Canada’s 2030 Emissions Reduction Plan and the expansion of tax credits for green technology

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On March 29, 2022, the Government of Canada delivered its 2030 Emissions Reduction Plan (the 2030 ERP), Canada’s first-issued emissions reduction plan under the *Canadian Net-Zero Emissions Accountability Act*. Within the 2030 ERP, the Government of Canada outlined its strategy to reduce climate change while promoting economic growth.

What you need to know

1. Canada is scaling up environmentally friendly technology and initiatives to meet its net-zero emissions commitment by 2050.
2. It is anticipated that Canada’s emission targets can only be achieved through the development and proliferation of clean technology, promoted in part using the Canadian tax regime and the adoption of clean technology tax credits.
3. Businesses should consider long- and short-term clean technology tax policies, and the effect these can have on their operations and achievement of strategic ESG outcomes.
4. These tax credits are available to all sizes of businesses and offer varying levels of taxation relief.

Background

We reviewed the 2030 ERP in an **April 2022 article** , which provides important context for our review of associated tax credits. The 2030 ERP outlines the current and new policies through which Canada intends to achieve its greenhouse gas reduction targets and, in some cases, associated funding. The 2030 ERP also identifies key sectors that are anticipated to assist Canada in meeting its greenhouse gas reduction targets, including clean fuels, buildings and building codes, oil and gas, transportation and sustainable finance.

This bulletin summarizes key Canadian federal tax credits associated with Canada’s clean technology plan, set to fuel growth and innovation in the clean technology sector.

Such credits include the refundable clean technology investment tax credit (the Clean Tech Credit), the clean hydrogen tax credit (the Clean Hydrogen Credit), the clean technology tax incentives for air-source heat pumps (the Clean Tech Incentives) and the investment tax credit for carbon capture, utilization and storage (the CCUS Tax Credit). Each of these tax credits is described in further detail below.

The Clean Tech Credit

The 2022 Federal Budget (Budget 2022) tabled on April 7, 2022, noted that the Department of Finance Canada (Finance) would engage with experts to establish an investment tax credit of up to 30 per cent for investments in clean technologies, with a focus on net-zero technologies, battery storage solutions, and clean hydrogen. On November 3, 2022, the Government of Canada released the Fall Economic Statement 2022 (the Economic Statement). The Economic Statement reiterated the Government of Canada’s intention to introduce the Clean Tech Credit.

Provided certain labour conditions are met, the full details of which have yet to be announced, the capital cost of eligible equipment that becomes available for use no earlier than when the 2023 Federal Budget (Budget 2023) is tabled will be subject to a temporary 30 per cent tax credit. The Clean Tech Credit is temporary in nature and will be gradually phased out beginning with eligible equipment available for use after 2032, then entirely phased out for equipment that becomes available for use after 2034.

Eligible equipment for purposes of the Clean Tech Credit include:

i. equipment used to generate electricity from solar, wind and water energy;
ii. stationary electricity storage equipment that does not use fossil fuels in its operation, including (but not limited to) batteries, flywheels, supercapacitors, magnetic energy storage equipment, compressed air storage equipment, pumped hydro storage equipment, gravity energy storage equipment and thermal energy storage equipment;
iii. low-carbon heating equipment, including active solar heating, air-source heat pumps and ground-source heat pumps;
iv. equipment to generate heat or electricity from small modular nuclear reactors; and
v. industrial zero-emission vehicles and related charging or refueling equipment, such as hydrogen or electric heavy duty equipment used in mining or construction.

To incentivize job creation, companies that adhere to certain labour conditions will be eligible for the 30 per cent credit, whereas those that do not will only be eligible for a 20 per cent credit. The labour conditions will include paying prevailing wages based on local labour market conditions and ensuring that apprenticeship training opportunities are created for employees. The Economic Statement noted that Finance will consult with a broad group of stakeholders (specifically referencing labour unions) on how best to attach labour conditions to the Clean Tech Credit.

The Clean Hydrogen Credit

Budget 2022 also announced the Government of Canada's intentions with respect to clean hydrogen, which was first advanced on August 23, 2022, when Canada and Germany entered into a joint declaration of intent with respect to investing in hydrogen projects and satiating the burgeoning global demand for clean and renewable energy. Under the "hydrogen alliance", the two countries agreed to invest in hydrogen, establish a "transatlantic Canada-Germany supply corridor" and export hydrogen by 2025. This agreement comes on the heels of other governmental plans and strategies to invest in hydrogen, namely, the federal Hydrogen Strategy for Canada and B.C.'s Hydrogen Strategy.

The Economic Statement further addressed the Government of Canada's goal of Canada becoming a reliable, premium supplier of energy in a net-zero world. It noted that clean hydrogen is an essential part of achieving this goal and confirmed that Canada is proceeding with the establishment of the Clean Hydrogen Credit to support investments in clean hydrogen production. The Economic Statement also noted that the Clean Hydrogen Credit will be refundable and available for eligible investments made as of the day of Budget 2023. Like the Clean Tech Credit, the Clean Hydrogen Credit will be temporary, with a planned phaseout of after 2030.

The lowest carbon intensity tier that meets all eligibility requirements (unannounced at this time) will receive an investment tax credit of at least 40 per cent, where certain unannounced labour conditions are met. Where the labour conditions are not met, the maximum Clean Hydrogen Credit will be reduced to 30 per cent. Similar to the Clean Tech Credit, the goal of the labour eligibility requirements is to incentivize companies to support and create employment opportunities in the clean technology sector.

The Economic Statement also noted that Finance will launch a consultation on how best to implement the Clean Hydrogen Credit, which is widely acknowledged as a response to *The U.S. Inflation Reduction Act* (the IRA). The IRA introduced carbon intensity tiers in the U.S., with support beginning when emissions from the production of clean hydrogen are 4.0 kg of CO2e or less per kilogram of hydrogen, and with the highest level of government support being provided when emissions are less than 0.45 kg of CO2e per kilogram. The goal of the IRA is to make clean hydrogen cost competitive with natural gas by reducing its cost of production to USD3.00/kg over the 10-year life of the IRA tax credit.

The Clean Tech Incentives

An air-source heat pump is a device that uses electrical energy to provide interior space heating or cooling by exchanging heat with the outside air. It is an alternative to fossil fuels for heating or providing a more efficient means of heating using electricity. Budget 2022 proposed to expand eligibility under the accelerated capital cost allowance regime (classes 43.1 and 43.2) to include air-source heat pumps primarily used for space or water heating.

Additionally, and in accordance with the temporary measure to reduce corporate income tax rates for qualifying zero-emission technology manufacturers tabled in the 2021 Federal Budget, Budget 2022 proposes to include the manufacturing of air-source heat pumps used for space or water heating as an eligible zero-emission technology manufacturing or processing activity. Consequently, the manufacturers of air-source heat pumps will have a reduced tax rate on eligible income of 7.5 per cent, where that income would otherwise be taxed at the 15 per cent general corporate tax rate.

The CCUS Tax Credit

The Economic Statement also confirmed the Government of Canada's intention to proceed with the CCUS Tax Credit, first announced in Budget 2022. The CCUS Tax Credit is refundable and available to businesses that incur eligible expenses starting in 2022. Eligible expenses include the cost of purchasing and installing eligible equipment used in an eligible carbon capture, utilization and storage (CCUS) project, so long as the equipment is part of a project where the captured CO_2 is put to an eligible use.

In order to claim the CCUS tax credit, the CCUS project must meet a validation and verification process, specified storage requirements and provide climate-related disclosure. Provided the foregoing conditions are met, eligible expenses incurred after 2021 through 2030 are subject to favorable tax credit rates ranging from 37.5 per cent to 60 per cent depending on the type of CCUS equipment. For tax years after 2030 and through 2040, the rates would vary from 18.75 per cent to 30 per cent depending on the type of CCUS equipment utilized by the facility.

In addition, CCUS equipment is included in two new capital cost allowance classes that have depreciation rates ranging from 8 per cent to 20 per cent. These classes are eligible for enhanced first-year depreciation. The CCUS Tax Credit applies to eligible expenses incurred after 2021 and before 2041.

Contact us

Taxpayers that have questions on the foregoing clean technology tax credits are encouraged to contact the authors listed below or any other member of BLG's Tax Group. We would be happy to provide you with additional information, to the extent available, on any legislative measure relevant to the clean technology sector.

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