusively as heating oil, but only the purchaser may claim a refund in respect of excise tax-paid diesel fuel used exclusively to generate electricity. (Applicable on royal assent of the enacting legislation).

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