



# TaxNewsFlash

Canada

## 2021 Federal Budget — First Impressions

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Canada's Deputy Prime Minister and Finance Minister Chrystia Freeland delivered the 2021 federal budget on April 19, 2021. The budget expects a deficit of \$354.2 billion for 2020-21 and forecasts a deficit of \$154.7 billion for 2021-2022.

Based on our initial reading, it appears that this year's budget focuses on Canada's post-pandemic economic recovery. Although the budget does not change the federal personal or corporate tax rates, it does extend the Canada Emergency Wage Subsidy (CEWS), the Canada Emergency Rent Subsidy (CERS) and the Lockdown Support until September 25, 2021 and introduces a new Canada Recovery Hiring Program.

The budget also announces interest expense limitations for certain Canadian corporations starting in 2023. Canadian multinationals may also be affected by new anti-hybrid rules. The budget also provides details of the digital services tax, which is scheduled to be effective for January 1, 2022.

Note that the budget did not increase the capital gains inclusion rate, change the principal residence exemption or introduce a wealth tax. In addition, Finance did not announce comprehensive tax reform.

### **Stay tuned for in-depth budget highlights**

In addition to this high-level summary of the 2021 federal budget, we are preparing a special budget edition of *TaxNewsFlash-Canada* to be released on our website soon that provides more comprehensive details of all the budget's tax measures.

## Highlights of new budget tax measures

### *Canada Recovery Hiring Program*

The budget introduces the new Canada Recovery Hiring Program to provide eligible employers with a subsidy of up to 50% on the incremental remuneration paid to eligible employees between June 6, 2021 and November 20, 2021. Eligible employers can claim either the hiring subsidy or the CEWS for a particular qualifying period, but not both.

### *COVID-19 support programs*

The budget extends the CEWS, the CERS and the Lockdown Support to September 25, 2021. However, the subsidy rates for these programs will gradually decline starting on July 4, 2021.

The budget also requires that any publicly listed corporation receiving the wage subsidy and found to be paying its top executives more in 2021 than in 2019 will need to repay the equivalent in wage subsidy amounts received for any qualifying period starting after June 5, 2021 and until the end of the wage subsidy program.

### *Interest deductibility limits*

The budget introduces an earnings-stripping rule consistent with OECD recommendations to limit the amount of net interest expense that a corporation may deduct in computing its taxable income to no more than a fixed ratio of “tax EBITDA”. This is that corporation’s taxable income before taking into account interest expense, interest income and income tax, and deductions for depreciation and amortization, where each of these items is as determined for tax purposes. The budget limits the amount of interest that certain businesses can deduct be limited to 40% of their earnings in the first year of the measure and 30% thereafter. Draft legislative proposals are expected to be released for comment later in 2021.

Exemptions from the new rule would be available for Canadian-controlled private corporations that, together with any associated corporations, have taxable capital employed in Canada of less than \$15 million (i.e., the top end of the phase-out range for the small business deduction). In addition, groups of corporations and trusts whose aggregate net interest expense among their Canadian members is \$250,000 or less would also be exempt.

This measure would apply to taxation years that begin on or after January 1, 2023 and would apply with respect to existing as well as new borrowings.

### *Reduced income tax rates for zero-emission technology manufacturers*

The budget temporarily reduces the corporate income tax rates for qualifying zero-emission technology manufacturers. Specifically, taxpayers would be able to apply reduced federal tax rates on eligible zero-emission technology manufacturing and processing income of

7.5% (where that income would otherwise be taxed at the 15% general corporate tax rate), and 4.5% (where that income would otherwise be taxed at the 9% small business tax rate).

### Other tax changes

The budget also introduces measures affecting the following areas:

#### Corporate tax changes

- Provides temporary immediate expensing for certain property acquired by a Canadian-Controlled Private Corporation (CCPC), for eligible property (i.e., capital property that is subject to the CCA rules, other than property included in CCA classes 1 to 6, 14.1, 17, 47, 49 and 51) acquired on or after April 19, 2021 that becomes available for use before 2024
- Changes the capital cost allowance eligibility criteria for certain types of clean energy equipment property that is acquired and that becomes available for use on or after April 19, 2021, with some exceptions
- Temporarily extends certain timelines for the Canadian Film or Video Production Tax Credit (CPTC) and the Film or Video Production Services Tax Credit (PSTC) to 12 months
- Announces a consultation on proposals to enhance Canada's mandatory disclosure rules that will address changes to the Income Tax Act's reportable transaction rules, a new requirement to report notifiable transactions, and a new requirement for specified corporations to report uncertain tax treatments
- Introduces rules to address planning transactions that Finance says attempts to circumvent the tax debt avoidance rule, for transfers of property that occur on or after April 19, 2021
- Announces a consultation to strengthen and modernize Canada's general anti-avoidance rule.

#### Personal tax changes

- Announces a consultation on a new national 1% tax on the value of non-resident, non-Canadian owned residential real estate considered to be vacant or underused, to be levied annually beginning in 2022
- Adjusts the requirements for the Disability Tax Credit for 2021 and subsequent taxation years
- Enhances the Canada Workers Benefit to increase the phase-in rate, phase out-rate and phase-out thresholds for 2021 and subsequent taxation years

- Expands access to the travel component of the Northern Residents Deductions for 2021 and subsequent taxation years
- Includes postdoctoral fellowship income in “earned income” for RRSP purposes
- Allows individuals to claim a deduction for the repayment of certain COVID-19 benefit amounts in computing their income for the year in which the benefit amount was received rather than the year in which the repayment was made, for benefit amounts repaid at any time before 2023
- Allows pension plan administrators of defined contribution pension plans to correct for both under-contributions and over-contributions for 2021 and subsequent taxation years
- Allows taxes that apply to registered investments under Part X.2 of the Income Tax Act be pro-rated based on the proportion of shares or units of the registered investment that are held by investors that are themselves subject to the qualified investment rules, for months after 2020
- Amends the registration and revocation rules for charities for listed terrorist entities, ineligible individuals and where false statements are made, effective on Royal Assent.

#### *International tax changes*

- Introduces rules to ensure that multinational enterprises cannot derive tax benefits from the use of hybrid mismatch arrangements, with proposed legislation expected later in 2021, and implementation in stages starting July 1, 2022
- Announces the government’s intention to consult on changes to Canada’s transfer pricing rules.

#### *Indirect tax changes*

- Implements a Digital Services Tax at a rate of 3% on revenue from digital services that rely on data and content contributions from Canadian users that would apply to large businesses with gross revenue of 750 million euros or more as of January 1, 2022, until an acceptable multilateral approach comes into effect
- Adjusts the rules that applies the GST/HST to e-commerce businesses, as announced in the 2020 fall economic update
- Increases the input tax credit information thresholds, effective after April 19, 2021
- Relaxes the GST New Housing Rebate Conditions to remove the condition that where two or more individuals buy a new home together, each of them must be acquiring the home for use as their primary place of residence or the primary place

of residence of a relation, effective to a supply made under an agreement of purchase and sale entered into after April 19, 2021

- Creates a joint election mechanism under the rebate of excise tax for goods purchased by provinces to specify that the vendor alone would be eligible to apply for the rebate only if it jointly elects with the province to be the eligible party
- Increases the tobacco excise duty rate by \$4 per carton of 200 cigarettes, effective after April 19, 2021
- Implements a tax on vaping products in 2022 through the introduction of a new excise duty framework
- Introduces a tax on the retail sale of new luxury cars and personal aircraft priced over \$100,000, and boats priced over \$250,000, effective January 1, 2022.

#### *Administrative and other changes*

- Changes the rules for electronic filing and the certification of tax and information returns
- Confirms that CRA officials have the authority to require persons to answer all proper questions, and to provide all reasonable assistance, for any purpose related to the administration or enforcement of a relevant statute, effective on Royal Assent
- Changes the rules for the collection of duties and taxes on imported goods.

#### **We can help**

Your KPMG adviser can help you assess the effect of the tax changes in this year's federal budget on your personal finances or business affairs, and point out ways to realize any benefits or ease their impact. We can also keep you abreast of the progress of these proposals as they make their way into law.

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