

Canada's Proposed Clean Energy Tax Credits: Where Are We Now?

Tax Law Bulletin | December 4, 2023

The Canadian government has proposed five new refundable investment tax credits (ITCs) designed to grow Canada's clean economy and allow Canada to remain competitive in attracting investment in clean energy projects.

- **The Clean Technology ITC**: A refundable tax credit of up to 30% of investments in eligible property acquired and available for use on or after March 28, 2023 and before 2034. For property that becomes available for use in 2034, this tax credit would be up to 15%. No tax credit would be available for property that becomes available for use after 2034.
- **The Carbon Capture, Utilization and Storage ("CCUS") ITC**: A refundable tax credit for expenditures incurred between January 1, 2022 and December 31, 2030 of:
 - up to 60% of Qualified Carbon Capture Expenditures incurred to capture carbon from ambient air;
 - up to 50% of Qualified Carbon Capture Expenditures incurred to capture carbon other than directly from ambient air; and
 - up to 37.5% of Qualified Carbon Transportation Expenditures, Qualified Carbon Storage Expenditures and Qualified Carbon Use Expenditures.

For the period January 1, 2031 to December 31, 2040, the tax credit would be reduced by one-half and no tax credit would be available after 2040.

- **The Clean Hydrogen ITC**: A refundable tax credit of up to 40% of investments in projects that produce hydrogen and become available for use on or after March 28, 2023 and before 2034. For investments that become available for use in 2034, this tax credit would generally be reduced by one-half. No tax credit would be available for property that becomes available for use after 2034.
- **The Clean Electricity ITC**: A refundable tax credit of up to 15% of investments in projects that generate clean electricity, store electricity without the use of fossil fuels, or transmit electricity between provinces and territories. This tax credit would be available as of the day that the 2024 federal budget is delivered for projects that did not begin construction before March 28, 2023. No tax credit would be available after 2034.
- **The Clean Technology Manufacturing ITC**: A refundable tax credit of 30% of investments in eligible property to be used in clean technology manufacturing and critical mineral extraction and processing that is acquired and available for use in 2024 to 2031. This tax credit would reduce to 20% for 2032, 10% for 2033 and 5% for 2034.

None of these tax credits have yet been passed into law:

- **The Clean Technology ITC and the Carbon Capture, Utilization and Storage ITC:** Draft legislation for these tax credits received first reading in Parliament on November 30, 2023.
- **The Clean Hydrogen ITC and the Clean Technology Manufacturing ITC:** According to the Fall Economic Statement tabled by the federal government on November 21, 2023 (the “**2023 Fall Economic Statement**”), consultations on draft legislation will launch this fall.
- **The Clean Electricity ITC** (for publicly-owned utilities): According to the 2023 Fall Economic Statement, consultations with provinces and territories will take place in 2024.
- **The Clean Electricity ITC** (for non-publicly-owned utilities): According to the 2023 Fall Economic Statement, design and implementation details will be published in early 2024.

These are refundable tax credits. That is, these tax credits would be treated as amounts that have been paid by the taxpayer on account of tax, and if no more tax is payable for the year, the taxpayer would receive a refund.

Taxpayers would generally be able to claim only one of these tax credits in respect of the acquisition of an eligible property, even if the particular property would be eligible for more than one of these tax credits.

This bulletin provides a description of each of these proposed tax credits. Following these descriptions, certain tax considerations that are relevant to the design of these tax credits are discussed.

The Tax Credits

1. *The Clean Technology ITC*

The Clean Technology ITC is designed “to encourage the investment of capital in the adoption and operation of clean technology property in Canada.”

The Clean Technology ITC would be available only to taxable Canadian corporations that make investments in eligible property, including taxable Canadian corporations that are members of a partnership that makes an investment in eligible property.

The Clean Technology ITC would provide a 30% refundable tax credit for investments in eligible property acquired and available for use on or after March 28, 2023 until December 31, 2033. Property that is acquired and available for use in 2034 would be eligible for a 15% refundable tax credit. No tax credit would be available for property that is acquired and available for use after 2034.

To be eligible for the Clean Technology ITC at the rates described above, a taxpayer must satisfy certain labour requirements. The labour requirements are generally met by paying “covered workers” in accordance with a collective agreement (or by paying amounts that similar workers are paid under a collective agreement) and by ensuring that at least 10% of the labour performed by workers in Red Seal trades is performed by registered apprentices. Taxpayers that do not elect to meet the labour requirements could claim the Clean Technology ITC at the above-noted rates reduced by 10 percentage points.

The types of property that would be eligible for the Clean Technology ITC include:

- certain equipment used to generate electricity from solar, wind and water energy;
- certain electricity storage equipment, but excluding equipment that uses any fossil fuel in operation;
- certain active solar heating equipment, air-sourced heat pumps and ground-source heat pumps;

- certain non-road zero-emission electric and hydrogen powered vehicles, and charging and refueling equipment that is used primarily for such vehicles;
- certain equipment used exclusively for the purpose of generating electrical energy and/or heat energy solely from geothermal energy, but excluding any equipment that is part of a system that extracts both heat from geothermal fluid and fossil fuel for sale;
- certain equipment used to generate heat and/or electricity from concentrated sunlight; and
- certain equipment that is used to generate electrical energy and/or heat energy from nuclear fusion.

However, to be eligible for the Clean Technology ITC,

- the property must generally be situated in Canada and intended for use exclusively in Canada;
- the property must be new when acquired by the taxpayer; and
- if the property is to be leased by the taxpayer to another person,
 - the lessee must be a taxable Canadian corporation or a partnership all the members of which are taxable Canadian corporations; and
 - the equipment must be leased in the ordinary course of carrying on a business in Canada by the taxpayer whose principal business is selling or servicing property of that type, or whose principal business is leasing property, lending money, purchasing conditional sales contracts, accounts receivable, bills of sale, chattel mortgages or hypothecary claims on movables, bills of exchange or other obligations representing all or part of the sale price of merchandise or services, or any combination thereof.

The Clean Technology ITC would potentially be subject to “recapture” if, within 20 calendar years of the acquisition of the eligible property the property is converted to a non-clean technology use, is exported from Canada or is disposed of by the taxpayer.

The 2023 Fall Economic Statement proposed to expand eligibility for the Clean Technology ITC to include systems that produce electricity and/or heat from waste biomass. The expansion of the Clean Technology ITC to include waste biomass systems would be available for eligible property that is acquired and becomes available for use on or after November 21, 2023.

2. The Carbon Capture, Utilization and Storage ITC

The CCUS ITC is designed “to encourage the investment of capital in the development and operation of carbon capture, transportation, utilization and storage capacity in Canada.”

The CCUS ITC would be available only to taxable Canadian corporations that make investments in eligible property, including taxable Canadian corporations that are members of a partnership that makes an investment in eligible property.

The CCUS ITC would provide a refundable tax credit for expenditures incurred between January 1, 2022 and December 31, 2030 as follows:

- 60% for Qualified Carbon Capture Expenditures incurred to capture carbon from ambient air;
- 50% for Qualified Carbon Capture Expenditures incurred to capture carbon other than directly from ambient air; and

- 37.5% for Qualified Carbon Transportation Expenditures, Qualified Carbon Storage Expenditures and Qualified Carbon Use Expenditures.

For the period January 1, 2031 to December 31, 2040, the tax credit would be reduced to one-half of the rates described above, and no tax credit would be available after 2040. Taxpayers that do not elect to meet the labour requirements (see the description of the labour requirement in the description of the Clean Technology ITC above) could claim the CCUS ITC at the above-noted rates reduced by 10 percentage points.

Qualified Carbon Capture Expenditures, Qualified Carbon Transportation Expenditures, Qualified Carbon Storage Expenditures and Qualified Carbon Use Expenditures would be required to be incurred in respect of a “Qualified CCUS Project” of a taxpayer.

- A Qualified CCUS Project must be a “CCUS Project” that is intended to support a “CCUS Process”. A CCUS Process is the process of carbon dioxide capture, utilization and storage that includes the capture of carbon dioxide that would otherwise be released into the atmosphere, the capture of carbon dioxide directly from the ambient air, and the storage or use of the captured carbon dioxide.
- A Qualified CCUS Project would also need to meet several conditions. The definitional regime is extremely complex. Simplified, a Qualified CCUS Project would be a CCUS Project if:
 - there is a “project plan” – which project plan reflects a front-end engineering design study, describes the quantity of captured carbon dioxide that the project is expected to support for storage or use over the project’s “total CCUS project review period” (which is generally approximately 20 years), contains information as required in guidelines published by the Minister of Natural Resources, and is filed with the Minister of Natural Resources before the first day of commercial operations;
 - it is expected, based on the project’s most recent project plan, to support the capture of carbon dioxide in Canada for a period at least equal to the total CCUS project review period;
 - an initial project evaluation has been issued by the Minister of Natural Resources;
 - its “projected eligible use percentage” is at least 10% for each year of the project’s total review period (an “eligible use” being the storage of captured carbon dioxide in dedicated geological storage or the use of captured carbon dioxide in producing concrete in Canada or the United States in a “qualified concrete storage process”, an “ineligible use” being any other use);
 - it is not a project that is operated to service a “unit” with a commissioning date that is on or before April 8, 2022; and
 - it is not a project that is undertaken for the purpose of complying with certain emission standards.

Qualified Carbon Capture Expenditures in respect of a Qualified CCUS Project would be a portion of an expenditure incurred to acquire property that is used for the capture aspect of a CCUS Project (in contrast to property used in other parts of a CCUS project, such as for transportation, storage or use). The portion of the expenditure that would be eligible depends on (i) the project’s “projected eligible use percentage” and (ii) the remaining portion of the project’s total review period (that is, the later in the project’s total review period in which the expenditure is incurred, the lower the percentage of the expenditure that would be included). The types of property that are ineligible for the CCUS ITC include equipment that is expected to be used for hydrogen production, natural gas processing or acid gas injection and property situated outside of Canada. The types of property that would be eligible for the CCUS ITC include:

- equipment that is to be used solely for capturing carbon dioxide that would otherwise be released into the atmosphere or solely for capturing carbon dioxide directly from the ambient air (but not including oxygen production equipment);

- equipment that prepares or compresses captured carbon dioxide for transportation;
- equipment that generates or distributes electrical energy and/or heat energy that solely supports a CCUS Process (excluding equipment that uses fossil fuels and emits carbon dioxide that is not subject to capture by a CCUS Process), including certain transmission equipment;
- equipment that collects, recovers, treats and/or recirculates water that solely supports a CCUS Process; and
- “dual use equipment” (but only a portion of the cost of dual use equipment would be included as a Qualified Carbon Capture Expenditure).

Qualified Carbon Transportation Expenditures in respect of a Qualified CCUS Project would be a portion of an expenditure incurred to acquire equipment situated in Canada that is to be used solely for transportation of captured carbon dioxide, including equipment used for the transportation system safety and integrity. As with Qualified Carbon Capture Expenditures, the portion of the expenditure that is eligible depends on the project’s “projected eligible use percentage” and the remaining portion of the project’s total review period.

Qualified Carbon Storage Expenditures in respect of a Qualified CCUS Project would be the cost of equipment situated in Canada that is used solely for storage of captured carbon dioxide in “dedicated geological storage” (other than for enhanced oil recovery) in a “designated jurisdiction” in Canada or the United States (currently, Alberta, Saskatchewan and British Columbia are designated jurisdictions).

Qualified Carbon Use Expenditures in respect of a Qualified CCUS Project would be the cost of equipment situated in Canada to be used solely for using carbon dioxide in industrial production (including for enhanced oil recovery) that is expected to support storage or use of captured carbon dioxide solely in producing concrete in Canada or the United States using a “qualified concrete storage process”.

Qualified Carbon Capture Expenditures, Qualified Carbon Transportation Expenditures, Qualified Carbon Storage Expenditures, and Qualified Carbon Use Expenditures would also include certain ancillary equipment that is physically and functionally integrated with the equipment described above and is used solely to support the equipment described above; equipment used for safety and integrity or as part of a control or monitoring system to support the equipment described above; and a building or other structure all or substantially all of which is used, or to be used, for the installation or operation of the equipment described above.

A few additional considerations:

- The CCUS ITC would only be available in respect of new property.
- The CCUS ITC regime contemplates a recovery tax that may apply where the “projected eligible use percentage” is no longer projected or is not achieved. Recovery tax may also be payable if the taxpayer disposes of the property or exports the property from Canada.

3. **The Clean Hydrogen ITC**

No draft legislation has been released to date for the proposed Clean Hydrogen ITC. The following description is based on the details provided in the 2023 federal budget and the 2023 Fall Economic Statement.

The Clean Hydrogen ITC would provide a refundable tax credit for investments in eligible equipment available for use in Canada for projects that produce hydrogen from electrolysis or from natural gas (provided that emissions are abated using CCUS). Hydrogen projects would need to have completed a front-end engineering study to be eligible for the Clean Hydrogen ITC.

For property that becomes available for use on or after March 28, 2023 and before 2034, the tax credit rate would be, depending on the carbon intensity of the hydrogen that is produced, 40%, 25% or 15%. For property that becomes available for use in 2034, the tax credit rate would be reduced by one-half. No tax credit would be available for property that becomes available for use after 2034.

Property that is required to convert clean hydrogen to clean ammonia would also be eligible for the Clean Hydrogen ITC at a tax credit rate of 15%.

Taxpayers that do not elect to meet the labour requirements (see description of the labour requirements in the description of the Clean Technology ITC above) could claim the Clean Hydrogen ITC at the above-noted rates reduced by 10 percentage points.

4. The Clean Electricity ITC

No draft legislation has been released to date for the proposed Clean Electricity ITC. The following description of the Clean Electricity ITC is based on the details provided in the 2023 federal budget and the 2023 Fall Economic Statement.

The Clean Electricity ITC would be available to taxable and non-taxable entities such as Crown corporations, publicly owned utilities, corporations owned by Indigenous communities, and pension funds.

The Clean Electricity ITC would provide a 15% refundable tax credit for eligible investments in:

- non-emitting electricity generation systems: wind, concentrated solar, solar photo-voltaic, hydro, wave, tidal and nuclear;
- certain abated natural gas-fired electricity generation;
- stationary electricity storage systems that do not use fossil fuels in operation; and
- equipment for the transmission of electricity between provinces and territories,

Both new projects and the refurbishment of existing facilities would be eligible.

Taxpayers that do not elect to meet the labour requirements (see description of the labour requirements in the description of the Clean Technology ITC above) would claim the Clean Electricity ITC at the above-noted rates reduced by 10 percentage points.

The Clean Electricity ITC would be available as of the day that the 2024 federal budget is delivered, for projects that did not begin construction before March 28, 2023. The Clean Electricity ITC would not be available after 2034.

The 2023 Fall Economic Statement proposed to expand eligibility for the Clean Electricity ITC to include systems that produce electricity or both electricity and heat from waste biomass. The expansion of the Clean Electricity ITC would be available as of the date of the 2024 federal budget for projects that did not begin construction before March 28, 2023.

5. The Clean Technology Manufacturing ITC

No draft legislation has been released to date for the proposed Clean Technology Manufacturing ITC. The following description of the Clean Technology Manufacturing ITC is based on the details provided in the 2023 federal budget.

It appears that the Clean Technology Manufacturing ITC would only be available to Canadian corporations.

The Clean Technology Manufacturing ITC would provide a refundable tax credit for investments in eligible property to be used in clean technology manufacturing and critical mineral extraction and processing.

The Clean Technology Manufacturing ITC would apply to eligible property acquired and available for use in 2024 to 2034. This tax credit would be 30% for property that becomes available for use in 2024 to 2031 and would reduce to 20% for 2032, 10% for 2033 and 5% for 2034.

Eligible property would include machinery and equipment, including certain industrial vehicles, used in manufacturing, processing or critical mineral extraction, as well as related control systems. Eligible activities would include:

- manufacturing of certain renewable energy equipment (solar, wind, water or geothermal);
- manufacturing of nuclear energy equipment;
- processing or recycling of nuclear fuels and heavy water;
- manufacturing of nuclear fuel rods;
- manufacturing of electrical storage equipment used to provide grid-scale storage or other ancillary services;
- manufacturing of equipment for air-source and ground-source heat pump systems;
- manufacturing of zero-emission vehicles, including conversions of on-road vehicles;
- manufacturing of batteries, fuel cells, recharging systems, and hydrogen refuelling stations for zero-emission vehicles;
- manufacturing of equipment used to produce hydrogen from electricity;
- manufacturing or processing of upstream components, sub-assemblies, and materials provided that the output would be purpose-built or designed exclusively to be integral to other eligible clean technology manufacturing and processing activities, such as anode and cathode materials used for electric vehicle batteries; and
- the extraction and processing activities related to six critical minerals essential for clean technology supply chains: lithium, cobalt, nickel, graphite, copper and rare earth elements.

Certain Tax Considerations

Use of Partnerships

As discussed above, the Clean Technology ITC and the CCUS ITC are available to taxable Canadian corporations that make investments in eligible property, including taxable Canadian corporations that are members of a partnership that makes an investment in eligible property.

With respect to the other refundable tax credits, the 2023 federal budget materials:

- do not provide guidance with respect to the types of taxpayers that would be eligible for the Clean Hydrogen ITC;

- provide that the Clean Electricity ITC would be available to “taxable and non-taxable entities such as Crown corporations and publicly owned utilities, corporations owned by Indigenous communities, and pension funds...”; and
- indicate that the Clean Technology Manufacturing ITC would be available in respect of “investments by corporations”.

That is, it is not entirely clear what entities are entitled to these three tax credits or whether these three tax credits would be available to taxpayers that are partners in a partnership that makes an investment in eligible property.

At-Risk Amount Limitation

The Clean Technology ITC and the CCUS ITC incorporate existing rules that limit the amount of investment tax credits that can be allocated to limited partners. Simplified, the amount of the credit that can be allocated to a limited partner is limited by the limited partner’s “expenditure base” and the limited partner’s “at-risk amount”. These amounts reflect, in part, the amount invested in the limited partnership by the limited partner.

Draft legislation released on August 4, 2023 addressing the Clean Technology ITC and the CCUS ITC left open the possibility that these rules could result in a denial of a Clean Technology ITC or a CCUS ITC otherwise available to be allocated to limited partners. This possibility would especially have been the case where the cost of the eligible property was financed with money borrowed by the limited partnership (and not by amounts contributed by the limited partners that would serve to increase the limited partner’s “expenditure base” or “at-risk amount”).

The draft legislation tabled in Parliament on November 30, 2023 has mitigated this issue.

Tax Shelters and Tax Shelter Investments

The Canadian *Income Tax Act* contains rules that apply to “tax shelters” and “tax shelter investments”. The tax shelter rules provide the government with an effective means of identifying tax shelters and the identity of the participants. The tax shelter investment rules can apply to reduce a taxpayer’s cost in a tax shelter investment and may deny any expenditures incurred by the tax shelter investment itself. All investments that are tax shelters are also tax shelter investments.

The Clean Technology ITC is denied if the clean technology property – or an interest in a person or partnership that has, directly or indirectly, an interest in such property – is a tax shelter investment.

The CCUS ITC is denied in respect of a CCUS project (the entire project!) if a property used in the project – or an interest in a person or partnership that has, directly or indirectly, an interest in such property – is a tax shelter investment.

Global Minimum Tax

The Canadian government released a draft *Global Minimum Tax Act* on August 4, 2023. If enacted, the *Global Minimum Tax Act* would implement a global minimum tax in connection with Canada’s membership in the OECD/G20 Inclusive Framework on BEPS. The *Global Minimum Tax Act* is proposed to be effective for fiscal years beginning on or after December 31, 2023.

Simplified, the *Global Minimum Tax Act* is meant to ensure that large multinationals (annual consolidated revenues of EUR 750 million or more) with a business presence in at least one foreign jurisdiction are subject to a tax rate of at least 15% of income for accounting purposes, as adjusted.

Refundable tax credits are generally treated as a reduction in the cost of the relevant asset for purposes of the Canadian *Income Tax Act*. However, refundable tax credits are generally treated as income for the purposes of the *Global Minimum Tax Act*. The inclusion of refundable tax credits in income for the purposes of the *Global Minimum Tax Act* could reduce the effective tax rate for the purposes of the Global Minimum Tax Act to a rate that is below 15%, resulting in the payment of a “top-up” tax.

Author



Alex Pankratz
Partner
+1 416 865 4459
apankratz@fasken.com

Fasken is a leading international law firm with more than 950 lawyers and 10 offices on three continents. Clients rely on us for practical and innovative legal services.

We provide results-driven strategies to solve the most complex business and litigation challenges.



VANCOUVER	550 Burrard Street, Suite 2900	+1 604 631 3131	vancouver@fasken.com
SURREY	13401 - 108th Avenue, Suite 1800	+1 604 631 3131	surrey@fasken.com
TSUUT'INA	11501 Buffalo Run Boulevard, Suite 211	+1 403 261 5350	tsuutina@fasken.com
CALGARY	350 7th Avenue SW, Suite 3400	+1 403 261 5350	calgary@fasken.com
TORONTO	333 Bay Street, Suite 2400	+1 416 366 8381	toronto@fasken.com
OTTAWA	55 Metcalfe Street, Suite 1300	+1 613 236 3882	ottawa@fasken.com
MONTRÉAL	800 Victoria Square, Suite 3500	+1 514 397 7400	montreal@fasken.com
QUÉBEC	365 Abraham-Martin Street, Suite 600	+1 418 640 2000	quebec@fasken.com
LONDON	6th Floor, 100 Liverpool Street	+44 20 7917 8500	london@fasken.com
JOHANNESBURG	Inanda Greens, 54 Wierda Road West, Sandton 2196	+27 11 586 6000	johannesburg@fasken.com

FASKEN

Own tomorrow

fasken.com