Canadian tax alert

2017-2018 federal budget highlights

March 22, 2017

The Minister of Finance, Bill Morneau, presented the 2017-2018 budget in the House of Commons this afternoon. The budget continues the theme of helping middle class families, growing the economy and creating jobs.

The government has introduced the “Innovation and Skills Plan” which will target six key areas: advanced manufacturing, agri-food, clean technology, digital industries, health/bio-sciences and clean resources.

The budget proposes a number of additional programs to support innovation and to foster growth in the clean technology sector. Some of these include the establishment of Innovation Canada, an investment in business-led “superclusters”, the creation of a new Strategic Innovation Fund, the launch of a new Venture Capital Catalyst Initiative and access to financing for clean technology firms.

The government has indicated its intention to close loopholes that result in unfair tax advantages for some at the expense of others. Furthermore, the budget proposes to invest an additional $523.9 million over five years to build on previous investments to support the Canada Revenue Agency's efforts to prevent tax evasion and improve tax compliance.

A summary of the economic and tax highlights contained in the budget is provided below.

Economic outlook

The deficit for 2016-2017 is estimated to be $23.0 billion and a deficit of $28.5 billion is predicted for 2017-2018. The deficit is projected to decline gradually, reaching $18.8 billion by 2021-2022.

The federal debt-to-GDP ratio is estimated to be 31.6% for 2017-2018. This ratio is estimated to decline to 30.9% in 2021-2022.

GDP is expected to grow by 1.9% in 2017 and by 2.0% in 2018.

The CPI inflation rate for 2017 is estimated at 2.0% and is expected to remain stable over the next few years.

The unemployment rate for 2017 is estimated to be 6.9% and is expected to decrease to 6.4% in 2021.

Tax measures concerning business

- The legislative meaning of *de facto* control is proposed to be expanded as a result of a recent court case. The revised meaning will apply for taxation years beginning on or after March 22, 2017, and will require consideration of factors other than legally enforceable rights to change the board of directors or its powers, or to influence other shareholders who have such rights.
- As anticipated, the budget indicates that Canada is pursuing signature of the Multilateral Instrument (MLI) released on November 24, 2016 as a result of the Organisation for Economic Co-operation and Development's Base Erosion and Profit Shifting initiative. The MLI has the potential to modify certain provisions of numerous tax treaties simultaneously.
- The government intends to release a paper outlining issues and providing proposed policy changes relating to tax planning strategies being used by private corporations that provide tax advantages which may be perceived to be unfair.
- The budget proposes to classify expenditures relating to drilling or completing a discovery well as Canadian development expense (CDE) as opposed to Canadian exploration expense (CEE) for expenditures incurred after December 31, 2018 unless that taxpayer has, prior to March 22, 2017, entered into a written commitment to incur those expenses.
- It is proposed that expenses qualifying as CDE that are incurred by an eligible small oil and gas corporation after 2018 and renounced to flow-through share

investors will no longer be able to be reclassified as CEE. Limited transitional relief is provided.

- Budget 2017 proposes an expansion of the accelerated capital cost allowance and Canadian renewable conservation expense regimes to further incentivize the development and use of geothermal energy for the production of both heat and electricity.
- The budget proposes that taxpayers be permitted to elect to have gains or losses included in income on a mark-to-market basis for certain eligible derivatives held on income account. Once made, the election will be valid for all subsequent years and is available for taxation years beginning after March 21, 2017.
- For any positions entered into after March 21, 2017, it is proposed that an anti-avoidance rule be introduced relating to straddle transactions that will prevent the realization of a loss to the extent of an unrealized gain on an offsetting position that has not been disposed of and is not subject to mark-to-market taxation.
- Budget 2017 proposes to allow a mutual fund corporation that is structured as a switch corporation to be reorganized into multiple mutual fund trusts on a tax-deferred basis on or after March 22, 2017 where the reorganization meets certain conditions.
- It is proposed that segregated funds be allowed to merge on a tax-deferred basis for mergers carried out after December 31, 2017.
- The budget proposes that non-capital losses incurred by segregated funds in years beginning after 2017 be allowed to be carried forward and applied in subsequent years, subject to the normal limitations of carrying forward and back losses.
- A series of new rules are proposed, applicable for taxation years of Canadian life insurers that begin on or after March 22, 2017, that will deem income from the insurance of Canadian risks earned through a foreign branch to be taxable in Canada where such income exceeds 10% of the branch's income.
- The budget proposes a supplementary anti-avoidance rule that deems a taxpayer (or one of its foreign affiliates) to have insured Canadian risks where foreign risks were insured as part of a transaction or series of transactions, one of the purposes of which was to avoid the rules which deem income from the insurance of Canadian risks to be taxable in Canada.
- It is proposed that the investment tax credit for child care spaces be eliminated for expenditures incurred after March 21, 2017. Expenditures incurred before 2020 pursuant to a written agreement entered into before March 22, 2017 will continue to be eligible.
- Budget 2017 proposes to eliminate the additional deduction for gifts of medicine for gifts made after March 21, 2017.
- The budget proposes to eliminate the tax exemption for insurers of farming and fishing property for taxation years beginning after 2018.

- It is proposed that the ability for designated professionals to elect to exclude the value of their work in progress in computing their income be eliminated for taxation years beginning after March 21, 2017. Transitional measures are proposed to bring into income work in progress that was previously excluded from income.
- The government indicated its intention to hold a consultation relating to the ability to defer income tax in respect of deferred cash purchase tickets received on the delivery of listed grains. Comments are due by May 24, 2017.

Tax measures concerning individuals

- Eligibility for the disability tax credit requires certification by an eligible medical practitioner. The budget proposes to add nurse practitioners to the list of eligible medical practitioners for this purpose, effective as of March 22, 2017.
- The ability to claim costs related to the use of reproductive technologies as a medical expense is proposed to be enhanced. This provision is to be applicable to 2017 and subsequent taxation years, with an election to apply the provision to any of the 10 preceding taxation years.
- The three tax credits available to caregivers (i.e., infirm dependant credit, caregiver credit and family caregiver credit) are proposed to be consolidated into one credit, the Canada Caregiver Credit. This credit amount will be consistent with the amounts available to under the three former programs. The credit will no longer be available in respect of non-infirm seniors who reside with their adult children.
- The 15% mineral exploration tax credit for flow-through share investors is proposed to be extended for another year, for flow-through share agreements entered into on or before March 31, 2018.
- Applicable as of the 2017 taxation year, the budget proposes to permit the electronic distribution of T4 slips by employers without first obtaining express advance consent from the employees. Privacy safeguards will be mandatory in order to take advantage of this efficiency.
- The tuition tax credit is proposed to be available for an expanded range of programs. Occupational skills courses that are offered at a university, college or other post-secondary institution and are not at the post-secondary level will be eligible for the credit for fees for courses taken after 2016. Students qualifying for the credit due to this change will be considered to be “qualifying students” for the scholarship and bursary income exemption, applicable as of 2017.
- The deduction in respect of eligible home relocation loans (i.e., loans used to a acquire a new residence where an employee starts work at a new location and the residence is at least 40 kilometres closer that the old residence to the new work location) is proposed to be eliminated for benefits arising in the 2018 and subsequent taxation years.
- The public transit tax credit is proposed to be eliminated as of July 1, 2017.

- The budget proposes to extend anti-avoidance rules applicable to registered retirement savings plans, registered retirement income funds and tax-free savings accounts to registered education savings plans and registered disability savings plans. This proposal will apply (with certain exceptions) to transactions occurring and investments acquired after March 22, 2017.
- A number of changes are proposed to the ecological gifts (ecogifts) program to ensure its integrity, including:
    - Where there is a transfer of ecogifts between organizations for consideration, the transferee will be subject to the 50% tax if the use of the land is changed or the property disposed of without permission of Environment and Climate Change Canada.
    - Private foundations will no longer be permitted to receive ecogifts.
- Certain non-accountable allowances for specified members of legislative assemblies and municipal officers will be required to be included in income beginning with the 2019 taxation year. Specific expense reimbursements will remain non-taxable.

Sales and other tax measures

- Effective July 1, 2017, it is proposed that the GST/HST rules applicable to taxi businesses be amended in order to ensure they are equally applicable to commercial ride-sharing services.
- The budget proposes to retroactively add Naloxone and its salts to the list of GST/HST-free non-prescription drugs, effective as of March 22, 2016. No relief is granted, however, for supplies in respect of which GST/HST has already been charged, collected, remitted or paid prior to budget day.
- Effective for supplies made after budget day, the budget proposes to repeal the rebate available to non-residents for GST/HST payable in respect of the accommodation portion of eligible tour packages. The rebate will continue to be available in respect of supplies made prior to January 1, 2018, provided that all of the consideration for the supply is paid prior to that date.
- Effective March 23, 2017, the budget proposes to repeal the surtax on manufacturers of tobacco products with a coordinated increase to the excise duty rates on tobacco.
- Excise duties on alcohol products are proposed to be increased by 2%, effective March 23, 2017, with annual indexing of rates on a go-forward basis.
- Regulatory amendments are proposed in order to permit a broader range of apparel products to be imported duty-free from the world’s least developed countries.
- Budget 2017 proposes a number of amendments to the Special Import Measures Act and related regulations that are intended to strengthen Canada’s trade remedy system and ensure it is aligned with Canada’s obligations under World Trade Organization rules.

For further details, we refer you to the Department of Finance website.

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