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Global Tax Alert

News from EY Americas Tax

Canada: Québec issues budget 2020-21

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Executive summary

On 10 March 2020, Québec Minister of Finance, Éric Girard, tabled the province's fiscal 2020-21 Budget. The budget, described by the Minister as showing confidence in the future, has three focuses: building a green economy; increasing individual and collective wealth; improving services for Québécois and addressing their needs.

The Minister provides for the maintenance of a balanced budget for the next five years, after contributions to the Generations Fund. In addition, the Government confirms that the objective to reduce the gross debt to 45% of gross domestic product (GDP) has been achieved. As at 31 March 2020, the ratio of gross debt to GDP will stand at 43%. The objective of reducing the ratio of accumulated deficits to 17% of GDP will be achieved in 2022-23, that is, three years ahead of schedule.

The following is a brief summary of the key tax measures.

Detailed discussion

Business tax measures

Corporate tax rates

No changes are proposed to the corporate tax rates or the CA\$500,000¹ small-business limit.

Québec's 2020 and 2021 corporate tax rates are summarized in Table A.

Table A - Québec (QC) corporate tax rates 2020-21

	2020		2021	
	QC	Federal and QC combined	QC	Federal and QC combined
Primary sector and M&P small -business tax rate*, **	4.00%	13.00%	4.00%	13.00%
Small-business tax rate*	5.00%	14.00%	4.00%	13.00%
General corporate rate	11.50%	26.50%	11.50%	26.50%

* The small-business rate is prorated based on a 31 December year-end and up to the business limit.

** CCPCs engaged in manufacturing and processing (M&P) activities in Québec may be eligible for a reduction in the regular small-business rate. The additional deduction rate reaches the maximum where the proportion of activities in the primary or M&P sector is 50% or more and is reduced linearly where the proportion is between 50% and 25%.

New tax measures

Tax credit for investments and innovation (C3i)

The C3i has been introduced to encourage productivity gains of businesses, while more particularly promoting investments in regions where the economic vitality index is low. In short, a qualified corporation may claim the C3i in respect of expenses incurred that exceed the exclusion threshold for the acquisition of manufacturing or processing equipment, computer equipment or certain software packages. The exclusion threshold is \$12,500 and is reduced to \$5,000 where the property is a specified property that is a property in Class 50 of Schedule B to the *Regulation respecting the Taxation Act* or a qualified management software package.

A specified property is a property that meets the following conditions:

- ▶ It is one of the following properties:
 - Manufacturing or processing machinery or equipment
 - General-purpose electronic data processing equipment and the systems software for that equipment
 - A property used mainly in the course of processing ore extracted from a mineral resource located in a country other than Canada
 - A qualified management software package
 - A property used mainly in activities involving the smelting, refining or hydrometallurgy of ore, other than ore from a gold or silver mine, extracted from a mineral resource located in Canada
- ▶ It must begin to be used within a reasonable time of its acquisition and be used during a period of at least 730 consecutive days
- ▶ It is not acquired to be used and is not used in the course of carrying on a recognized business of the corporation or partnership relating to a large investment project²
- ▶ It is not used in the course of operating an ethanol, biodiesel or pyrolysis oil production plant
- ▶ It was not used, before its acquisition, for any purpose or acquired to be used or leased for any purpose whatsoever
- ▶ It must be used only in Québec except for a management software package, which must be used mainly in Québec

The C3i rate will be 10%, 15% or 20% of the specified expenses depending on whether the property is acquired for use mainly in the high economic vitality zone, the intermediate zone or the low economic vitality zone. In addition, the refundability criterion of the credit will be determined based on the qualified corporation's assets and gross income. The refundability rate of the C3i will decrease linearly when assets or gross income exceed \$50 million and the C3i becomes non-refundable when gross income exceeds \$100 million.

Given the similarity in the conditions for applying the C3i and the existing investment tax credit, a corporation that acquires a property that can both qualify as a specified property and create entitlement for the C3i and qualify as an eligible property and create entitlement for the investment tax credit will be able to elect that the property be an eligible property and thus benefit from the investment tax credit under the current terms and conditions. However, the election can no longer be made beginning from the taxation year in which the corporation or an associated corporation first claimed the C3i.

In addition, the total expenses for which the C3i may be claimed and the total eligible expenses for which a corporation may benefit from an increased rate or the refundable nature of the investment tax credit are subject to a cumulative limit of \$100 million over a 48-month period. This limit must be shared with associated companies.

The C3i is available for a property acquired after 10 March 2020 and before 2025, and the investment tax credit will remain available for a property acquired before 1 January 2023.

In view of the introduction of the C3i, the refundable tax credit relating to IT integration will be eliminated.

Incentive deduction for the commercialization of innovations in Québec (IDCI)

The IDCI is a measure introduced to support the commercialization of Québec innovations and foster the retention and valorization of intellectual properties (IPs) developed from activities in Québec.

In brief, the IDCI is a deduction that will allow a qualified innovative corporation to benefit from a reduced effective tax rate of up to 2% on the qualified portion of its taxable income attributable to that qualified IP asset, which corresponds to a maximum reduction of 9.5% compared with the basic corporate income tax rate of 11.5%.

The IDCI is calculated taking into account factors such as the ratio of the gross income of the qualified innovative corporation from the commercialization of a qualified IP asset of the total gross income of the qualified innovative corporation, the ratio of the qualified amount of research and development (R&D) expenditures related to Québec, for the purposes of the IDCI, of the overall amount of R&D expenditures of the qualified innovative corporation, for the purposes of the IDCI, as well as an estimate of the routine return to be subtracted from the qualified profits.

A qualified IP asset of a qualified innovative corporation means a legally protected incorporeal property that is either an invention protected by a patent, a certificate of supplementary protection or a plant breeders' rights certificate, or software protected by copyright.

A special tax could become payable by a corporation to reimburse the IDCI if the corporation benefits from the IDCI and, at a later time, either a request for legal protection is denied, no document is issued by the competent authority, the legal protection is invalidated or a reassessment cancels the R&D expenses of the corporation included in the calculation of the IDCI.

The IDCI will apply as of 2021.

In light of the introduction of the IDCI, the deduction for innovative manufacturing corporations will be eliminated for a corporation whose taxation year begins after 31 December 2020.

Introduction of the synergy capital tax credit

The 2020-21 Budget provides for the introduction of the synergy capital tax credit which will be granted to a corporation (qualified investor), other than a financial institution, a real estate sector corporation or a corporation whose activities consist mainly in granting loans or making investments, and that subscribes shares of the capital stock of a qualified corporation in the life sciences, manufacturing or processing, green technologies, artificial intelligence or information technologies sectors. It will be calculated at a rate of 30% on the amount of the eligible investment. The tax credit will be non-refundable and can be, for a corporation, up to \$225,000 annually. The portion of the tax credit that cannot be used in the year it is claimed may be carried back to the preceding three years or forward to the following 20 years, except for a taxation year ended before 1 January 2021.

An eligible investment of a qualified investor, for a taxation year, will correspond to the amount paid for the subscription, in the year, of shares of a qualified corporation. To be an eligible investment, certain conditions relating to the characteristics of the shares and their ownership must also be met. Among others, the corporation (qualified corporation) must be a Canadian-controlled private corporation for a defined term and the shares subscribed must be retained by the corporation for a minimum period of five years.

A qualified corporation wishing to issue shares of its capital stock to a qualified investor pursuant to the synergy capital tax credit will be required to obtain from Investissement Québec an authorized placement certificate. The funds from the issuing of shares of a corporation's capital stock related to an authorized placement certificate must be used for investments related to the carrying on of the qualified corporation's business in connection with its eligible activities, in compliance with the description presented to Investissement Québec. A corporation that does not qualify for the credit may incur a penalty equal to 30% of the aggregate of the amounts each of which is an amount received on account of the issuing of shares of its capital stock related to an authorized placement certificate.

Investissement Québec will be able to accept an application for the issuing of an authorized placement certificate that is filed after 31 December 2020. Also, the synergy capital tax credit will apply in respect of a share subscription carried out after 31 December 2020.

Introduction of a refundable tax credit for SMEs for persons with a severely limited capacity for employment

To further support small and medium-sized businesses (SMEs) and promote the hiring and retention of workers with a severely limited capacity for employment, a refundable tax credit will be granted to a qualified corporation with an employee having a severe and prolonged impairment in mental or physical functions.

The refundable tax credit will be equal to the amount of the employer contributions paid by the corporation in respect of such an employee (contributions relating to the legislation on parental insurance, labor standards, the Régie de l'assurance maladie du Québec (RAMQ) and the Québec Pension Plan (QPP).

To be eligible for this credit, a corporation must carry on a business in Québec, have an establishment in Québec, its paid-up capital for the year must be less than \$15 million

and its total number of remunerated hours for the year must exceed 5,000, unless it is a corporation in the primary and manufacturing sectors.

Amended tax measures

Elimination of the exclusion threshold for R&D tax credits fostering collaboration with research entities

To further stimulate innovation, which fosters the productivity and the competitiveness of Québec businesses, the tax legislation will be amended to eliminate the exclusion threshold for qualified expenditures relating to a university research contract, an eligible research contract entered into with an eligible public research centre, a pre-competitive research project carried out in private partnership, or fees or dues paid to an eligible research consortium.

For greater clarity, the elimination of the expenditure exclusion threshold will not apply to the "R&D salary" refundable tax credit. However, for the purposes of calculating that tax credit, the rule providing for the splitting of the exclusion threshold among the various R&D tax credits will continue to apply as if the definition of reducible expenditures still applied to the other refundable R&D tax credits.

These changes will apply to excluded expenditures incurred by a taxpayer or partnership for a taxation year or fiscal period, as applicable, beginning after the day of the budget speech, respecting R&D work carried out after that day.

Change in activities eligible for the tax credits for the development of e-business

The refundable tax credit for the development of e-business (TCEB) was introduced to provide tax assistance to specialized businesses that carry out innovative, high value-added activities related to e-business in the information technology sector, chiefly in the fields of computer systems design and software publishing.

To refocus the TCEB on high value-added activities in the information technology sector, a change will be made to the activities that are eligible activities for the purposes of the TCEB.

More specifically, the *Act respecting the sectoral parameters of certain fiscal measures* will be amended so that an activity involving the design or development of e-commerce solutions allowing a monetary transaction between the person on behalf of whom the design or development is carried out and that person's customers will no longer be an eligible activity for the purposes of the TCEB. However, such an activity may

be an eligible activity if it is incidental to an eligible activity relating to the development or integration of information systems or of technology infrastructures.

This change will apply in respect of a taxation year of a corporation beginning after the day of the Budget Speech.

Change to the notion of interactivity for the purposes of the refundable tax credits for multimedia titles

For a multimedia title to be an eligible multimedia title, it must, in particular, contain a substantial volume of three of the following four types of information, in digital form: text, sound, still images and animated images. It must also be published on an electronic medium and controlled by software allowing interactivity.

A title is considered to be controlled by software allowing interactivity if the user participates in the action of the title. To determine whether this condition is met, the following elements must be taken into account: the feedback capability of the title, the control that the user may exert on the action of the title and the adaptation potential of the title to the user's needs.

However, a multimedia title may have different levels of interactivity. To specify the level of interactivity required for a multimedia title to be recognized by Investissement Québec as an eligible multimedia title for the purposes of both the tax credit - general component and the tax credit - specialized component, an amendment will be made to the *Act respecting the sectoral parameters of certain fiscal measures*.

A title may thus be considered to be controlled by software allowing interactivity if the conditions respecting the user's participation in the action of the title are met for all or substantially all of the action.

This amendment will apply, in respect of both the tax credit - general component and the tax credit - specialized component, to an application for a certificate filed with Investissement Québec after the day of the budget speech for a taxation year beginning after that day.

Increase in the refundable tax credit for sound recordings

Currently, the refundable tax credit for the production of qualified sound recordings, qualified digital audiovisual recordings and qualified clips is equal to 35% of qualified labor expenditures which are capped by a limit corresponding to 50% of the production costs of the recording.

To encourage the growth of this industry, the Government will amend tax legislation to raise the limit on the production costs of the said sound recordings to 65%.

This amendment will apply in respect of a qualified property for which an application for an advance ruling, or an application for a qualification certificate if no application for an advance ruling was previously filed, is filed with the Société de développement des entreprises culturelles after the day of the budget speech.

Increase in the refundable tax credit for the production of performances

The refundable tax credit for the production of performances is equal to 35% of the amount of qualified labor expenditures, which are, however, capped by a limit corresponding to 50% of the production costs of the performance.

Recognizing that labor expenditures in the entertainment industry have increased in recent years and wishing to support the creation of performances, the Government is increasing the limit on production costs to 65%.

It should be noted that no changes have been made to the maximum amounts of the tax credit in respect of a qualified performance.

This change will apply in respect of a performance whose first eligibility period ends after the day of the budget speech and for which an application for an advance ruling, or an application for a qualification certificate if no application for an advance ruling was previously filed for that period, is filed with the Société de développement des entreprises culturelles after that day.

Changes to the compensation tax for financial institutions

The Government will make changes to the compensation tax for financial institutions to distinguish loan corporations, trust corporations and corporations trading in securities that are not part of a group including a bank or other large financial institution.

Consequently, an independent loan corporation, an independent trust corporation and an independent corporation trading in securities will pay the compensation tax based on the wages according to the rates applicable to other persons and not those prescribed for the financial institutions. Likewise, the amount on which they will be required to pay the compensation tax will be limited based on the maximum amount subject to other persons and not that prescribed for banks.

A loan corporation, a trust corporation or a corporation trading in securities will be considered as “independent” if it is not associated with a bank, savings and credit union or insurance corporation.

The changes will apply as of 1 April 2020.

Consequently, these corporations will be subject to the compensation tax for financial institutions, as of 1 April 2020, at the following rates:

- ▶ For the period from 1 April 2020 to 31 March 2022: 1.32%
- ▶ For the period from 1 April 2022 to 31 March 2024: 0.90%

Lastly, the maximum amount subject to tax that will be applicable to those corporations, as of 1 April 2020, will be \$275 million.

Extension of the time limit for submitting an application for the initial qualification certificate for the tax holiday for large investments projects

Briefly, a corporation that carries out a large investment project in Québec may, under certain conditions, claim a tax holiday in respect of the income from its eligible activities relating to the project and a holiday from employer contributions to the Health Services Fund (HSF) regarding the portion of wages paid to its employees that is attributable to the time they devote to such activities.

To enable more investment projects to qualify for the tax holiday for large investment projects, the time limit for submitting an application for an initial qualification certificate or for amending the initial qualification certificate will be extended by four years. A corporation or partnership will be required to file an application for an initial certificate with the Minister of Finance in writing before its large investment project begins to be carried out and no later than 31 December 2024.

Also, to claim the tax holiday for a second investment project that builds on the first investment project, a corporation or partnership will be required to file the application for amending the initial qualification certificate to add the second investment project before the second large investment project begins to be carried out, no later than 31 December 2024 and no later than the date the application for the first annual certificate is made for the first investment project.

All other terms remain unchanged.

Changes to the refundable tax credit for Québec film or television production

To allow more Québec corporations to benefit from the higher base credit rates, changes have been made to the definition of a film adapted from a foreign format and to the requirements for application of the higher rate for a French-language film.

Briefly, the conditions defining a film adapted from a foreign format in the case of a film whose primary market is the television market will also apply to a film whose primary market is the online broadcasting market. Also, to further encourage French-language film productions, certain French-language films whose primary market is online broadcasting will benefit from the higher base rate for French-language film productions.

Personal tax measures

Personal income tax rates

No changes to personal income tax rates were announced in the budget.

Table B provides a summary of Québec personal income tax rates for 2020.

Table B - Québec personal income tax rates for 2020

Rate applicable to the first bracket	Rate applicable to the second bracket	Rate applicable to the third bracket	Rate applicable to the fourth bracket
\$0 to \$44,545	\$44,546 to \$89,080	\$89,081 to \$108,390	Above \$108,390
15.00%	20.00%	24.00%	25.75%

Table C shows the combined federal and provincial personal income tax rates for 2020 for taxable income above \$108,390.

Table C - Combined 2020 federal and provincial personal tax rates

Bracket	Ordinary income*	Eligible dividends	Non-eligible dividends
\$108,391 to \$150,473	47.46%	32.04%	40.42%
\$150,474 to \$214,368**	50.15%	35.75%	43.51%
Above \$214,368	53.31%	40.11%	47.14%

* The rate on capital gains is one-half the ordinary income tax rate.

** An additional federal basic personal amount may be available for individuals with taxable income below \$214,368. The additional tax credit is \$117 for individuals with taxable income below \$150,474; this additional amount is gradually phased out for individuals with taxable income between \$150,474 and \$214,368, resulting in an additional 0.18% to 0.25% of federal income tax on taxable income in this bracket.

Québec sales tax

Since 1 January 2019, foreign suppliers of incorporeal property and services to Québec consumers are required to register for the Québec sales tax (QST). This measure does not apply to supplies of corporeal movable property.

The Québec Government had instead agreed to participate in a pilot project in collaboration with the Canada Border Services Agency to ensure collection of the QST upon the entry into Québec of corporeal property from abroad.

Since the said pilot project did not produce the expected success, the Québec Government is reiterating its determination to require foreign suppliers of corporeal property to Québec consumers to register for the QST.

In this respect, Québec will collaborate with the federal Government³ to implement in 2021 harmonized rules for the collection of the QST and the Goods and Services Tax (GST)/Harmonized Sales Tax (HST) for foreign suppliers.

Other tax measures

Strengthening corporate transparency

The Government is continuing its efforts to more effectively combat schemes that aim to conceal the identity of beneficial owners and foster tax evasion and abusive tax avoidance, money laundering and the financing of criminal activities. In the 2020-21 Budget, the Government has stipulated certain measures, particularly:

- ▶ The introduction of a requirement that businesses carrying on activities in Québec must declare information on their beneficial owners to the Registraire des entreprises du Québec.
- ▶ The Government intends to make it possible for the public to do searches using a natural person's name in the enterprise register subject to the limits related to the protection of personal information and privacy.
- ▶ The Government intends to expressly prohibit the issue of subscription warrants or stock options in bearer form.

Stepping up actions to fight tax evasion and tax avoidance

To step up actions to fight tax evasion and abusive tax avoidance, the Government is introducing targeted initiatives in sectors where specific problems have been observed. In particular, in the 2020-2021 Budget, the Government intends to make it mandatory for personnel placement agencies holding a license issued by the Commission des normes, de l'équité, de la santé et de la sécurité du travail under the *Act respecting labour standards to hold an Attestation de Revenu Québec that is valid at all times*.

Endnote

1. Currency references in this Alert are to CA\$.
2. *Taxation Act*, s. 737.18.17.1.
3. On 13 December 2019, the federal Government announced its intention to legislate the registration of foreign suppliers.

For additional information with respect to this Alert, please contact the following:

Ernst & Young LLP (Canada), Montréal

- ▶ Jonathan Bicher jonathan.bicher@ca.ey.com
- ▶ Stéphanie Jean stephanie.jean@ca.ey.com
- ▶ Stéphane Leblanc stephane.leblanc@ca.ey.com
- ▶ Sandy Maag sandy.maag@ca.ey.com
- ▶ Benoît Millette benoit.millette@ca.ey.com
- ▶ Kimrang Te kimrang.te@ca.ey.com

Ernst & Young LLP (Canada), Québec

- ▶ Nancy Avoine nancy.avoine@ca.ey.com
- ▶ Sylvain Paquet sylvain.paquet@ca.ey.com

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