

FINANCE PUTS THE BRAKES ON PROPOSED EMPLOYEE STOCK OPTION AMENDMENTS

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In Budget 2019, the federal government announced its intention to introduce an annual cap on the preferential treatment of stock option grants for employees of companies labeled by the Department of Finance (“**Finance**”) as “large, long-established, mature companies”. Certain aspects of the budget proposals (as modified by a June 17, 2019 announcement by Finance discussed below) were to have application in respect of stock options granted on or after January 1, 2020. However, Finance issued a release on December 19, 2019 advising that the stock option amendments would not come into effect as of January 1, 2020 as originally scheduled.

The existing employee stock option regime under the *Income Tax Act* (Canada) effectively provides preferential capital gains-like tax treatment on the portion of a qualifying stock option’s accrued value that would otherwise be deemed to be employment income to the employee at the time the option is exercised (or the underlying shares are disposed of, in the case of a Canadian-controlled private corporation (“**CCPC**”). The proposed changes would have limited the stock option deduction available to employees of these large employers to stock option grants of up to \$200,000 per year. The proposed changes would not have applied to restrict the preferential treatment for stock option grantees employed by “start-ups and rapidly growing Canadian businesses.” The announcement indicated that draft legislation in respect of the proposals would be forthcoming. (Our coverage of these budget proposals can be found [here](#).)

Subsequently on June 17, 2019, Finance tabled draft legislation in order to implement the proposals announced in Budget 2019. The draft legislation generally exempted from the \$200,000 cap stock options granted by CCPCs and certain non-CCPCs that met certain prescribed conditions. The intent of the draft legislation was to operationalize Finance’s goal of continuing to provide preferential tax treatment for stock option grantees employed by “start-ups and rapidly growing Canadian businesses.” As part of the release of the draft legislation, Finance invited comments from stakeholders on what the prescribed conditions should be for purposes of categorizing certain companies as “start-ups, emerging, or scale-up companies”. The legislation was intended to apply to employee stock options granted on or after January 1, 2020. The consultation period in respect of such comments was to close on September 16, 2019. (Our coverage of the draft legislation can be

found [here](#).)

On December 19, 2019, Finance issued an update (the “**Update**”) advising that it is in the process of reviewing input received from stakeholders during the consultation period “to ensure that the new regime meets both of its key objectives”. The stated “key objectives” were to limit the availability of the preferential employee stock option regime in a manner that would purportedly make the tax regime “fairer and more equitable for Canadians”, and to ensure that start-ups and emerging Canadian businesses that are creating jobs can continue to grow and expand.

Importantly, the Update indicates that the proposed changes to employee stock options will no longer come into force on January 1, 2020. The Update states that the government will provide more information on how and when it intends to move forward with the measures in Budget 2020. As such, the door to implementation of some iteration of these measures is not yet fully closed.

This announcement comes as welcome relief to taxpayers given the ambiguity in attempting to delineate between “large, long-established, mature companies” and “start-ups and rapidly growing Canadian businesses”. However, it remains to be seen whether any replacement rules announced in Budget 2020 will be a material improvement over what was previously announced.

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A Cautionary Note

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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