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Canada to Enforce Capital-Gains Tax Increase Without Implementing Legislation

By Paul Vieira

OTTAWA--To the ire of business groups, Canadian authorities intend to collect proceeds based on a higher capital-gains tax even though the Liberal government failed to pass implementing legislation before outgoing Prime Minister Justin Trudeau dissolved parliament.

Representatives for business owners argue the lack of legislation should prevent Canada's tax-collection agency from enforcing the measure, given the lack of legislation and the likelihood the current government is ousted in an election that must be held this year. Business executives, including those at Canadian tech company Shopify, had warned the policy change risked scaring away investment.

The Liberal government unveiled in April an increase in how much profit, or capital gain, realized in an asset sale is subject to tax. The measure stipulates that 66% of a realized capital gain is subject to tax, up from 50%, and that took effect in late June. Lawyers and financial advisers say clients sold assets ahead of that late June deadline to avoid that higher rate.

On Monday, in announcing his resignation, Prime Minister Justin Trudeau said he received approval from the country's Governor General to dissolve parliament until March 24 while Liberal Party members pick his successor. The dissolution means all pending legislation--including a bill to increase capital-gains taxes--was terminated, and must be reintroduced when parliament resumes.

Under Canada's parliamentary system, taxation measures are effective as soon as a minister introduces a so-called ways and means motion in the legislature. Legislation may be introduced at a later date.

An official at Canada's Department of Finance said authorities will enforce the higher capital-gains inclusion rate. Collection ceases only in the event that the government of the day abandons implementing the legislation, the official said.

"This is a fine kettle of fish," said David Rotfleisch, a Toronto-based tax lawyer. He said the current Liberal government could introduce retroactive tax legislation once parliament resumes.

That scenario appears unlikely, with all three main Canadian opposition parties saying they will topple the Liberal government, possibly under a new leader, when the legislature returns in late March. The Conservative Party holds a 20-point-plus lead in opinion polls over the incumbent Liberals, and in June said they opposed the capital-gains tax measure.

Tax lawyers and experts say it is common for measures to be enacted without legislation, although most of the time they tend to affect a small segment of taxpayers and focus on technical changes to tax law. The capital-gains tax increase, however, is a novel case because it affects a wide swath of taxpayers. The Liberal government expected the measure to raise about 20 billion Canadian dollars, or the equivalent of $14 billion, over a five-year period.

Kim Moody, president of advisory firm Moodys Tax, said he understands why Canada's tax authorities are proceeding with collection, citing parliamentary conventions. "In this case, I think they need to 'read the room' and adjust their policy accordingly," he said, noting there is a "high probability" the measure dies under a new Conservative government.

If the government reverses course, tax authorities would have to issue refunds to tax filers who paid the higher capital-gains inclusion rate, Rotfleisch said.

Canadian authorities "will collect billions in capital gains taxes, with no legislation authorizing it, until a government officially tells it to stop. This means that it could be a long time before any clarity is provided to taxpayers," said Dan Kelly, president of the Canadian Federation of Independent Business.

Kelly said tax collection should stop because of political developments, such as the resignation of Trudeau and his former finance minister, Chrystia Freeland, who introduced the capital-gains increase. She stepped down in a shock move, citing policy disagreements with Trudeau.

Benjamin Bergen, president of the Council of Canadian Innovators, said his members from the technology sector are angry because they scrambled to sell assets before late June to comply with a tax law that never came to pass.

"We find ourselves in an uncomfortable decision--they have scared off investment, they have created uncertainty," said Bergen, who once worked as an aide to former finance minister Freeland.