Tax Notes

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ACCELERATED CCA AND OTHER MEASURES FROM THE 2018 FALL ECONOMIC STATEMENT

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The 2018 Fall Economic Statement announced several tax measures to support Canadian businesses. The most notable among them is the Accelerated Investment Incentive for capital cost allowance ("CCA"). As the name implies, the Accelerated Investment Incentive will accelerate the amount of CCA that can be deducted for the year in which depreciable property is acquired and available-for-use. The Accelerated Investment Incentive will also provide 100% CCA deductions for newly-acquired manufacturing and processing property (Class 53) and eligible clean energy property (Classes 43.1 and 43.2). To this end, the Minister of Finance tabled a Notice of Ways and Means Motion that proposes amendments to the *Income Tax Regulations* — this article provides a comprehensive overview of these proposals. The few other tax measures announced in the Statement are discussed below as well.

Accelerated Investment Incentive Property

Property must be accelerated investment incentive property ("AIIP") to qualify for the accelerated CCA. AIIP is defined under proposed Reg. 1104(4) as property that is acquired after November 20, 2018, and becomes available for use before 2028. However, AIIP excludes property acquired in circumstances where the taxpayer was deemed to have previously deducted CCA under 20(1)(*a*) (i.e., property acquired on a rollover basis) or where the undepreciated capital cost ("UCC") was reduced by an amount determined by reference to the amount by which the capital cost of the property to the taxpayer exceeds its cost amount (e.g., where section 87 applies to the acquisition of the property). AIIP also excludes any property that was previously owned by the taxpayer or by a non-arm's length person or partnership. Therefore, with these exceptions, AIIP includes all depreciable property: full stop.

Suspended Half-Year Rule

Depreciable property belonging to most classes is depreciated on a declining-balance basis. For these classes, Reg. 1100(2) currently provides that the amount of CCA that can be deducted with respect to any assets that are acquired in the year is limited to 50% of the amount that could otherwise be deducted — this is often referred to as the "half-year rule". Reg. 1100(2) applies the half-year rule by reducing the UCC of a class by 50% of net additions for the purposes of computing the CCA deduction under Reg. 1100(1).

The proposed amendment to Reg. 1100(2) provides that, among other changes discussed below, the half-year rule no longer applies to AIIP, but appropriately will continue to apply with respect to any property that is not AIIP. Since the proposed definition of AIIP under Reg. 1104(4) requires that the property must be available for use before 2028, the suspension of the half-year rule will expire for property that becomes available for use after 2027. The preservation of the half-year rule and its exception for AIIP are provided in the amount "0.5(I)" of the formula under proposed Reg. 1100(2).

Accelerated First-Year CCA for Declining-Balance Classes

In addition to suspending the half-year rule for newly-acquired AIIP, a taxpayer's first-year CCA deduction with respect to the AIIP that becomes available for use in the year is increased by a factor of 50%. More specifically, net additions to the UCC of the class are grossed-up by 50% for the purposes of computing CCA, which is similar to how the half-year rule halves the UCC for computing CCA when an asset is acquired.

For example, a Class 8 asset is acquired for $1,000, it is AIIP, and is the only asset in the class. As discussed above, the half-year rule is suspended and not applicable. Normally Class 8 allows a taxpayer to claim an allowance for 20% of the UCC, or $200. However, the first-year additional allowance is computed as if the addition to Class 8 was 50% higher, or $1,500. Therefore the taxpayer can claim 20% of $1,500, or $300, for the first year. For subsequent years, the CCA deduction amount returns to normal since the accelerated allowance is only available in the first year that the property is available for use. So in the second year, the taxpayer can deduct 20% of the remaining $700 UCC, or $140.

The accelerated first-year allowance is provided by the amount "A(B)" in the formula under proposed Reg. 1100(2). It is only available with respect to property that becomes available for use before 2024. Any property that becomes available for use after 2023 (even if it was acquired before that time) is not eligible for the accelerated first-year allowance, though it would be exempt from the half-year rule if it is available for use prior to 2028.

Full CCA Write-Off for Clean Energy Property and Manufacturing and Processing Property

Currently, manufacturing and processing ("M&P") property is included in Class 53 (50% allowance), but any property acquired after 2025 will be included in Class 43 (30% allowance). Various types of clean energy equipment are included in Classes 43.1 and 43.2, which are eligible for 30% and 50% allowances, respectively. The CCA for these classes is computed on a declining-balance basis. Where assets in these classes are acquired after November 20, 2018, are available for use before 2024, and meet the definition of AIIP, the taxpayer is eligible for CCA deduction for the entire cost of the asset.

Technically speaking, the 100% deduction is provided by proposed Reg. 1100(2), which suspends the half-year rule and grosses up the addition to the UCC by a factor (which varies based on the class), but the key takeaway is that the entire cost is deductible at once.

The full deduction will be phased-out for property acquired after 2023. Property that becomes available for use after 2023 and before 2028 will still be eligible for an accelerated CCA deduction in the year it is acquired, and will not be subject to the half-year rule, but it will not be a 100% write-off. For any assets that become available for use after 2027, the rule is completely phased out so the CCA computation will return to normal (including the application of the half-year rule).

The following chart illustrates the current and proposed CCA rates for the affected classes, including the rates applicable during the phase-out period:

CCA for Year of Acquisition
(Before proposed changes, with half-year rule)

Year Asset Becomes Available for Use	Class 53 and Class 43 after 2025	Class 43.1	Class 43.2 (closed after 2024)	Proposed First-Year CCA (Classes 43.1, 43.2, 53)
November 21, 2018 – December 31, 2023	25%	15%	25%	100%
2024	25%	15%	25%	75%
2025	25%	15%	—	75%
2026	15%	15%	—	55%
2027	15%	15%	—	55%
2028	15%	15%	—	—

Where eligible property becomes available for use during the phase-out period and thus is not fully written-off in the first year, it is important to note that this accelerated allowance is only for the first year, similar to how the accelerated allowance applies to other AIIP.

For example, a Class 43.1 asset is acquired and available for use in 2026. The capital cost is $1,000,000 and there are no other assets in the class. The taxpayer's accelerated CCA deduction in the first year is computed as 55% of $1,000,000, or $550,000, leaving $450,000 in the UCC balance. In the second year, the CCA deduction is computed using the normal 30% rate for Class 43.1 property, which results in a CCA deduction of $135,000 and a remaining UCC balance of $315,000. And this normal computation continues in future years.

Additional Miscellaneous CCA Changes

The proposed accelerated investment incentive rules are also applicable to property that is depreciated on a straight-line basis, depreciated on the basis of use, or which is subject to other special rules, so further amendments for these classes are proposed accordingly.

Leasehold Interests (Class 13)

Class 13 allows a taxpayer to deduct CCA with respect to the cost of improvements or alterations to leased tangible property. Generally, Schedule III of the Regulations provides that the CCA deduction for Class 13 is the lesser of: (a) $^1/_5$ of the capital cost, and (b) the amount equal to the capital cost divided by the number of years in the lease.

Where a leasehold interest is an AIIP, proposed Reg. 1100(1)(*b*)(i) will provide an enhanced first-year CCA deduction. This first-year deduction is 150% of the amount that would otherwise be allowed under Schedule III, and the half-year rule does not apply. This provision only applies to AIIP that is acquired before 2024, so the regular CCA rate and half-year rule apply for property acquired after 2023.

Patents, Franchises, Concessions, and Licenses (Class 14)

Class 14 includes patents, franchises, concessions, and licenses that exist for a limited time period. Reg. 1100(1)(*c*) provides that the CCA deduction for property included in Class 14 is basically a straight-line depreciation of the property's capital cost over its life.

Proposed Reg. 1100(1)(*c*) provides that where the Class 14 property is AIIP, the first-year CCA deduction otherwise determined for the year the property is acquired will increase by:

- 50% in the case of AIIP acquired before 2024, and
- 25% in the case of AIIP acquired after 2023.

Canadian Vessels (Class 7)

Canadian vessels are included in Class 7, and are subject to a 33$^1/_3$% CCA rate and the half-year rule. The proposals include an amendment to Reg. 1100(1)(*v*), which provides an accelerated first-year allowance for a Canadian vessel that is AIIP. The accelerated depreciation rates are:

- 50% for AIIP acquired before 2024; and
- 33$^1/_3$% for AIIP acquired after 2023 (i.e., no half-year rule).

Property Depreciated on the Basis of Use

There are certain types of depreciable property, the CCA deduction with respect to which is determined based on how much timber is cut or the amount of minerals extracted in a year. These include:

- property that is acquired for the purpose of cutting and removing timber from a timber limit (Class 15, Reg. 1100(1)(*f*), Schedule IV);
- an industrial mineral mine or a right to remove minerals from an industrial mineral mine (not included in a class, but see Reg. 1100(1)(*g*) and Schedule V); and
- a timber limit or a right to cut a timber limit (not included in a class, but see Reg. 1100(1)(*e*) and Schedule VI).

The provisions mentioned above will be amended to provide for an accelerated first-year CCA deduction. The deduction otherwise determined will be grossed-up by an additional:

- 50% for AIIP acquired before 2024; and
- 25% for AIIP acquired after 2023.

Other Tax Measures

Accelerated CDEs and COGPEs

Section 66.2 allows a taxpayer to deduct 30% of their cumulative Canadian development expense pool at the end of the year. The Notice of Ways and Means Motion contains amendments to section 66.2 to provide an additional first-year deduction for Canadian development expenses (“CDEs”) that are incurred after November 20, 2018, and before 2028. The additional deduction rates are:

- 15% for taxation years that end before 2024; and
- 7.5% for taxation years that begin after 2023.

The rates are prorated for taxation years that straddle the end of 2023.

The proposals provide for a similar accelerated deduction for Canadian oil and gas property expenses (“COGPEs”) incurred after November 20, 2018, and before 2028. Section 66.4 allows a taxpayer to deduct 10% of their cumulative Canadian oil and gas property expenses at the end of the year. The proposals contain amendments to accelerate the first-year deduction for COGPEs incurred after November 20, 2018, and before 2028. The additional deduction rates are:

- 5% for taxation years that end before 2024; and
- 2.5% for taxation years that begin after 2023.

Again, the rates are prorated for taxation years that straddle the end of 2023.

Mineral Exploration Tax Credit

The 2018 Fall Economic Statement also announced that the mineral exploration tax credit, which was most recently extended by Budget 2018, will be extended by an additional five years until March 31, 2024.

Tax Support for Canadian Journalism

The government has promised several tax incentives to support Canadian journalism. These include: a refundable tax credit for labour costs associated with producing news content, giving not-for-profit journalism organizations qualified donee status (so they can issue donation receipts), and a temporary non-refundable tax credit for digital subscriptions to Canadian news media. Further details on these measures will be provided in Budget 2019.

CURRENT ITEMS OF INTEREST

Progress of Legislation

Bill C-86, *Budget Implementation Act, 2018, No. 2*, received Royal Assent on December 13, 2018.

Update on Quebec's Economic and Financial Situation Released

On December 3, 2018, the new Coalition Avenir Québec government released their Update on Quebec's Economic and Financial Situation. There were a number of tax changes announced, including the following:

- Effective 2019, the refundable tax credit for child assistance will be renamed the refundable tax credit granting an allowance to families, and the child assistance payment that it includes will be renamed the family allowance. Additionally, the maximum amount of the child assistance payment for second and third children will be increased by $500 per year as of 2019.
- Effective for the 2018 taxation year, a new refundable tax credit for senior assistance is introduced. For the lowest-income seniors, this refundable tax credit may be up to $200 for a single senior and $400 for a senior couple per year. The credit will be reduced at a rate of 5% for each dollar of family income over $22,500 for a single individual or $36,600 for a married individual. These amounts will be indexed in future years.
- Adjustments to the calculation of work premiums reduction thresholds, as of 2019, to take into account changes in QPP deductions and additional contributions.
- The Quebec government will follow the accelerated capital cost allowance rules announced by the Department of Finance Canada announced on November 21 in its 2018 Fall Economic Statement, namely to:
    - allow taxpayers to write off the full cost of machinery or equipment used in manufacturing or processing and clean energy generation equipment, for the taxation year in which the property becomes available for use, where such property becomes available for use before 2024, with a gradual reduction afterwards;
    - introduce an accelerated investment incentive, namely, an accelerated capital cost allowance making it possible to claim up to three times the amount that could otherwise be deducted for nearly all other types of assets, for the taxation year in which the property becomes available for use.
- Special depreciation rules will apply to an accelerated investment incentive property that is:
    - qualified intellectual property that is
        - included in Class 14 or 44 of Schedule B to the *Regulation Respecting the Taxation Act*, or
        - incorporeal capital property; or

    - composed of general-purpose electronic data processing equipment and systems software for that equipment, namely, property included in Class 50 of Schedule B to the *Regulation Respecting the Taxation Act*.

- Elimination of the additional capital cost allowance of 60%, announced earlier in the year. Among the changes announced:

    - The additional capital cost allowance of 60% is eliminated as of December 4, 2018, but may apply to property acquired before July 1, 2019, if an obligation in writing was entered into on or before December 3, 2018; and

    - Transitional rules will apply for qualified property acquired between November 21, 2018, and December 3, 2018.

- Introduction of an additional capital cost allowance of 30%, effective December 4, 2018, for the investment in manufacturing and processing equipment, clean energy generation equipment, general-purpose electronic data processing equipment, and certain intellectual property.

FOCUS ON CURRENT CASES

This is a regular feature examining recent cases of special interest, coordinated by *John C. Yuan* and *Christopher L.T. Falk* of McCarthy Tétrault LLP. The contributors to this feature are from McCarthy Tétrault LLP, Montreal, Toronto, Calgary, and Vancouver. *Focus on Current Cases* will return next month.

RECENT CASES

Appeal allowed where deduction properly claimed for spousal support payments

The taxpayer made five payments to his former spouse during the 2015 tax year, in the amounts and on the schedule set out in their separation agreement, and he claimed a deduction for each in his return for the year. The Minister disallowed the deduction for some of those payments, on the basis that they did not constitute spousal support eligible for a deduction, as they were not "paid as an allowance on a periodic basis for the maintenance of a former spouse". The taxpayer appealed from that assessment.

The appeal was allowed. The Tax Court of Canada reviewed the agreement made between the spouses, as well as the elements of the statutory definition of spousal support payments and the jurisprudence interpreting those elements. It held that the payments made by the taxpayer fulfilled those statutory requirements. There was no doubt that the payments had been made to the taxpayer's former spouse, pursuant to a separation agreement. While the nature of the payments made were somewhat unusual, in that they were in unequal amounts, were seasonal in nature, and included a payment-in-kind, they reflected the seasonal nature of the taxpayer's income and the fact that more conventional monthly payments would, in light of the taxpayer's irregular cash flow, have been difficult for him to make on a timely basis. The Court noted in particular that the date of each payment coincided on or near the predictive payment dates of the taxpayer's personal and seasonal (not periodic) cash flow. In the factual circumstances, and as held in the jurisprudence, the irregular nature of the payments did not render the payments lump sum capital amounts, where the balance of the analysis of the other factors tilted toward their characterization as payments on a periodic basis for maintenance. The payments constituted spousal support payments which were properly deducted by the taxpayer.

Ross v. The Queen

2018 DTC 1154

Application for judicial review dismissed where conclusions of decision-maker reasonable

The taxpayer, who had participated in an employee stock option plan, was assessed as having received a taxable benefit under section 7 of the *Income Tax Act* (the "ITA") as the result of his purchase of shares at less than fair market value. He objected to the assessment and the amount of the taxable benefit received was reduced, on consent, by 30%. On the sale of the shares, the taxpayer realized a capital loss but, owing to the application of the ITA rules, was unable to claim that capital loss to offset the taxable benefit assessed. The taxpayer then made a request for a remission order with respect to the remaining income tax and interest arising from the taxable employment benefit assessed. A CRA official refused to recommend that the Minister provide a remission order. The taxpayer brought an application for judicial review of that decision, arguing that remission orders had been provided to other taxpayers who were in similar circumstances. Specifically, he argued that such relief had been provided to those who had been unable to offset taxable employment benefits with a subsequent capital loss on the sale of employee stock purchase shares, and that the decision maker had failed to recognize the similarities between a stock option plan and a stock purchase plan. He argued as well that the process by which the official's decision was made lacked procedural fairness.

The application was dismissed. The Federal Court noted that the empowering legislation conferred a broad discretion on the Minister with respect to the issuance of remission orders and that the Court must therefore exercise restraint and discretion in reviewing a decision to refuse such a remission order. It held as well that the decision was subject to a reasonableness standard of review, and, in applying such standard, it was necessary that the Court consider the justification, transparency, and intelligibility of the decision-making process, be able to understand from the reasons why the decision under review was made, and to determine whether the conclusions reached were within the range of possible acceptable outcomes. The Court held that the decision maker had reviewed the facts of the taxpayer's circumstances, had addressed both of the taxpayer's grounds for relief, and had clearly identified why he considered that the taxpayer was not in the same situation as other taxpayers for whom relief had been granted. The decision maker also identified why there were no extenuating circumstances in the taxpayer's case. The decision, when read as a whole, fell within the range of possible acceptable outcomes which were defensible in respect of the facts and the law. The Court also rejected the taxpayer's argument that the decision maker failed to exercise procedural fairness. Overall, the Court concluded that, given the highly discretionary nature of the remission of tax scheme and the considerable deference owed to the decision maker, it was not persuaded that intervention was warranted.

Fink v. Canada (AG)

2018 DTC 5123

Appeal from denial of application to withdraw guilty pleas dismissed

The appellants had entered guilty pleas to charges of making false statements in their income tax returns, with such pleas based on an Agreed Statement of Facts. They later applied unsuccessfully to be allowed to withdraw their guilty pleas, on the basis that the Agreed Statement of Facts did not disclose the necessary intent that would support their convictions. They were then granted permission to appeal from that dismissal, on the issue of whether "an actor can be wilfully blind if he or she does not suspect that a belief he or she strongly holds is probably unwarranted".

The appeals were dismissed. The Alberta Court of Appeal held that the issue on which leave to appeal had been granted did not arise on the record. The appellate Court held that if the accused knew that their view of the law was mistaken, their mistake would not be an answer to the charges. The Court held that the appellants had intentionally filed tax returns in which they intentionally did not include amounts received from their corporation as income and such actions satisfied the requirement of intent. As well, it was not necessary for the Crown to show that the appellants were "wilfully blind" about their mistake, because they were properly convicted even if they were genuinely mistaken. The Court concluded, however, that such wilful blindness was clearly made out on the record. The appellants had been warned by the Canada Revenue Agency prior to filing that their taxation theories were unsupportable and the Agreed Statement of Facts acknowledged that "they should have made further inquiries". Their applications to withdraw their guilty pleas were properly dismissed, and, no reviewable error having been shown, their appeals from that decision were also dismissed.

R. v. Steinkey et al.

2018 DTC 5121

Appeal allowed where Tax Court committed errors of law in dismissing application to extend time

The corporate taxpayer appealed from the denial of its claim for a scientific research and experimental development ("SR&ED") tax credit and related investment tax credits ("ITCs"). It did not, however, perfect its appeal by the applicable deadline and its appeal was eventually dismissed. It did not apply to set aside the resulting default judgments within the statutory 30-day time period, but then filed a motion requesting an extension of time to bring such application. Its motion was dismissed by the Tax Court, and the taxpayer appealed.

The appeal was allowed. The Federal Court of Appeal held that the only issue on the appeal was the taxpayer's application for an extension of time to file its application to have the default judgment set aside. The appellate Court held, however, that in the reasons of the Tax Court, it was not entirely clear whether the focus was on the application for an extension of time or on the application to set aside the default judgment. In the appellate Court's view, the only delay that was relevant to the application was the one with respect to the motion for an extension of time, and that any previous delays in pursuing the appeal were not relevant. In the Court's view, the Tax Court committed errors of law in not identifying the relevant period for the delay, in not considering the relevant facts, and in not addressing the jurisprudence which set out the four factors to be considered. Consequently the Federal Court of Appeal concluded that the decision of the Tax Court in relation to the application for an extension of time could not stand. The appellate Court held, however, that as all of the relevant facts relating to such application were on the record before it, it should decide the application for an extension of time on the merits. The Court noted that the four factors to be considered on an application for an extension of time were whether the taxpayer had a continuing intention to pursue the application to set aside the judgment, whether the application to set aside the default judgment had some merit, whether there was any prejudice to the Crown arising from the delay, and, finally, whether there was a reasonable explanation for the delay; further, that it was not necessary that all four factors be satisfied. It held as well that, in an application for an extension of time, the central question was which outcome better served the interests of justice. The Court reviewed each of the four factors as they applied to the taxpayer's circumstances and concluded that three of the four factors weighed in the taxpayer's favour. That finding, together with the significant amounts which were in dispute, led the appellate Court to conclude that the interests of justice supported a finding that the taxpayer's application for an extension of time should be granted. An order was therefore issued allowing the appeal, setting aside the order of the Tax Court, and allowing the application for an extension of time for the taxpayer to bring an application to set aside the default judgments.

Akanda v. The Queen

2018 DTC 5122

Application of gross negligence penalty overturned on Appeal

The taxpayer failed to report a dividend from his corporation in his 2013 return, which had been prepared by his accountant. On reassessment, the Minister imposed penalties for gross negligence, which the taxpayer contested on appeal. The application of the gross negligence penalty is the sole issue involved in the appeal.

The appeal was allowed. A simple error or negligence is insufficient to apply the gross negligence penalty. In allowing his appeal, the Tax Court of Canada noted that 2013 was the first year where the corporation requested the external auditor to prepare the T5 forms. Previously these were prepared by the internal auditor who prepared them at the same time as the T4s. In addition, the external auditor had changed firms in 2012 but retained the taxpayer's business. The taxpayer was not aware that the auditor had changed firms. The auditor sent the T5 form to the personal address of the taxpayer. Finally, in 2014 the corporation did not declare an annual dividend in favour of the taxpayer. Based on these facts, in essence, the Court found that: (a) the Minister had failed to demonstrate gross negligence on the taxpayer's part amounting to a disregard for the law; and (b) the taxpayer had simply made a reasonable error and could not be expected to know that the accountant who prepared his return possibly missed the T5 reporting the unreported dividend in issue. Indeed, the taxpayer had followed the same process, with the same professionals he depended on in previous years. Accordingly, the appeal was allowed.

Phénix v. The Queen

2018 DTC 1145

TAXATION OF CANNABIS IN CANADA

The below excerpt is from the upcoming book, Taxation of Cannabis. This book provides an overview of the regulation and taxation of cannabis federally and in the provinces and territories. If you wish to order this book, please visit http://www.cch.ca/product.aspx?WebID=5426 *or call customer service at 1-800-268-4522.*

Chapter 1: Introduction

Legalize, regulate, tax.

Recreational cannabis became available for legal retail sale in Canada on October 17, 2018. The legalization of recreational cannabis is a new frontier for consumers, sellers, and regulators in Canada. There will be growing pains, and there will be adjustments. It's important to keep in mind, especially at these early stages, that the regulation of recreational cannabis isn't so much a landscape as it is the weather: Subject to change, perhaps with very little notice. What's the law today may not be the law in six months. Government-run monopolies may be opened to private companies, duties may increase, and new regulations passed. Keep watching the skies.

All the provinces and territories except Manitoba (at the time of publication, Manitoba is negotiating an agreement) executed Coordinated Cannabis Taxation Agreements ("CCTAs") with the federal government in 2017, facilitating the legalization and taxation of cannabis in Canada. The signatories agreed the combined rate of all federal, provincial, and territorial cannabis-specific duties and taxes will not exceed the higher of $1 per gram, or 10% of a producer's selling price.

The revenues from excise duties on cannabis (which are collected by the feds) will be shared, with approximately 75% going to provincial and territorial governments (based on duties collected in their jurisdiction) and the remaining 25% to the federal government. Federal revenues from the excise duty are capped at $100 million per year for the 24 months following legalization. Federal revenues over the $100 million cap will be distributed to provinces and territories that have concluded a CCTA with the federal government.

Recreational cannabis is subject to excise duties (pursuant to newly enacted Part IV.1 of the federal *Excise Act, 2001*), GST/HST, and provincial sales taxes. Excise duties are included in the price on which the GST/HST/provincial tax is calculated. PST, GST/HST, and QST apply at the applicable sales tax rate in the province of distribution. Manitoba imposes mark-ups on recreational cannabis but not PST. British Columbia imposes a mark-up and PST. In addition, Health Canada extracts cost recovery fees from cannabis producers (see Chapter 2, *The Cannabis Act and Federal Regulation of Cannabis*).

The excise duty is imposed at the production level of cannabis and is paid to the federal government by the cannabis producer. It's the higher of the federal flat-rate duty (calculated per gram of cannabis in the product) and the *ad valorem* duty (a percentage of the sales price of the product)[1] *plus* the higher of the province or territory's flat-rate duty and the *ad valorem* duty.[2]

All jurisdictions that signed a CCTA with the federal government ("specified provinces") will receive the basic provincial portion of the duty — this includes all provinces and territories with the exception of Manitoba (which levies its own provincial tariffs). Some jurisdictions have requested — and received — an adjustment to their portion of the duties to offset varying sales tax rates in Canadian provinces and territories. Those "listed specified provinces" receive the basic provincial duty plus a supplementary duty rate as follows:

- Ontario, + 3.9% of the base or dutiable amount;
- New Brunswick, + 0% of the base or dutiable amount;
- Prince Edward Island, + 0% of the base or dutiable amount;
- Alberta, + 16.8% of the base or dutiable amount;
- Saskatchewan, + 6.45% of the base or dutiable amount;
- Newfoundland and Labrador, + 0% of the base or dutiable amount; and
- Nunavut, + 19.3% of the base or dutiable amount.

New Brunswick, Prince Edward Island, and Newfoundland and Labrador are "listed specified provinces" with adjustment rates of 0%, but may request a further adjustment at some time in the future. There is no indication whether additional provinces or territories will be added to the "listed specified provinces".

The federal *Cannabis Act* and the regulations set minimum health and safety standards that must be incorporated into the provincial and territorial legislation regulating recreational cannabis. Individual provinces and territories then decide how recreational cannabis is sold. Provinces and municipalities may enact their own rules with respect to consumption and distribution of cannabis, and limitations on personal cultivation.

The regulation of the production of cannabis is mostly the domain of the federal government, though jurisdictions in Canada where a producer operates may require them to be licensed or registered (in additional to federal licensing). Producers cannot sell directly to consumers, but can sell their products across Canada to wholesalers or retailers (depending on the rules of the particular province or territory).

Where private sales are allowed, retailers (and wholesalers in some cases) are licensed by the individual provinces and territories. These licensed private sellers can only sell within their home province — they cannot sell to consumers outside their provincial/territorial jurisdiction. In other jurisdictions, where there are no private sales, consumers purchase cannabis from government-operated sellers (who, like their private counterparts, cannot sell cannabis to parties outside their home province or territory).

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Chapter 2: The *Cannabis Act* and Federal Regulation of Cannabis

This chapter helps unpick the Gordian knot of a surprisingly tentative and complex approach to legalization, in particular the federal *Cannabis Act* ("CA") and the *Cannabis Regulations*, with emphasis on cannabis production (cultivation and/or processing).

[1] This represents the federal government's 25% share of the revenues.

[2] This is the province or territory's 75% share.

Federal Versus Provincial Regulation of Cannabis

CA s. 69–72

Production and processing of cannabis is regulated by the federal government, while retail sales are governed by the individual provinces and territories. Except for licensed commercial producers, cannabis cannot be grown (aside from limited personal cultivation), exported, or imported in Canada.

Health Canada licenses commercial cannabis growers and oversees the cannabis supply chain. Producers grow and package cannabis for ultimate sale to the public, but they do not sell directly to consumers. Cannabis must be packaged by a federally licensed producer, complete with an excise stamp for the province where it will be sold. Retailers are not allowed to open packages before selling, sell partial packages, or re-package cannabis. Licensed producers can grow and sell product for both the medicinal and non-medicinal markets.

Provinces and territories have authority over the possession, distribution, and sale of recreational cannabis in their jurisdictions — if their legislation contains the following requirements for cannabis sellers:

- they may sell only cannabis produced by a person authorized under the *Cannabis Act* to produce cannabis for commercial purposes;
- they may not sell cannabis to young persons;
- they are required to keep appropriate records respecting their activities in relation to cannabis that they possess for commercial purposes; and
- they are required to take adequate measures to reduce the risk of cannabis they possess for commercial purposes being diverted to an illicit market or activity.

As of October 17, 2018, all the provinces and territories have created viable regimes to administer and regulate the sale of recreational cannabis in their jurisdictions. See the individual chapters for details relating to a specific province or territory.

TAX NOTES

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