
# 2023 Canadian Federal Budget:

# Clean Energy and Technology Tax Incentives

## Introduction

On March 28, 2023 (Budget Day), Minister of Finance Chrystia Freeland tabled the Liberal Government's budget, *A Made-in-Canada Plan: Strong Middle Class, Affordable Economy, Healthy Future* (Budget 2023).

To help build Canada's clean economy, Budget 2023 includes numerous measures incentivizing the development of projects related to clean energy and technology.

This publication summarizes the following tax incentives included in Budget 2023:

- Clean Hydrogen Investment Tax Credit (CH Tax Credit);
- Clean Technology Investment Tax Credit (CTI Tax Credit);
- Clean Electricity Investment Tax Credit (CEI Tax Credit);
- Clean Technology Manufacturing Investment Tax Credit (CTM Tax Credit);
- Carbon Capture, Utilization and Storage Investment Tax Credit (CCUS Tax Credit);
- Flow-Through Shares and Critical Mineral Exploration Tax Credit; and
- an extension and expansion of reduced corporate income tax rates for zero-emission technology manufacturers.

Further, this publication addresses some questions that McCarthy Tétrault LLP has frequently been asked by participants in the energy and power industries.

Unless otherwise stated, all statutory references are to the *Income Tax Act* (Canada) (Tax Act).

## Budget 2023 Energy and Technology Tax Incentives

A frequent theme in Budget 2023 is that no draft legislation was provided in respect of many of the new or expanded tax incentives. In many instances, the Notice of Ways and Means Motion tabled with Budget 2023 refers to the budget documents tabled by the Minister of Finance stating "[T]he Act is modified to give effect to the proposals relating to…as described in the budget documents tabled by the Minister of Finance in the House of Commons on Budget Day". At some

point more detailed draft legislation will be introduced. In the meantime, this leaves industry and the tax community with significant uncertainty with respect to how these incentive programs will be implemented.

Some general characteristics of the tax credits discussed herein are as follows:

- All of the tax credits are described as fully refundable tax credits which means that the credit reduces the taxpayer's tax payable, if any, to nil and to the extent it exceeds the tax payable, it is paid in cash to the taxpayer.
- A taxpayer will be able to claim only one of the investment tax credits if a particular property could be eligible for more than one credit, but it is possible that a project could include properties that are entitled to different credits.
- Budget 2023 confirms that a taxpayer can claim the CH Tax Credit, the CTI Tax Credit, the CEI Tax Credit or the CTM Tax Credit without affecting its claim for the Atlantic Investment Tax Credit, but does not comment on the interaction of the CCUS Tax Credit and the Atlantic Investment Tax Credit.
- Budget 2023 did not propose any new mechanism by which a taxpayer entitled to tax credits may monetize them.
- The CEI Tax Credit specifies that it is available to be claimed by both taxable and tax-exempt entities while the CH Tax Credit, CTI Tax Credit and CTM Tax Credit do not specify whether tax-exempt entities will be entitled to claim the credits. The draft legislation released on August 9, 2022 in respect of the CCUS Tax Credit provides that tax-exempt entities are not entitled to claim the credit.

## CLEAN HYDROGEN INVESTMENT TAX CREDIT

Budget 2023 introduces the CH Tax Credit (previously announced in November 2022 in the Government's 2022 Fall Economic Statement (2022 FES)), which applies to eligible equipment that is acquired and becomes available for use (in accordance with the available for use rules applicable to depreciable property) in Canada for an eligible hydrogen project after Budget Day.

The CH Tax Credit is a refundable tax credit claimed at the following rates based on assessed carbon intensity (CI) of the hydrogen that is produced (measured in kg of carbon dioxide equivalent per kg of hydrogen):

- 40% of eligible capital costs for CI less than 0.75 kg;
- 25% of eligible capital costs for CI greater than or equal to 0.75 kg but less than 2 kg; and
- 15% of eligible capital costs for CI greater than or equal to 2 kg but less than 4 kg.

Budget 2023 proposes to phase out the CH Tax Credit gradually, with property that becomes available for use in 2034 eligible for one-half of the applicable credit and no credit available for property that becomes available for use after 2034.

Budget 2023 does not state whether the CH Tax Credit will be refundable to tax-exempt entities. By contrast, Government specifically stated that the CEI Tax Credit would be available to taxable and non-taxable entities. Draft legislation released on August 9, 2022 relating to the CCUS Tax Credit specifically provided that tax-exempt entities are not entitled to the CCUS Tax Credit.

### *Measuring CI*

The developer of a hydrogen project must assess the CI of the hydrogen to be produced by the project using the Government's Fuel Life Cycle Assessment Model (LCA Model) maintained by Environment and Climate Change Canada and submit the assessment to the Government for verification. Once the assessment is verified, the expected CI of the produced hydrogen is used to determine the CH Tax Credit rate. The CH Tax Credit is subject to a clawback or recovery based on the actual CI of the hydrogen produced by the project, as determined by assessment of the project after the start of operations, as discussed below.

*Projects Eligible for CH Tax Credit*

The CH Tax Credit is available in respect of projects where hydrogen is the only by-product of the production process or makes up substantially all of the by-products of the production process. For the purpose of determining whether hydrogen constitutes all or substantially all of a project's production, any carbon dioxide that is captured, stored or used, or excess electricity that is generated and sold to the grid (subject to certain limitations) is ignored.

The CH Tax Credit will be available in respect of the cost of purchasing and installing "eligible equipment" for a project producing hydrogen either from electrolysis or from natural gas if carbon capture, utilization and storage (CCUS) is used to abate the resulting emissions.

The Government intends to review eligibility for the CH Tax Credit for other low-carbon hydrogen production processes going forward.

*Equipment Eligible for CH Tax Credit*

The CH Tax Credit is available in respect of the cost of equipment if all or substantially all of the use of the equipment is to produce hydrogen through electrolysis of water including: (i) electrolyzers, rectifiers and other ancillary electrical equipment, (ii) water treatment and conditioning equipment, and (iii) equipment used for hydrogen compression and on-site storage.

The CH Tax Credit will also be available in respect of the cost of equipment required to produce hydrogen from natural gas with emissions abated using CCUS, excluding equipment already described in Class 57 or Class 58 which is eligible for the CCUS Tax Credit. This will include equipment if all or substantially all of its use is to "produce hydrogen from natural gas through natural gas reformation, including auto-thermal reformers, steam methane reformers, pre-heating equipment, shift reactors, purifiers, water treatment and conditioning equipment, and equipment used for hydrogen compression and on-site storage." The production of carbon dioxide will not count in determining whether the equipment is all, or substantially all, used to produce hydrogen if the carbon dioxide is captured through a CCUS process.

The following will also be eligible for the CH Tax Credit:

- oxygen production equipment used in hydrogen production if the resulting carbon dioxide is captured by a CCUS process;
- equipment that produces heat or power from natural gas or hydrogen;
- dual-use power or heat production equipment if more than 50% of the energy balance is expected to be primarily (i.e., more than 50%) used to support the CCUS process or hydrogen production that is eligible for the CH Tax Credit; and
- equipment required to convert clean hydrogen to clean ammonia but only at a tax credit rate of 15%.

To be eligible for the CH Tax Credit, the equipment must be made available for use in Canada.

Expenses incurred in the development of a hydrogen project that do not relate to the acquisition or installation of equipment (e.g., feasibility studies, front-end engineering design studies and operating expenses) do not qualify for the CH Tax Credit.

*Applying for the CH Tax Credit and Compliance Requirements*

In order to apply for the CH Tax Credit, Budget 2023 requires that a front-end engineering design study for the hydrogen production project be submitted. An initial CI assessment of the project will be made based on the design of the project using the LCA Model and whether the project design "can reasonably be expected to achieve the modelled outcomes." If a project undergoes a significant redesign, it must be re-assessed.

The CH Tax Credit is subject to a clawback or recovery based on the actual CI of the hydrogen produced by the project, as determined by subsequent assessment after the project commences operations. The Government intends to release

further guidance on the process for this assessment at a later date. Where a project fails to meet the CI of hydrogen at which it was initially assessed, the CH Tax Credit is subject to recovery equal to the difference between the amount of the CH Tax Credit claimed based on the assessed CI and the amount of the CH Tax Credit that would apply based on the actual CI observed during the operations phase. A full recovery of the CH Tax Credit applies if the project produces hydrogen from natural gas without the resulting emissions being abated by CCUS.

## EXPANSION OF CLEAN TECHNOLOGY INVESTMENT TAX CREDIT

The 2022 FES announced the Government's intention to introduce the CTI Tax Credit. The CTI Tax Credit is a 30% refundable tax credit applicable to investments in eligible property that is acquired and becomes available for use on or after Budget Day.

Budget 2023 did not provide more detail regarding what constitutes eligible equipment than what was included in the 2022 FES. The 2022 FES described eligible equipment as follows:

- equipment to generate electricity from solar, wind and water energy that is described under subparagraphs (d)(ii), (iii.1), (v), (vi), and (xiv) of capital cost allowance Class 43.1 (as described in Schedule II to the *Income Tax Regulations* (Canada));
- stationary electricity storage equipment that is described under subparagraphs (d)(xviii) and (d)(xix) of Class 43.1, but that does not use any fossil fuels in operation, which includes, but is not limited to, batteries, flywheels, supercapacitors, magnetic energy storage, compressed air energy storage, pumped hydroelectric energy storage, gravity energy storage, and thermal energy storage;
- active solar heating equipment, air-source heat pumps, and ground-source heat pumps that are described under subparagraph (d)(i) of Class 43.1;
- equipment to generate heat or electricity from concentrated solar energy;
- equipment to generate heat or electricity from small modular nuclear reactors; and
- non-road zero-emission vehicles described in Class 56 (e.g. hydrogen or electric heavy duty equipment used in mining or construction) and charging or refuelling equipment described under subparagraph (d)(xxi) of Class 43.1 or subparagraph (b)(ii) of Class 43.2 that is used primarily for such vehicles.

Notably, the 2022 FES stated that the Government would continue to consult regarding additional eligible technologies, including large scale-nuclear and large-scale hydroelectric.

However, Budget 2023 only expands the property eligible for the CTI Tax Credit to include certain geothermal energy systems. Specifically, property eligible for the credit will include property acquired and available for use on or after Budget Day that is described in subparagraph (d)(vii) of Class 43.1 and that is used primarily for the purpose of generating electrical and/or heat energy solely from geothermal energy. Equipment used for geothermal energy projects that also produce fossil fuels (including oil and gas) is not eligible for the CTI Tax Credit.

Budget 2023 modifies the phase-out of the CTI Tax Credit. The Government now proposes to phase it out gradually, with property that becomes available for use in 2034 eligible for only a 15% credit with no credit being available for property that becomes available for use after 2034.

As noted above, Budget 2023 does not specify whether the CTI Tax Credit will be refundable to tax-exempt entities.

## CLEAN ELECTRICITY INVESTMENT TAX CREDIT

Budget 2023 announces the Government's intention to introduce the CEI Tax Credit to support investments in clean electricity in Canada. The CEI Tax Credit will be a 15 % refundable investment tax credit. It appears there will be significant overlap between equipment eligible for the CTI Tax Credit and the CEI Tax Credit.

Budget 2023 states that both taxable and non-taxable entities may claim the CEI Tax Credit. This significantly differentiates this credit from the CTI Tax Credit.

The credit will be available in respect of costs incurred in developing new projects as well as refurbishing existing facilities and will apply to investments in:

- non-emitting electricity generation systems (wind, concentrated solar, solar photovoltaic, hydro (including large-scale), wave, tidal, nuclear (including both large-scale reactors and small modular reactors));
- abated natural gas-fired electricity generation (subject to an emission intensity threshold compatible with a net-zero grid by 2035);
- stationary electricity storage systems that do not use fossil fuels in operation, including batteries, pumped hydroelectric storage, and compressed air storage; and
- equipment for the transmission of electricity between provinces and territories.

The CEI Tax Credit will be available as of Budget Day 2024 in respect of projects that commenced construction on or after Budget Day. The CEI Tax Credit will not be available after 2034.

Budget 2023 also states that the Government will engage with "provinces, territories, and other relevant parties to develop the design and implementation details of the [CEI Tax Credit]" and that it will "conduct targeted consultations on the possibility to introduce reciprocal treatment in light of some of the eligibility conditions associated with certain tax credits under the U.S. *Inflation Reduction Act*".

## LABOUR REQUIRMENTS FOR CH TAX CREDIT, CTI TAX CREDIT, CEI TAX CREDIT AND CCUS TAX CREDIT

Budget 2023 confirms the Government's intention to apply certain labour requirements to the availability of the CH Tax Credit, CTI Tax Credit and CEI Tax Credit. The labour requirements will apply to work performed on or after October 1, 2023 and the Government states that it wants to receive feedback as it prepares draft legislative proposals.

Specifically, the maximum tax credit rate for the various clean energy tax credits will be available only if the taxpayer satisfies the labour requirements and a reduced rate will apply if the labour requirements are not satisfied as follows:

- the variable rate up to a maximum 40% under the CH Tax Credit (depending on the applicable CI tier) will be reduced by 10%;
- the 30% rate under the CTI Tax Credit will be reduced to 20%;
- the 15% rate under the CEI Tax Credit will be reduced to 5%; and
- the rate during the phase-out periods of the CTI Tax Credit and the CH Tax Credit will be reduced by 10% (to a minimum of 0%).

The labour requirements will apply only in respect of workers whose duties are primarily of a physical or manual nature (*i.e.*, not workers whose duties are administrative, clerical, supervisory or executive). The labour requirements will include a "prevailing wage requirement" that will require workers to be compensated at a level that meets or exceeds the prevailing market wages. The labour requirements will also include an "apprenticeship requirement" that requires not less than 10% of the total labour hours on a subsidized project to be performed by registered apprentices.

A mechanism will be created that will permit a taxpayer to pay corrective remuneration to workers (with interest) and penalties to cure any non-compliance and be deemed to have met the labour requirements.

An exemption from the labour requirements will be available with respect to the application of the CTI Tax Credit to the acquisition of zero-emission vehicles and the acquisition or installation of low-carbon heat equipment.

Budget 2023 also announces the Government's intention to apply labour requirements to the availability of the CCUS Tax Credit. Additional details regarding this measure are to be announced at a later date.

## CLEAN TECHNOLOGY MANUFACTURING INVESTMENT TAX CREDIT

The CTM Tax Credit will be a refundable tax credit for investments in clean technology manufacturing and processing or investments in critical mineral extraction and processing. It will be equal to 30% of the capital cost of "eligible property" that is associated with "eligible activities" and that is acquired and becomes available for use on or after January 1, 2024.

*Eligible Property*

The CTM Tax Credit will be available in respect of certain depreciable property that is used all or substantially all for eligible activities. Eligible property would generally include machinery and equipment, including certain industrial vehicles, used in manufacturing, processing, or critical mineral extraction, as well as related control systems. If the property becomes subject to a change in use, or is sold, within a certain (unspecified) period of time, a portion of the CTM Tax Credit will be clawed back.

*Eligible Activities*

Eligible activities will be:

- processing or recycling nuclear fuels and heavy water;
- extracting (and certain processing related to) critical minerals for clean technology (*i.e.*, lithium, cobalt, nickel, graphite, copper and rare earth elements);
- manufacturing the following:
  - certain solar, wind, water or geothermal energy equipment;
  - nuclear energy equipment and nuclear fuel rods;
  - electrical energy storage equipment for use in providing grid-scale storage or ancillary services;
  - equipment for air and ground source heat pump systems;
  - zero-emission vehicles (including converting an on-road vehicle);
  - batteries, fuel cells, recharging systems and zero-emission vehicle hydrogen refuelling stations (unless, in the case of property used in the production of battery cells or modules if such production benefits from direct support through a Special Contribution Agreement with the Government);
  - equipment for the production of hydrogen from electrolysis; and
  - upstream components, sub-assemblies and materials that are purpose-built for or "designed exclusively to be integral to" eligible clean technology manufacturing and processing activities.

The Government proposes to gradually phase-out the CTM Tax Credit starting with property that becomes available for use in 2032 and to fully phase-out the credits for property that becomes available for use in 2034.

The Government did not specify whether the CTM Tax Credit will be refundable to tax-exempt entities.

## CARBON CAPTURE, UTILIZATION AND STORAGE INVESTMENT TAX CREDIT

In Budget 2021, the Government announced its intention to introduce an investment tax credit for investments in CCUS projects. Following a consultation period that ended on December 2, 2021, Budget 2022: (i) announced the CCUS Tax Credit, (ii) stated that the CCUS Tax Credit would be available to taxpayers incurring eligible expenses on or after January 1, 2022, and (iii) proposed that the CCUS Tax Credit be made available for expenses incurred in a taxation year to acquire or install eligible equipment used in an eligible CCUS project that results in carbon dioxide being used for an eligible use. The Government subsequently released draft legislation in respect of the CCUS Tax Credit on August 9, 2022.

Budget 2023 announces new details regarding the CCUS Tax Credit in response to consultations following the release of the August 9, 2022 draft legislation. The CCUS Tax Credit is now expected to "apply to eligible expenses incurred after 2021 and before 2041" and revised legislative proposals are expected to be released "in the coming months".

*Eligible Equipment*

Eligible equipment is equipment that is put to use in Canada solely to capture, transport, store or use carbon dioxide in an eligible project. Equipment that captures carbon dioxide in Canada, compresses it and transports it to another jurisdiction to be stored will be considered to be used in Canada.

*Eligible Project*

An eligible project is a new project that meets the following conditions:

- captures carbon dioxide directly from the ambient air (Direct Air Capture) or captures carbon dioxide that would otherwise be released into the atmosphere;
- prepares the carbon dioxide for compression;
- compresses and transports the carbon dioxide;
- stores or uses the captured carbon dioxide in a manner that satisfies the storage requirements; and
- is not connected with electricity generation facilities that are required to reduce emissions under the *Reduction of Carbon Dioxide Emissions from Coal-fired Generation of Electricity Regulations* and the *Regulations Limiting Carbon Dioxide Emissions from Natural Gas-fired Generation of Electricity.*

It was not clear from Budget 2022, and it is still not clear, what constitutes a new project.

For geological carbon dioxide storage, the storage requirement is that the project must be located in a jurisdiction where there are sufficient regulations to ensure that carbon dioxide is, according to Environment and Climate Change Canada determinations, permanently stored (as of Budget 2022, only Alberta and Saskatchewan qualified). For concrete storage projects, the storage requirement is that the process used by the project is approved by Environment and Climate Change Canada and 60% of the carbon dioxide injected into the concrete is successfully mineralized and locked into the resulting concrete.

*Eligible Use*

Eligible uses are:

- the storage of carbon dioxide in underground geological formations in eligible jurisdictions; or
- the storage of carbon dioxide in concrete that meets the 60% mineralization requirement as validated by a qualified third party.

The use of carbon dioxide to enhance oil and gas recovery is not an eligible use. If a portion of the eligible expense will not be utilized for an eligible use, the CCUS Tax Credit is reduced by the percentage of carbon dioxide that will be put to the ineligible use.

*CCUS Tax Credit Rates*

The rate of the CCUS Tax Credit depends on the type of expense and when the expense is incurred. Between January 1, 2022 and December 31, 2030, the following rates apply:

- 60% for expenses related to Eligible Equipment used in Direct Air Capture projects;
- 50% for expenses related to Eligible Equipment used in projects other than Direct Air Capture projects; and

- 37.5% for expenses related to eligible transportation, storage and use equipment.

Between January 1, 2031 and December 31, 2040, the rates are one-half of those rates described above.

*Expansion of CCUS Tax Credit*

Budget 2023 outlines the following changes to the CCUS Tax Credit.

- Dual use equipment producing heat or power, or that uses water, and that is used for CCUS together with another process will now be eligible for the CCUS Tax Credit (on a pro-rated basis based on the proportion of energy balance or material balance of the equipment supporting the CCUS process over the first 20 years of the project) provided that the following conditions are satisfied:
  - the equipment meets all other conditions for the availability of the CCUS Tax Credit;
  - where the equipment produces heat or power, more than 50% of the energy balance must be expected to be used to support either the CCUS process or hydrogen production eligible for the CH Tax Credit; and
  - any carbon dioxide emissions resulting from equipment producing heat or power must be used, or must be captured and stored.
- With respect to expenses incurred on or after January 1, 2022, the Province of British Columbia is added to the list of eligible jurisdictions for "dedicated geological storage".
- Instead of obtaining approval from Environment and Climate Change Canada that the process for using and storing carbon dioxide in concrete meets the minimum 60% mineralization requirement, a taxpayer's process must be validated by a "qualified third party" by having their process for carbon dioxide storage evaluated against the ISO 14034:2016 standard "Environmental management – Environmental technology verification" (ISO 14034:2016). For this purpose, a "qualified third party" is proposed to mean a person accredited as a "verification body" under ISO 14034:2016 and ISO/IEC 17020:2012 "Conformity assessment — Requirements for the operation of various types of bodies performing inspection", the Standards Council of Canada, the ANSI National Accreditation Board (U.S.), or any other accreditation organization that is a member of the International Accreditation Forum.

*CCUS Tax Credit for Refurbishment Costs*

Budget 2023 includes a proposal that CCUS Tax Credits related to "eligible refurbishment costs" (Refurbishment Tax Credits) incurred once a project is in the operations phase are to be calculated based on the average expected eligible use ratio for the five-year period in which the refurbishment costs are incurred and in each subsequent five-year period that they contribute to the useful life of the project. The eligible use ratio refers to the portion of the use of the equipment on which refurbishment costs are incurred that are an eligible use as outlined above.

Projects will be eligible for Refurbishment Tax Credits only over the first 20 years of the project. During that 20-year period, the total eligible refurbishment costs are capped at 10% of the aggregate pre-operational costs that were eligible for the CCUS Tax Credit.

The Government proposes that Refurbishment Tax Credits will generally be recovered in the same manner as credits claimed during the construction phase, subject to a shorter recovery period since refurbishment costs are incurred in the operations phase of the project. If the portion of carbon dioxide going to ineligible uses in a particular five-year period is more than 5% higher than the weighted average stated in the project plan for that period, the Refurbishment Tax Credits will be recalculated based on the actual determination of the amount of carbon dioxide going to eligible uses instead of ineligible uses. Where the 10% minimum eligible use threshold is not met in any year during a particular five-year period then Refurbishment Tax Credits in respect of the project will be prohibited in any subsequent five-year period.

### FLOW-THROUGH SHARES AND CRITICAL MINERAL EXPLORATION TAX CREDIT

Canadian exploration expense (CEE) includes certain expenses incurred by a taxpayer for the purpose of determining the existence, location, extent or quality of a mineral resource in Canada. Canadian development expense (CDE) includes certain expenses incurred by a taxpayer in respect of a mine in bringing a new mine in a mineral resource into production and the cost of rights to explore for minerals in a mineral resource.

Lithium was identified as a critical mineral for the purposes of the 30% non-refundable investment tax credit for flow-through critical mineral mining expenditures (CMETC) which applies to certain CEE incurred by a principal-business corporation in conducting mining exploration activity primarily targeting critical minerals and renounced to a subscriber for a flow-through share.

Budget 2023 proposes to include lithium from brines as a mineral resource. This responds to a contrary position taken by the CRA.

Accordingly, eligible exploration and development expenses incurred in relation to lithium brine deposits can qualify as CEE or CDE and can be renounced to flow-through share subscribers and, in the case of CEE, may entitle the subscriber to the CMETC.

Eligible expenses related to lithium from brines made after Budget Day would qualify as CEE and CDE. The expansion of the eligibility for the CMETC to lithium from brines will apply to flow-through share agreements entered into after Budget Day and before April 2027.

### EXTENSION AND EXPANSION OF REDUCED CORPORATE INCOME TAX RATE FOR ZERO-EMISSION TECHNOLOGY MANUFACTURERS

In Budget 2021, the Government announced a temporary measure to reduce corporate income tax rates for certain zero-emission technology manufacturers. In Budget 2023, the Government proposes to extend the reduced tax rates for zero-emission technology manufactures by three years with a gradual phase-out now starting in taxation years beginning in 2032 (previously taxation years beginning in 2029) and fully phased-out for taxation years beginning after 2034 (previously taxation years beginning after 2031).

Budget 2023 expands the activities eligible for the reduced corporate income tax rates for zero-emission technology manufacturers to include certain nuclear manufacturing and processing activities. Specifically, the following activities will now qualify for such reduced rates:

- nuclear energy equipment and nuclear fuel rod manufacturing;
- nuclear fuel processing or recycling; and
- heavy water processing or recycling.

## Frequently Asked Questions[1]

**Can tax exempt entities benefit from the investment tax credits?**

Budget 2023 specifically notes that the CEI Tax Credit described above can be claimed by taxable and non-taxable entities.

[1] All comments herein are of a general nature only and do not constitute tax advice of McCarthy Tétrault LLP. Many of the tax incentives discussed herein are described only in Budget materials and draft legislation has not yet been released or draft legislation is subject to further change. Significant uncertainty regarding the form of legislation that will implement these Budget measures remains. The answers to these questions reflect our current understanding based on imperfect information.

No such specificity was provided in the description of the CH Tax Credit, CTI Tax Credit or CTM Tax Credit for which no draft legislation has been provided.

Draft legislation in respect of the CCUS Tax Credit was released on August 9, 2022 (subject to certain changes specified in Budget 2023 not relevant to this question) and subsection 127.44(3) of the draft legislation provides that tax exempt entities should not benefit from the CCUS Tax Credit.

### When can ITCs in respect of the acquisition of a piece of equipment or property be claimed?

Budget 2023 indicates that, in order to claim CH Tax Credits, CTI Tax Credits or CTM Tax Credits, eligible property must be acquired and be available for use. The available for use requirement relies on the concept of available for use for depreciable property on which a taxpayer can claim capital cost allowance. The delay of a credit until equipment or property is available for use implies that tax credits will not be a source of construction funds because of potential delay between the expenditure and eligibility for the tax credit.

In order to claim CCUS Tax Credits, eligible property need only be acquired (*i.e.*, the tax credit is not subject to the equipment being available for use).

The description of the CEI Tax Credit in Budget 2023 indicates that the credit will be available as of Budget Day 2024 in respect of projects that commenced construction on or after Budget Day (*i.e.*, March 28, 2023). This suggests that no available for use requirement will apply although the description of the program lacks significant detail.

### What is the difference between the CTI Tax Credit and the CEI Tax Credit? Which should we apply for?

There is significant (although not perfect) overlap between the types of equipment that will qualify for both the CTI Tax Credit and the CEI Tax Credit. For instance, non-emitting electricity generation systems such as wind and solar and stationary electricity storage systems that do not use fossil fuels fit the descriptions of equipment that is eligible for both credits. However, for instance, large nuclear reactors are eligible equipment for the CEI Tax Credit but are not currently eligible equipment for the CTI Tax Credit and active solar heating equipment, air-source heat pumps and ground-source heat pumps are eligible equipment for the CTI Tax Credit but are not eligible equipment for the CEI Tax Credit.

Other differences between the two tax credits are as follows:

- the maximum tax credit rate for the CTI Tax Credit is 30% while the tax credit rate for the CEI Tax Credit is 15%;
- the CTI Tax Credit does not appear to be available to tax-exempt entities (or at least the description of the credit in the 2022 Fall Economic Statement and Budget 2023 is silent on the matter) while the CEI Tax Credit is available to taxable entities and tax-exempt entities;
- the CTI Tax Credit is available in respect of eligible property that is acquired and becomes available for use on or after Budget Day while the CEI Tax Credit is available after Budget Day 2024 in respect of projects that commenced construction on or after Budget Day; and
- the CEI Tax Credit includes certain refurbishment costs of existing facilities and there is no indication that refurbishment costs could qualify for the CTI Tax Credit.

A taxpayer considering whether to apply for the CTI Tax Credit or the CEI Tax Credit, in circumstances where acquired equipment clearly satisfies the eligibility requirements of both, should weigh the above differences in making a choice. It appears a tax-exempt entity will prefer the CEI Tax Credit (unless further clarity regarding the potential for a tax-exempt entity to claim the CTI Tax Credit is provided). In other circumstances, a taxpayer likely will prefer the CTI Tax Credit because of the higher tax credit rate of 30% and the current availability of the credit.

**Can ITCs be transferred to an arm's length purchaser of a project? What is the effect of a sale of a project to an arm's length purchaser before completion on the ability of a taxpayer to claim an investment tax credit?**

ITCs are claimed by a taxpayer and are generally not transferrable under Canadian tax law. Budget 2023 did not indicate that any such rules would be introduced.

If a project is sold prior to completion, there is no indication in Budget 2023 or the related documents that a taxpayer's ability to claim an ITC should be compromised. As explained in answer to the prior question, if the relevant ITC is the CCUS Tax Credit, the taxpayer is eligible for the ITC when the eligible property is acquired. If the relevant ITC requires that eligible property be available for use, then paragraph 13(27)(c) should deem the property to have become available for use immediately prior to its disposition.

If control of a taxpayer is acquired, the Tax Act contains certain rules that restrict the carry-forward and carry-back of ITCs. However, these rules are generally of no consequence when dealing with refundable ITCs because refundable ITCs are generally claimed in the year of entitlement reducing tax payable to nil and the remainder paid in cash rather than being carried forward or back. All ITCs discussed herein are described in Budget 2023 and related documents as refundable ITCs.

**Will hybrid projects (*i.e.,* solar and storage or wind and storage) qualify for the CTI Tax Credit?**

Eligibility for the CTI Tax Credit will depend on the specific type of equipment acquired as opposed to the overall project in which the type of equipment is integrated.

Budget 2023 did not provide more detail regarding what constitutes eligible equipment than what was included in the 2022 Fall Economic Statement. The 2022 Fall Economic Statement described eligible equipment as follows:

- equipment to generate electricity from solar, wind and water energy that is described under subparagraphs (d)(ii), (iii.1), (v), (vi), and (xiv) of capital cost allowance Class 43.1;
- stationary electricity storage equipment that is described under subparagraphs (d)(xviii) and (d)(xix) of Class 43.1, but that does not use any fossil fuels in operation, which includes, but is not limited to, batteries, flywheels, supercapacitors, magnetic energy storage, compressed air energy storage, pumped hydroelectric energy storage, gravity energy storage, and thermal energy storage;
- active solar heating equipment, air-source heat pumps, and ground-source heat pumps that are described under subparagraph (d)(i) of Class 43.1;
- equipment to generate heat or electricity from concentrated solar energy;
- equipment to generate heat or electricity from small modular nuclear reactors; and
- non-road zero-emission vehicles described in Class 56 (e.g. hydrogen or electric heavy duty equipment used in mining or construction) and charging or refuelling equipment described under subparagraph (d)(xxi) of Class 43.1 or subparagraph (b)(ii) of Class 43.2 that is used primarily for such vehicles.

Budget 2023 expanded the type of equipment eligible for the credit to include depreciable property acquired and available for use on or after Budget Day that is described under subparagraph (d)(vii) of Class 43.1 and that is used primarily for the purpose of generating electrical and/or heat energy solely from geothermal energy (provided the equipment has not been used for any purpose before its acquisition).

**Is there a limited pool of Government funds from which ITCs will be provided? Will projects compete for ITCs?**

There is no indication in Budget 2023 or related documents that there is a limited pool of funds from which the ITCs described herein will be provided. There is no indication that projects will compete for ITCs.

**How do the investment tax credits interact with one another? How do the investment tax credits interact with the Atlantic Investment Tax Credit?**

Where a particular property or equipment could be eligible for more than one of the tax credits described herein, a taxpayer will be able to claim only one of the tax credits. It is possible that a particular project could include properties or equipment that are entitled to different credits.

It is intended that a taxpayer can claim the CH Tax Credit, the CTI Tax Credit, CTM Tax Credit and CEI Tax Credit without affecting its claim for the Atlantic Investment Tax Credit. It is not apparent at the time of publication whether this is also true of the CCUS Tax Credit (although we expect that such clarification will be provided).

**What are the labour conditions required to maximize the investment tax credits?**

As indicated in the 2022 Fall Economic Statement and confirmed in Budget 2023, in order to claim maximum CH Tax Credits, CTI Tax Credits and Clean Energy Investment Tax Credits, taxpayers will need to satisfy certain labour condition requirements. Budget 2023 also announces the Government's intention to apply labour requirements to the availability of the CCUS Tax Credit. Budget 2023 states that the labour requirements will apply to work performed on or after October 1, 2023 and that the Government is interested in receiving feedback as it prepares draft legislative proposals.

Budget 2023 outlines that the labour requirements will only apply in respect of workers whose duties are primarily of a physical or manual nature (*i.e.*, not workers whose duties are administrative, clerical, supervisory or executive) and will apply to workers directly employed or indirectly employed to work on the project. The labour requirements will include a "prevailing wage requirement" that will require workers to be compensated at a level that meets or exceeds the relevant wage. The labour requirements will also include an "apprenticeship requirement" that requires not less than 10% of the total labour hours on a subsidised project to be performed by registered apprentices.

The Government intends to create a mechanism that will permit taxpayers to pay corrective remuneration to workers (with interest) and penalties to resolve non-compliance and be deemed to have met the labour requirements.