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Québec Announces Tax Relief for Individuals Holding Interests in Public Corporations

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On February 21, 2017, Québec's Ministère des Finances released Information Bulletin 2017-3 announcing tax measures (i) to increase the deduction for stock options of publicly traded large businesses; (ii) to extend, to all sectors of activity, tax relief for the transfer of family businesses; and (iii) to allow for the deferral of income tax payment on certain deemed dispositions of interests in a qualified public corporation..

Increase in Deduction for Stock Options of Publicly Traded Large Businesses

Stock options receive preferential tax treatment. In general, an employee is required to include, in computing his or her income, the value of a benefit the employee was deemed to have received for a stock option granted by the employer. Such an employee may deduct, in computing his or her taxable income, an amount ranging from 25% to 50% of the value of the benefit, subject to certain conditions.

At the federal level and in all Canadian provinces other than Québec, the deduction is 50%. Since March 31, 2004, Québec had deviated from the Canadian approach by applying a deduction rate of 25%, except for small or medium-sized businesses engaged in innovative activities.[1]

In order to offer a comparably competitive tax environment relative to the rest of Canada, Québec announced that the rate of the stock option deduction will increase to 50%, from 25%, in the case of options for shares of publicly traded corporations having a strong presence in Québec; this generally refers to corporations that pay wages of at least $10 million to employees who work at an establishment in Québec.[2]

The increased stock option deduction rate will apply to options granted after February 21, 2017.

Extension, to All Sectors of Activity, of Tax Relief for the Transfer of Family Businesses

In the March 2016 budget speech, the government of Québec had announced that, subject to certain conditions, shareholders disposing of shares in a small business corporation in the primary or manufacturing sector to non-arm's-length persons after March 17, 2016 could treat the gain arising therefrom as a capital gain rather than a dividend; previously, this tax treatment had been reserved for transactions between persons dealing at arm's length. This relief allows individuals to whom this measure applies to benefit from the capital gains exemption in certain cases.

This relief is being extended to all sectors of the economy and will apply retroactively to dispositions after March 17, 2017.

Deferral of Income Tax Payment on Certain Deemed Dispositions of Interests in a Qualified Public Corporation

Lastly, Information Bulletin 2017-3 introduces a measure for the deferral of income tax payments on capital gain arising from the deemed disposition of shares of certain public corporations upon the death of the shareholder or upon the application of the 21-year rule to a trust that owns the shares. This measure applies to any deemed disposition of a qualified share that occurs after February 21, 2017.

The announced measure will allow for the deferral of income tax payment as long as the shares of the corporation are not actually sold or as long as the qualification criteria are met, up to a maximum of 20 years. The measure also provides additional payment flexibility if the value of the shares decreases between the date of the initial income tax deferral and the date on which the tax becomes payable.

For a public corporation to qualify for the income tax deferral, it must have its head office in Québec and maintain an average payroll in Québec, over three years, equal to at least 75% of the payroll in Québec at the time of the application for deferral. It remains to be seen if a minimum payroll in Québec will be required, as is the case for the increase of the deduction for stock options of publicly traded large businesses discussed above.

For an individual or trust to qualify for the income tax deferral, it must hold, directly or indirectly, for as long as the income tax is being deferred, a number of shares representing more than one-third of the corporation's voting rights. It is unclear how this criterion will apply in the case of a succession where there is a deemed disposition of the shares upon death.

A share of a private corporation is qualified if more than 95% of its value is attributable to shares of a public corporation that, in all circumstances, give it more than one-third of the public corporation's voting rights.

To take advantage of the deferral, the taxpayer will be required to furnish security whose value, at all times, is at least 120% of the amount of the deferred income tax.

[1] For an option granted after March 13, 2008, by a small or medium-sized business engaged in innovative activities, the amount that may be deducted is increased to 50% of the value of the benefit.

[2] Or wages that the corporation is deemed to pay to employees of such an establishment in Québec.

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