The last four years:

A look back at Canadian tax policy under Prime Minister Trudeau's government

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Families

Growth

Canada

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A recap of some of the most significant tax changes during the last four years

Under the leadership of Justin Trudeau, the Liberal Party won the 2015 federal election pledging to ease the financial burden of "middle class" Canadians and raise taxes on the wealthiest one percent.

Over the following four years, Trudeau's government made substantial changes to tax policy, with these twin campaign promises cited as the driving force behind the most substantial changes.

In this report, our top tax policy specialists have compiled a timeline that dissects over 30 of those changes in order to understand how we arrived where we are today and what might be in store for the years ahead. For Canadian entrepreneurs, business leaders and investors, this look back will provide insight into the options that might be available to mitigate new headwinds and maximize available opportunities.

The year ahead

It remains to be seen whether the returning Liberal government will implement bold new changes moving forward or maintain the status quo. In the meantime, our report considers options that may shape future policy moves.

At Grant Thornton, we understand how the complexities of the tax landscape can create uncertainty and burdens, and we're committed to helping Canadians achieve their greatest potential in any given tax environment.

2015

October: Winning with pledges for deficit spending, a middle class tax cut and higher taxes for the wealthy

Five years ago, Stephen Harper's Conservatives were seeking to form a government for a fourth consecutive time. The Conservatives had held power in Ottawa for the last decade and, heading into the 2015 election, held a majority of seats in Parliament. Justin Trudeau had recently won the leadership of the Liberal party following his party's relegation to third place behind the late Jack Layton's New Democratic Party, which had held the official opposition for the past four years.

The Liberals were the only party that campaigned on a platform of running deficits during its mandate, with a plan to balance the budget in 2019 (which did not materialize). Their campaign also focused on helping a group of Canadians styled by Justin Trudeau as "the middle class" and pledged to raise taxes on the wealthiest one percent to do so.

At the end of the campaign, the Liberals won both the popular vote and the most seats in Parliament, providing them with a strong majority to implement their mandate over the next four years—a mandate they embraced to make significant changes to tax policies.

December: The middle class tax cut

The new Liberal government didn't waste any time implementing its mandate, particularly in regard to tax changes. In December 2015, it introduced its "middle class tax cut", which reduced the personal tax rate for 2016 from 22% to 20.5% on taxable income in the second bracket (i.e., between $45,282 and $90,563 in 2016).

In addition to the middle class tax cut, the Trudeau government introduced a new top tax bracket for 2016, which included a tax rate of 33% applicable on taxable income over $200,000. This new tax bracket also meant that other entities taxed as individuals, including some trusts and estates, would have to pay a federal tax at the new top rate of 33%.

Additional regulatory changes impacting charitable donations and investment income earned in a private corporation were also made to take into account this new top tax rate. Furthermore, the Liberals also reduced the maximum annual contribution to a tax-free savings account (TFSA), effective January 1, 2016, from $10,000 (as was introduced by the previous Conservative government) down to $5,500.

2016

February: The first Liberal budget - realigning individual tax credits, adjustments for small businesses

The Liberal government's first budget presented a $29.4 billion deficit, largely used to finance spending in many key areas that were in line with its campaign promises. The budget introduced several changes intended to benefit middle class Canadians, as well as some adjustments placing new limits on businesses accessing certain tax provisions. These changes were an early indicator of things to come in the Liberal government's effort to crack down on what it characterized as "wealthier Canadians," including small business owners.

Individuals: Income splitting and tax credits

After adding a new top tax bracket, and making changes like the TFSA contribution reduction to limit tax breaks that the Liberals felt were benefiting "rich Canadians", the government continued down this path with its first federal budget. Several Harper-era personal tax measures were eliminated in the 2016 budget, including

- the income splitting tax credit for spouses,
- the children's fitness tax credit and
- the children's arts tax credit.

The first Liberal budget also eliminated other tax credits (e.g., the education and textbook tax credits) effective January 1, 2017. According to the government, the purpose of eliminating these credits was to leverage the savings and provide assistance to lower and middle income students.[1] The government set out to achieve this by increasing Canada Student Grant amounts and changing the Canada Student Loan program—steps that were intended to make it easier for students to repay their debts.

Another major policy initiative was the introduction of the Canada Child Benefit (CCB). The CCB combined existing child-related payments into one, non-taxable benefit, paid to Canadian families based on their income level.

1 Department of Finance. "Chapter 1 - Help for the Middle Class." Budget 2016, March 22, 2016. https://www.budget.gc.ca/2016/docs/plan/ch1-en.html#_Toc446106647

2016

Businesses

The 2016 budget also introduced several tax changes to areas affecting Canadian business. These included: the small business tax rate, specified corporate income and specified partnership income rules and the eligible capital property regime.

A new small business tax rate

The Liberals did not proceed with the planned reduction to the small business tax rate. While the previous Conservative government had introduced an annual half-percent reduction to the small business tax rate (from 10.5% in 2016 to 9% in 2019). The "small business tax deduction" was implemented a year later—with a tax rate of 10% in 2018 and 9% in 2019.

Changes to specified corporate income and specified partnership income rules

The budget introduced limitations on the ability to claim the small business tax rate (or, technically-speaking, the small business deduction) in certain partnerships and corporate structures. These types of structures were sometimes used by professionals, such as lawyers and doctors, to organize their businesses. Changes to the definition of "specified partnership income" were introduced, as well as a new definition: "specified corporate income." Overall, the changes were intended to eliminate the use of certain corporate structures that allowed companies to effectively multiply the small business deduction.

Elimination of the eligible capital property regime

The budget introduced changes to the rules governing eligible capital property (ECP)—which included intangible capital property such as goodwill. These changes, which were effective January 1, 2017, altered the playing field for certain businesses.

Previously, if a business owner decided to sell their business through an asset sale, a portion of the proceeds would often be attributable to goodwill as well as other intangible assets (e.g., trademarks, customer lists, etc.). This goodwill, which loosely-speaking represented the intrinsic value of the business, was considered eligible capital property. When the business was sold, the resulting gain attributed to the goodwill was taxed as business income and subject to the small business tax rate (if applicable).

Fast forward: 2020

Since the new changes, gains on goodwill and certain other intangibles that were once considered ECP are now treated as a taxable capital gain—meaning they're not subject to the small business tax rate. Furthermore, since taxable capital gains are considered investment income, this income is subject to additional refundable tax payable at the corporate level. This creates greater incentive to pay out corporate dividends to recoup refundable taxes. When that happens, however, the business owner—presumably an individual—is taxed on those dividends at their marginal tax rate, thus reducing the deferral benefit of leaving funds inside a corporation.

2016

International tax changes

To cooperate with the Organization for Economic Cooperation and Development's (OECD) base-erosion and profit-shifting (BEPS) project, the 2016 budget introduced measures based on recommendations from that BEPS project. This included a requirement for large multinationals to adopt country-by-country reporting, as well as changes to the use of the arm's length principle for transfer pricing purposes. Furthermore, the government committed to the development of a multi-lateral instrument, together with the international community, that would more easily allow for the implementation of further treaty-related changes stemming from BEPS.

September: The CPP enhancement

Changes to Canada Pension Plan (CPP) rules were introduced that would require both employers and employees to increase their rates of contribution to the CPP. These changes, which began to take effect in 2019, were introduced in order to increase the amount of a retiree's pension income, as well as to ensure the CPP is sufficiently funded overall.

Fast forward: 2020

The rate of contribution increased by one percent in 2019, and it's scheduled to increase annually by the same amount until 2023. In 2024, a new additional CPP contribution will be required for employees earning greater than a given earnings threshold ($70,100 in 2024).

October: Principal residence rules tightened

In October 2016, the federal government announced additional administrative changes impacting homeowners and would-be homeowners. For tax years ending after October 2, 2016, taxpayers who dispose of a principal residence will be required to report the disposition in their tax return[2] and provide some basic information, including the sale proceeds and the date the home was originally purchased. If a homeowner forgets to report the sale, they could face penalties of up to $8,000. The government stated the purpose of this rule was to improve tax compliance, although many saw it as an attempt to target those who "flip" properties and don't correctly report the income.[3]

2 Additional forms are also required to be completed, depending on circumstances. For example, most individuals have to complete Form T2091(IND) to report the designation of the property as the principal residence.

3 "Flipping" a property in the context of housing refers to purchasing a home with the intention of adding value to it in order to sell for a profit, rather than living in and occupying it. The profit on this type of sale would generally be taxed as income, not a capital gain, and would not be eligible for the principal residence exemption (the exemption would generally reduce the taxable amount of the capital gain to nil on the sale of a home).

2016

The October announcement also included measures to allow the Canada Revenue Agency (CRA) to assess taxpayers beyond the normal reassessment period (typically three years after the tax return is assessed) if they fail to report the disposition or don't file a tax return. Furthermore, individuals who are not resident in Canada in the year they purchase the home can't claim the principal residence exemption on the sale of the property.

The principal residence rules with respect to trusts have also become stricter. Previous to the changes, a personal trust[4] that was resident in Canada and met certain other requirements would be able to claim the principal residence exemption. One of the main requirements was that a beneficiary of the trust, their spouse or common-law partner, or their child would ordinarily inhabit the home. However, with the changes to the rules, in order for a trust to claim the exemption, it must be a certain type of personal trust[5] for each year, beginning after 2016, in which it will claim the exemption. Furthermore, the beneficiary must be a resident of Canada and that beneficiary must have a right to use the property as a residence throughout the year it is owned by the trust.

Although not specifically a tax measure, an additional rule—known as the mortgage stress test—was also introduced at the same time as the principal residence rule changes. The mortgage stress test, which requires borrowers to qualify for a mortgage at a rate at least two percentage points higher than their actual rate, has undergone several changes since it was first introduced. These changes, along with the previously-noted tax measures, were the beginning of the government's strategy to deal with home affordability in Canada, which it continued to address in future budgets as well.

4 Prior to the changes, the Income Tax Act generally defined a "personal trust" as a testamentary trust or inter vivos trust. The definition has been modified slightly in 2016 to refer specifically to a graduated rate estate or a trust where no consideration was paid for the beneficial interest in the trust to either the trust or a person or partnership that made a contribution to the trust by way of transfer, assignment or other disposition of property.

5 Generally, after 2016, only a spousal or common-law partner trust, alter ego trust, qualifying disability trust or a trust for the benefit of a minor child of deceased parents would be able to claim the principal residence exemption.

2017

March: Budget 2017

At the start of 2017, it did not appear that there would be much tax-talk, considering the tax changes that had been introduced in late 2015 and 2016. The 2017 budget did not have as many significant tax-related changes as in previous years, although it did suggest that changes were coming, particularly with respect to high-income individuals who own private corporations. Yet, when details of the proposed changes came to light that summer, it was clear they would have a dramatic impact on not just the wealthy, but on all small business owners.

The Liberal government's second budget did not include many significant tax changes. For businesses, or more specifically, professionals earning business income, changes to the taxation of work-in-progress (WIP) was arguably the most significant tax change. These changes resulted in the elimination of the deferral of WIP (excluding the profit portion), and were effective for tax years starting on or after March 22, 2017. Other tax changes were introduced in the 2017 Budget, although many of those changes would not commonly affect the average small business owner. Additionally, the budget amended the meaning of "control", which likely resulted from the CRA losing a court case based on the interpretation of the meaning of that word.

The budget also introduced the Canada Caregiver Credit, which combined previously existing credits into one. This credit became available to taxpayers who are responsible for taking care of a dependent relative. Plus, changes to excise taxes were introduced, including the requirement for ride share service (e.g., Uber) drivers to charge GST/HST on their fares (similar to taxi drivers) and an increase to excise duties on tobacco and alcohol.

July: Private company tax proposals

On July 18, 2017, after much anticipation, the details of the government's proposed tax rule changes were announced. Minister of Finance Bill Morneau released a consultation paper which introduced several measures to address specific "areas of concern". These included:

- Income sprinkling
- Passive investment income (earned in a corporation)
- Converting dividend income into capital gains (commonly known as surplus stripping)

Rather than simply targeting high-income individuals who owned corporations, the government's proposed measures dramatically impacted small business owners—and a backlash ensued. The consultation deadline for submissions was set for October 2, 2017, and the response from the business and tax community was harsh and swift, with over 21,000 submissions received during the 75-day consultation period.

In the end, the Liberal government pushed through changes to its first two areas of concern, but abandoned proposed changes in the third.

Here is what the proposed changes looked like:

Income sprinkling

Prior to the proposed changes, rules already existed to prevent income splitting with non-arm's length minors (e.g., children under age 18). These rules, previously referred to as the "kiddie tax" rules, resulted in certain types of income—particularly dividends from shares in a privately-held corporation—being labeled as split income, which is taxed at the highest marginal tax rate. The July 18 proposals looked to expand these rules to apply to non-arm's length adults as well, including spouses, parents and siblings. Furthermore, other types of income, such as interest on non-arm's length debt, would also be considered split income, and would be subject to the new rules, referred to as the TOSI (tax on split income) rules. In response to these proposals, Grant Thornton and many other interested parties provided a detailed submission explaining the potential negative impact on small businesses across Canada. Nonetheless, the proposals were passed into law, applicable for the 2018 tax year.

Passive investment income

The government also proposed to eliminate the purported "tax advantage" available to owners of private corporations who held their passive investments, such as publicly-traded shares, within their corporations. Since corporations are generally taxed at a lower tax rate than individuals, the government asserted that small business owners had an advantage over the average individual taxpayer since the starting capital with which to purchase such investments was higher if purchased within a corporation.

Converting dividend income to capital gains

Finally, additional proposals included both changes to an existing rule to combat surplus stripping as well as a new rule with the same goal. The changes to existing section 84.1 of the Income Tax Act were meant to prevent an increase in cost base to shares on certain non-arm's length transactions by expanding the circumstances in which the rule would apply. Additionally, proposed section 246.1 would apply to deem a dividend to be paid in circumstances where an individual receives an amount from a non-arm's length person and one of the purposes was to effect a significant reduction of assets in a corporation to avoid tax.

In the end, both of these proposals were abandoned, possibly due to the significant questions raised by the tax community, given that the proposals had the potential for serious unintended negative consequences for families seeking an intergenerational transfer of their businesses, as well as the potential for double taxation in some post-mortem scenarios.

2017

Our view

Highlights of Grant Thornton's response to the government consultation paper

- You can read our complete and detailed response here, but our chief concerns were for the myriad of unintended negative consequences these changes would impose on Canadian entrepreneurs and businesses.
- At a high level, we took issue with the government's use of the term "loophole" to describe these matters. These were tax policy features that produced the results they were supposed to achieve when they were enacted. These features fostered new business investment and enabled business owners to innovate, expand and contribute more to our economy.
- We expressed concern that, while the stated intent of these proposals was to target the "wealthy", the practical impact would affect a wide variety of private business owners, including lower and middle class business owners who structured their businesses appropriately based on longstanding tax laws.
- In addition, we raised the issue of the added complexity these piecemeal changes would introduce to the tax system, which would place additional burdens on businesses and individuals, and make compliance more difficult.
- Finally, we were concerned that the truncated timeframe for consultation and implementation did not allow business owners enough time to prepare and make the necessary changes.

We remain concerned more than two years later, as these complex changes have created uncertainties about where and how they are applied that make it difficult for Canadians to plan for the future and achieve maximum growth.

The government released its final proposals for the TOSI rules in December 2017. The rules outlined when TOSI would apply and also provided exceptions. With respect to the passive income rules, the government confirmed that it would be moving forward, with details to be forthcoming in the 2018 budget. By the end of its second full year in office, the Liberal government had already made significant changes to the rules affecting high-net-worth individuals, small businesses and small business owners, with more changes yet to come.

2017

December: Voluntary disclosure program

In December 2017, the CRA released changes to the Voluntary Disclosure Program (VDP)—a program that allows taxpayers to voluntarily come forward to correct inaccuracies or disclose formerly unreported income from a previous year. Historically, the program has allowed taxpayers to avoid certain interest and penalties, as long as the application was voluntary (e.g., the taxpayer was not already under audit) and complete, a penalty was involved and the amount owing was outstanding for at least one year.

Essentially, the CRA's new changes to the VDP created two tracks available to taxpayers, depending on the type of taxpayer and/or types of disclosure. On March 1, 2018, the two tracks came into effect:

- the General Program, which applies to errors and minor non-compliance cases, provides partial interest relief and provides relief from penalties and criminal prosecution; and

- the Limited Program, which applies to cases of major non-compliance and intentional misconduct, corporations with revenues greater than $250 million and sophisticated taxpayers, and provides relief from penalties and criminal prosecution but no interest relief.

In addition to these changes, the CRA now requires taxpayers to include the payment of the estimated tax owing and adhere to certain other requirements.

2017

December: US tax reform

South of the border, talk of tax reform began from the early days of Donald Trump's presidency. At the end of 2017, one of the most significant US tax reforms in decades, the Tax Cuts and Jobs Act (TCJA), was made official. Although this article doesn't focus on changes to US tax rules in detail, it's important to consider some of these changes at a high level to provide context to Canada's response in the following year. Some of the more significant tax changes include:

- A reduction in the corporate tax rate from 35% to 21%
- Full write-off of capital assets purchased and in use after September 27, 2017
- The elimination of corporate alternative minimum tax
- The introduction of the Global Intangible Low-Taxed Income (GILTI), which imposes a tax on certain earnings of a US company's foreign subsidiary
- The introduction of the Base Erosion and Anti-abuse Tax (BEAT) applied to certain payments made by a US company to foreign related parties

Many of the new rules contain sunset provisions, meaning they are not permanent changes and will expire at a future date (for example, many of the tax changes impacting individuals will expire in 2026). Overall, these changes improved the competitiveness of the US tax system vis-à-vis other countries, including Canada. This could have the effect of encouraging investment in the US as well as retaining earnings to be taxed inside the US (e.g., by not paying dividends up to a Canadian parent company), putting pressure on other countries, including Canada, to adopt tax changes of their own to remain competitive.

2018

The year for implementing income sprinkling and passive income tax changes, trade and Trump

The year 2018 saw the initial implementation for the new TOSI rules as well as an introduction of the passive income rules within the 2018 Budget. Along with other new tax legislation introduced in that year's budget, the Liberal government made significant changes to the capital cost allowance rules later in the year, as a response to the US Tax reform introduced in 2017. After President Donald Trump's significant tax changes, the Canadian government was under considerable pressure to respond with changes that would allow Canadian businesses and the economy to remain competitive. The year also included additional pressures on the Liberal government due to the renegotiation of the North American Free Trade Agreement (NAFTA) with the US and Mexico.

January: New TOSI rules take effect

The changes to the TOSI rules first applied starting in 2018. Many taxpayers—particularly small business owners—had to re-evaluate their business structures to determine if certain payments to non-arm's length individuals would now fall under the new rules.

Although several exceptions were provided, a lack of clarity regarding when the rules might apply resulted in confusion, inaction and additional administrative burden on taxpayers. While the CRA released several interpretations to provide some clarity, and participated in roundtables in an attempt to answer direct questions from the tax community, the net effect of these efforts was not always positive. In some cases, the CRA interpretations actually resulted in more confusion and less clarity.

Fast forward: 2020

Today, while the TOSI rules remain difficult to understand, income splitting can still be an effective tool for many taxpayers. Due to several available exceptions, many business owners still have an opportunity to manage the transfer of family assets to future generations. By closely monitoring their ownership structure and improving record-keeping, the prudent business owner can still achieve their estate planning goals in a tax-effective manner.

2018

February: Budget includes Passive income and new reporting requirements for trusts and foreign affiliates

Budget 2018 continued where the government left off the previous year in implementing changes affecting small business owners. Two significant new measures were introduced that targeted the ownership of passive investments in a private corporation. The Budget also introduced changes to reporting requirements for trusts and for foreign affiliates, as well as new rules surrounding cannabis taxation, resulting from the legalization of cannabis at the beginning of the year.

Passive income changes

One of the most significant changes for the small business owner from the 2018 budget did not come as a surprise. The desire to curtail the use of private corporations to earn passive income had been clearly communicated by the Liberal government the previous summer. Although the proposals released that summer did not ultimately make it into the budget, two new measures were proposed:

Limiting access to the small business tax rate

To discourage owners of private corporations from owning passive investments in their corporations, budget 2018 included measures to reduce the availability of the small business deduction (SBD) when the passive income[6] of a corporation exceeded $50,000. These new measures would apply for taxation years starting after 2018. Although the majority of provinces adopted legislation to parallel these rules, both Ontario and New Brunswick did not.

Limiting access to refundable taxes

The changes to the refundable tax rules were meant to limit the ability of a private corporation to obtain a refund of taxes by paying out eligible dividends, which are taxed at the low rate, to shareholders. Passive income[7] is subject to an additional tax that is refundable to the corporation upon payment of taxable dividends. To receive the refund, a corporation could pay out either an eligible or non-eligible dividend. Since eligible dividends are subject to a lower tax rate than non-eligible dividends, shareholders would normally prefer to designate the payment of the former to trigger the refund.

6 For purposes of the SBD grind, passive income would generally include property income, excluding dividends received from connected corporations, and net taxable capital gains from dispositions of property, excluding net taxable capital gains on property used in an active business (e.g., a machine used to manufacture inventory sold by the corporation).

7 For purposes of the refundable tax rules, passive income would generally include all property income, excluding dividends, and all net taxable capital gains less carryforward capital losses deducted in the year. In other words, it's a slightly different definition of "passive income" compared to the one for the SBD grind, in footnote 6.

2018

Fast forward: 2020

With the rule changes, private corporations are now required to bifurcate the taxes paid on passive income between two pools: one that tracks taxes paid on eligible dividends received (the eligible refundable dividend tax on hand, or ERDTOH, pool) and one that tracks taxes paid on all other passive income (the non-eligible refundable dividend tax on hand, or NERDTOH, pool).[8] Since most passive income will flow into the NERDTOH pool, this change will effectively force private corporations to pay out higher-tax non-eligible dividends to shareholders to recover the refundable taxes paid by the corporation.

While these measures apply for taxation years starting after 2018, they may also be applicable in circumstances where a short taxation year was created to prevent the application of these measures.

Changes to reporting requirements

Trust reporting

Budget 2018 introduced new reporting requirements for trusts starting in 2021. Express trusts[9] resident in Canada with a tax year ending after December 30, 2021 will be required to file a T3 (trust) tax return on an annual basis. Certain trusts are excepted from the rule (e.g., graduated rate estates, qualified disability trusts, trusts in existence for less than three months, trusts with less than $50,000 in assets, etc.). Furthermore, the T3 will now require the following information to be included:

- The identity of all trustees
- The beneficiaries of the trust
- The settlors of the trust
- The identity of all persons who have the ability (through the trust terms or a related agreement) to exert control over trustee decisions regarding the apportionment of income or capital of the trust.

8 Passive income flowing into the NERDTOH pool would, for the most part, include non-eligible dividends, other property income and net taxable capital gains. Eligible dividends received would be included in the ERDTOH pool.
9 An "express trust" is one that was deliberately created and includes many of the most commonly-used types of trusts, including family trusts, testamentary trusts and living trusts.

2018

New penalties have also been introduced to encourage compliance with the new rules. New penalties of $25 per day (minimum of $100, and a maximum of $2,500) have been introduced to encourage compliance with the new rules, with additional penalties applicable in circumstances amounting to gross negligence.

Taken together, these new reporting requirements—and the process the trustees of an estate must undertake to determine if they apply—add to the growing administrative burden Canadian taxpayers face.

Foreign affiliate reporting

Corporations with an interest in a foreign affiliate are required to file Form T1134. The filing deadline has been shortened to 12 months after the taxation year-end for tax years that begin in 2020, and to 10 months after the taxation year-end for tax years that begin after 2020. Corporations with a taxation year beginning prior to 2020 were required to file Form T1134 within 15 months of the tax year-end.

Tax on cannabis

Although the process to legalize cannabis for recreational use started soon after the Liberals were officially sworn into office in 2015, it was not officially legalized until 2018. The 2018 budget stated the government's intention to amend the Excise Tax Act to allow for the appropriate taxation of cannabis products, based on the agreement reached by the federal government and most of the provincial and territorial governments.

March: The "Netflix" tax—Provinces and states target e-commerce

In its 2018 budget, Quebec introduced a new Quebec sales tax (QST) regime to collect QST from non-resident businesses that sell products or services to Quebec consumers. The new rules required these businesses to register through a new online registration system by January 1, 2019 to continue to make sales in Quebec. Furthermore, these businesses were required to charge QST at a rate of 9.975% on certain goods and services sold in Quebec.

Part of the reason for the Quebec system was to allow the province to charge and collect QST on sales by suppliers in the e-commerce sector and providers of digital property and service distribution platforms. With the advent of new technologies, and the use of these technologies by businesses to provide their goods and services becoming more widespread, many tax jurisdictions (e.g., federal, provincial, state, etc.) have fallen behind in their ability to effectively tax such sales. This appears to be changing, however, as evidenced by the new QST regime, as well as the drafting of similar legislation in several states, such as South Dakota, that applies sales tax on a company's online sales transactions, despite the lack of a physical presence in that state.

2018

November: Fall Economic Statement and the Trump effect

In his second year in office, President Trump managed to cause quite a stir among the Canadian business community, first with the TCJA and then with the ongoing free trade negotiations between the US, Canada and Mexico, which continued into 2019.

As such, 2018 proved to be difficult for the Liberal government when it came to dealing with Canada's largest and most important trading partner.

Since the implementation of the TCJA in 2017, the Liberal government had been under significant pressure to respond with similar changes to the tax environment for businesses.

Many were calling for an equal cut in corporate taxes to help Canadian businesses remain competitive with those in the US and it finally arrived in the 2018 Fall Economic Statement.

The most significant change was the adoption of accelerated capital cost allowance (CCA), allowing for a faster write-off of capital purchases. The accelerated CCA rules included:

- 100% write-off of manufacturing and processing assets
- 100% write-off of clean energy assets
- Up to three times the available first-year write-off for all other assets

The accelerated CCA rules apply to assets purchased after November 20, 2018 and prior to 2024, with the full write-off being gradually phased out by 2027.

The Fall Economic Statement also introduced and/or reiterated funding for programs to enhance Canadian businesses' exposure to global markets, particularly those with which Canada had recently negotiated free trade agreements. In particular, it introduced additional funding for several programs aimed at small and medium enterprises, in a bid to enhance exports, competitiveness and entrepreneurship. Three new tax measures to support Canadian journalism were also introduced, with supplementary details provided in the federal budget the following year.

November: A new trade agreement in principle, if not in acronym (CUSMA/USMCA/T-MEC)

The North American Free Trade Agreement (NAFTA) was ratified in 1994. Since then, significant changes to e-commerce, the global mobility of labour and capital, and in many other areas have occurred. Perhaps as a response to these changes, President Trump followed through on his campaign promise to revisit the trade deal, and the United States initiated the renegotiation of NAFTA in 2017. After a long and often difficult negotiation, then-Minister of Foreign Affairs Chrystia Freeland and her US and Mexican counterparts were able to agree on most terms in the fall of 2018.

The new Canada-United States-Mexico Agreement[10] (CUSMA) introduced changes to several policy areas including

- automobile manufacturing,
- the dairy industry,
- intellectual property rights,
- digital trade and
- labour regulations.

The CUSMA also includes a sunset clause--previously missing from NAFTA—that gives the agreement an expiration period of 16 years, with an opportunity to review and extend it every six years. Another clause has the potential to limit future trade agreements between Canada and certain other countries, known as “non-market countries”. This rule is widely seen as an attempt by the United States to limit both Canada and Mexico from entering into free trade discussions with China.

The NAFTA renegotiations finally resulted in an agreement between the three countries in November 2018; however, as of February 18, 2020, only the United States and Mexico have ratified it. Canada has not yet ratified the agreement, which could prove tricky with a minority Liberal government. Nevertheless, until this process is complete, the three countries continue free trade under the original 1994 NAFTA.

10 Referred to as Canada-United States-Mexico Agreement (CUSMA) in Canada, United States-Canada-Mexico Agreement (USMCA) in the US and Tratado entre México, Estados Unidos y Canadá (T-MEC) in Mexico.

2019

The calm before the storm

With a federal election on the horizon and many of the government's tax policies already set into place, 2019 proved to be a somewhat less eventful year for tax policy, at least compared to the previous three years. Budget 2019 had few significant tax policy proposals, although the vaguely-worded proposed changes to the taxation of stock options did cause a bit of a stir when announced.

March: Zero-emission vehicle, worker and homeowner incentives, intentions to address stock options

Business measures

Budget 2019 didn't have many significant tax measures aimed at businesses. It did, however, include measures to promote the purchase of zero-emission vehicles (ZEV).[11] A ZEV purchased brand-new and placed in use after March 18, 2019 and before 2024 is eligible for an accelerated capital cost allowance (CCA) rate of 100% in the first year it is acquired.

Qualifying ZEVs that would otherwise be included in Class 10 or 10.1 (i.e., passenger vehicles) would instead be included in Class 54 and would be subject to a maximum limit of $55,000. Qualifying ZEVs that would otherwise be included in Class 16 (e.g., freight-hauling trucks or tractors, taxis, aircraft, etc.) would instead be included in Class 55. For qualifying ZEVs purchased in a later year, the first-year CCA rate gradually decreases to 75% if purchased in 2024 and 2025 and then again to 55% if purchased in 2026 and 2027. The CCA rate in subsequent years (after the first year) decreases to 30% or 40%, depending on the type of vehicle.

Additionally, to help promote the purchase of ZEVs, the budget also introduced an incentive of up to $5,000 on ZEVs purchased or leased on or after May 1, 2019 that are priced at $45,000 or less, depending on the type of vehicle.[12] However, taxpayers that purchase ZEVs for business purposes would only be able to benefit from either the accelerated CCA or the incentive.

The government also made an effort to provide tax relief to farmers and fishers. The budget expanded relief from the specified corporate income rules (introduced in 2016, noted above) to ensure access to the small business deduction on sales to any arm's length corporation. Budget 2019 included a note specifically stating that "the government will continue its outreach to farmers, fishers and other small business owners," particularly with respect to intergenerational transfers of businesses. As this

11 The federal government classifies the following three types of vehicles as ZEVs: (1) battery-electric, (2) plug-in hybrid electric with a battery capacity of at least 15 kWh or (3) hydrogen fuel cell.

12 The incentive is applied at the point-of-sale, either at the dealership or online. Some higher-priced vehicle trims with a manufacturer's suggested retail price of $55,000 or less will also be eligible for the incentive.

has been a subject of interest throughout the Liberal government's first mandate, it will be interesting to see what might be included in an upcoming budget that will address this issue.

Additionally, the budget proposed changes to several international tax rules, including expanding the application of the foreign affiliate dumping rules to non-resident individuals and trusts, and changing the rules applicable to securities lending arrangements and transfer pricing. As a member of the OECD, Canada also continues to work towards applying several initiatives that came out of the BEPS action plan (mentioned above).

Individual measures

Help for workers and homeowners

Measures targeting workers and homeowners were major components of the tax policy that targeted individual Canadians. Some of these measures included:

- the Canada training credit, providing Canadians with up to $5,000 to finance future training costs;
- the Employment Insurance training support benefit, providing workers with up to four weeks of paid leave every four years to cover living costs while undergoing training;
- a new First-time Home Buyer Incentive, providing funding on up to 10% of the cost of a newly-built home (and 5% for resale homes); and
- an increase to the Home Buyers Plan withdrawal limit from $25,000 to $35,000.

Limiting the stock option deduction

Arguably the most significant changes to tax rules affecting Canadian individuals were only vaguely introduced (but not yet implemented) in Budget 2019: changes to the stock option deduction. Budget 2019 introduced the government's intent to place limits on a taxpayer's ability to use the stock option deduction. Although specific measures were not included with the budget, some guidance was provided on what the government planned to do.

When an individual exercises a stock option, the difference between the share's market price and the option price is considered an employment benefit, taxable to the employee upon purchase of the shares.[13] Currently, individuals who have exercised stock options can get a deduction equal to half the amount of the income inclusion when certain conditions are met. Budget 2019 stated that the government intends to place a $200,000 annual cap on the amount of stock options that would be eligible for the half deduction. Furthermore, the government intends to apply these rules only to employees of "large, long-established, mature firms."[14]

13 If the corporation is a Canadian-controlled private corporation, the recognition of the benefit is delayed until the owner of the shares sells those shares.

14 Honourable William Francis Morneau, Minister of Finance "Investing in the Middle Class, Budget 2019". March 19, 2019. See Chapter 4, section beginning on p. 202.

2019

Fast forward: 2020

As outlined in Grant Thornton's follow-up to Budget 2019, the wording quoted above presents much uncertainty. What would be considered a "large, long-established, mature firm"? What happens if a start-up becomes a large, long-established, mature firm and at what point does a firm reach this milestone? If stock options were granted prior to the firm being considered large, long-established and mature but exercised after, would the half deduction still be available?

The proposed measures were updated by Finance Minister Bill Morneau in June 2019 and the government requested feedback from interested stakeholders. As a result, in December 2019 the government decided to postpone the application of these measures, which were set to commence January 1, 2020. However, the government stated its intent to proceed with these measures and include them in budget 2020.

October: Liberals win a minority

In the fall of 2019, Canadians went to the ballot boxes for the federal election. The major political parties released their party platforms, providing insights on where each party's priorities lay. There were some areas of alignment. For example, both the Liberals and Conservatives offered to reduce corporate taxes for green businesses. The Liberals, Conservatives, NDP and Green parties all included measures to apply a tax on the income of certain international corporations[15] conducting e-commerce in Canada. However, there were also areas of divergence, including the taxation of capital gains, where both the NDP and the Greens included measures to increase the inclusion rate, while the Liberals and Conservatives took no specific position on the matter.

In the end, the election saw Trudeau and the Liberals return to power, albeit as a minority government.

15 International digital corporations would be subject to the tax if their worldwide income was at least $1 billion and Canadian revenues were over $40 million, per the Liberal platform. The other parties had similar thresholds.

Fast forward: 2020

It remains to be seen whether the returning Liberal government will implement bold new changes moving forward or play it safe as minority governments often do. It also remains to be seen how long its mandate will hold—a shorter timeframe may impose limits on its ability to act, as minority governments in Canada historically don't make it past the second year.

The government will likely be forced to make concessions in various areas to gain sufficient support to survive confidence votes. Depending on the measures the government hopes to implement, it may be able to gain such support from any of the three political parties that hold enough seats to help it pass legislation (i.e., Conservatives, Bloc Quebecois or NDP). Now, at the start of 2020, it will be interesting to see what some of these proposed measures might include as we approach the minority Liberal government's first federal budget. In another article, we examine some of the new government options—you can read that analysis here.

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