



TaxNewsFlash

Canada

Canada Moves to Enact Remaining Budget Measures

May 8, 2026

No. 2026-31

Canada has now released a second budget bill containing the remaining tax measures proposed in the 2025 federal budget, among other measures. The proposed legislation, which is included in Bill C-31 (Budget Bill #2), introduces new changes to the immediate expensing rules and the dividend suspension rules. In addition, the proposed legislation includes tax measures related to areas including clean economy incentives, the 21-year anti-avoidance rule for indirect transfers to trusts, global minimum tax, and the CRA's expanded audit powers, among others.

The business income tax measures in Budget Bill #2 are considered substantively enacted for IFRS and Accounting Standards for Private Enterprise (ASPE) purposes as of May 6, 2026, the date the bill received first reading, as Canada has a majority government. These measures will be considered enacted for U.S. GAAP on the date these proposals receive Royal Assent.

Note that this publication discusses select income tax measures, and does not address proposed amendments to various other Acts, such as the *Excise Tax Act*, *Select Luxury Items Tax Act*, *Bank Act*, and the *Bankruptcy and Insolvency Act*, among others. Affected businesses and individuals should act quickly to identify opportunities and confirm how their tax obligations may be affected by this proposed legislation. Your KPMG tax adviser can help you determine how to take advantage of business-friendly tax measures or mitigate the effects of other tax changes in these wide-ranging proposals.

Background

The Department of Finance Canada has proposed many significant business and personal tax measures over the last several years including in the 2025 federal budget. For details, see *TaxNewsFlash-Canada* 2025-41, "[2025 Federal Budget Highlights](#)".

Some 2025 federal budget measures are in Bill C-15, which implement changes related to transfer pricing, Scientific Research and Experimental Development (SR&ED), substantive Canadian-controlled private corporations (CCPCs), clean economy investment tax credits, the Excessive Interest and Financing Expenses Limitation (EIFEL) rules, accelerated capital cost allowance (CCA), trust reporting and the lifetime capital gains exemption limit, among others. For details, see *TaxNewsFlash-Canada* 2026-20, "[Canada Enacts 2025 Budget Measures](#)".

Business tax changes

Immediate expensing for manufacturing and processing (M&P) buildings

The proposed legislation tweaks the temporary immediate expensing for eligible manufacturing or processing (M&P) buildings measure, as previously announced in the 2025 federal budget and released as draft legislation on January 29, 2026. Under this measure, a taxpayer may claim immediate expensing (generally a 100% capital cost allowance (CCA) deduction of the building's capital cost) in the taxation year in which at least 90% of the building's floor space is first used for M&P activities, effective for eligible buildings and qualifying additions acquired on or after November 4, 2025 and used for manufacturing and processing before 2030. The CCA deduction rate is gradually reduced for the years after 2030 and is eliminated after 2033. Otherwise, M&P buildings designated to a separate class remain eligible for CCA at a rate of 6%. Anti-avoidance rules also apply to prevent taxpayers from stacking CCA deductions and undertaking transfers to access the immediate expensing deduction.

The proposed legislation refines certain eligibility and compliance requirements for this measure, as compared to the draft legislation released on January 29, 2026. The new wording explicitly states that each eligible M&P building must be included in Class 1 and designated to a separate CCA class. The proposed legislation states that this designation can now be made in the taxpayer's income tax return, rather than through a separate letter election attached to the tax return. The proposed legislation also clarifies the recapture rules that apply where, within 10 years of claiming immediate expensing, the floor space used in M&P activities falls below 90% ("manufacturing building recapture event"). The proposed legislation states that, if a manufacturing building recapture event occurs, the taxpayer is deemed to have disposed of the building at its notional undepreciated capital cost (UCC) and immediately reacquired it at the same amount. The notional UCC is the UCC that would have existed if the maximum CCA rate of 6% had been claimed each year rather than the 100% write-off in the first year. This change essentially modifies the

recapture mechanics so that only the excess CCA deducted due to the immediate expensing provision is subject to recapture and included in taxable income.

Tax deferral through tiered corporate structures rules

Finance has revised the previous draft legislation released on January 29, 2026 for the dividend suspension rules that curb tax deferral achieved through tiered corporate structures, effective for taxation years beginning on or after November 4, 2025. Prior to the introduction of these rules in the 2025 federal budget, a dividend could trigger an immediate refund to the payer while deferring Part IV tax in an affiliated corporation with a later balance-due day allowing deferral of refundable tax for up to nearly one year without shareholder-level tax.

To address concerns related to the regime's complexity and the risk of permanently trapped refundable tax, Finance's new revisions in the proposed legislation significantly refine the rules and will now capture corporate structures with taxation year-end mismatches, rather than balance-due day mismatches. Under the new proposed legislation, a dividend refund is now suspended where a dividend is paid to an affiliated corporation (including certain non-private "subject corporations") with a later taxation year-end.

KPMG observation

The proposed legislation eliminates a potential timing issue. Certain small private corporations that claim the small business deduction and are within certain taxable capital limits can extend their final tax payment to three months after taxation year-end (as opposed to two months for all other corporations). Therefore, even if a chain of private corporations had the same taxation year-end, the prior version of the dividend suspension rules could apply if one of the corporations were able to extend their balance-due day to three months post-year-end.

Finance has also revised the exclusion rule in the proposed legislation. The rule now requires dividends equal to the payer's proportion of the dividend refund multiplied by 2.6 (the "suspended dividend") to flow up the chain before the payer's balance-due day, instead of an equivalent dividend of the same amount and character. Finance also expanded the loss restriction exception to apply not only within 30 days after the payment of the dividend but also when a loss restriction event occurs within 12 months after the payment of dividend if the dividend is paid in contemplation of a loss restriction.

KPMG observation

It appears that the exclusion rule may have been changed to deal with situations where the corporate group did not have sufficient assets or general rate income pool (GRIP) to pay a dividend of the same amount and character up the corporate chain. By basing the dividend on the amount of the dividend refund multiplied by 2.6, this change aligns the refund with real economic distributions and not just intercompany distributions. The

addition of the loss restriction event exception to 12 months after payment of a dividend in contemplation of the event allows for pre-closing purification dividends after 30 days of the event and situations where the corporation is being sold to a trust and the pre-closing dividend is deemed to be received at calendar year-end.

Finally, Finance has clarified the refund release rule in the proposed legislation by introducing a quantitative threshold. As a result, qualifying dividends paid within the group must at least equal the payer's proportionate share of the suspended amount (suspended dividend refund \times 2.6) to unlock the refund.

Avoidance of tax debts

The proposed legislation supplements the rules intended to prevent the avoidance of tax debts by addressing planning that uses an arm's length intermediary. These rules address the use of third-party intermediaries (referred to as "planners") who engage in "planning activity" by organizing, creating, or promoting tax arrangements that result in tax avoidance. Under these rules, which apply to transactions occurring on or after April 16, 2024, where a tax debtor transfers assets that ultimately benefit a non-arm's length person, the recipient may be held jointly and severally liable for the transferor's tax debt. The additional proposed legislation allows the CRA to look through multi-step transfers made through an intermediary or planner as well as to pursue collections in respect of the amount of any fee retained by the planner.

KPMG observation

While existing provisions of the Income Tax Act allow tax avoidance planning activity to be challenged and penalties to be imposed, the proposed rules strengthen the tax-debt anti-avoidance regime by imposing joint and several liability on transferors and transferees for the tax debt, including fees paid to a planner.

Clean economy tax changes

Canadian Exploration Expense — Eligible activities

The proposed legislation clarifies that expenses incurred for the purpose of determining the quality of a mineral resource do not include expenses related to determining the economic viability or engineering feasibility of the mineral resource, as announced in the 2025 federal budget. This amendment applies as of November 4, 2025.

CCUS ITC

The proposed legislation introduces technical amendments to the Carbon Capture, Utilization, and Storage (CCUS) Investment Tax Credit (ITC). In particular, the proposed legislation clarifies the criteria for dual-use equipment. It also confirms that where CO₂ placed in dedicated geological storage is subsequently released for bona fide reasons

beyond the taxpayer's control the CO₂ will continue to be treated as having been put to an eligible use and does not trigger ITC recapture.

The CCUS ITC is a refundable tax credit that supports eligible expenditures relating to carbon capture, utilization, and storage projects. The applicable credit rate depends on the purpose of the equipment, with different credit rates (ranging from 37.5% to 60%) applying to eligible CCUS expenditures incurred from the start of 2022 to the end of 2035. Eligible expenditures that are incurred from the start of 2036 to the end of 2040 are subject to reduced credit rates (ranging from 18.75% to 30%).

KPMG observation

It is unclear what constitutes a “bona fide reason” that CO₂ is released in a way that is considered beyond the taxpayer's control.

Clean Hydrogen ITC

The proposed legislation expands eligibility to the Clean Hydrogen ITC (CHITC) by adding hydrogen produced through methane pyrolysis as an eligible production pathway effective December 16, 2024. For pyrolysis projects, the first filing deadline is extended to the later of December 31, 2027 and one year after the taxpayer's filing due date for the year.

The CHITC is a refundable tax credit of up to 40% of the cost of purchasing and installing eligible equipment for qualifying hydrogen production projects. In addition, property used to convert clean hydrogen into clean ammonia is eligible for the ITC at a 15% rate, subject to certain conditions.

Other Clean Economy ITCs

The proposed legislation amends the Clean Electricity ITC (CEITC), Clean Technology ITC (CTITC), and Clean Technology Manufacturing ITC (CTMITC) to expand the rules where a qualified project asset is transferred between related qualifying entities. The amendments deem the purchaser to inherit the acquisition date, capital cost and ITC claim history, effectively ensuring that ITCs are not duplicated in respect of the same capital cost. The proposed legislation also introduces anti-stacking rules to prevent the same eligible expenditure from being claimed under both the Clean Economy ITCs and the SR&ED and adds enhanced audit powers and record keeping obligations.

These ITCs are generally available to taxable Canadian corporations, including taxable Canadian corporations that are members of partnerships. The CTITC is also available to a real estate investment trust. The CEITC is also available to certain Crown corporations, corporations owned by municipalities and Indigenous communities, and pension investment corporations.

Trust tax changes

Trust indirect transfers and the 21-year rule

The proposed legislation includes new changes to the previously proposed extension of the anti-avoidance rule for direct trust-to-trust transfers to indirect transfers of property. In general, personal trusts are deemed to have disposed of their capital property and certain other property for proceeds equal to fair market value (FMV) on the 21st anniversary of their creation, and every 21st anniversary thereafter (the “21-year rule”). In the 2025 federal budget, Finance announced it would broaden the anti-avoidance provision to the 21-year rule to include indirect transfers of trust property to other trusts occurring on or after November 4, 2025. This measure is intended to address tax planning that avoids the 21-year rule, such as arrangements under which trust property is transferred on a tax deferred basis to a corporate beneficiary owned by a newly created trust.

KPMG observation

The proposed legislation amends the wording of the previous draft legislation released on January 29, 2026 that proposed expanding the existing anti-avoidance rule to apply where trust property is transferred “directly or indirectly in any manner whatever” to another trust. The proposed amendments address concerns that the previous wording was overly broad and could inadvertently capture routine estate and trust planning transactions, including refreezes. The revised wording more clearly targets the intended planning by explicitly extending the anti-avoidance rule to transfers made to a beneficiary of the transferor trust, where an interest in that beneficiary is held directly or indirectly by another trust. As a result, where such transfers occur on or after November 4, 2025, the transferee trust inherits the original trust’s 21-year anniversary, preventing the deferral or resetting of the deemed disposition timeline.

International tax changes

Global minimum tax

The proposed legislation also includes several global minimum tax measures. These measures, which amend the *Global Minimum Tax Act* (GMTA), were previously included in the August 12, 2024 draft legislation and the August 15, 2025 draft legislation. These measures include:

- A new framework for the Undertaxed Profits Rule (UTPR), that applies to fiscal years of a qualifying multinational enterprise (MNE) group that begin on or after December 31, 2025
- A new transitional “side-by-side” safe harbour and related election, that applies to fiscal years of a qualifying MNE group that begin on or after January 1, 2026

- A de-consolidation rule for certain qualifying MNE groups that include one or more private investment entities (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
- Updated rules for allocating covered taxes in respect of certain entities (e.g., tax transparent entities), effective for fiscal years of a qualifying MNE group that begin on or after December 31, 2023
- New provisions for deferred tax assets and liabilities, including pre-Global Anti-Base Erosion (GloBE) arrangement deferred tax assets, effective for fiscal years of a qualifying MNE group that begin on or after December 31, 2023
- Transitional rules for constituent entities' pre-GloBE transactions in fiscal years before their GloBE transition year, effective for fiscal years of a qualifying MNE group that begin on or after December 31, 2023.

Note that the proposed legislation also includes changes to the *Income Tax Act* regarding foreign accrual tax (FAT), foreign tax credits, and foreign affiliate (FA) surplus accounts regarding Domestic Minimum Top-Up Tax (DMTT) regimes in foreign jurisdictions.

KPMG observation

Notably, the proposed legislation delays the introduction of the UTPR framework by one year to apply to qualifying MNEs' fiscal years that begin on or after December 31, 2025 (previously, the UTPR in the August 12, 2024 draft legislation was proposed to apply for years that begin on or after December 31, 2024). The UTPR framework which acts as a backstop to the Income Inclusion Rule (IIR) under the Pillar Two rules, subjects Canadian constituent entities of certain MNE groups to additional tax, in order to collect residual top-up tax arising for low-taxed profits of other constituent entities that are not already subject to an IIR or Qualified Domestic Minimum Top-Up Tax (QDMTT).

The proposed legislation also introduces a new "side-by-side" safe harbour that may be available for fiscal years beginning on or after January 1, 2026. This transitional safe harbour appears to reflect the OECD/G20 Inclusive Framework's agreement on a "side-by-side" package from earlier in 2026 to preserve global progress to implement the Pillar Two rules, while also addressing U.S. concerns about these rules. For more details on the "side-by-side" package, see *TaxNewsFlash-Canada* 2026-01, "[Global Minimum Tax — OECD Agrees on Side-by-Side System](#)".

Administrative tax changes

CRA audit powers

The proposed legislation provides the CRA with enhanced audit powers to more effectively obtain information and documents from taxpayers and third parties, and to impose new non-compliance penalties. These changes were previously announced in the 2024 federal budget, and included in draft legislation released on August 12, 2024 and August 15, 2025.

The proposed legislation introduces a new penalty that may apply where a judge issues a compliance order. This penalty is equal to 10% of tax payable by the taxpayer for each taxation year of the taxpayer to which the order relates, unless the tax payable is less than \$50,000 for each taxation year covered by the compliance order, or the taxpayer reasonably believed that the required information was protected from disclosure by solicitor-client privilege. The proposed legislation also provides that if the CRA determines that the compliance order penalty is disproportionate or unfair, it must waive or cancel all or part of the penalty (and any related interest) that it considers appropriate. In addition, the proposed legislation provides that taxpayers cannot rely on the taxpayer relief provisions to request that the CRA waive or cancel penalties and interest related to this compliance order penalty.

Moreover, the proposed legislation allows the CRA to issue a “notice of non-compliance”, which carries a penalty of \$50 for each day that the notice is outstanding, to a maximum of \$25,000. The penalty for failing to comply with this new type of notice will not apply if the taxpayer reasonably believed that the required information was protected from disclosure by solicitor-client privilege. However, the proposed legislation also includes a new “unrelated person requirement” exception that generally provides that the CRA cannot issue a notice of non-compliance to a third party for an underlying requirement or notice requiring information from the third party about unrelated or unnamed persons, absent a compliance order.

KPMG observation

The proposed legislation does not include the previously announced measure to allow the CRA to require that answers to questions, information or documents be provided orally under oath or affirmation, or by affidavit.

Notably, the proposed legislation clarifies that the compliance order penalty is a fixed 10% of tax payable for each taxation year covered by a compliance order. Although the fixed 10% penalty is consistent with the wording from the 2024 federal budget and August 12, 2024 draft legislation, it differs from the August 15, 2025 draft legislation, in which the penalty was described as “up to” 10% of tax per tax year.

Note that the unrelated person requirement exception for a notice of non-compliance was not included in earlier draft legislation. The proposed legislation indicates that this change restricts the CRA’s ability to issue a notice of non-compliance to a third party for

an underlying requirement or notice (i.e., “unrelated person requirement”) in situations where the underlying unrelated person requirement either:

- Requires the third party to provide information or documents relating to unrelated persons, or
- Is an unnamed persons requirement for information.

In either case, the restriction applies only if a compliance order has not been made in respect of the unrelated person requirement.

Personal tax changes

The proposed legislation includes many personal tax measures in the 2025 federal budget, including measures related to:

- Post-emigration relief — Allow taxpayers that sell property post-emigration to carry back a loss and claim a foreign tax credit after the normal reassessment period
- Tax On Split Income (TOSI) – Definition of “excluded amount”
- Qualified investments for registered plans
- Employer contributions to group sickness and accident insurance plans
- Canada Carbon Rebate (CCR) payments – Winding down
- Automatic federal benefits for lower-income individuals.

Other tax changes

The proposed legislation also includes the following tax measures:

- Changes to remove bankrupt corporations, trusts and partnerships from the exception to the debt forgiveness rules
- New framework for registered foreign charities
- Crypto-asset reporting framework.

KPMG observations

Budget Bill #2 does not contain certain notable tax measures from the 2025 federal budget, including elective exemptions for EIFEL, the second package of the Hybrid Mismatch rules and reporting for non-profit organizations.

We can help

Your KPMG adviser can help you assess the effect of these new developments. For more details, contact your KPMG adviser.

kpmg.com/ca



[Contact Us](#) | [KPMG in Canada Privacy Policy](#) | [Legal](#)

Information is current to May 7, 2026. The information contained in this *TaxNewsFlash-Canada* is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.

© 2026 KPMG LLP, an Ontario limited liability partnership and a member firm of the KPMG global organization of independent member firms affiliated with KPMG International Limited, a private English company limited by guarantee. All rights reserved.