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HARMONIZATION WITH CERTAIN FEDERAL TAX MEASURES AND CHANGES TO VARIOUS MEASURES OF A FISCAL NATURE

This information bulletin states the position of the Ministère des Finances on certain tax measures announced in the federal budget tabled on February 27, 2018.

It also states the position of the Ministère des Finances regarding other tax measures proposed by the federal government in recent months.

In addition, it amends tax legislation regarding certain measures applicable to formal demands for information and orders, and describes certain changes to the parameters of the Capital régional et coopératif Desjardins investment fund, both with regard to Québec tax legislation and its statute of incorporation.

Lastly, this information bulletin amends the Québec sales tax system for aboriginal taxation to take into account the implementation of new legislative provisions aiming at the legalization of the cannabis.

For information concerning the matters dealt with in this information bulletin, contact the Secteur du droit fiscal, de l'optimisation des revenus et des politiques locales et autochtones at 418 691-2236.

The English and French versions of this bulletin are available on the Ministère des Finances website at www.finances.gouv.qc.ca.

**HARMONIZATION WITH CERTAIN FEDERAL TAX MEASURES AND
CHANGES TO VARIOUS MEASURES OF A FISCAL NATURE**

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1. HARMONIZATION WITH CERTAIN TAX MEASURES ANNOUNCED IN THE FEDERAL BUDGET OF FEBRUARY 27, 2018

On February 27, 2018, the Minister of Finance of Canada presented the federal government's budget for 2018. At that time, he tabled, in the House of Commons, supplementary information describing in detail each of the tax measures proposed in the budget, along with notices of ways and means motions and draft amendments to amend federal tax legislation and regulations accordingly.¹

In the 2018-2019 Budget² and in *Information Bulletin 2018-3*,³ the Ministère des Finances du Québec announced its position regarding some of the measures announced when the federal budget of February 27, 2018 was presented. The Ministère des Finances also mentioned that it would announce at a later date its position on other fiscal measures. With the exception of its position concerning certain measures, which will be announced at a later date, Québec's position can be found herein.

Québec's tax legislation and regulations will be amended to incorporate certain income tax-related measures proposed in federal budget 2018. However, the changes to Québec's tax system will only be adopted following the assent given to any federal legislation or adoption of any federal regulation giving effect to the measures retained, which will take into account technical amendments that may be made prior to assent or adoption, as the case may be. More specifically, these changes will apply on the same dates as those retained for the purposes of the federal measures with which they harmonize.

□ Budget resolutions retained

The Québec tax legislation and regulations will therefore be amended⁴ to incorporate, with adaptations on the basis of their general principles, the budget resolutions concerning:

1. the addition of expenses incurred for an animal that is specially trained to the list of eligible expenses for the application of the medical expense tax credit (BR 5);⁵
2. the extension of the temporary measure to allow certain individuals to become the holder of a registered disability savings plan (BR 6);
3. the elimination of the requirement that universities outside Canada be prescribed in the *Income Tax Regulations* in order to be a qualified donee (BR 13 to BR 15);
4. the extension of the accelerated capital cost allowance for certain investments in equipment for the generation and conservation of clean energy (BR 21);

¹ Department of Finance Canada, *Tax Measures: Supplementary Information*, Budget 2018 Companion Paper, February 27, 2018.

² Ministère des Finances du Québec, *The Québec Economic Plan – Additional Information 2018-2019*, March 27, 2018, p. A.132.

³ Ministère des Finances du Québec, *Information Bulletin 2018-3*, May 28, 2018.

⁴ Some of the measures retained do not require any amendments to Québec's tax legislation or its regulations.

⁵ The references in parentheses correspond to the number of the budget resolutions (BRs) of the *Notice of Ways and Means Motion to Amend the Income Tax Act and Other Related Legislation* tabled in the House of Commons on February 27, 2018.

5. the at-risk rules for tiered partnerships (BR 26).

❑ Budget resolutions not retained

Certain budget resolutions were not retained because they are out of step with the characteristics of the Québec tax system, or because the Québec tax system is satisfactory or has no analogous provisions. These budget resolutions concern:

- the enhancement of the Canada Workers Benefit (BR 1 to BR 4);
- the deductibility of employee contributions to the enhanced portion of the Québec Pension Plan (BR 7);⁶
- retroactive eligibility of Foreign-Born status Indians for child benefits and the sharing of confidential information related to the Canada child benefit (BR 8 to BR 10);
- the recognition of municipalities as eligible donees for the application of the revocation tax for charities (BR 11 and BR 12);
- the extension of the mineral exploration tax credit for flow-through share investors (BR 16);
- the restrictions that apply to refunds of the refundable dividend tax on hand (RDTOH) and the addition of an RDTOH account (BR 19 and BR 20);
- the reassessment period with regard to requirements for information and compliance orders (BR 32 to BR 34).⁷

❑ Clarification regarding measures pertaining to health and welfare trusts

A health and welfare trust is a trust established by an employer for the purpose of granting certain health and welfare benefits to its employees. The tax treatment of such trusts is not explicitly set out in federal and Québec tax laws; it is based on administrative positions.

Furthermore, in 2010, rules concerning employee life and health trusts were added to federal tax legislation. These trusts also provide employees with health benefits. Notwithstanding the characteristics specific to the Québec tax system, Québec's tax legislation is harmonized with federal tax legislation on this point.

Federal Budget 2018 proposes that a single set of rules apply to health and welfare trusts and employee life and health trusts (BR 27). As a result, the Canada Revenue Agency (CRA) will not apply its administrative positions to health and welfare trusts established after February 27, 2018. The CRA will apply, until the end of 2020, its administrative positions to trusts established before February 28, 2018. It will then apply the usual tax rules for trusts to health and welfare trusts that have not converted or wound up.

⁶ Québec's position on employee contributions to the enhanced portion of the Québec Pension Plan was made at the time *Information Bulletin 2017-11* was published on November 21, 2017 (pp. 18-21).

⁷ The tax legislation will be amended to include a provision that provides for the suspension of the prescription period in certain circumstances. See measure 3 of this information bulletin: Measures concerning formal demands for information and orders.

In keeping with the announced restrictions to the application of administrative positions regarding health and welfare trusts under the federal tax system, Revenu Québec will not apply its administrative positions to health and welfare trusts established after February 27, 2018 and will apply, until the end of 2020, its administrative positions to trusts established before February 28, 2018. Thereafter, it will apply its usual tax rules for trusts to health and welfare trusts that have not converted or wound up.

□ Subsequent announcements

The Department of Finance Canada announced that it intends to improve the collection of beneficial ownership information with respect to trusts. It has therefore proposed to require that certain trusts provide additional information each year, obligate certain trusts to file returns in cases where such an obligation does not currently exist and add penalties which would be applicable if the trust fails to file a return. It is proposed that the new reporting requirements apply as of 2021. The Ministère des Finances du Québec will make known its position on the matter at a later date (BR 17).

This also applies to the lowering of the Canadian-controlled private corporation's business limit on the basis of passive investment income (BR 18).

In addition, under the proposed changes to the tax system applicable to health and welfare trusts, the Department of Finance Canada has stated that transitional legislative rules to facilitate the conversion of health and welfare trusts to employee life and health trusts and administrative guidance relating to the winding up of health and welfare trusts would be made public once stakeholders have been consulted. The Ministère des Finances du Québec will also make known its position on the matter at a later date.

2. HARMONIZATION WITH CERTAIN MEASURES IN THE ACT IMPLEMENTING THE 2018 BUDGET

On June 21, 2018, Bill C-74, the *Act to implement certain provisions of the budget tabled in Parliament on February 27, 2018 and other measures* (hereinafter, the "Budget Implementation Act") received Royal Assent. Among other things, the Budget Implementation Act aims to implement certain tax measures proposed in the federal budget of February 27, 2018⁸ and in News Release 2017-124.⁹

The Ministère des Finances has already made known Québec's position on the majority of the tax measures in the Budget Implementation Act. However, Part 1 of the Act also implements other income tax measures. Those measures concern:

- the inclusion, in the computation of income, of amounts received as an income replacement benefit payable under the *Veterans Well-being Act*¹⁰ (sections 2 and 3¹¹);

⁸ See note 1.

⁹ Department of Finance Canada, News Release 2017-124, "Government Simplifies Measures to Restrict Income Sprinkling," December 13, 2017.

¹⁰ S.C. 2005, c. 21.

¹¹ The references in parentheses correspond to the number of the section in the Budget Implementation Act.

- the non-inclusion, in the computation of income, of payments received as pain and suffering compensation payable under the *Veterans Well-being Act* (subsections 5(1), (2), (4) and (5));
- the non-inclusion, in the computation of income, of amounts received under the Memorial Grant Program for First Responders established under the authority of the *Department of Public Safety and Emergency Preparedness Act*¹² (subsections 5(3) and (6));
- eligibility, for the purposes of the pension income splitting and the pension credit, of income replacement benefit payable to Canadian Forces veterans who have reached age 65 in accordance with the *Veterans Well-being Act* (section 4 and subsections 11(2) and (5)).

Given that, in general, the Québec tax system is harmonized with the federal tax system regarding the tax treatment applicable to various sources of income, the Québec tax legislation will be amended to incorporate the measures, with adaptations on the basis of its general principles.

More specifically, these amendments will apply on the same dates as those retained for the purposes of the federal measure with which they harmonize.

3. MEASURES CONCERNING FORMAL DEMANDS FOR INFORMATION AND ORDERS

□ Changes to the November 10, 2017 announcement

On November 10, 2017,¹³ the Ministère des Finances du Québec announced, for the purpose of bolstering the fight against aggressive tax planning, the suspension of the prescription period for issuing a reassessment where the reassessment is issued in respect of a taxpayer that is the subject of a formal demand concerning unnamed persons and the assessment involves the application of the general anti-avoidance rule (hereinafter, “FD-UP”).

Given the court delays for challenges, a clarification will be made to the tax legislation to suspend the prescription period for issuing a reassessment involving taxpayers who are the object of an FD-UP as of the day on which the demand is filed. The suspension will be lifted as soon as the demand has been settled definitively and the taxpayer, if applicable, has complied with the demand.

This amendment will apply to any demand filed after the day of publication of this information bulletin.

¹² S.C. 2005, c. 10.

¹³ Ministère des Finances du Québec, *Information Bulletin 2017-10*, November 10, 2017, p. 2.

□ **Additional provision providing for the suspension of the prescription period**

The *Tax Administration Act*¹⁴ grants Revenu Québec general powers concerning the collection of information that allows it to request information and examine documents in the course of an audit. Among the information collection tools at Revenu Québec's disposal are formal demands made directly by Revenu Québec and orders issued by the Court.

The tax legislation will be amended to include a provision which provides for the suspension of the prescription period for issuing a new assessment as of the earlier of either the day on which the formal demand for information is notified by registered mail or personal service, or the day a demand for an order is filed, regardless of whether the information is held outside Canada or not. However, given the previous change, this change will not affect an FD-UP. The suspension will end as soon as the taxpayer complies with the demand or order or, where it is contested, as soon as the matter has been settled definitively and the taxpayer, if applicable, has complied with the demand or order.

This change will apply to any demand or order made after the day of publication of this information bulletin.

4. CHANGES TO VARIOUS PARAMETERS OF CAPITAL RÉGIONAL ET COOPÉRATIF DESJARDINS

Capital régional et coopératif Desjardins was constituted on July 1, 2001 and is governed by the *Act constituting Capital régional et coopératif Desjardins*.¹⁵ Its mission is to raise venture capital for the benefit of Québec's resource regions and the cooperative sector.

In this regard, a tax benefit in the form of a non-refundable tax credit is granted to an individual who acquired, as first purchaser, shares of the capital stock of Capital régional et coopératif Desjardins. The shares are redeemable at the request of the investor who acquired the shares at least seven years prior to redemption.

When the 2018-2019 budget was tabled, it was announced that the capital stock of Capital régional et coopératif Desjardins would be changed so that investors who have held shares of the capital stock for at least seven years can exchange them for shares of a new class of capital stock of Capital régional et coopératif Desjardins that will also be redeemable after a new, mandatory seven-year retention period.¹⁶

Investors that exchange their shares will benefit from a non-refundable tax credit corresponding to 10% of the value of the shares or fractions of shares exchanged, up to a maximum of \$15 000, namely a maximum non-refundable tax credit of \$1 500 annually.

¹⁴ CQLR, chapter A-6.002

¹⁵ CQLR, chapter C-6.1.

¹⁶ See note 2, pp. A.105-A.109.

The purpose of the change to the capital stock of Capital régional et coopératif Desjardins is to offset the risk of a liquidity shortage in the short or medium term in the event of a massive redemption of shares of the capital stock of Capital régional et coopératif Desjardins. The change will allow Capital régional et coopératif Desjardins to proceed with the exchange of shares for a maximum value of \$100 million for the periods that begin on March 1, 2018, 2019 and 2020 and that end on the last day of February of the year following each of these years.

Capital régional et coopératif Desjardins must meet an investment requirement for each fiscal year. If it does not, it becomes limited in its capacity to issue shares during the following fiscal year, since the capital that investors invest with Capital régional et coopératif Desjardins is facilitated by the tax incentive they are granted.

Briefly, the *Act constituting Capital régional et coopératif Desjardins* requires that, for each fiscal year, its eligible investments represent at least 63%¹⁷ of its average net assets for the preceding fiscal year and that investments representing at least 35% of that percentage be made in eligible cooperatives or in entities situated in the resource regions of Québec.

For the purposes of this requirement, eligible investments include investments in small and medium-size Québec enterprises, investments in major projects with a structuring effect on the economy, investments made in certain local venture capital funds created and managed in Québec, as well as participation in certain investment funds constituted as limited partnerships.

Changes will be made to various parameters of Capital régional et coopératif Desjardins.

First, clarifications will be made to tax legislation as well as to the *Act constituting Capital régional et coopératif Desjardins* so that the rules for exchanging capital stock of Capital régional et coopératif Desjardins, announced when Budget 2018-2019 was tabled, have full effect.

In addition, the *Act constituting Capital régional et coopératif Desjardins* will be amended so that new investments that Capital régional et coopératif Desjardins could make are recognized for the purposes of its investment requirement.

□ Clarification concerning the rules for exchanging shares

■ Subscription right respecting shares or fractional shares of the new class of capital stock of Capital régional et coopératif Desjardins

When the new rules concerning the exchange of capital stock of Capital régional et coopératif Desjardins were announced, it was mentioned that the non-refundable tax credit that an investor could claim concerned shares or fractional shares of the new class of capital stock of Capital régional et coopératif Desjardins that investors acquired during one of the three periods beginning on March 1, 2018, 2019 and 2020 and ending on the last day of February of the year following each of these years.

¹⁷ This percentage applies to the fiscal year ending on December 31, 2018. It will increase to 64% for the fiscal year ending on December 31, 2019 and to 65% for fiscal years beginning after December 31, 2019.

However, the formalities surrounding the change to the capital stock of Capital régional et coopératif Desjardins may not be completed before the end of the first exchange period described above. As a result, investors who have committed to purchasing a share of the new class of capital stock of Capital régional et coopératif Desjardins by exchanging shares of the existing class of capital stock that they have held for at least seven years may not actually be able to make the purchase by the end of the first exchange period.

Given the context, a clarification will be made to the tax legislation so that investors who, after February 28, 2018, have irrevocably committed to purchasing shares or fractional shares of the new class of capital stock of Capital régional et coopératif Desjardins by exchanging shares or fractional shares of the existing class of capital stock that they have held for at least seven years may claim the non-refundable tax credit in accordance with the rules previously announced, with the necessary adaptations.¹⁸

Investors will have to acquire such shares or fractional shares through such an exchange once the change to the capital stock of Capital régional et coopératif Desjardins has been completed.

More specifically, if, in the meantime, investors request the redemption of, or purchase by agreement, shares or fractional shares of the existing class of capital stock of Capital régional et coopératif Desjardins that they have agreed to exchange for shares or fractional shares of the new class, the non-refundable tax credit granted will be recovered through a special tax, in accordance with rules similar to those applicable to the redemption, or purchase by agreement, of shares or fractional shares of the existing class of capital stock of Capital régional et coopératif Desjardins. Furthermore, they will no longer be eligible for a non-refundable tax credit for either the new or existing class of capital stock of Capital régional et coopératif Desjardins.

The *Act constituting Capital régional et coopératif Desjardins* will also be amended so that the mandatory seven-year retention period provided under the Act¹⁹ begins on the day the subscription for shares or fractional shares of the new class of the capital stock of Capital régional et coopératif Desjardins is accepted where, under the conditions previously described, the subscription is accepted before the formalities surrounding the changes to the capital stock of Capital régional et coopératif Desjardins have been completed.

These changes will apply as of the day of publication of this information bulletin.

■ Deferral of the tax effects of the exchange of shares

When the 2018-2019 budget was tabled, it was mentioned that the exchange of shares or fractional shares of capital stock of Capital régional et coopératif Desjardins would have no immediate tax consequences.²⁰

It was also announced²¹ that Québec tax legislation would be harmonized with the federal tax measures concerning the taxation of switch fund shares.²²

¹⁸ See note 2, pp. A.108-A.109.

¹⁹ *Act respecting Capital régional et coopératif Desjardins*, s. 12, 1st para.

²⁰ See note 2, p. A.109.

²¹ Ministère des Finances du Québec, *Information Bulletin 2016-5*, May 6, 2016, p.1.

²² *Income Tax Act*, subs. 131(4.1).

In summary, the provisions provide that investors that switch between classes of shares of a mutual fund corporation in order to switch their economic exposure between the mutual fund corporation's different funds cannot take advantage of a deferral of the tax effects that would otherwise be granted due to such an exchange of shares.

The tax policy underpinning the provisions differs from the objectives of the change to the capital stock of Capital régional et coopératif Desjardins that was announced at the time Budget 2018-2019 was tabled.

As a result, a clarification will be made so that the previously-mentioned harmonization of the Québec tax legislation with the federal tax measures concerning the taxation of switch fund shares does not cover the type of exchanges of shares that are expected to be part of the change to the capital stock of Capital régional et coopératif Desjardins.

The change will apply to exchanges of shares or fractional shares after the day of publication of this information bulletin.

□ Recognition of investments made by Capital régional et coopératif Desjardins as part of a transatlantic partnership

Over the years, the investment requirement described above, to which Capital régional et coopératif Desjardins is subject, has been changed to better adapt it to the capital requirements of Québec companies and to allow Capital régional et coopératif Desjardins to play a greater role in the growth of Québec's economy.

One of the challenges facing Québec companies in an era of globalized trade is their ability to become more active on international markets.

As a result, the investment requirement will be changed to recognize new investments, in Québec and French businesses that plan to become more active on international markets, that may be made by Capital régional et coopératif Desjardins through the twin funds, which have a common investment policy.

According to the joint investment agreement, the twin funds—Desjardins Capital Transatlantique, S.E.C. (hereinafter, "Desjardins Capital Transatlantique") and Siparex Transatlantique, a professional private equity fund governed by articles L.214-159 and following of the Monetary and Financial Code (hereinafter, "Siparex Transatlantique")—have both committed to invest jointly in businesses:

- whose main economic activity is in Québec and that have a detailed, documented project to develop economic activity in France or elsewhere in Europe (Québec targets);
- whose main economic activity is in France and that have a detailed, documented project to develop economic activity in Québec or elsewhere in North America (French targets).

In this regard, the objective of the twin funds is to hold investments in a balanced number of French and Québec targets.

As a result, the *Act constituting Capital régional et coopératif Desjardins* will be amended so that, for one, investments made by Capital régional et coopératif Desjardins in the twin Desjardins Capital Transatlantique and Siparex Transatlantique funds under the investment agreement described previously may be recognized as eligible investments for the purpose of calculating the investment requirement applicable to it, notwithstanding the investments that the funds make in Québec targets, as described below.

For greater clarity, these eligible investments may not be considered in the calculation of the regional component of the investment requirement.

This amendment will apply to a fiscal year of Capital régional et coopératif Desjardins that begins after December 31, 2017 but ends before January 1, 2023.

In addition, the *Act constituting Capital régional et coopératif Desjardins* will be amended so that investments in Québec targets made by Desjardins Capital Transatlantique and Siparex Transatlantique under the investment agreement described previously—as well as investments that have been agreed to and for which funds have been committed but not yet disbursed²³ at the end of a given fiscal year—may be recognized as eligible investments for the purpose of calculating the investment requirement applicable to Capital régional et coopératif Desjardins, up to its proportional participation in either of the twin funds.

These investments will be deducted proportionally from investments made by Capital régional et coopératif Desjardins in Desjardins Capital Transatlantique and Siparex Transatlantique for the purpose of calculating the investment requirement.

Investments made by the twin funds in Québec targets could include securities or hypothecs.

For greater clarity, these eligible investments may be considered in the calculation of the regional component of the investment requirement.

Furthermore, any changes to the joint investment agreement described previously must be disclosed promptly to the Minister of Finance.

This amendment will apply to a fiscal year of Capital régional et coopératif Desjardins that begins after December 31, 2017.

²³ These investments will be included in the calculation of the authorized limit of 12% applicable to non-disbursed investments.

5. MEASURES RELATED TO ABORIGINAL TAXATION TAKING INTO ACCOUNT THE LEGALIZATION OF CANNABIS

□ Amendment to the legislative framework for imposing Aboriginal consumption taxes

Further to a request by the Québec government, the federal government announced in its 2004 Budget Plan that it intended to authorize and facilitate the conclusion of taxation arrangements between the Québec government and the bands contemplated by the *Indian Act*.²⁴ To that end, the *First Nations Goods and Services Tax Act* was amended.²⁵

The amendments allow band councils to enter into agreements with the Québec government to implement Aboriginal taxes that are harmonized with Québec consumption taxes within the limits of their reserves. However, such Aboriginal taxes may be applied only if Québec and the band councils pass a law to that effect.

Québec therefore implemented the legislative framework needed for band councils who so desire to impose consumption taxes that are harmonized with the following Québec taxes:

- Québec sales tax (QST);
- QST applicable only to alcoholic beverages or fuel;
- tax on alcoholic beverages;
- tax on insurance premiums;
- tobacco tax;
- fuel tax.

Considering the implementation of a process leading to the legalization of cannabis, the *Act respecting the Québec sales tax* will be amended so that the QST applicable to cannabis may be subject to an agreement which would allow such harmonized taxes to be implemented.

■ Effective date

The amendment will apply as of the date the applicable provisions of the federal and Québec legislation authorizing the sale of cannabis in Québec will come into force.

²⁴ R.S.C., 1985, c. I-5.

²⁵ S.C. 2003, c. 15, as amended.

❑ **Changes to the exclusions of the special exemption applicable to Kahnawake Mohawks**

In 1999, a transitional measure was introduced granting a QST exemption off-reserve when a property is supplied for consumption or personal use to a Kahnawake Mohawk, who ordinarily resides on the reserve, by a supplier whose establishment is situated in a specified municipality, on presentation of certain pieces of identification. The transitional measure, which is still in effect, concerns the QST only.

Alcoholic beverages, fuel and meals sold in restaurants are currently excluded from the goods covered by the QST exemption off-reserve.

Considering the implementation of a process leading to the legalization of cannabis, and to be consistent with the current exclusions, an amendment will be made to the Québec regulations pertaining to the QST so that the QST applicable to the purchase of cannabis will not be covered by the QST exemption off-reserve for Kahnawake Mohawks.

❑ **Effective date**

The amendment will apply to the QST payable on the sale of cannabis as of the date the applicable provisions of the federal and Québec legislation authorizing the sale of cannabis in Québec will come into force.