February 28, 2018

2018 FEDERAL BUDGET COMMENTARY

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Finance Minister Bill Morneau released his third budget (the "Budget") on February 27, 2018 (the "Budget Date"). The Budget forecasts a deficit of $18.1 billion, which is improved from the fall economic statement estimate of $18.6 billion. Canada's current net debt to GDP ratio of roughly 30% remains the lowest by a considerable margin of the G7 countries, and among the lowest of the G20 countries. Canada's economy remains one of the fastest growing among the G7 countries, and its unemployment rate has fallen from 7.1% to 5.9% since November, 2015, close to its lowest level in nearly four decades. Of concern is that the Budget provides no timeline as to when the current government intends to balance its finances and to commence reducing the size of its cumulative debt in excess of $700 billion.

Against this backdrop, many business owners and their professional advisers have been nervously awaiting the Budget, in respect of the final clarification of Finance Minister Morneau's proposals concerning the taxation of investment income earned by a Canadian controlled private corporation ("CCPC"). When initially proposed on July 18, 2017, the Department of Finance signaled its intention to increase the level of taxation arising on investment income earned by a CCPC where it can be traced to reinvested business earnings. The measures, if enacted, would have increased the combined level of corporation and personal taxation of such investment income from approximately 56% presently to as much as 73% for an Ontario resident. Then, on October 18, 2017, further announcements were released by the Department of Finance following the expiration of the public consultation period on October 2, 2017. At that time, it was announced that all past investments and the income earned from those investments will not be subject to the new taxation regime, and a $50,000 per annum threshold on passive income earned by a CCPC would not be subject to the new taxation regime. Still, numerous questions remained about how this new investment income taxation system would be implemented because, on the surface, it appeared to be horrendously complex to administer and extremely punitive financially.

Fortunately, the Budget announced a more practical approach to dealing with the foregoing tax issue, likely because of the difficulty in drafting workable legislation to implement what the government had originally announced, not to mention that they likely didn't want to raise any further ire from the business community (it was reported that the government had received 23,000 submissions on their four proposed tax measures during the public consultation period). A description of these new tax measures is contained under the Business Income Tax Measures section of this Budget Summary that follows this introduction.

Interestingly, no specific tax reduction measures were announced in this Budget to keep pace with the reduced corporate and personal taxation in the US resulting from their recent tax reform legislation effective in 2018. The Budget offered no further insight on this other than a statement to the effect that the government will review the impact of the US tax reform measures and their impact on the Canadian economy in

the coming months. While the Budget didn't reduce corporate or personal income taxes – other than to reaffirm the previously announced reduction in the federal small business deduction ("SBD") rate to 10% in 2018 and 9% in 2019 and beyond – at the very least, corporate and personal income tax rates were not increased. In particular, the Budget does not include the rumoured increase to the current 50% capital gains inclusion rate.

BUSINESS INCOME TAX MEASURES

Passive investment income earned by private corporations

The Budget proposes to introduce measures to reduce perceived tax advantages where a private corporation earns passive income. The Budget proposals bear little resemblance to the measures initially announced on July 18, 2017.

The Budget proposes two new sets of rules. One set is intended to reduce the $500,000 SBD business limit otherwise available to a group of associated CCPCs, where the group earns passive income in excess of $50,000. The second set reduces, but does not eliminate, the ability of a corporation to obtain refunds of refundable dividend tax on hand (RDTOH).

Both of these Budget measures will apply to taxation years commencing after 2018. Therefore, excluding corporations who experience a short taxation year-end (i.e. one whose length is less than 365 days), the first batch of corporations to be affected by these new measures will be corporations having December 31, 2019 taxation year-ends.

The SBD business limit reduction

The SBD enables a CCPC to pay a low rate of income tax on the first $500,000 of Canadian active business income earned in a taxation year. In his fall economic statement of October 16, 2017, Bill Morneau announced that the federal SBD rate would decline to 10% for 2018 and 9% for 2019 and beyond. In addition to the foregoing, Ontario Finance Minister Charles DeSouza announced on November 14, 2017 that the Ontario SBD rate would decline to 3.5%, effective for 2018 and beyond. Therefore, as may be noted, the combined federal and Ontario corporate SBD rate amounts to 13.5% for 2018 and 12.5% for 2019 and beyond.

That $500,000 business limit must be shared by an *associated* group of corporations. That said, the $500,000 business limit of an associated group of CCPCs for a calendar year is clawed back where the group's "taxable capital employed in Canada" for its taxation years ending in the preceding calendar year exceeds $10 million. The $500,000 SBD business limit is completely clawed back where the taxable capital is $15 million or greater i.e. the SBD business limit is clawed back at a rate of $1 for every $10 of taxable capital in excess of $10 million.

The proposed provisions will also provide a second SBD business limit clawback measure, which will reduce the group's SBD business limit on a straight line basis where the group earns "adjusted aggregate investment income" ("AAII") in excess of $50,000. The SBD business limit clawback rate will be $5 for every $1 of AAII in excess of $50,000. Consequently, a group's $500,000 SBD business limit will be reduced to zero in a particular calendar year, if its AAII is $150,000 or more in its taxation years ending in the preceding calendar year i.e. ($150,000 - $50,000) x 5 = $500,000.

A group's AAII for the year will be based on the definition of aggregate investment income ("AII") for purposes of computing RDTOH, but subject to the following adjustments:

- Dividends from non-connected corporations will be included.
- Taxable capital gains will be excluded, to the extent that they arise from the disposition of assets used principally in an active business carried on primarily in Canada by the CCPC or a related CCPC.
- Taxable capital gains will be excluded, to the extent that they arise from the disposition of shares of a connected CCPC where all or substantially all of the fair market value of the assets of the connected CCPC is attributable to assets that are used principally in an active business carried on primarily in Canada.
- Net capital losses carried over from previous taxation years will be excluded.
- Income from savings in a life insurance policy that is not an "exempt policy" will be included, to the extent that it is not otherwise included in AII.

This Budget proposal will provide no grandfathering of passive income earned on investments made by a corporation before it is affected by these new measures. Consequently, all future investment earnings will be included in this annual test, regardless of when the applicable investments were accumulated.

The reduction of a corporation's $500,000 SBD business limit for a particular year will be the greater of the reduction under the existing taxable capital rule and the proposed AAII rule.

Anti-avoidance measures will discourage transactions designed to delay or avoid the new rules, such as a transaction which causes a short taxation year-end, or the transfer of property to a related but unassociated corporation.

Changes to the RDTOH system

Presently, a corporation has only one RDTOH account. To the extent that it pays a taxable dividend, regardless whether the dividend is an eligible dividend or not, it recovers corporate tax equal to the lesser of its RDTOH account and 38.33% of its taxable dividends paid.

A CCPC can pay an eligible dividend, to the extent that it has an available General Rate Income Pool ("GRIP") account. Paying an eligible dividend is less costly to an individual than receiving a taxable dividend which is not. For example, for 2018, the highest marginal personal tax rate for an Ontario resident is 39.34% in respect of an eligible dividend received versus 46.84% for a taxable dividend which is not an eligible dividend.

The Budget proposes to introduce measures that will limit the ability of a CCPC to recoup RDTOH where it pays eligible dividends. To accomplish this, the Budget proposes to create an "eligible RDTOH" account and a "non-eligible RDTOH" account. An eligible RDTOH account will only include: (i) Part IV tax paid on the receipt of eligible dividends from non-connected corporations; and (ii) part IV tax paid on dividends received from a connected corporation, to the extent of its proportionate share of the connected corporation's dividend refund arising from its eligible RDTOH account. All other AII which generates RDTOH will be included in the non-eligible RDTOH account.

The rules which will apply to recover eligible and non-eligible RDTOH are as follows:

i) If a corporation pays an eligible dividend, it can only recoup RDTOH to the extent of its eligible RDTOH account.

ii) If a corporation pays a non-eligible dividend, it will recoup non-eligible RDTOH first, and then eligible RDTOH thereafter.

A summary of the foregoing change is reflected in the grid below. The dividend refund rate of 38.33% remains unchanged.

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	Non-Eligible RDTOH	Eligible RDTOH
Eligible Dividend	Cannot Recover Taxes	Can Recover Taxes
Non-Eligible Dividend	Can Recover Taxes	Can Recover Taxes*

* Provided there is no further Non-Eligible RDTOH account.

As a transitional measure, a CCPC's RDTOH account at the end of its taxation year before being subject to this new measure, will first be allocated to its eligible RDTOH account, to a maximum of 38.33% of its GRIP account. The remainder, if any, of its existing RDTOH balance will be allocated to its non-eligible RDTOH account. On the other hand, a non-CCPC's RDTOH account at the end of its taxation year before being subject to this new measure, will be wholly classified as eligible RDTOH.

An anti-avoidance measure will prevent the deferral of the new measures by creating a short taxation year.

Tax support for clean energy

Capital cost allowance (CCA) Classes 43.1 and 43.2 provide accelerated CCA rates for investments in specified clean energy generation and conservation equipment. Class 43.2 was introduced in 2005 and is currently available in respect of property acquired before 2020. The Budget proposes to extend eligibility for Class 43.2 by five years to include property acquired before 2025.

Artificial losses using equity-based financial arrangements

A corporation can generally deduct dividends received on a share of a corporation resident in Canada (a "Canadian share"). However, the current "dividend rental arrangement" rules deny this deduction, where the main reason for an arrangement is

to enable the taxpayer to receive a dividend on a Canadian share, and the risk of loss or opportunity for gain or profit accrues to someone else.

The Government is concerned that certain taxpayers are still engaging in abusive arrangements that are intended to circumvent the dividend rental arrangement rules and result in an artificial tax loss. Consequently, the Budget proposes an amendment which broadens the dividend rental arrangement rules and securities lending arrangement rules, in order to prevent taxpayers from claiming a deduction for inter-corporate dividends received in situations where substantially all of the opportunity for profit or loss in respect of a Canadian share rests with certain persons other than the taxpayer. Similar rules are proposed to clarify situations in which a dividend compensation payment can be deducted.

These proposed rules are generally effective for dividends paid, or dividend compensation payments made, on or after February 27, 2018.

Stop-loss rule on share repurchase transactions

The Budget proposes an amendment to the dividend stop-loss rule to decrease the tax loss on a repurchase of shares held by the taxpayer as mark-to-market property, where it receives a tax deductible intercorporate dividend on the repurchase. This amendment generally reduces the tax loss by the full amount of the deemed dividend.

This proposal will apply to share repurchases occurring on or after February 27, 2018.

At-risk rules for tiered partnerships

The Budget proposes to enact legislation on the allocation of limited partnership losses to members of a top-tier partnership in tiered partnership structures, in response to a recent Federal Court of Appeal decision which quashed a long-standing Canada Revenue Agency ("CRA") position on the subject.

For taxation years that end on or after February 27, 2018, including losses incurred in tax years that ended prior to that date, the allocable losses of a lower-tiered limited partnership will be restricted by the at-risk amount of the top-tiered partnership. Any unused limited partnership losses will not be eligible to be carried forward, but rather will be added to the top-tiered partnership's adjusted cost base of its interest in the lower-tiered limited partnership.

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Health and Welfare Trusts ("HWT")

An HWT is a trust established by an employer to provide health and welfare benefits to its employees. Since the tax treatment of HWTs is not set out in the Income Tax Act ("ITA"), the CRA has published administrative positions which sets out the requirements of HWTs and its income tax consequences.

In order to encourage conversion of HWTs to employee life and health trusts ("ELHTs"), for which there are specific rules in the ITA, the Budget proposes to:

i) Discontinue the application of the CRA's administrative positions after December 31, 2020; and

ii) eliminate the ability to create HWTs after the Budget Date.

By December 31, 2020, existing HWTs will have to convert to an ELHT. If the HWT does not convert to an ELHT, nor is it wound up by then, then the HWT will be taxed in the same manner as regular inter vivos trusts.

The Department of Finance has requested the public's comments by June 29, 2018, on the transitional rules for the manner in which this conversion to an ELHT would operate.

PERSONAL INCOME TAX MEASURES

Canada Workers Benefit ("CWB")

The Budget enhances the existing Working Income Tax Benefit and renames it as the Canada Workers Benefit, effective for 2019 and subsequent years.

The CWB will be 26% of "earned income" in excess of $3,000, to a maximum of $1,355 for single taxpayers without dependents and $2,335 for families (couples and single parents). The CWB is reduced where net income exceeds a threshold amount. The CWB disability supplement for individuals certified as eligible for the disability credit will be $700. Amounts will be indexed after 2019.

The Budget also proposes to allow the CRA to determine if a taxpayer is eligible for the CWB, even if not claimed on their tax return, and assess the tax return as if it had been claimed.

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Medical Expense Tax Credit ("METC") — service animals

The Medical Expense Tax Credit is currently available in respect of expenses incurred for a service animal specially trained to assist an individual in coping with blindness, profound deafness, severe diabetes, severe epilepsy, severe autism or a severe and prolonged impairment that markedly restricts the use of the individual's arms or legs. The Budget proposes to extend the METC to expenses for animals specially trained to perform tasks for an individual with a severe mental impairment. An example is a psychiatric service dog trained to assist an individual with post-traumatic stress disorder. Expenses for animals that provide comfort or emotional support, but are not specially trained, will not qualify.

Qualifying expenses include the cost of the animal, costs for care and maintenance such as food and veterinary care, and costs for training the individual in handling the animal. This measure will apply in respect of expenses incurred after 2017.

Registered Disability Savings Plans ("RDSP")

The plan holder of an RDSP must be the individual's legal representative, where the capacity of the individual to enter into a contract is in doubt e.g. where the individual has a cognitive disability. Where the individual does not have a legal representative in place, certain family members (parents, spouses and common-law partners) are allowed to be the RDSP plan holder. This provision was to expire at the end of 2018. The Budget extends it to the end of 2023. If a family member becomes a plan holder before the end of 2023, they will be able to continue as the plan holder after 2023.

Child benefits

Foreign-born Status Indians who legally reside in Canada, but are neither Canadian citizens nor permanent residents, are eligible for the Canada Child Benefit ("CCB"), provided all other eligibility requirements are met. The Budget proposes to make them retroactively eligible for the Canada Child Tax Benefit, the National Child Benefit supplement and the Universal Child Care Benefit, the predecessors to the current CCB.

The Budget also proposes to provide authority for the federal government to share taxpayer CCB information with the provinces for the purpose of administering their social assistance payment regimes. This measure is effective July 1, 2018.

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Mineral Exploration Tax Credit for flow-through share investors

Eligibility of the Mineral Exploration Tax Credit is proposed to be extended for one year under the Budget. The credit will apply to expenses renounced under flow-through share agreements entered into on or before March 31, 2019.

Employment Insurance Parental Sharing Benefit

The Budget proposes a new five-week Employment Insurance Parental Sharing Benefit, effective June 2019. This benefit will be available as a top-up, in situations where both parents agree to share parental leave. It will be available to eligible two-parent families, including same sex-couples and adoptive parents. This new benefit is intended to provide greater flexibility, particularly for mothers, to return to work sooner.

Apprenticeship Incentive Grant for Women

Current legislation provides for the Apprenticeship Completion Grant which is a one-time taxable cash grant of $2,000 to a registered apprentice who has completed their apprenticeship training and obtains their journeyperson certification. The Budget proposes a new Apprenticeship Incentive Grant for Women. Under this program, women in male-dominated Red Seal trades will be able to receive $3,000 per year for each of their first two years of training. Nearly 90 per cent of Red Seal trades would be eligible, according to the Budget documents. Presumably this grant would be taxable, but this is not clear from the Budget documents.

INTERNATIONAL INCOME TAX MEASURES

Surplus Stripping

Section 212.1 is a provision that is intended to prevent a non-resident (the "Transferor") from stripping surplus out of a Canadian resident corporation ("Canco") as a capital gain, which might avoid Canadian tax, rather than being taxed as a dividend that would be subject to Canadian withholding tax. In the absence of section 212.1, the Transferor could achieve the foregoing by selling the Canco shares with accumulated surplus to another non-arm's-length Canadian corporation ("Holdco"), in return for non-share

consideration such as cash or a promissory note, or shares of Holdco with a high paid-up capital ("PUC").

By virtue of section 212.1, a Transferor that receives non-share consideration in such circumstances would be deemed to have received a dividend, to the extent that the non-share consideration exceeds the PUC of the transferred shares. If the Transferor receives high PUC shares, the PUC of the shares received would be ground down to the PUC of the transferred shares.

The Budget proposes to introduce an anti-avoidance measure, effective for transactions on or after Budget Day, to prevent section 212.1 from being circumvented, where, for example, the non-resident transfers the Canco shares to a partnership or trust as part of a corporate reorganization. The rule will effectively look through the partnership or trust for this purpose, by allocating the assets and liabilities of the partnership or trust to its members or beneficiaries, as the case may be, based on the fair market value of their interests.

Foreign Accrual Property Income ("FAPI")

In broad terms, FAPI is passive income earned by a *foreign affiliate* of a Canadian resident. FAPI is taxed on the accrual basis to the Canadian shareholder of a *controlled foreign affiliate*. If earned by a non-controlled foreign affiliate, it is not taxed in Canada on the accrual basis, but is taxable when repatriated to Canada.

Foreign-source income that would otherwise be treated as passive income would, in certain circumstances, be considered to be active where the entity earning the income employs more than five full-time employees (or the equivalent thereof), in the active conduct of the business.

Taxpayers whose passive foreign operations would not require more than five employees could pool their investments with other taxpayers in a similar position in a foreign corporation, in which they would hold shares the return on which would be tracked to their own investments (commonly referred to as "tracking shares"). The pooled entity would then employ more than five full-time employees, thus converting the income of all the investors in the foreign corporation to active business income, and thereby avoiding the FAPI rules.

The Budget proposes to introduce measures that would prevent the circumvention of the "more than five full-time employee" rule in this fashion. Each of the tracked pools would be treated as a separate business, and only those employees employed by that

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separate business would count in determining whether the investment business could be considered an active business.

The Budget also proposes to introduce measures that are intended to prevent the avoidance of controlled foreign affiliate status by the use of tracking shares or other arrangements, where the Canadian taxpayer does not participate in a controlling interest in the foreign affiliate. Under the tracking arrangement, each taxpayer retains control over its contributed assets and any returns from those assets accrue to its benefit. This proposal would deem a foreign affiliate of a taxpayer in this type of scenario to be a controlled foreign affiliate.

Regulated foreign financial institutions earning what would otherwise be FAPI are considered to be earning active business income if, among other conditions, they meet certain minimum capital requirements. These minimum requirements have heretofore not applied to trading or dealing in indebtedness. The Budget proposes to introduce measures that will apply the same minimum capital requirements to trading or dealing in indebtedness.

All of these measures will apply to taxation years of foreign affiliates that begin on or after Budget Day.

Reassessments

The Budget proposes to extend the normal four-year reassessment period that is generally applicable to income arising from a taxpayer's foreign affiliate by three years. The extended reassessment period will now coincide with that available to the CRA in connection with transactions between Canadian residents and non-arm's-length non-residents. This measure will apply to taxation years that begin on or after the Budget Day.

Where a taxpayer has transactions with a non-arm's-length non-resident, because the normal reassessment period available to the CRA is extended three years, there are circumstances that can prevent the CRA from reassessing a now statute-barred earlier year to which a taxpayer has carried back a loss. The Budget proposes to allow the CRA an additional three years to reduce a loss carried back to a prior taxation year, to the extent that the reassessment involves the adjustment, in a later year, of the loss carry back. This measure will apply where the loss is carried back from a taxation year that ends on or after the Budget Day.

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Reporting requirements

The Budget proposes to shorten the filing deadline for foreign affiliate information reporting (Form T1134) from the current 15 months after the taxpayer's year-end to six months after the taxpayer's year-end. This proposal applies to taxation years that begin after 2019.

Sharing information for criminal matters

The Budget proposes to allow the legal tools available under the Mutual Legal Assistance in Criminal Matters Act to be used by CRA in order to facilitate the sharing of information related to tax offenses under Canada's tax treaties, tax information exchange agreements and the Convention on Mutual Administration Assistance in Tax Matters. In addition, the Budget proposes to enable the sharing of tax information with Canadian mutual legal assistance partners in respect of acts that, if committed in Canada, would constitute terrorism, organized crime, money laundering, criminal proceeds or designated substance offenses. These proposals will also enable confidential information under Part IX of the Excise Tax Act and the Excise Act, 2001 to be disclosed to Canadian police officers in respect of those offenses where such disclosure is currently permitted under the ITA.

TRUSTS

Reporting requirements

The Budget proposes extensive new reporting requirements for most family trusts, effective for returns required to be filed for 2021 and subsequent taxation years. These requirements could impose an obligation to file a return where none currently exists, such as where the trust earned no income in the year. The trust will be required to report the identity of all trustees, beneficiaries and settlors of the trust. In addition, the identity of each person who has the ability to exert control, through the trust terms or a related agreement, over trustee decisions in respect of the appointment of income or capital must be disclosed (commonly referred to as the "Trust Protector").

The reporting requirements will apply to Canadian-resident trusts and to non-resident trusts currently required to file a Canadian return. This would include most personal "family" trusts used in tax planning. The following trusts are excluded from these filing requirements:

- Mutual fund trusts, segregated funds and master trusts,
- trusts governed by registered plans such as RRSPs,
- lawyers' general trust accounts,
- graduated rate estates (generally, the first 36 months of a deceased individual's estate),
- qualified disability trusts,
- trusts that qualify as registered charities or non-profit organizations,
- trusts in existence for less than three months and
- trusts that hold less than $50,000 in assets throughout the year as long as the assets are deposits, government debt obligations and/or listed securities; the Budget documents do not indicate if the $50,000 is based on the cost or fair market value of the assets.

These new reporting requirements are designed to improve information on the beneficial ownership of a trust's property.

The Budget also introduces penalties for failure to file a trust return where the new reporting requirements apply. The penalty will amount to $25 per day the return is late-filed, with a minimum $100 penalty and a maximum $2,500 penalty applying. If the failure to file is made knowingly, or as a result of gross negligence, there will be an additional penalty of five per cent of the maximum fair market value of property held during the year, with a minimum $2,500 penalty applying.

CHARITIES

Municipalities as eligible donees

Where a registered charity's registration is revoked, either at its request or because of non-compliance, a revocation tax of 100 per cent of the net value of the charity's assets is imposed. This tax can be reduced by making qualifying expenditures, including gifts to "eligible donees," generally being another registered charity where its directors/trustees are arm's length with those of the revoked charity.

The Budget proposes to allow transfers of property to municipalities to be qualified expenditures for this purpose, subject to case-by-case approval, thus reducing the revocation tax. This measure will apply to transfers made on or after February 27, 2018.

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Universities outside Canada

Certain categories of "qualified donees," including universities outside Canada, are required to register with the CRA and are listed on the CRA website. Foreign universities are also required to be prescribed in the Income Tax Regulations. The Budget proposes to eliminate this duplication in respect of universities, by removing the Income Tax Regulation requirement as of February 27, 2018.

SALES TAX AND EXCISE TAX MEASURES

GST/HST and investment limited partnerships

The Budget confirms the Federal Government's intention to proceed with the legislative and regulatory proposals released on September 8, 2017, relating to the application of GST/HST to investment limited partnerships, with the following modifications:

- GST/HST only applies to management and administrative services rendered by the general partner on or after September 8, 2017, unless the general partner has charged the GST/HST in respect of such services before that date.
- GST/HST will generally be payable on the fair market value of the management and administrative services in the period in which they are provided.
- An investment limited partnership will have the ability to make an election to advance the application of these rules as of January 1, 2018.

Consultation on the GST/HST holding corporation rules

The government intends to consult on the application of the "holding corporation rule" that allows a parent corporation to claim input tax credits to recover GST/HST paid on expenses that can reasonably be regarded as relating to the ownership of shares or indebtedness of a related commercial operating corporation.

The consultations will address the limitation of the rule to corporations and not other entities, and the degree of relationship between the parent corporation and the commercial operating corporation.

The government intends on clarifying the expenses of the parent corporation that are in respect of shares or indebtedness of a related commercial operating corporation that qualify for input tax credits under this rule.

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Tobacco taxation

The Budget proposes to increase the excise duty on tobacco products on an annual basis rather than to automatically increase it every five years to account for inflation. These inflationary increases will take effect on April 1 of every year, starting in 2019. Effective February 28, 2018, tobacco excise duty rates will be adjusted to account for the inflation since the last adjustment in 2014.

The excise duty rate is proposed to increase by an additional $1 per carton of 200 cigarettes with corresponding increases to the excise duty rates on other tobacco products.

Cigarette inventories held by manufacturers, importers, wholesalers and retailers at the end of Budget Day will be subject to an inventory tax of $0.011468 per cigarette subject to certain exemptions. Taxpayers will have until April 30, 2018, to file returns and pay the cigarette inventory tax.

Cannabis taxation

The Budget proposes a new excise duty framework for cannabis products to be introduced as part of the Excise Act, 2001. The duty will generally apply to all products available for legal purchase including fresh and dried cannabis, cannabis oils and seeds and seedlings for home cultivation. Cannabis cultivators and manufacturers (cannabis licensees) will be required to obtain a cannabis license from the CRA and remit the applicable excise duty.

Excise duties will apply at the higher of a flat rate on the quantity of cannabis contained in the final product and a percentage of the dutiable amount as sold by the producer. Generally, the dutiable amount is the portion of the producer's selling price that does not include cannabis duties.

The proposed excise duty will be applied as follows:

- A flat rate duty will be imposed on a dollar-per-gram basis at the time of packaging for final retail sale. For seed and seedlings, the duty rate will be applied on a dollar-per-seed/seedling basis.
- At the time of delivery by a cannabis licensee that packaged the cannabis product to a purchaser (i.e., a provincially authorized distributor), an ad valorem rate will also be imposed on the dutiable amount.
- Cannabis licensees will be liable to pay duty at the higher of the flat rate or the ad valorem rate at the time of delivery to a purchaser.

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The framework requires all cannabis products to have an excise stamp before they can be removed from the premises of a cannabis licensee and enter the Canadian market for a retail sale. Cannabis licensees who packaged the cannabis product will have the responsibility to determine and apply the appropriate excise stamp based on the provincial or territorial market in which the product is intended to be sold.

The new excise duty would not apply to packaged products that contain concentrations of no more than 0.3 per cent Tetrahydrocannabinol (THC) and pharmaceutical products that can only be acquired through a prescription.

The GST/HST rules for basic groceries will be amended to ensure that any sales of cannabis products will not meet the zero-rating provisions and will be subject to GST/HST in the same way as sales of other cannabis products. In addition, the relieving rules for agriculture products will be changed to ensure that sales of cannabis products including seeds or seedlings will also be subject to GST/HST.

OTHER MEASURES

The Budget confirms that the Department of Finance will proceed with the implementation of the December 13, 2017 draft legislative proposals that address income sprinkling involving private corporations. These draft legislative proposals represent a major broadening of the old Tax on Split Income ("TOSI"), rules and will become effective on January 1, 2018. Zeifmans' analysis of these new TOSI rules will be forthcoming as part of a separate newsletter in the month of March, 2018.

For more information on this year's Federal Budget and how it may impact you, contact your Zeifmans advisor today or connect with Nathan Choran, Partner at 416.256.4000 or nc@zeifmans.ca.