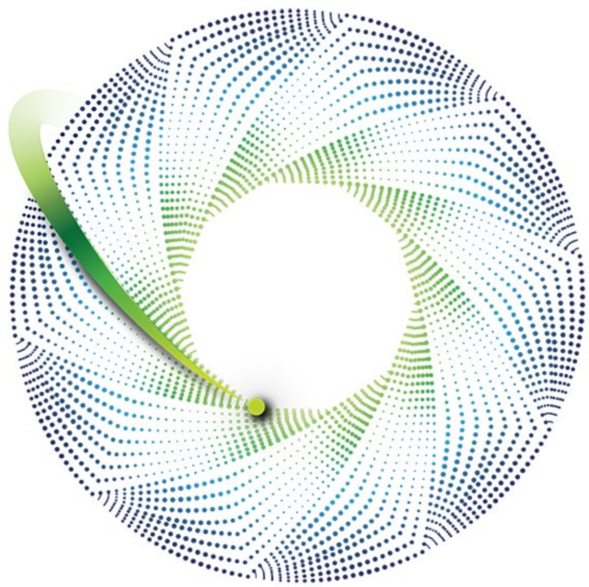

Canadian Tax & Legal Alert

2024 federal budget: Grants and incentives announcements and updates

May 22, 2024

Context

Deputy Prime Minister and Minister of Finance, the Honourable Chrystia Freeland, presented Budget 2024 entitled "Fairness for Every Generation" in the House of Commons on April 16, 2024.

Budget 2024 included several new announcements and updates on grants and incentives, with a focus on the clean economy, decarbonization, innovation, productivity, and investment in Canada. Budget 2024 reaffirmed the government's commitment to achieving net-zero carbon emissions by 2050 and expressed its intention to proceed with the important clean economy tax measures outlined in Bill C-59,[1] which is currently under consideration by Parliament.

[1] Bill C-59, *Fall Economic Statement Implementation Act, 2023*, first reading on November 30, 2023, Committee report presented with amendments, May 6, 2024, and expected to reach third reading very soon (House of Commons).

In the coming months, the government will continue to analyze the results of previous consultations, including those on the clean economy investment tax credits (ITCs), the Scientific Research and Experimental Development (SR&ED) program, and the creation of a new patent box regime in Canada. Additionally, the government announced in Budget 2024 its intention to launch a second phase of SR&ED consultations.[2] This second phase will address specific policy parameters and seek further input from businesses and industries on specific and technical reforms. The objective is to determine how the additional funding designated for the SR&ED program announced in Budget 2024 (see below) can be effectively targeted to enhance research and development (R&D) and innovation in Canada.

Budget 2024 proposes some measures to address Canada's historical lack of productivity by investing in artificial intelligence (AI) and offering businesses the opportunity to get a full-cost deduction by investing in assets that could accelerate productivity in Canada.

Clean Economy

In Budget 2024, the government reaffirmed its commitment to developing the clean economy by introducing clean economy ITCs, which include:

- Carbon Capture, Utilization and Storage (CCUS) ITC
- Clean Technology ITC
- Clean Hydrogen ITC
- Clean Technology Manufacturing ITC
- Clean Electricity ITC

Budget 2024 provides specific details on the **design and implementation of the Clean Electricity ITC**, which was previously announced in Budget 2023. Additionally, the **Clean Technology Manufacturing ITC will be expanded** to include businesses engaged in polymetallic projects. Budget 2024 also indicates that the **government anticipates,** with the support and collaboration of Parliamentarians, **Bill C-59,[3] which will enact the CCUS and Clean Technology ITCs, and other provisions (including labour requirements and special rules for partnerships), receiving Royal Assent before June 1, 2024**.

Contacts:

Rob Jeffery
National Tax Policy Leader
Tel.: 902-721-5593

Jelle Donga
National Global Investment and Innovation Incentives Leader
Tel.: 519-751-6674

David Arthur
National Tax & Legal Sustainability & Climate Leader
Tel.: 403- 261-8176

Louis Boivin
Tel.: 418- 696-3951

Gérald Lemelin
Tel.: 450- 978-3548

Related links:

Deloitte Tax Services

Global Investment and Innovation Incentives

Design and implementation of the Clean Electricity ITC

Budget 2024 sets out the design and implementation details for the previously announced refundable Clean Electricity ITC. As noted in our previous tax alert[4] on clean economy ITCs, the Clean Electricity ITC will offer a tax credit rate equal to 15% of the capital cost of eligible property when certain labour requirements are met. If these labour requirements are not met, the tax credit rate is reduced to 5%. Budget 2024 provides much expected clarifications about entities exempt from tax that could claim the ITC and about the mechanism that will be put in place so these entities can have access to the refundable ITC while not paying any income tax. This ITC will be available for taxable Canadian corporations, and it will also be available under certain conditions to the following non-taxable entities:

- Provincial and territorial Crown corporations (that are in designated jurisdictions after complying with specific conditions around their commitment to net-zero goals and passing on the benefit to ratepayers – see below for more details);
- Corporations owned by municipalities;
- Corporations owned by Indigenous communities; and
- Pension investment corporations.

[2] The second phase of consultations was launched on April 24, 2024.
[3] Supra note 1.
[4] Deloitte, "Clean energy tax credits introduced by the government of Canada to support the decarbonization of the economy," March 13, 2024; see also Canadian Tax & Legal Alert, "2023 federal budget: Canada has committed $83 billion to foster decarbonization of the economy," June 13, 2023.

Any entity exempt from tax would have to agree to be subject to the provisions of the *Income Tax Act* related to the tax credit, including provisions related to audit, enforcement, and collection. However, Budget 2024 does not provide details on how these entities would agree to this requirement in order to have access to the ITC.

Canadian corporations that are partners in a partnership will be allowed to claim their share of the partnership's Clean Electricity ITC, in a manner similar to the rules proposed for the Clean Technology ITC contained in Bill C-59.[5] In situations where property of a partnership is eligible for both tax credits, partners may claim their share of either credit, but not both, in respect of the same property.

Budget 2024 reiterates the list of qualifying properties that could be eligible for the ITC (qualifying expenditures could include the capital cost to refurbish existing facilities):

- Equipment used to generate electricity from solar, wind, or water energy (more specifically those described in subparagraphs (d)(ii), (v), (vi), or (xiv) of CCA Class 43.1 of Schedule II of the *Income Tax Regulations* but with no capacity limitation in the case of hydroelectric installations);
- Concentrated solar energy equipment used to generate electricity;
- Nuclear fission equipment used to generate electricity or both electricity and heat;
- Geothermal energy equipment used to generate electricity or both electricity and heat described in subparagraph (d)(vii) of Class 43.1;
- Equipment that generates electricity or electricity and heat from specified waste materials (as described in the 2023 Fall Economic Statement);
- Stationary electricity storage equipment described under subparagraph (d)(xviii) of Class 43.1 and equipment used for pumped hydroelectric energy storage described under subparagraph (d)(xix), excluding equipment that uses any fossil fuel in operation;
- Equipment that is part of an eligible natural gas energy system that generates electricity or electricity and heat from fuel that is all or substantially all natural gas and uses a carbon capture system to limit emissions to within certain specified emission intensity levels;
- Equipment and structures used for the transmission of electricity between provinces and territories.

Budget 2024 provides more details and clarifications regarding eligible electricity generation and cogeneration systems from natural gas with carbon capture that could qualify for the ITC, and for eligible interprovincial and territorial electrical transmission property.

Additional conditions would apply for provincial and territorial Crown corporations to get access to the Clean Electricity ITC. The Minister of Finance would designate a province or a territory, provided that the Minister was satisfied that the provincial or territorial government has:

1) Publicly committed to:
    - Work towards a net-zero electricity grid by 2035; and
    - Provincial and territorial Crown corporations passing through the value of the Clean Electricity ITC to electricity ratepayers in their province or territory to reduce ratepayers' bills.
2) Directed provincial and territorial Crown corporations claiming the tax credit to publicly report annually on how the tax credit has improved ratepayers' bills.

Where a provincial or territorial Crown corporation claiming the tax credit fails to report annually on how the tax credit has improved ratepayers' bills, the Crown corporation would be subject to a penalty.

To be eligible for the ITC, property must be acquired and becomes available for use on or after April 16, 2024, and before 2035, and must not be part of a project that began construction before March 28, 2023. Similar rules would apply to the acquisition of eligible property by provincial and territorial Crown corporations, with the following adjustments:

[5] Supra note 1.

- If a province or territorial government has satisfied all the conditions by March 31, 2025, and subsequently been designated by the Minister of Finance, then provincial and territorial Crown corporations investing in that jurisdiction would be able to access the Clean Electricity ITC for property that is acquired and becomes available for use on or after April 16, 2024, for projects that did not begin construction before March 28, 2023.
- If a provincial or territorial government has not satisfied all the conditions by March 31, 2025, then provincial and territorial Crown corporations investing in that jurisdiction would not be able to access the Clean Electricity ITC until the province or territory is designated. The Clean Electricity ITC would apply to property that is acquired and becomes available for use from the date when the province or territory is designated by the Minister of Finance, for projects that did not begin construction before March 28, 2023.

Based on the above requirements, it may be interpreted that provincial and territorial Crown corporations are not required to have the qualifying property available for use before 2035. We intend to ask the government to provide clarifications on this matter in the upcoming draft legislation for the Clean Electricity ITC.

Budget 2024 also indicates that:

- Natural Resources Canada (NRCan) would have to perform a review to determine whether various eligibility criteria have been satisfied for certain properties (i.e., natural gas energy systems).
- Recapture rules and repayment requirements generally in line with those proposed in respect of the Clean Technology ITC would apply (a ten-year period except in the case of eligible natural gas energy systems which will be a 20-year period).
- The Clean Electricity ITC cannot be claimed in respect of a particular expenditure if one of the other federal clean economy ITCs is claimed in respect of that same expenditure by the taxpayer.
- Eligible corporations can fully benefit from both the Clean Electricity ITC and the Atlantic ITC with respect to the same expenditure, provided that the expenditure is eligible for both these ITCs.

Clean Technology Manufacturing ITC: clarification and changes to the required proportion of the qualifying mineral activities

Revisions to the Clean Technology Manufacturing ITC were announced in Budget 2024. Budget 2023 proposed to introduce the Clean Technology Manufacturing ITC, a refundable tax credit equal to 30% of the cost of investments in "eligible property" that is "used all or substantially all for eligible activities." Legislation[6] for this credit was introduced in Parliament on May 2, 2024.

Activities eligible for this credit include "qualifying mineral activities" that produce qualifying materials such as copper, nickel, cobalt, lithium, graphite, and rare earth elements. Qualifying mineral activities cover extraction; certain processing activities at mine or well sites, tailing ponds, mills, smelters or refineries; certain recycling activities, and certain graphite activities. Budget 2024 proposes several adjustments to improve clarity and facilitate access to critical mineral projects. These adjustments recognize that the production of qualifying materials can occur in projects involving the production of multiple metals, known as polymetallic projects.

Budget 2024 announces that the value of qualifying materials will be used to assess how much property is used for qualifying mineral activities that produce qualifying materials. Additionally, Budget 2024 proposes to modify eligible expenditures to include investments in eligible property used in qualifying mineral activities that are expected to **produce primarily (i.e., 50% or more of the financial value of the output) qualifying materials** at mine or well sites, including tailing ponds and mills located at such sites.

To support this expectation and ITC claims, claimants would have to submit an attestation from an arm's-length qualified engineer or geoscientist to the Canada Revenue Agency (CRA) for each relevant mine or well site.

[6] Bill C-69, An Act to implement certain provisions of the budget tabled in Parliament on April 16, 2024, first reading on May 2, 2024 (House of Commons).

This adjustment will be effective for property acquired on or after January 1, 2024. A safe harbour rule is proposed to mitigate the impact of price volatility on the recapture mechanism in respect of the ITC (proportion calculated on the average value of the critical mineral processed over the last five years).

New Electric Vehicle Supply Chain ITC

The new Electric Vehicle (EV) Supply Chain ITC announced in Budget 2024 is a strategic move to bolster Canada's role in the rapidly growing EV industry. The introduction of this new 10% ITC on the cost of buildings used in certain key EV segments is intended to encourage investments in three EV supply chain segments, namely:

- EV assembly,
- EV battery production, and
- Cathode active material production.

Eligible property must be acquired and available for use on or after January 1, 2024. The ITC would be reduced to 5% for 2033 and 2034 and would be eliminated after 2034. So far, similar to the Clean Technology Manufacturing ITC, claimants would not be required to meet any labour requirements to have access to the maximum ITC of 10%.

To be eligible, taxpayers together with related parties must also claim the Clean Technology Manufacturing ITC in all three of the specified supply chain segments described above. Alternatively, groups may claim the Clean Technology Manufacturing ITC across two of the segments and hold a minority interest in an unrelated party that claims the credit with respect to the third segment.

The 2024 Fall Economic Statement should provide details on the design and implementation of the EV Supply Chain ITC. The design will incorporate elements of the Clean Technology Manufacturing ITC, where applicable.

Timeline to implement and deliver the clean economy ITCs

In Budget 2024, the government provides additional insights about its plan to seize the investment opportunities of the global clean economy, and how it will implement and deliver its six major clean economy ITCs, building on the delivery timeline announced in the 2023 Fall Economic Statement. The government anticipates Bill C-59[7] – which introduced legislation in Parliament for the Clean Technology ITC, the CCUS ITC, labour requirements for some ITCs, and new provisions related to claiming the clean economy ITCs in partnerships – to receive Royal Assent before June 1, 2024, with the support and collaboration of Parliamentarians.

Bill C-69, which included legislation for the Clean Hydrogen ITC and the Clean Technology Manufacturing ITC, received first reading in Parliament on May 2, 2024. Legislation for the Clean Electricity ITC (except for provincial/territorial Crown corporations) and for the Clean Technology ITC (biomass expansion) is targeted to be introduced in Parliament in Fall 2024, with draft legislation expected prior to the introduction.

Legislation for the Clean Electricity ITC (all corporations) and the Clean Technology ITC (biomass expansion) is targeted to be introduced in Parliament in Fall 2024, with draft legislation to be released for consultation in summer 2024. There were no announced timelines for the new EV Supply Chain ITC, either for consultation or for the introduction in Parliament.

Finally, in order to deliver the clean economy ITCs without delay and recognizing the key role that they will play in delivering these support measures, the government is increasing resources at CRA, NRCan and the Department of Finance Canada, by providing up to $119.7 million over 11 years to these agencies starting in 2024-2025, with the vast majority ($90.9 million) being allocated to the CRA for the administration of the new economic investment tax credits.

Canada Carbon Rebate for Small Businesses (CCRSB)

Budget 2024 proposes a **new rebate to return certain amounts collected in some provinces under the federal backstop pollution pricing fuel charge to eligible small businesses through a refundable tax credit** that will be available upon the

[7] Supra note 1.

filing of a corporate tax return for the corporation's 2023 taxation year on or before July 15, 2024, and will continue to apply for future fuel charge years. With respect to the 2019-20 to 2023-24 fuel charge years, the CCRSB would be available to Canadian-controlled private corporations with fewer than 500 employees throughout Canada in the calendar year in which the fuel charge year begins.[8]

The CCRSB would be determined for each applicable province in which the eligible corporation had employees in the calendar year in which the fuel charge year begins. The tax credit amount would be equal to the number of persons employed by the eligible corporation in the province in that calendar year, multiplied by a payment rate that will later be specified by the Minister of Finance for that province for the corresponding fuel charge year.

Eligible corporations would not be required to apply for this refundable tax credit. The CRA would automatically determine the CCRSB amount for an eligible corporation and pay that amount directly to the corporation.

The Canada Growth Fund – Carbon contracts for difference

Budget 2024 includes several items related to the Canada Growth Fund, aimed at attracting private capital and investing in Canadian projects and businesses. With a substantial allocation of $15 billion (previously announced), this public investment vehicle is led by Canada's renowned public sector pension professionals. Key highlights of the Budget 2024 announcements include:

- **Focus on clean energy and clean technology**: The Canada Growth Fund places a primary emphasis on investments in clean energy and clean technology. This strategic focus aligns with the government's objective of fostering a robust and sustainable economy while creating job opportunities across the country.
- **Carbon contracts for difference (CCFDs) offerings:** Budget 2024 indicates that the Canada Growth Fund is actively developing an expanded range of CCFD offerings tailored to different markets. These offerings are designed to address the unique risks and opportunities associated with CCFDs. By providing bespoke CCFDs and carbon offtake agreements, the fund aims to support projects and businesses contributing to the reduction of greenhouse gas emissions.
- **Provincial focus on greenhouse gas emissions reductions**: The Canada Growth Fund will focus on provinces that are making substantial contributions to greenhouse gas emissions reductions. This approach will ensure that investments are targeted towards regions with the greatest potential for environmental impact and sustainable development.

This strategic approach aligns with the goal of building a sustainable economy and creating job opportunities across the country.

Incentivizing innovation and productivity

Boosting R&D and innovation in Canada: A second phase of consultations and additional funding for the SR&ED program

The government announced several updates to the Canadian SR&ED program in Budget 2024. These updates aim to modernize and improve the tax incentives offered by the program, with a focus on supporting innovative businesses and driving economic growth. In order to enhance the SR&ED program, the government launched consultations on January 31, 2024. The purpose of these consultations was to explore cost-neutral ways to improve the program's delivery and support for Canadian small- and medium-sized enterprises (SMEs). The government sought input from Canadian researchers and innovators on how to better deliver SR&ED support and enable the next generation of innovators to scale up, create jobs, and contribute to economic growth. The first phase of consultations closed on April 15, 2024 (*to which Deloitte participated*).

Budget 2024 announced that **the government will launch a second phase of SR&ED consultations**.[9] This phase will focus on more specific policy parameters and seek further views from businesses and industry on specific and technical reforms. One of the key areas of exploration is the **eligibility of Canadian public companies for the enhanced credit**. To support these

[8] For example, eligibility for receiving a payment in respect of the 2022-23 fuel charge year would be based on the number of persons employed by the eligible corporation for the 2022 calendar year.
[9] Supra, note 2.

enhancements, the government proposes **to provide $600 million over four years, starting in 2025-26. This funding will be supplemented with $150 million per year ongoing for future enhancements to the SR&ED program**. The second phase of consultations will help determine how this additional funding can be effectively targeted to boost R&D and innovation.

Boosting intellectual property retention: Creation of a new patent box regime

The government also launched consultations on January 31, 2024, on creating a patent box regime (*to which Deloitte participated*). The purpose of this regime is to encourage the development, commercialization, and retention of intellectual property (IP) in Canada. A patent box would provide a preferential income tax rate to income derived from certain types of IP. The patent box consultation closed on April 15, 2024, and the government is currently reviewing submissions. In Budget 2024, the government mentioned that these submissions will help inform future government decisions regarding the implementation of a patent box regime in Canada.

Other research support

To increase core research grant funding and support Canadian researchers, **Budget 2024 proposes to provide $1.8 billion over five years, starting in 2024-25, with $748.3 million per year ongoing to the federal granting councils** – the Natural Sciences and Engineering Research Council (NSERC), the Canadian Institutes of Health Research (CIHR), and the Social Sciences and Humanities Research Council (SSHRC).

In Budget 2024, the government recognizes that while Canada's granting councils are already doing excellent work in their respective fields, **more needs to be done to maximize their impact on the Canadian economy** and to modernize federal research support. To this end, the following announcements have been made:

- To provide better coordination across the federally funded research ecosystem, Budget 2024 announces the **creation of a new capstone research funding organization**. The granting councils will continue to exist within this new organization, and continue supporting excellence in investigator-driven research, including linkages with the Health portfolio.
- To help guide research priorities moving forward, Budget 2024 also announces that the **government will create an advisory Council on Science and Innovation**. This Council will be made up of leaders from the academic, industry, and not-for-profit sectors, and be responsible for a national science and innovation strategy to guide priority setting and increase the impact of these significant federal investments.
- Budget 2024 also proposes to provide a further $26.9 million over five years, starting in 2024-25, with $26.6 million in remaining amortization and $6.6 million ongoing, to the granting councils to **establish an improved and harmonized grant management system**.

Accelerated capital cost allowance (CCA) on patents and other technology properties

Budget 2024 **proposes immediate expensing of the cost of the following types of new property that could accelerate productivity in Canada** and where the property is acquired and becomes available for use on or after April 16, 2024, and before 2027: patents, rights to patented information (CCA Class 44), data network infrastructure equipment and related systems software (CCA Class 46), and general-purpose electronic data-processing equipment and systems software (CCA Class 50). The enhanced allowance would provide a 100% first-year deduction in the taxation year in which the property becomes available for use. The accelerated CCA would be prorated for short taxation years and would not be available in the following taxation year. Property that becomes available for use after 2026 and before 2028 would continue to benefit from the Accelerated Investment Incentive.

Other grants and incentives

A focus on AI and additional funding for three government programs

From a grants and incentives perspective, Budget 2024 has a strong emphasis on AI with an increase in AI support totalling $2.4 billion over five years. The breakdown of this funding is as follows:

- $2 billion over five years, starting in 2024-25, to launch a new AI Compute Access Fund and Canadian AI Sovereign Compute Strategy to help Canadian researchers, start-ups, and scale-up businesses access the computational power they need to compete and help catalyze the development of Canadian-owned and located AI infrastructure.
- $200 million over five years, starting in 2024-25, to Canada's Regional Development Agencies to incentivize AI start-ups in bringing new technologies to market, and accelerate AI adoption in strategic sectors such as agriculture, health care, manufacturing, and clean technology.
- $100 million over five years, starting in 2024-25, to the National Research Council's AI Assist Program to help SMEs and innovators to build and launch new AI solutions.
- $50 million over four years, starting in 2025-26, to support workers who may be impacted by AI through the Sectoral Workforce Solutions Program, which will provide new skills training for workers in potentially disrupted sectors and communities.

Budget 2024 also makes other announcements to ensure the safe and responsible use of AI, which include the creation of the AI Safety Institute of Canada, providing the AI and Data Commissioner Office with the resources it needs to begin enforcing the proposed *Artificial Intelligence and Data Act*, and the establishment by Transport Canada of the Pre-Load Air Cargo Targeting Program leveraging AI to screen 100% of air cargo bound for Canada.

Budget 2024 also proposes to provide the Canadian Space Agency with $8.6 million in 2024-25 for the Lunar Exploration Accelerator Program, which supports the space industry in accelerating the development of new technologies.

Additional government funding is proposed in Budget 2024 for the following incentive programs:

- An additional $158.5 million over two years, starting in 2024-25, to Regional Economic Growth through Innovation program, which focuses on job creation and regional economic growth.
- Reprofiled funding of $776.3 million, available from 2024-25 to 2029-30, to extend the Clean Fuels Fund for an additional four years and support clean fuel projects.

Another important note regarding the Clean Fuels Fund is the fact that the program will move to a continuous intake format. It is expected that NRCan will launch another call for proposals under the new extended Clean Fuels Fund by the end of 2024.

Deloitte's perspective

Budget 2024 reflects the government's commitment to driving clean and sustainable economic growth, supporting R&D, AI and innovation, and positioning Canada as a leader in the global clean economy sector.

Budget 2024 announcements for Clean Electricity ITC will have a particular impact on Indigenous communities, who are partners in the government's climate change strategy, and it is agreed that the design and implementation of energy projects must be done in collaboration with these communities, which will contribute to advancing reconciliation with Indigenous peoples. As noted in our previous tax alerts,[10] we reiterate that clean economy ITCs should all be designed to ensure that Indigenous communities themselves, or through their organization, are eligible to all ITCs. This would contribute to a more equitable and inclusive relationship with Indigenous communities.

Although Budget 2024 proposes some measures aligned with a productivity-led growth agenda (such as the $2.4 billion investment in Canada's AI future), overall, it signals a more-of-the-same approach to fostering productivity at a time when bold action is needed.

Budget 2024 comes at a critical moment. Our country lags in productivity growth and significant affordability challenges are impacting all Canadians. These challenges alone could lead to a sustained decline in quality of life and reduced trust in our institutions and values. The choices in this budget are critical and will have far-reaching implications for Canadians' prosperity.

[10] Supra note 3.

By making the right choices today, our country can get on a path to overcome obstacles, drive innovation and productivity, and create a more prosperous and equitable future for all Canadians. Hence, the government's choices will have an impact on future productivity growth and affordability.

The government will have to invest time and resources to deliver and implement all the announced initiatives. To encourage business participation and to achieve its objectives, the government must focus on keeping the incentive programs as simple as possible and to reduce administrative burdens. Businesses need certainty to invest in Canada, and the way the announced programs will be deployed and implemented will play a crucial role in this regard.

For more perspectives, you can also read the 2024 federal budget analysis from Deloitte's Future of Canada Centre.

How can Deloitte help?

Deloitte professionals will continue to monitor the legislative process and any changes to the eligibility or criteria for these clean economy investment tax credits.

We can help you understand how these incentive measures, or any previously announced measures, may impact your business or your investment and innovation projects. If you have any questions, please reach out to your Deloitte advisor or any of the individuals noted in this alert. More specifically, Deloitte's *Gi*³ group is available to assist you in identifying potential incentives, current and/or forthcoming, to support your investments and innovations.

Deloitte LLP
Bay Adelaide Centre, East Tower
8 Adelaide Street West, Suite 200
Toronto ON M5H 0A9
Canada