



TaxNewsFlash

Canada

Finance Releases Plethora of Draft Legislation

August 19, 2025

No. 2025-35

Finance released draft legislation on August 15, 2025 related to certain excessive interest and financing expenses limitation (EIFEL) exemptions, enhancements to the Scientific Research and Experimental Development (SR&ED) Tax Incentive Program, changes to the substantive Canadian-controlled private corporations (CCPCs) rules, the capital gains deferral on small business share rollovers, reporting required for certain trusts and non-profit organizations, and the capital gains exemption for certain sales of businesses, among other measures. Alongside this draft legislation, Finance also released draft legislation for the *Global Minimum Tax Act*, the *Excise Tax Act* and several other *Income Tax Act* technical tax amendments.

Finance is accepting comments on the draft legislative proposals until September 12, 2025.

Notably absent from this large package of draft legislation are several previously announced measures including the government's intended rescission of the Digital Services Tax (DST), transfer pricing legislative proposals, certain clean energy credits, accelerated capital cost allowance (CCA) proposals, changes to the hybrid mismatch rules and the Canadian Entrepreneurs' Incentive.

Background

Most of these measures in the draft legislation released August 15, 2025 were previously announced in the 2024 federal budget, August 12, 2024 draft legislation, and the 2024 federal Fall Economic Statement. For more information, see *TaxNewsFlash-Canada* 2024-48 "[Highlights of the 2024 Federal Fall Economic Update](#)", *TaxNewsFlash-*

Canada 2024-32 "[Reporting Relief on the Way for Trusts?](#)" and TaxNewsFlash-Canada 2024-17 "[2024 Federal Budget Highlights](#)".

Excessive interest and financing expenses limitation (EIFEL)

The draft legislation reintroduces two elective exemptions from the EIFEL rules (which are substantially the same as those included in the August 12, 2024 draft legislation), along with certain new technical amendments. Specifically, the draft legislation proposes to add:

- The previously announced elective exemption from the EIFEL rules for certain interest and financing expenses incurred before January 1, 2036 for arm's length borrowings used to build, acquire or convert property to a purpose-built residential rental in Canada
- The previously announced elective exemption from the EIFEL rules for certain interest and financing expenses that are reasonably attributable to borrowings used for the purpose of gaining or producing income from a Canadian regulated energy utility business
- Adjustments to the definition of "adjusted taxable income" to allow for negative taxable income, effective for taxation years ending after August 15, 2025
- The excluded interest election, specified pre-regime loss election, and the foregone foreign accrual property loss (FAPL) election to the list of elections that taxpayers may submit to the CRA for permission to late-file, amend or revoke, effective as of October 1, 2023.

The two elective exemptions apply to taxation years beginning on or after October 1, 2023, except that the filing deadline for these elections is the later of the taxpayer's normal filing-due date or 90 days after Royal Assent of the enacting legislation.

Scientific research and experimental development (SR&ED) tax incentive program

The draft legislation includes several enhancements to the SR&ED program that generally apply to taxation years that begin on or after December 16, 2024. The enhancements are the same as those announced in the 2024 federal Fall Economic Statement. In particular, the proposed legislation:

- Raises the annual expenditure limit for CCPCs to claim an enhanced 35% SR&ED investment tax credit to \$4.5 million (from \$3 million)
- Increases the taxable capital phase-out thresholds for determining the expenditure limit for the enhanced 35% SR&ED investment tax credit to between \$15 million and \$75 million (from \$10 million to \$50 million)

- Allows “eligible Canadian public corporations” (a newly defined term for “small” Canadian public corporations) to also qualify for the enhanced 35% tax credit on expenditures up to \$4.5 million
- Reduces the enhanced expenditure limit where the average gross revenue of the corporation or consolidated corporate group is between \$15 million and \$75 million over the three preceding years
- Allows CCPCs to elect to have their expenditure limit for the enhanced investment tax credit determined based on the same gross revenue phase-out structure proposed for eligible Canadian public corporations
- Restores the ability for businesses to claim capital expenditures for certain capital property (i.e., similar to the pre-2014 rules, applies to property that is shared use equipment or that is all or substantially used in SR&ED) acquired on or after December 16, 2024, and in the case of lease costs, to amounts that first became payable on or after December 16, 2024.

Substantive CCPC rules — Elimination of deferral using foreign affiliates

The draft legislation includes the substantive CCPC measures that were included in the August 12, 2024 draft legislation related to the elimination of the tax deferral advantage for CCPCs and substantive CCPCs that earn investment income through controlled foreign affiliates (CFAs). These measures generally apply to taxation years that begin on or after April 7, 2022, and includes, among other related measures:

- A reduction to the relevant tax factor (RTF) for CCPCs and substantive CCPCs (1.9 instead of 4) that will reduce the grossed-up deduction available to such corporations for tax paid by its CFA on its foreign accrual property income (FAPI)
- The previously announced, but significantly modified, elective foreign accrual business income (FABI) and FABI surplus regimes, which permit CCPCs and substantive CCPCs to access the tax deferral on certain investment income of its CFAs
- Consequential amendments to the calculation of the general rate income pool (GRIP), the capital dividend account (CDA) and safe income.

Capital gains deferral on small business share rollovers

The draft legislation expands what qualifies as an eligible small business corporation share and relaxes certain conditions to be eligible for the capital gains rollover, effective for qualifying dispositions that occur on or after January 1, 2025, as announced in the 2024 federal Fall Economic Statement. In particular, the proposed amendments:

- Increase the period to acquire replacement Eligible Small Business Corporation (ESBC) shares to encompass the year of disposition and the entire calendar year after the year of disposition (from 120 days)
- Increase the limit to the carrying value of the assets of the ESBC and related corporations to \$100 million (from \$50 million)
- Provide that an ESBC share includes both common and preferred shares.

Trust reporting rules

The draft technical amendments include several proposals related to the trust reporting rules that are generally effective for fiscal periods starting after December 30, 2025, with certain exceptions. These rules are similar to the August 12, 2024 draft legislation but have certain differences.

The exceptions to the trust reporting rules have been amended to include the following:

- Retirement compensation arrangements and employee ownership trusts
- Trusts that have been in existence for less than 3 months
- Trusts that own less than \$250,000 of Canadian deposits and GICs
- Certain bare trusts.

There is a new relieving provision for certain alter ego trusts or a joint spousal or common-law partner trusts regarding the disclosure of contingent beneficiaries.

Notably the draft legislation does not include the changes in the August 12, 2024 draft legislation to the capital loss carry back rules that would have extended the period for which an election can be made to three taxation years (from one taxation year).

Reporting by non-profit organizations (NPOs)

The draft legislation enhances the reporting requirements for non-profit organizations (NPOs) as announced in the 2024 federal Fall Economic Statement. In particular, NPOs and other tax-exempt organizations (i.e., agricultural organization, board of trade, or chamber of commerce) with receipts, including capital receipts, over \$50,000 will be required to file the annual NPO information returns. Entities that do not meet the annual information return filing thresholds will be required to file a new, short-form return that contains prescribed information about the organization. These proposed amendments apply to fiscal periods that begin on or after January 1, 2026.

Employee ownership trust (EOT) tax exemption

The August 15, 2025 draft legislation builds upon previously announced measures to adjust the tax exemption for EOTs on up to \$10 million in capital gains realized on the sale of a business to an EOT and is generally effective on January 1, 2024. It proposes to:

- Prevent multiplication of the capital gains deduction
- Ensure that the holding period and the active business asset tests operate effectively where shares are received in substitution for other shares
- Clarify that the sale of shares of a holding corporation may qualify for the exemption under certain circumstances
- Clarify the requirement for active engagement in a business for the 24 months holding period prior to disposition
- Provide exceptions to disqualifying events where an active business of a qualifying business ceases due to the disposition of all assets to satisfy certain debts
- Provide a new ordering rule where an individual claims two or more exemptions on the sale of a business to an EOT, effective August 12, 2024.

Workers cooperatives

The August 15, 2025 draft legislation builds upon previously announced workers cooperatives measures and is generally effective on January 1, 2024. It introduces new rules to facilitate the use of a worker cooperative to acquire and hold shares of a business. Under these rules, an individual who sells shares of their business to a worker cooperative in 2024, 2025 or 2026 may claim a capital gains exemption of up to \$10 million if certain conditions are met. It appears the proposals do not extend the capital gains reserve from 5 to 10 years for dispositions of shares pursuant to a qualifying cooperative conversion.

Global minimum tax (Pillar Two)

Finance also released draft legislation for the *Global Minimum Tax Act*, with key updates including:

- A new de-consolidation rule for certain qualifying multinational enterprise (MNE) groups that include one or more private investment entities (newly defined as a private entity that owns a controlling interest in a publicly listed Canadian corporation), effective for fiscal years of a qualifying MNE group that begin on or after December 31, 2023

- New and refined provisions for the allocation of covered taxes in respect of tax transparent entities, controlled foreign companies, hybrid and flow-through entities
- New provisions for deferred tax assets and liabilities, including pre-global anti-base erosion (GloBE) arrangement deferred tax assets
- New transitional rules for constituent entities' pre-GloBE transactions in fiscal years before their GloBE transition year.

Notably, the legislative proposals do not include a framework for the undertaxed profits rule (UTPR).

Enhanced CRA audit powers

The draft legislation provides the CRA with enhanced audit powers to more easily obtain information, including through a new penalty for non-compliance. Proposed amendments to the CRA's audit powers were included in the 2024 federal budget, and also in the August 12, 2024 draft legislation.

The August 15, 2025 draft legislation provides that the proposed penalty related to the issuance of a compliance order is up to 10% of tax payable and does not apply in the context of a third-party request for information, and adds an exception to the penalty if the taxpayer reasonably believed that the required information was protected from disclosure from solicitor-client privilege. Moreover, upon an objection to an assessment of this penalty, the CRA must vacate or vary the assessment if it determines that the penalty is disproportionate or unfair, and the CRA may reduce the amount of the penalty or provide any other relief it deems appropriate.

An exception also applies to the proposed penalty on persons issued a notice of non-compliance if the person reasonably believed that the required information was protected from disclosure by solicitor-client privilege.

Indirect tax

Input tax credits for payments for redeemed coupons

Finance also released draft legislation to amend the GST/HST rules in the *Excise Tax Act* (ETA) to clarify that a person may claim input tax credits related to payments for redeemed coupons only if they are made exclusively in the course of commercial activities, effective August 16, 2025. The proposals also limit input tax credits for any such payments made before August 16, 2025, that were not made exclusively in the course of commercial activities if the related input tax credits were not claimed in a GST/HST return filed before August 16, 2025.

The draft legislation also includes the following GST/HST measures:

- Amendments to section 193 of the ETA to adjust input tax credits related to previously unrecoverable tax at the time of the taxable sale of real property under certain circumstances, that appear targeted at Selected Listed Financial Institutions (SLFIs)
- Changes to the GST/HST return filing obligations for deceased individuals, including changes to filing obligations related to the financial institution annual information returns (e.g., GST111 returns) for individuals that qualified as financial institutions
- Changes to the Selected Listed Financial Institution Attribution Method (GST/HST) Regulations to exclude some GST on surety expenses from the Special Attribution Method (SAM) calculations.

Other tax measures

Finance also released other technical measures covering a range of personal, business and international tax measures. These measures include:

- Detailed adjustments to the calculation of foreign accrual tax (FAT), foreign tax credits and foreign affiliate surplus accounts to account for income or profits tax paid by foreign affiliates of Canadian corporations under domestic minimum top-up tax regimes (DMTT) in foreign jurisdictions (i.e., other countries' domestic Pillar Two rules)
- Changes that may affect Canadian resident corporations that operate international shipping businesses (e.g., treatment of capital gains and recapture on disposition of a ship that was used to earn income from international shipping)
- Clarifications that a taxpayer's share of governmental assistance related to a Canadian resource property or an exploration or development expense incurred in Canada will not include certain government loans (i.e., "excluded loans" as defined in the *Income Tax Act*)
- Clarifications to the share buyback tax related to "reorganizations" that may be excluded from the tax
- Implementation of the OECD's Crypto-Asset Reporting Framework in Canada, with related adjustments to the Common Reporting Standard, announced in the 2024 federal budget (generally applies to the 2026 and subsequent calendar years).

We can help

Your KPMG adviser can help you assess the effects of the tax changes in the August 15, 2025 draft legislation on your personal finances and business affairs. We can also keep you abreast of the progress of these proposals as they make their way into law.

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