

2023 Federal Budget: Where Are We Now?

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We previously provided our top four key takeaways for tax planning from Budget 2023 in our March 30, 2023 article “**2023 Federal Budget: Top 4 Changes for Tax Planning.**”

Fast-forward almost a year, and where are we now? Bill C-47, *An Act to implement certain provisions of the budget tabled in Parliament on March 28, 2023*, received royal assent on June 22, 2023, and Bill C-59, *An Act to implement certain provisions of the fall economic statement tabled in Parliament on November 21, 2023 and certain provisions of the budget tabled in Parliament on March 28, 2023*, is currently in reading in the House of Commons.



1. ALTERNATIVE MINIMUM TAX FOR HIGH-INCOME INDIVIDUALS

Status: Pending – has not been introduced to Parliament.

Last March, Budget 2023 proposed to amend the Alternative Minimum Tax (“AMT”) as follows:

1. Increasing the federal AMT rate from 15% to 20.5%;
2. Increasing the exemption amount for all individuals and certain trusts from \$40,000.00 to the threshold of the fourth federal tax bracket (approximately \$173,000.00 for the 2024 tax year); and
3. Broadening the AMT base by further limiting tax preferences as follows:
 - Increasing the general capital gains inclusion rate from 80% to 100%;
 - Applying a 50% rate to capital loss carry-forwards and allowable business investment losses;
 - Including 30% of the capital gains on donations of publicly listed securities;
 - Including 100% of the benefit associated with employee stock options;
 - Disallowing 50% of certain deductions; and
 - Allowing only 50% of most non-refundable tax credits to reduce the AMT.

In August 2023, draft legislative proposals to implement these changes were released; however, these draft legislative proposals were notably not included in Bill C-59. To date,

additional information regarding the amendments has not been released.

2. BILL C-208 - INTERGENERATIONAL BUSINESS TRANSFERS

Status: Pending – Bill C-59 is currently in reading in the House of Commons.

Last March, Budget 2023 proposed to amend the criteria proposed in private member Bill C-208 for *bona fide* intergenerational business transfers as follows:

1. An immediate intergenerational business transfer (three-year test) based on arm's-length sale terms; or
2. A gradual intergenerational business transfer (five-to-ten-year test) based on traditional estate freeze characteristics (an estate freeze typically involves a parent crystallizing the value of their common shares of a corporation into fixed-value preference shares to allow future growth to accrue to their children while the value of the parent's interest is gradually reduced by the corporation repurchasing the parent's preference shares).

In August 2023, draft legislative proposals to implement these changes were released, and on November 30, the first reading of Bill C-59 was completed, which included similar legislative proposals. If enacted without considerable changes, these amendments will apply to dispositions of shares that occur on or after January 1, 2024.

3. THE GENERAL ANTI-AVOIDANCE RULE

Status: Pending – Bill C-59 is currently in reading in the House of Commons.

Last March, Budget 2023 proposed to amend the General Anti-Avoidance Rule ("GAAR") as follows:

1. Preamble: A preamble would be added to clarify that the GAAR:
 - draws a line that while taxpayers are free to arrange their affairs so as to obtain tax benefits intended by Parliament, they cannot misuse or abuse the tax rules to obtain unintended benefits;
 - is intended to strike a balance between taxpayers' need for certainty in planning their affairs and the government's responsibility to protect taxpayers and the fairness of the tax system; and
 - is intended to apply regardless of whether or not the tax planning strategy used to obtain the tax benefit was foreseen.
2. Avoidance Transaction: The threshold for the avoidance transaction test in the GAAR would be reduced from a "primary purpose" test to a "one of the main purposes" test. This means that a transaction could be considered an avoidance transaction if the associated tax benefit of the transaction was one of the taxpayer's main purposes for undertaking or arranging the transaction.
3. Economic Substance: The proposed amendments provide that economic substance is to be considered at the "misuse or abuse" stage of the GAAR analysis and that a lack of economic

substance tends to indicate abusive tax avoidance; however, Budget 2023 states that a lack of economic substance will not always mean that a transaction is abusive whereas a significant lack of economic substance could factor into a finding of misuse or abuse.

4. **Penalty:** A penalty equal to 25% of the amount of the tax benefit would be introduced for transactions subject to the GAAR. The penalty will not apply until the year in which the tax attribute is applied to reduce the tax payable.
5. **Reassessment Period:** A three-year extension to the normal reassessment period would be provided for GAAR assessments.

As with intergenerational transfers, in August 2023, draft legislative proposals to implement these changes were released, and on November 30, the first reading of Bill C-59 was completed, which included similar legislative proposals. If enacted without considerable changes, the amendments will apply to transactions occurring on or after January 1, 2024, except for the preamble, which will become effective upon royal assent.

4. EMPLOYEE OWNERSHIP TRUSTS

Status: Pending – has not been introduced to Parliament.

Last March, Budget 2023 proposed new rules to facilitate the use of Employee Ownership Trusts (“EOTs”) to acquire and hold shares of a business, define qualifying conditions to be an EOT and propose changes to tax rules to facilitate the establishment of EOTs:

1. **Qualifying Conditions:** To be an EOT, the trust would need to be resident in Canada and satisfy certain conditions, including but not limited to the following:
 - the trust holds a controlling interest in the shares of one or more qualifying businesses (defined as a Canadian-controlled private corporation that meets certain conditions, including that all or substantially all of the fair market value of its assets is attributable to assets used in an active business carried on in Canada) for the benefit of the employee beneficiaries;
 - the trust makes distributions to employee beneficiaries and generally treats beneficiaries in a similar manner, except where it applies a distribution formula that considers an employee’s length of service, remuneration and hours worked;
 - the trustees are Canadian residents who are elected by the trust beneficiaries at least once every five years; and
 - the trust beneficiaries must consist exclusively of qualifying employees (defined as all individuals employed by a qualifying business and any other qualifying businesses it controls, with the exclusion of employees who are significant economic interest holders or who have not completed a reasonable probationary period of up to 12 months).
2. **Facilitating the Establishment of EOTs:** To better accommodate the establishment and use of EOTs, certain existing tax rules will be modified. Currently:
 - taxpayers are permitted to defer recognition of a capital gain until the year they receive proceeds, with a minimum of 20% of the gain brought into income each year. Budget 2023 proposes to extend this five-year capital gains reserve to a ten-year capital gains reserve for qualifying business transfers to an EOT;
 - taxpayers who receive a shareholder loan are generally required to include the loan amount in income in the year the loan is received, unless the loan is repaid within a year. Budget 2023

- proposes to extend the repayment period from one to 15 years for amounts loaned to the EOT from a qualifying business to purchase shares in a qualifying business transfer; and
- certain trusts are deemed to dispose of their capital property at 21-year intervals. Budget 2023 proposes to exempt EOTs from the 21-year rule.

In August 2023, draft legislative proposals to implement these changes were released, and on November 21, the Fall Economic Statement confirmed the government's intention to proceed with EOTs and additionally proposed an exemption from taxation for the first \$10 million in capital gains realized on the sale of a business to an EOT, subject to certain conditions. However, on November 30, the first reading of Bill C-59 was completed, which did not contain details regarding this \$10 million capital gains exemption. If enacted without considerable changes, the amendments establishing EOTs will apply as of January 1, 2024.

As the tax landscape continues to change following Budget 2023, we encourage you to contact **one of our TDS tax lawyers** to advise how you can navigate and take advantage of post-Budget 2023 tax planning.

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