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Update on Manufacturing Enterprises in Quebec

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On-line Tax Strategies

Manufacturing enterprises are the pillars of the Quebec economy. Over the years, several tax measures have been announced to encourage investments in this sector.

The following is a summary of the principal tax measures that deal more specifically with manufacturing enterprises in 2019.

TAX RATES

The following table illustrates the tax rates in effect for federal and Quebec purposes in 2019:

Business income	Eligible for the SBD[1] %	Other %
Quebec	6.0[2]	11.6[3]
Federal	9.0	15.0
Combined rates	*15.0*	*26.6*

Reduced rate for primary and manufacturing sectors SMEs - Quebec

In Quebec, primary and manufacturing[4] sectors small and medium enterprises (SMEs) benefit from an additional deduction of up to 2%[5] from their income that is otherwise eligible for the SBD such that the tax rate applicable to this income can be reduced by up to 4%.

Generally, an eligible corporation may benefit from the full additional deduction if its labour expenditures attributable to primary and manufacturing sectors activities represent 50% or more of its total labour expenditures for the year.[6]

Deduction for innovative manufacturing corporations – Quebec

The deduction for innovative manufacturing corporations (DIC) is available to large manufacturing corporations[7] that are not eligible for the SBD and that market a product incorporating a patent. The DIC reduces to 4 % the tax rate on income from the sale or lease of qualifying property, i.e. property incorporating a patented feature.[8]

CAPITAL COST ALLOWANCE

Generally, all depreciable properties acquired after November 20, 2018 and available for use before 2024 are eligible for an accelerated capital cost allowance (CCA) in the first year equal to 150% of the CCA otherwise calculated using the rate applicable to the class.[9] In addition, certain properties used for manufacturing and processing (M&P) purposes are eligible for an enhanced or additional CCA.

Machinery and equipment used for M&P purposes[10]

Machinery and equipment used for the M&P of goods destined for sale or lease are eligible for an accelerated CCA in the first year, [11] at the following rates:

- 100% of the cost of property that becomes available for use before 2024;

1 Generally, the small business deduction (SBD) is granted to Canadian-controlled private corporations (CCPC) for the first $500,000 of business income. The SBD is gradually reduced when the paid-up capital of all associated corporations exceeds $10M and is completely eliminated when it reaches $15M.

2 This rate will drop to 5% in 2020 then to 4% in 2021.

3 This rate will decrease to 11.5% in 2020.

4 That is, activities attributable to the agriculture, forestry, fishing and hunting sector or the mining, quarrying and oil and gas extraction sector, which are grouped under NAICS codes 11 and 21.

5 Additional deduction reduced to 1% in 2020 and completely eliminated in 2021 whereas the rate of income eligible for the SBD will reach 4% for all SMEs in Quebec.

6 The rate of the additional deduction is reduced when the proportion is between 25% and 50% (nil when it reaches 25%).

7 That is, a corporation whose labour expenditures attributable to manufacturing activities represent 50% or more of its total labour expenditures for the year.

8 The corporation must be the owner, alone or with others, of the patent and the invention that led to the patent must result in part or in whole from research and development work carried out in Quebec.

9 The "half-year rule", which limits the CCA granted for the first taxation year on property to one-half of the depreciation otherwise calculated, is suspended (and therefore not applicable) for property acquired after November 20, 2018 that becomes available for use before 2028.

10 Property included in Class 53.

11 For property acquired after November 20, 2018. Before this date, the property benefitted from a CCA calculated at a rate of 50% on the declining balance.

- 75% of the cost of property that becomes available for use in 2024 or 2025;
- 55% of the cost of property that becomes available for use in 2026 or 2027.

Example: A taxpayer acquires Class 53 property for $1,000 in 2019. He/she will be able to deduct the full cost of this property ($1,000) in the year.

Building used for M&P purposes

New buildings acquired for M&P purposes qualify for an additional CCA, which increases the CCA rate from 4%[12] to 6% or 10%, as applicable:

- Building used 90% or more for M&P purposes: CCA rate of 10%;
- Building used 90% or more for non-residential purposes: CCA rate of 6%.

Additions and modifications to an eligible building can also benefit from the additional CCA.

Trucks and tractors designed to transport merchandise (Class 16)

Vehicles designed for the transportation of property included in Class 16 are eligible for a CCA calculated at a rate of 40% for federal purposes. In Quebec, a 60% enhanced CCA rate applies to such new vehicles.

Thanks to the enhanced temporary CCA measure applicable to all properties in the first year, the CCA is particularly interesting for these vehicles in general. In addition, if the vehicle is a new zero-emission[13] vehicle acquired after March 18, 2019 and before 2024, a 100% CCA is granted in the first year.

Example: A corporation acquires a new truck included in Class 16 for $100,000 in 2019. It will be able to deduct $60,000[14] for federal purposes and $90,000[15] in Quebec in the first year.[16] The following year, if no new acquisition is made, the corporation will be able to claim a CCA of 40% for federal purposes and 60% in Quebec on the undepreciated capital cost (UCC) of the class. If it is a zero-emission vehicle, a CCA of $100,000 can be claimed in 2019.

The following table illustrates this example.

Vehicle included in Class 16	Federal et Quebec	Federal (40%)	Quebec (60%)
	Zero-emission	Other type of vehicle	
Cost in 2019	$100,000	$100,000	$100,000
CCA in 2019	($100,000)	($60,000)	($90,000)
UCC balance at end of 2019	Nil	$40,000	$10,000

Additional capital cost allowance - Quebec

In Quebec, an additional capital cost allowance is available for M&P and computer equipment[17] acquired after December 3, 2018. [18] This additional deduction is equal to 30% of the CCA claimed in the previous year on the qualifying property until the property is fully depreciated.

Example: A taxpayer acquires property included in Class 53 [50% CCA rate] for a cost of $100,000 in 2019.

He/she will be able to deduct $100,000 for the CCA in the first year and $30,000 for an additional capital cost allowance in 2020.

INVESTMENT TAX CREDITS

Tax credit for investments relating to M&P equipment - Quebec

In Quebec, a investment tax credit (ITC) is available for new property used mainly in the M&P of items to be sold or leased that are acquired:[19]

- before January 1, 2023 for the remote zone, [20] the eastern portion of the Lower St. Lawrence[21] administrative region and the intermediate zone; [22]
- after August 15, 2018, but before January 1, 2020 for the **other regions**.[23]

Excluded expenditures threshold and credit rate

The first $12,500 spent by a taxpayer are not eligible for the credit. This exclusion threshold applies on a per-property basis.

The basic credit rate is 5%[24] but corporations may be eligible for an increased rate based on where the investment is made and their consolidated paid-up capital.[25] A temporary additional increase of up

12 Base rate applicable to buildings (Class 1).

13 That is, an fully electric, plug-in hybrid vehicle equipped with a battery of at least 7 kWh or fully powered by hydrogen.

14 That is, 150% of the CCA of $40,000 ($100,000 * 40%) otherwise calculated in respect of the property for the year.

15 That is, 150% of the CCA of $60,000 ($100,000 * 60%) otherwise calculated in respect of the property for the year.

16 Instead of the $20,000 (50% of $40,000) that it could have deducted for federal purposes and the $30,000 (50% of $60,000) that it could have deducted for Quebec purposes under the half-year rule.

17 Electronic data processing equipment.

18 Before that date, an additional deduction of 35% or 60% of the CCA was granted for the year in which the property was put into service and for the following year.

19 That is, goods included in Classes 29, 43, 50 and 53.

20 Abitibi-Témiscamingue, Côte-Nord, Nord-du-Québec, Gaspé-Îles-de-la-Madeleine.

21 Matapédia RCM, La Matanie RCM and La Mitis RCM.

22 Saguenay-Lac-Saint-Jean, Mauricie, La Vallée-de-la-Gatineau RCM, Pontiac dans l'Outaouais RCM, Antoine-Labelle dans les Laurentides RCM, Rivière-du-Loup RCM, Rimouski-Neigette RCM, Témiscouata RCM, Kamouraska RCM and Les Basques RCM.

23 The property must not be acquired pursuant to a written obligation entered into before August 16, 2018, and construction must not have commenced before that date.

24 For property acquired after August 15, 2018, but before January 1, 2020; 4% in other cases.

25 A corporation whose consolidated paid-up capital (including the paid-up capital of associated corporations) is less than $250M may benefit from an increased credit rate. At the top of this threshold, the increased credit rates are reduced linearly until the 5% floor rate is reached when the paid-up capital amounts to $500M. Similarly,

to 10% is also available for corporations in the metal processing sector.[26]

The following table summarizes the **increased ITC rates** by location and time of investment:

Increased ITC rates	Before August 16, 2018 and after 2019	After August 15, 2018 and before 2020	
		Sectors other than metal processing sector	Metal processing sector
Remote zone	24%	40%	45%
Eastern portion of Lower St. Lawrence	16%	30%	35%
Intermediate zone	8%	20%	25%
Other zones	-	10%	20%

Investment tax credit in the Atlantic region - Federal

Businesses are eligible for a 10% investment tax credit for certain new buildings,[27] machinery and equipment[28] used in the Atlantic provinces, the Gaspé peninsula and their offshore zones principally in certain activity sectors, including:

- the M&P of merchandise to sell or lease;
- logging, farming or fishing;
- energy saving and production, including the production or transformation of electric or steam energy.

HSF CONTRIBUTION RELIEF – QUEBEC

Primary and manufacturing sectors SMEs

Primary and manufacturing sectors SMEs benefit from a reduced Health Services Fund (HSF) contribution rate.

For employers in these sectors whose payroll is equal to or less than $1M, the rate is 1.25% and it varies between 1.25% and 4.26% when their payroll is between $1M and $6M.[29]

Contribution holiday for innovative SMEs

SMEs whose payroll is $6M[30] or less are eligible for reduced contributions to the HSF until 2020 with respect to increases in payroll attributable to the hiring of specialized employees in the natural and applied sciences sector.

For employers whose payroll is equal to or less than $1M, the reduction makes it possible to completely eliminate the HSF contribution payable for salaries attributable to new specialized employees.

OTHER TAX INCENTIVES

Additional deduction for transportation costs of manufacturing SMEs - Quebec

An additional deduction for transportation costs is granted in the calculation of net income of manufacturing SMEs.The amount of this additional deduction varies based on several parameters such as the region in which the corporation carries on its manufacturing activities, the level of its manufacturing activities, the size of the corporation, its gross income for the taxation year and a regional cap.[30]

This deduction rate is 1% for the central zone and can reach 10% of the corporation's gross income for the most remote regions.[31]

Tax credit promoting employment in Gaspésie and certain maritime regions of Quebec – Quebec

Corporations in Gaspésie and other maritime regions of Quebec can benefit from a refundable tax credit on their payroll attributable to the following sectors of activity:[32]

	Gaspésie-Îles-de-la-Madeleine	Côte-Nord	Bas-Saint-Laurent
Manufacturing activities	X		
M&P of finished or semi-finished products from slate or peat	X	X	X
Wind power generation and wind turbine manufacturing	X		La Matanie RCM only
Seafood processing	X	X	La Matanie RCM only
Marine biotechnology and mariculture	X	X	X

The credit is equal to 15%[33] of the salaries paid to eligible employees, up to a maximum annual salary of $83,333 per employee. The corporation must be able to demonstrate that a minimum of three full-time jobs will be created within a reasonable amount of time in the

the credit is either fully, partially or not refundable at all according to these paid-up capital limits.

26 That is, summarily a corporation whose proportion of wages attributable to metalworking activities exceeds 50% of total wages.

27 A prescribed building includes a building or silo included in Classes 1, 3, 6, 8 or 20 or built on land owned or leased by the taxpayer.

28 The definition of prescribed machinery and equipment is very broad and includes most capital expenditures incurred to acquire property from Classes 8, 9, 10, 15, 21, 22, 24, 27, 28, 29, 34, 39, 40, 41 and 43 as well as electricity generating equipment included in Classes 1 and 2, ships included in Class 7, clean energy generating and energy conservation equipment described in Classes 43.1 and 43.2 and electricity generating equipment described in Classes 17 and 48.

29 The payroll takes into account the payroll of the employer and all associated employers, on a global basis. The $6M threshold will be increased to $6.5M in 2021 and then to $7M starting in 2022. For sectors other than primary and manufacturing, the reduced contribution rate is 1.7% in 2019 (1.65% as of 2020).

30 The regional cap could amount to $50,000, $150,000, $350,000 or nil, based on the region where the corporation carries on its business. The regional cap must be shared between associated corporations.

31 Rules apply for corporations carrying on a business in more than one region.

32 Credit also applicable to the recreational tourism sector in the Iles-de-la-Madeleine.

33 30% for the marine biotechnology, mariculture and recreational tourism sectors.

territory of one or more eligible regions and the amount of eligible salaries is limited to the increase in the payroll paid by the corporation throughout the province for the year.[34]

Refundable Tax Credit for the Integration of information technology (IT) in primary and manufacturing sectors SMEs

The tax credit for the integration of IT in SMEs in the primary and manufacturing sectors enables corporations to benefit from a refundable tax credit with respect to expenses in an IT integration contract[35] for which *Investissement Québec* has issued a certificate.[36]

This 20% credit is granted to corporations whose paid-up capital[37] for the previous year does not exceed $35M. Above this threshold, the rates are reduced linearly and become nil when the paid-up capital reaches $50M or more.

The balance of the cumulative expenditures cap for a taxation year corresponds to the excess of $250,000 (for a maximum credit of $50,000) over the total expenditures for which the tax credit for the integration of IT was claimed for a previous taxation year. This cap must be determined by considering the expenditures of associated corporations.

CONCLUSION

Other than the specific measures described in this document, let us reiterate that corporations operating in the manufacturing sector can also be eligible for various other tax incentives based on their activities and particular situations. Such an example would be the tax credits for scientific research and experimental development and the tax credit for design. Various tax credits are also available for training and job creation, including the refundable tax credit to encourage the qualifying training of workers in employment in SMEs, the Quebec tax credit for on-the-job training, the credit for SMEs promoting the retention of experienced workers and the federal tax credit for the creation of apprenticeships. Lastly, Quebec grants a tax holiday for major investment projects realized by a corporation in the manufacturing sector.

Do not hesitate to contact your Raymond Chabot Grant Thornton advisor who can help you determine which measures apply to your situation and assist you with the steps needed to benefit from these measures.

For further information, visit our website at rcgt.com.

[34] An eligibility certificate must be issued by *Investissement Québec*.

[35] Costs relating to an eligible IT integration contract correspond to 80% of the contract amount that is reasonably attributable to the supply of an eligible management software program intended to be used mainly in Quebec.

[36] Such certification may be issued for contracts for which negotiations begins before January 1, 2020.

[37] Including that of associated corporations.