Canada – Federal Budget for 2024 Presented

Canada's Deputy Prime Minister and Finance Minister Chrystia Freeland delivered Canada's 2024 federal budget on April 16, 2024.[1]

Featured in the budget's tax measures that could impact individuals (including globally-mobile employees) and their employers were changes related to: the capital gains inclusion rate, the 15-percent withholding tax on payments to nonresident service providers, the Home Buyer's Plan, and administrative measures that allow the Canada Revenue Agency (CRA) to issue notices of non-compliance for failures to comply with documentation requests.

For the complete analysis, see special edition of *TaxNewsFlash-Canada* summarizing the announced tax changes prepared by members of the KPMG National Tax Centre, as well as other publications and communications from KPMG in Canada by clicking here.

WHY THIS MATTERS

1) **Capital Gains Inclusion Rate (and stock option deduction)** – Potential impacts on tax-equalization policies and Canada's departure tax; therefore, employers may need to re-consider their compensation plan structures.

2) **Regulation 105 Waiver** – The waiving of the 15-percent withholding tax on payments to nonresident service providers, if they would be exempt from Canadian taxation under a treaty, offers some potential relief.

3) **Home Buyers' Plan** – When a Canadian resident breaks residency, to the extent he or she has an outstanding balance in the Home Buyers' Plan, this needs to be repaid within 60 days of departing. The increased threshold for additional withdrawal can lead to a higher repayment obligation in the year of departure.

4) **CRA Notices for Information Requests** – The budget proposes to allow CRA to issue a notice of non-compliance for failure to comply with documentation requests, with a maximum penalty of $25,000. Tax service providers, employers, and taxpayers need to be diligent vis-à-vis such requests.

Capital Gains Inclusion Rate (and Stock Option Deduction)

The budget increases the inclusion rate for capital gains realized on or after June 25, 2024. In particular, the budget increases the inclusion rate for individuals to 2/3 (from 1/2) on the portion of capital gains realized in the year that exceed $250,000. For corporations and trusts, the inclusion rate increased to 2/3 (from 1/2) for which there is no $250,000 threshold.

The change in the capital gains rates applies to any dispositions of assets, including deemed dispositions on a departure from Canada or death.

Where an individual claims the employee stock option deduction, the budget provides a 1/3 deduction of the taxable benefit to reflect the new capital gains inclusion rate, but that individual would be entitled to a deduction of 1/2 the taxable benefit up to a combined limit of $250,000 for both employee stock options and capital gains.

This change won't affect the taxation of cash settled RSUs or PSUs, as they are not eligible for any deduction. For eligible stock options, one must also consider the rules that took effect July 1, 2021, which potentially limited the amount of options eligible for any deduction.

The budget notes that net capital losses of prior years would continue to be deductible against taxable capital gains in the current year by adjusting their value to reflect the inclusion rate of the capital gains being offset. As a result, a capital loss realized prior to the rate change would fully offset an equivalent capital gain realized after the rate change.

The budget also provides transitional rules for tax years that begin before and end on or after June 25, 2024, where two different inclusion rates would apply. Effectively, the annual $250,000 threshold for individuals would not be prorated in 2024 and would apply only in respect of net capital gains realized on or after June 25, 2024.

KPMG INSIGHTS

The budget notes that it intends to make other consequential amendments to reflect the new inclusion rate, and that it will release additional design details soon. One such outstanding issue is whether employers will need to withhold taxes on option exercises on the assumption that the 1/3 deduction applies, even for employees who could be entitled to the 50-percent deduction. Another outstanding issue is how to allocate the lower deduction rate between capital gains and option benefits; this can be relevant where tax equalizations do not cover personal income.

Lifetime Capital Gains Exemption

The budget increases the Lifetime Capital Gains Exemption (LCGE) on, generally, dispositions of shares of Canadian-controlled private corporations that are primarily involved in an active business in Canada, to $1.25 million (from $1,016,836), with indexation of the LCGE resuming in 2026. This tax measure applies to dispositions that occur on or after June 25, 2024.

Withholding for Nonresident Service Providers

The budget provides that the CRA may waive the requirement for a person who pays a nonresident for services provided in Canada to withhold 15 percent of the payments and remit it to the CRA, over a specified period, provided that:

- the payments are exempt from Canadian income tax because of a tax treaty between the nonresident's country of residence and Canada or are exempt income from international shipping or from operating an aircraft in international traffic, and
- the conditions established by the CRA are met.

This proposal would allow the CRA to waive the withholding requirement on multiple transactions with a single waiver. This measure would come into force on royal assent of the enacting legislation.

Note that this proposal does not cover waivers for payroll taxes for nonresident employees. The current rules, including the employer certification procedure, continue to apply here.

Housing

One of the major themes of this year's budget is to increase the affordability of housing. (For earlier housing-support measures, see *GMS Flash Alert* 2022-085, April 12, 2022.) In particular, the budget provides several incentives for purpose-built rental housing in Canada, including an elective exemption from the interest deductibility limitation and enhanced Capital Cost Allowance (CCA) for certain new additions of property. There are also new measures intended to benefit first-time home buyers. Finance's budget also focuses on clean economy changes, including to provide expected detail on the Clean Electricity investment tax credit, among others.

Home Buyers' Plan

The budget increases the withdrawal limit under the Home Buyers' Plan to $60,000 (from $35,000) for 2024 and subsequent calendar years in respect of withdrawals made after April 16, 2024. This increase would also apply to withdrawals made for the benefit of a disabled individual.

The budget also temporarily defers the start of the 15-year repayment period to the fifth year following the year in which a first withdrawal was made (from the second year) for participants making a first withdrawal between January 1, 2022 and December 31, 2025.

The CRA and Compliance Enforcement

The budget gives CRA the authority to issue a notice of non-compliance to a person if the minister believes that the person has not complied with a requirement to provide assistance or information. A person who receives a notice may request in writing, within 90 days of receiving the notice, that the minister review the notice. Within 180 days of receiving the request to review the notice, the minister must confirm, vary, or vacate the notice, and must vacate the notice if the minister determines that the notice was unreasonable or that the person had already reasonably complied with the request for assistance or information. After the person receives notification of the minister's decision, the person may apply, within 90 days, to a judge to review the minister's decision. While a notice is outstanding, the person served with the notice is liable for a penalty of $50 for each day of non-compliance, to a maximum of $25,000.

Also, if a notice related to a taxpayer is issued to the taxpayer or to a person who does not deal at arm's length with the taxpayer, the normal reassessment period for the relevant taxation years of the taxpayer is suspended.

In addition, the budget allows the minister to include in a requirement or notice for information or documents under the minister's general audit power, the minister's domestic requirement power, or the minister's foreign-based information or document requirement power, an explicit requirement that the person provide any answers to questions, information, or documents sought by the minister be provided orally, under oath or affirmation, or by affidavit.

Further, the budget gives the minister the power to seek a compliance order from the court for the alleged failure to comply with a requirement for foreign-based information or documents. Previously, the minister had the power to seek a compliance order in relation to requests under the minister's general audit power and domestic requirement letters, but not for requests for foreign-based information or documents.

The budget also introduces a new penalty in situations where the minister obtains a compliance order against a taxpayer. The penalty is 10 percent of the aggregate tax payable by the taxpayer for the relevant taxation years, if the tax payable for each taxation year to which the compliance order relates is $50,000 or more. Previously, the primary consequence of non-compliance with a compliance order was a contempt order.

These changes would come into force on royal assent of the enacting legislation.

Previously-Announced Tax Changes

The budget confirms that Finance intends to proceed with certain previously-announced tax measures, as modified by recent consultations and deliberations. These measures include:

- Short-term rentals
- Proposals relating to the Underused Housing Tax.

KPMG INSIGHTS

The provisions that will impact mobile employees the most are the reductions in the stock option deduction amount and the increases in the capital gains inclusion amount. We are currently waiting for draft legislative proposals that could answer some questions as to the interaction between the two regimes, as well as provide guidance to employers on how to administer payroll withholdings and reporting given the new rates.

Prior to June 25, 2024, there will likely be a focus on potentially crystallizing the application of the current rates by selling assets or exercising options early. Employers that have employees with unvested stock options may want to consider whether to accelerate the vesting of such options prior to the June 25, 2024 date.

After June 24, 2024, employers may want to revisit their compensation plan mix, as the taxation of options may become less preferential than currently. As an example, as stock options generally do not allow employers to claim a corporate tax deduction, which cash-settled RSUs do, employers may evaluate whether replacing options with cash-settled RSUs could result in a better combined tax rate.

Employers may also have to re-calculate the estimated costs of their tax-equalization policies, particularly if they cover personal income, as well as re-evaluate the desirability of equalizing for personal capital gains and accelerating any potential moves from Canada before June 25 if practical.

FOOTNOTE:

1 For the budget speech and related documentation, see: https://budget.canada.ca/2024/home-accueil-en.html.

* * * *

Contact us

For additional information or assistance, please contact your local GMS or People Services professional or the following professional with the KPMG International member firm in Canada:

Sonia Gandhi
Partner and Canadian Leader
KPMG LLP – Tax
Tel. +1-416-549-7870
soniagandhi@kpmg.ca

The information contained in this newsletter was submitted by the KPMG International member firm in Canada.

www.kpmg.com

Some or all of the services described herein may not be permissible for KPMG audit clients and their affiliates or related entities.

Learn about us: **kpmg.com**

GMS Flash Alert is a publication of the KPMG LLP Washington National Tax practice.