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Tax Alert – Canada

Finance releases draft income tax technical amendments

EY Tax Alerts cover significant tax news, developments and changes in legislation that affect Canadian businesses. They act as technical summaries to keep you on top of the latest tax issues. For more information, please contact your EY advisor or EY Law advisor.

On 9 August 2022, the Department of Finance released for public comment draft legislative proposals (and accompanying explanatory notes) relating to long-awaited technical amendments to the *Income Tax Act* (the Act) and *Income Tax Regulations*. Many of the technical amendments included in this release respond to issues raised by taxpayers and their representatives, or are part of an ongoing effort by the Department of Finance to improve the certainty and integrity of the tax system.

These amendments include various minor technical amendments, as well as a number of more significant technical amendments and new rules. In total, there are more than 130 new or amended provisions included in this technical amendments package. The following is a summary of some of the more significant proposed amendments.

Interested parties are invited to submit comments on the legislative proposals by 30 September 2022.

Building a better working world

Business income tax measures

- **Corporate tax-attribute trading** – Amendments to clarify that the definitions of "attribute trading restriction" and "specified provision" in subsection 256.1(1) also refer to a section 251.2 loss restriction event. In addition, the anti-avoidance rule in subsection 256.1(6) is amended to clarify that the provision applies (to deem the tax attribute restrictions to apply as if an acquisition of control occurred) when one of the main reasons of any transaction or event or any transaction or event in the series of transactions or events is so that a specified provision does not apply to one or more corporations. These amendments are deemed to be effective as of 9 August 2022.

- **Shareholder debt exception** – Amendment to provide that money lending businesses whose outstanding loans to arm's length borrowers are less than 90% of their total outstanding loans (e.g., captive money lenders within a corporate group) are no longer eligible for the ordinary money lending business exception to the rules requiring shareholder debt to be included in income. Related interpretive rules for applying the arm's length test are also provided to address situations where the borrower or the lender, or both, is a partnership (including multi-tiered partnership situations). These amendments apply to loans made after 2022, as well as to any portion of a loan made before 2023 that remains outstanding on 1 January 2023, as if that portion were a separate loan made on 1 January 2023.

- **Partnerships ceasing to exist** – Amendments to the tax-deferred rollover rules in subsections 98(3) and 98(5) for the distribution of property to members of a Canadian partnership that ceases to exist. In general terms, the amendments impose a new limit on the maximum bump-up that a member may designate in respect of property received from the dissolving partnership that is a membership interest in another partnership, by ensuring that the bump-up does not include unrealized gains and recapture income in respect of property that would be ineligible for a bump-up if the property were held directly by the partnership (e.g., depreciable property). These amendments respond to transactions involving tiered partnership structures that were being undertaken by some taxpayers to obtain a bump-up in the cost of an undivided interest in a capital property (e.g., the taxpayer's undivided interest in a partnership in which the dissolving partnership has a direct interest) by an amount in respect of property that would be ineligible for a bump-up if the property had been held directly by the dissolving partnership. These amendments are effective in respect of partnerships that cease to exist on or after 9 August 2022.

- **Eligible capital property – payments received after 2016** – Introduction of a new transitional rule to address situations where eligible capital property was disposed of prior to the announcement of the repeal of the eligible capital property regime (i.e., before 22 March 2016) and a portion of the proceeds of disposition did not become receivable by the seller until after 2016, but before 2024, under a condition of the supporting agreement which, at the end of 2016, the parties to the agreement were unsure would be met. If certain conditions are met, this new rule allows taxpayers to elect to treat the amount that would be a taxable capital gain (as a result of the new rules that came into effect on 1 January 2017) as business income from the disposition of eligible capital property and not as a taxable capital gain (except for capital dividend

account purposes). In effect, this election provides the taxpayer with generally the same treatment it would have received if such payments had been received prior to 2017. This new rule responds to a 29 July 2019 comfort letter issued by the Department of Finance and is deemed to be effective retroactively on 1 January 2017.

- **Deduction for mining taxes** – Amendments to allow for the deduction, under paragraph 20(1)(v), of eligible provincial or territorial mining taxes that were paid by a taxpayer in a taxation year in respect of a taxpayer's income from mining operations (or non-Crown royalty income included in the taxpayer's income) in a previous taxation year, where that previous year is statute-barred and a valid waiver in respect of the normal reassessment period for the previous taxation year had not been filed by the taxpayer. A further amendment also allows for a deduction of interest paid in the year to a province or territory on any deductible eligible mining taxes on income from mining operations or on non-Crown royalty income. The amendments respond to a 3 September 2019 comfort letter issued by the Department of Finance and are effective for taxation years ending after 2007. An assessment for any taxation year ending before 9 August 2022 that would otherwise be precluded because of the year being statute-barred or because no relevant waiver has been filed in respect of it will only be made to take into account the above-mentioned amendments if the taxpayer elects in writing on or before the day that is six months after the implementing legislation receives Royal Assent.

- **Reclassification of Canadian development expenses for preceding years** – Amendments to ensure that certain oil or gas discovery well expenses incurred after 2018 (including expenses incurred in 2019 that were deemed to have been incurred in 2018 because of the "look-back" rule) can no longer be reclassified as Canadian exploration expenses (CEE), and expenses that were incurred before 2021 continue to be eligible to be reclassified as CEE if the expenses relate to a discovery well that was the subject of a written commitment to incur those expenses that was entered into by the taxpayer before 22 March 2017 (including a commitment to a government under the terms of a license or permit).

- **Definition of "term preferred share"** – Amendments to the definition of "term preferred share" in subsection 248(1) to include references to paragraph 258(3)(a) with the intent to allow the specific anti-avoidance rules contained in paragraphs (i.1) and (j) of the definition to apply equally to shares that were issued to avoid (or limit) the application of the dividend denial rule under paragraph 258(3)(a) for dividends received by a specified financial institution resident in Canada from foreign affiliates. This amendment applies to amounts received on or after 9 August 2022.

International income tax measures

- **Foreign affiliates** – Various amendments to the foreign affiliate rules, including:

  - **Foreign affiliate share-for-share exchange exception** – Amendments that expand the scope of the subsection 85.1(4) anti-avoidance rule, which provides exceptions to the foreign affiliate rollover rules on a transfer of shares of a foreign affiliate to another foreign affiliate, and that are meant to address a range of unintended tax deferral circumstances. In this regard, the amendments include the expansion of the relevant subsequent acquirers to include non-arm's length nonresidents and

partnerships with arm's length members or non-arm's length nonresident members; the narrowing of the carve-out for foreign affiliate subsequent acquirers such that only foreign affiliates that are controlled foreign affiliates for the purposes of section 17 are excepted from the anti-avoidance rule; the express capture of subsequent dispositions of one or more properties substituted for the shares of the first affiliate, or that derive any of their fair market value from the first affiliate shares or any substituted property; and the introduction of a new provision to ensure that a rollover is not available if the property that is disposed of is excluded property of a foreign affiliate of the taxpayer at the time of the subsequent disposition. Other amendments also provide interpretative rules essentially for applying the arm's length test where the taxpayer or the acquirer, or both, is a partnership. These amendments apply to dispositions that occur on or after 9 August 2022.

- **Foreign merger anti-avoidance** – Amendments to expand the scope of the foreign merger anti-avoidance rule in subsection 87(8.3), which is intended to prevent the use of certain corporate structures to circumvent the anti-avoidance rule relating to foreign affiliate rollovers on transfers of shares of a foreign affiliate to another foreign affiliate in subsection 85.1(4). These amendments, which parallel the amendments made to the foreign affiliate share-for-share exchange exception above, further restrict the parties to which a disposition of shares of the new foreign corporation may be made without triggering subsection 87(8.3) and expand the categories of property the disposal of which may trigger the application of the provision. Similar to the amendments made to the foreign affiliate share-for-share exchange exception above, other amendments also provide interpretative rules for applying the arm's length test in certain situations involving partnerships. These amendments apply to dispositions that occur on or after 9 August 2022.

- **Foreign affiliate suppression election** – Amendment to limit the application of subsection 88(3.3), which allows a taxpayer to elect to reduce the amount for which a distributed property is considered disposed of under paragraph 88(3)(a) by a disposing foreign affiliate on a qualifying liquidation and dissolution of the disposing foreign affiliate, to distributed property of the disposing foreign affiliate that is shares of another foreign affiliate. This amendment is intended to align the rule more clearly with its original policy intent by ensuring that any gain that could otherwise be realized on the disposition of the disposing foreign affiliate's shares cannot be eliminated or deferred when a deferral would be inappropriate. This amendment applies to dispositions that occur on or after 9 August 2022.

- **Definition of eligible controlled foreign affiliate** – Amendments to the definition of "eligible controlled foreign affiliate", which is relevant to the "relevant cost base" definition used in the context of foreign affiliate reorganizations, to remove the circularity that would otherwise arise in situations where the participating percentage (used in the "eligible controlled foreign affiliate" definition) of shares owned by a taxpayer in respect of a foreign affiliate could depend on whether a valid "relevant cost base" election has been made (the ability to elect a higher cost base of a foreign affiliate property is based on whether the foreign affiliate is an eligible controlled foreign affiliate). The amendments also ensure that paragraph (b) of the definition "eligible controlled foreign affiliate" can be satisfied even if the controlled foreign affiliate's foreign accrual property income (FAPI) for the year is not more than $5,000.

While these amendments apply to determinations made after 19 August 2011, a taxpayer may elect, in respect of all of its foreign affiliates, an alternate "read-as" version of paragraph (b) of the definition for determinations made before 9 August 2022.

- **Upstream loans from foreign affiliates** – Amendments to the exception to the upstream loan rules for loans made in the ordinary course of an ordinary money lending business to exclude a business if, at any time during which an upstream loan is outstanding, less than 90% of the total outstanding amount of the loans of the business is owing by borrowers that deal at arm's length with the business (e.g., captive money lenders within a corporate group). Related interpretative rules for applying the arm's length test are also provided to address situations where the borrower or the creditor, or both, is a partnership. These amendments, which parallel the amendments made to the shareholder debt exception described above, apply to loans made after 2022, as well as to any portion of a loan made before 2023 that remains outstanding on 1 January 2023, as if that portion were a separate loan made on 1 January 2023.

- **Base erosion rule for provision of services** – Amendments to the base erosion rule in subparagraph 95(2)(b)(i), including the introduction of a new exception (provided for in new subsection 95(3.03)). The base erosion rule in subparagraph 95(2)(b)(i) deems the provision of services (or an undertaking to provide services) by a payee foreign affiliate of a taxpayer to be a separate business of the foreign affiliate other than an active business and deems income from that business (or that pertains or is incident to it) to be income from a business other than an active business and thus FAPI, provided certain conditions in clauses 95(2)(b)(i)(A) or (B) are met. The amendments ensure that, where the conditions in clause 95(2)(b)(i)(B) are met (i.e., the amount paid or payable for the services (or the undertaking) is deductible (or can reasonably be considered to relate to a deductible amount) in computing the FAPI of another foreign affiliate (the payer foreign affiliate) for a taxation year), the services income is included in the payee affiliate's FAPI only in proportion to the aggregate interests, of taxpayers of which the payer foreign affiliate is a foreign affiliate, in the payer foreign affiliate's income. These amendments, which respond to a 12 June 2017 comfort letter issued by the Department of Finance, apply in respect of taxation years of a foreign affiliate of a taxpayer that begin after 2015.

  The new subsection 95(3.03) exception from the application of subparagraph 95(2)(b)(i) applies, under conditions similar to those in clause 95(2)(a)(ii)(D) for the recharacterization of certain income as active business income, in circumstances where the services (or the undertaking) are provided for a taxation year by a qualifying interest foreign affiliate or a controlled foreign affiliate of a taxpayer to another foreign affiliate of the taxpayer in which the taxpayer has a qualifying interest. Only the specific provision of services (or the undertaking) that give rise to the services income for the year is excepted from subparagraph 95(2)(b)(i). Consequential amendments are also made to the descriptions of variables A and D in the definition of FAPI in subsection 95(1) and to Regulation 5907(2.7) for the computation of earnings or loss from an active business, to ensure (by not deducting the amounts paid or payable by the payer foreign affiliate in its FAPI and deducting them in its earnings (or loss) from an active business) symmetrical treatment

between the payer and payee foreign affiliates in cases where new subsection 95(3.03) applies to the inter-affiliate payment for the services. These amendments, which respond to a 23 December 2016 comfort letter issued by the Department of Finance, apply in respect of taxation years of a foreign affiliate of a taxpayer that end after 2016.

- **Foreign affiliates – packaging of assets for sale** – Amendment to Regulation 5907(2.01), which overrides certain tax rollover exceptions in certain circumstances (such as where transactions that would otherwise be structured as direct asset sales are structured or "packaged" as share sales for foreign commercial reasons), to clarify that the shares received by the transferor as consideration for the packaged assets must be shares of the transferee. In addition, the conditions for the application of Regulation 5907(2.01) are relaxed to permit the consideration received by the transferor to include an assumption of debts that arise in the ordinary course of the business to which the transferred assets relate. These amendments, which clarify an issue raised in CRA document 2014-0550451E5, apply to dispositions that occur on or after 9 August 2022.

- **Foreign affiliate dumping rules – paid-up capital reinstatement** – Amendments to clarify that a recipient corporation's receipt of property due to any of the enumerated transactions or events (in the description of A in subparagraph 212.3(9)(b)(ii)) does not lead to a reinstatement of paid-up capital (PUC) to the extent the recipient corporation received the property in two scenarios: (i) as a result of an investment (by a recipient corporation) that is eligible for the "more closely connected business" exception in subsection 212.3(16) or one of the corporate reorganization exceptions in subsection 212.3(18), or (ii) as proceeds from a disposition of property to a corporation resident in Canada for which the acquisition is an investment to which one of those exceptions applies (or to a partnership of which such a corporation is a member). The amendments also extend the above-mentioned restrictions to dividends or returns of capital on foreign affiliate shares, or in respect of payments of interest on foreign affiliate debt, to ensure that for all enumerated transactions and events the PUC reinstatement is subject to the same restrictions. These amendments apply to transactions and events that occur on or after 9 August 2022.

- **FAPI and tracking interest rules** – Amendment to the rules in section 94.2, which generally deem certain nonresident trusts of which a taxpayer is a beneficiary (or in which the taxpayer has an interest through a controlled foreign affiliate) to be nonresident corporations controlled by the taxpayer (thereby resulting in the potential attribution of the trust's FAPI to the taxpayer), to ensure that the tracking interest rules in subsection 95(11) (as adapted in the amendment) apply in circumstances where the trust takes the form of an "umbrella trust" (i.e., a single trust consisting of several sub-funds, with a separate class of participating interests typically being issued for each sub-fund). The amendment, which introduces new subsection 94.2(5) as a "read-as" rule for the purpose of applying the tracking interest rules in subsection 95(11), is intended to ensure that in these circumstances, the portion of the trust's FAPI that is attributable to the taxpayer (as well as any related deductions and filing requirements) is determined based on the income, gains and losses realized in the particular sub-fund in which the taxpayer is invested, and not on the basis of the income, gains and losses of other sub-funds of the

umbrella trust. These amendments apply to taxation years of trusts beginning after 26 February 2018 (i.e., in line with when the tracking interest rules in subsections 95(8) to (12) generally came into effect).

It should be noted that the Department of Finance indicated in the accompanying explanatory notes that the exception recommended in a 25 March 2019 comfort letter to the tracking interest rules, in respect of nonresident umbrella corporations, will not apply (if implemented) to the above-mentioned nonresident umbrella trusts in respect of which the rules in section 94.2 apply — the comfort letter recommends an exception where it is not reasonable to expect that one of the reasons for a taxpayer acquiring or holding a tracking interest in a foreign corporation (or for investing through an umbrella corporation) is to avoid a FAPI income inclusion.

- **Specified trusts** – Expansion of the rules in section 93.3, which deem certain trusts resident in Australia to be a nonresident corporation essentially for the purpose of determining the Canadian tax results of a taxpayer in respect of the shares of a foreign affiliate (as well as for applying the foreign affiliate dumping rules where relevant), to apply to certain trusts resident in India, effective as of 1 January 2022. As a result, a specified trust under this provision is treated as a foreign affiliate of a taxpayer, and distributions from the trust to another foreign affiliate of the taxpayer are treated as inter-affiliate dividends.

- **Functional currency tax reporting** – Various amendments to the functional currency tax reporting rules, including:

  - **Qualifying currency** – Amendment to include the Japanese yen as a qualifying currency. This amendment is in response to a 29 July 2019 comfort letter issued by the Department of Finance and is effective for taxation years that begin after 2019.

  - **Functional currency anti-avoidance rule** – Amendment to expand the anti-avoidance rule in subsection 261(18) to include situations where the transferee reports in a functional currency at the time of the property transfer and the transferor has a different tax reporting currency (such as a situation involving the amalgamation of two Canadian dollar tax reporters to form a new corporation that is a functional currency tax reporter, with the purpose of retroactively restating some tax results in the elected functional currency). This amendment applies to transfers of property that occur on or after 9 August 2022.

  - **Functional currency stop-loss rule** – Amendment to the conditions in subsection 261(20) for the application of the stop-loss rule in subsection 261(21) to ensure that corporations that enter into specified transactions with a related individual will also be subject to the stop-loss rule. This amendment applies to "accrual periods" (as defined in subsection 261(20)) that begin on or after 9 August 2022. The intention, as stated by the Department of Finance, is for the amended rule to apply only to loans and other transactions that are entered into on or after 9 August 2022.

- **Foreign property reporting definitions** – Amendments to the definitions of "specified Canadian entity" and "specified foreign property" for purposes of the foreign property reporting requirements under section 233.3 — in general terms, specified Canadian entities must file an information return with respect to their specified foreign property if the total cost amount of such property exceeds $100,000. The definition of specified Canadian entity is amended to expand the exception for partnerships such that a partnership will be a specified Canadian entity only if less than 90% of the partnership's income is allocable to members that are nonresident persons or are listed in any of subparagraphs (a)(i) to (viii) of that definition (i.e., generally tax-exempt or flow-through entities). The definition of specified foreign property is amended to exclude certain superannuation and pension plans that are resident in Australia or New Zealand for income tax purposes (and are subject to a reduced rate of income tax in the respective country) so that such plans are on the same footing as most other foreign pension plans for the purposes of the foreign property reporting requirements under section 233.3. These amendments apply to taxation years and fiscal periods that end after 9 August 2022.

Personal income tax measures and measures relating to trusts

- **Automobile standby charge and operating expense benefit** – Amendments to maintain consistency with the general taxable benefit rules in paragraph 6(1)(a). Accordingly, the amendments ensure that an automobile standby charge and operating expense benefit are included in an employee's income when a person who does not deal at arm's length with the employee receives a benefit (previously, the person had to be related to the employee, so the amendments broaden the income inclusion rules to other non-arm's length relationships). Additional amendments clarify that whenever an automobile is made available "in respect of, in the course of, or because of a taxpayer's office or employment", a standby charge is included in an employee's income regardless of whether the employer (or a person related to the employer) makes the benefit available or if an employee-employer relationship exists at the time. Similarly, in the context of the operating expense benefit, the operating expenses need only to be paid or payable by the person that made the automobile available, instead of by the employer (or a person related to the employer). These amendments apply to taxation years that begin after 2022.

- **Home buyers' plan** – Amendments to clarify that the special rule in paragraph 146.01(2)(b), which deems an individual to have acquired a condominium unit on the day the individual is entitled to immediate vacant possession of it and which is intended to provide relief if an individual is able to occupy a unit but not able to acquire it prior to the completion date, does not apply to restrict the 30-day withdrawal requirements or relax the residency requirements under the definitions of "regular eligible amount" and "supplemental eligible amount" in subsection 146.01(1), effective as of 9 August 2022. As a result of these amendments, the date an individual actually acquires a condominium unit will apply for purposes of determining the latest date at which a home buyers' plan (HBP) withdrawal may be made from an RRSP. This amendment appears to address the inequity that was pointed out (in *obiter dicta*) by the Tax Court of Canada in *Chitalia v. The Queen*, 2017 TCC 227. In addition, an individual will be required to be resident in Canada until such time as the condominium unit is actually acquired.

- **Principal residence of a personal trust** – Amendments to the definition of a principal residence to add a fourth category of trusts that are eligible to designate a property as a principal residence. In general terms, the amendments will allow an *inter vivos* trust established for the benefit of an individual eligible for the disability tax credit to qualify for the principal residence exemption, subject to certain conditions being met. This amendment responds to a 4 September 2019 comfort letter issued by the Department of Finance and is effective for taxation years beginning after 2016.

- **Employee life and health trusts** – Amendments to clarify that the condition in paragraph 144.1(2)(f) for a trust to qualify as an employee life and health trust (ELHT), with respect to the rights of key employees who are beneficiaries of the trust, applies only where the trust meets the beneficiary condition set out in subparagraph 144.1(2)(e)(i) to qualify as an ELHT and does not apply where a trust meets the alternative condition set out in subparagraph 144.1(2)(e)(ii) that provides a benefit limit for key employees. These amendments clarify an issue raised in CRA document 2022-0928801C6 and are effective as of 27 February 2018 (the date subparagraph 144.1(2)(e)(ii) came into force). In addition, an amendment is made to require deductions at source to be withheld for any amounts paid from an ELHT that are included in the recipient's income under paragraph 56(1)(z.2), effective as of 9 August 2022.

- **Pooled registered pension plans** – Various changes including amendments to permit a qualifying survivor of a deceased pooled registered pension plan (PRPP) member to surrender benefits to the extent permitted under PRPP legislation or similar provincial law, and to extend joint and several liability rules in respect of benefits paid out of an RRSP to benefits paid out of a PRPP, effective as of 9 August 2022. Additional amendments clarify the requirement for PRPP administrators to file an annual information return (i.e., contribution receipts) in respect of each member account under the plan for which contributions were made by the member's employer in the taxation year of the member that ends in the contribution year and by the member in the contribution year, effective for contribution years and taxation years ending after 9 August 2022. Further amendments clarify that these annual contribution receipt returns must be electronically filed and are subject to late filing penalties under subsection 162(7.01), effective as of 1 January 2022.

- **Registered disability savings plans** – Amendment that prohibits a registered disability savings plan (RDSP) trust from deducting income payable to a beneficiary in the year, when computing the trust's tax on income earned from carrying on a business or in respect of a non-qualified investment. This amendment and other terminology-related amendments are effective as of 9 August 2022.

- **Registered retirement income funds** – Changes that extend the requirement for the carrier of a registered retirement income fund (RRIF) to retain sufficient property to ensure that the minimum amount for the year is paid to the RRIF annuitant if the carrier transfers all or part of the property held in connection with the RRIF to another RRIF or to a money purchase provision of a registered pension plan (RPP), to similar transfers of RRIF property to an account under a PRPP, a money purchase provision of a specified pension plan (i.e., the Saskatchewan Pension Plan), or a licensed annuities provider to acquire an advanced life deferred annuity, effective as of 9 August 2022.

- **Registered pension plans** – Various amendments to the RPP rules, including:
  - **Assignment of rights** – Amendment to allow for the surrender (under an RPP) of retirement benefits payable to a dependant of a member after the member's death (i.e., survivor benefits), to the extent permitted under the *Pension Benefits Standards Act, 1985* or a similar law of a province, effective as of 9 August 2022. For example, it is common for provincial pension standards legislation to permit a surviving spouse to relinquish an entitlement to survivor benefits so that the children of the deceased member may become entitled to the benefits.
  - **Eligible period of reduced pay** – Amendment to reduce the number of months that an employee must be employed to qualify for an eligible period of reduced pay under the RPP rules, from 36 months to three months, effective as of 1 January 2022.
  - **Permissible benefits** – Amendment to permit certain retirement benefits to be paid under a defined benefit provision of an RPP where the benefits replace retirement benefits that otherwise would have been payable to an RPP member or to the surviving spouse or common-law partner of the member and the recipient has a significantly shortened life expectancy and certain other conditions are met, effective 30 September 2015. In addition, amendments are made with respect to lump-sum payments under a variable payment life annuity that are permissible benefits under a money purchase provision of an RPP, effective as of 1 January 2020.
  - **Prohibited investments** – Amendment to exclude from the list of prohibited investments for RPPs (other than for an RPP that is an individual pension plan) investments in shares of, an interest in, or a debt of a person or partnership operating at non-arm's length with a participating employer, if the principal activity of the employer is to manage the investments or provide investment advice to one or more RPPs, the federal or provincial government, or certain other entities. For example, under this exception, an RPP that deals with an investment management company that has employees that are members of the RPP will not be prohibited from investing in pooled funds or partnerships created by the investment management company. This amendment is deemed to come into force on 1 June 2017 and is made in response to a 12 June 2017 comfort letter issued by the Department of Finance.
- **Tax-free savings accounts** – Introduction of new subsection 146.2(4.1) to permit an indebtedness of a holder of a tax-free savings account (TFSA) deposit that is owed to the issuer of the TFSA or a person related to the issuer to be set off against the holder's interest in the TFSA, provided the right of offset and indebtedness are on arm's length terms and conditions and it is reasonable to conclude that none of the main purposes of the right of offset is to enable another person or partnership to benefit from the tax exemption provided in respect of a TFSA, effective as of 9 August 2022. In addition, an amendment is made to permit the late filing of an election to register an arrangement as a TFSA at "such later date as is acceptable" to the Minister of National Revenue (the minister), effective for 2009 and subsequent taxation years (i.e., retroactive to the coming into effect of the TFSA rules in the Act).

- **Undeducted RRSP premiums** – Amendments to the formula for determining the amount of an individual's undeducted RRSP premiums (used to calculate an individual's cumulative excess amount in respect of an RRSP for the purposes of the Part X.1 tax on over-contributions) to subtract from an individual's balance of undeducted RRSP premiums amounts that are not received in the year but are still included in the individual's income for the year under the HBP or lifelong learning plan (LLP) rules. Under these rules, there is an income inclusion for a taxpayer where insufficient RRSP contributions are designated as HBP or LLP repayments in a year. These amendments are effective for 2018 and later taxation years.

- **Tax on excess employees profit sharing plan amounts** – Amendments to Part XI.4 penalty tax on excess employees profit sharing plan (EPSP) amounts, which are essentially based on employer EPSP contributions that are allocated to a specified employee, to change the portion of the tax rate that approximates provincial tax on excess EPSP amounts of a nonresident specified employee, from 14% to the rounded-up percentage determined by multiplying the federal highest marginal personal income tax rate (currently 33%) by the rate used to determine the federal surtax on income not earned in a province or territory (currently 48%) — thus 16%, effective for 2022 and subsequent taxation years. This change is consequential to the introduction of the 33% federal marginal personal income tax rate in 2016 (previously 29%).

- **Taxes in respect of registered plans – definition of "advantage"** – Amendments to the definition of "advantage" to include two new exemptions from the Part XI.01 advantage tax rules. The first amendment exempts a loan or an indebtedness for which the conditions for a right of set-off against a TFSA deposit are met (this amendment is consequential to the introduction of new subsection 146.2(4.1) described above), effective as of 9 August 2022. The second amendment exempts a payment (not exceeding a reasonable amount) by a controlling individual of a registered plan to a person or partnership that provides investment advice or administration services described in paragraph 20(1)(bb) to registered plans (i.e., RDSP, RESP, RRIF, RRSP or TFSA), effective for 2018 and subsequent taxation years. The second amendment responds to a 26 August 2019 comfort letter issued by the Department of Finance and ensures that the payment of investment management fees (in relation to registered plan assets) by a registered plan holder, subscriber or annuitant using funds outside of the registered plan will not be treated as an advantage. New subsection 207.01(2) is also added to include section 83 dividends (i.e., capital dividends) in income for the purposes of section 207.01 in Part XI.01, notably in respect of the determination of income earned on non-qualified investments held by registered plans. This amendment applies to dividends received on or after 9 August 2022.

Other income tax measures

- **Nonresident withholding tax** – Amendments to focus the application of the Part XIII withholding tax, where the payee is a partnership, to amounts paid or credited by the partnership to a nonresident person, in respect of any portion of such an amount that is deductible in computing a partnership member's share of the partnership's income or loss, to the extent that the member's share is taxable under Part I of the Act (i.e., if the member is resident in Canada or, in the case of a nonresident member, if the member's share is included in the member's taxable income earned in Canada or is income taxable under Part I because of a section 216 election (i.e., certain Canadian-source rent or timber royalty income)). Related interpretative rules (e.g., to address tiered partnerships situations) have also been added, and related and consequential amendments have been made on the application of the Part XIII tax to authorized foreign banks. These amendments are intended to apply to amounts paid or credited no earlier than the date of a future release of draft legislative proposals following the current consultation period (as previously mentioned, comments can be submitted up to 30 September 2022). In addition, amendments extend the application of the Part XIII withholding tax, where the payee is a nonresident person, to situations where the nonresident makes a payment to a non-Canadian partnership and also address situations where the nonresident payer makes a section 216 election, applicable for amounts paid or credited after 2022. Consequential amendments have been made on the application of the Part XIII tax to authorized foreign banks, and for which the NR4 information return filing requirements have been extended for amounts paid or credited after 2022. As well, an amendment is made to ensure that Part XIII of the Act applies to amounts paid or credited to a nonresident that is in receipt of designated investment services by a Canadian service provider and is considered not to be carrying on business in Canada because of subsection 115.2(2). This amendment is effective as of 9 August 2022.

- **Charity registration revocation or suspension** – Amendments to change the requirement for a charity to file a return in respect of a revocation tax for a taxation year from when the charity is liable for the revocation tax to when the charity has had its registration revoked, applicable in respect of taxation years ending after 9 August 2022. As a result, a charity will not have to file a return in respect of the revocation tax where the minister has issued a notice of intention to revoke the charity's registration but subsequently abandons that intention. In addition, amendments are made to extend the application of certain administrative provisions to a notice issued by the minister to suspend a registered entity's tax-receipting privileges and to allow the minister to share publicly the effective date of any suspension of an entity's registration, effective as of 9 August 2022. A further amendment allows the minister to share whether or not a public information return has been filed by the filing deadline, effective for taxation years that end after 9 August 2022.

Learn more

For more information on the draft legislative proposals discussed in this Tax Alert, contact your EY or EY Law tax advisor.

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