ISSUE IN FOCUS

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SASKATCHEWAN CHAMBER of COMMERCE

Proposed Changes to Tax Planning Using Private Corporations

Background:

The Federal Minister of Finance, Bill Morneau unveiled draft legislation that was intended to make changes to the Income Tax Act and deal with tax planning strategies related to the use of private corporations. Accompanying Minister Morneau's announcement was the release of the discussion paper, Tax Planning Using Private Corporations released by the Federal Department of Finance. The tone of the discussion paper centers squarely around the concept of "tax fairness" for the middle class. For the Government of Canada, these actions are a part of a larger effort to improve the "fairness" of the tax system by cracking down on tax avoidance and the underground economy. The Federal Government has launched a very short 75-day consultation period with stakeholders that is set to expire October 2, 2017.

Issue:

Ottawa has taken the stance that all income is equal from a taxation perspective and has failed to accurately recognize the unique and important role played by private investment in business and how those businesses are recognized by the current tax system. The changes proposed will impact tens of thousands of businesses negatively by raising taxes, reducing the incentive for private investment, increasing the administrative burden, and creating additional challenges to the inter-generational transfer of business shares to family members. The changes have been advanced to eliminate perceived loopholes when in fact they were fair and balanced tax regulations that promoted growth in private investment across the county in all sectors.

While the proposed amendments are aimed primarily at the top 1% of earners, the changes would apply to all private corporations in Canada, many of which are small and medium-sized enterprises (SMEs), like family-owned businesses. Far from being the wealthy top 1% of earners, small business owners are overwhelmingly middle class and in-fact employ much of the middle class. The unintended consequences of these proposed tax changes mean that small business owners will be significantly worse off as a result.

Recommendations:

1. That the Federal Government provide a more accurate & truthful comparison that will inform a full-scale impact analysis of the proposed changes for entrepreneurs versus salaried employees.
2. That the Federal Government extend the Stakeholder Consultation Period to March 31, 2018.
3. That the Federal Government complete an external review on the administrative impacts of any changes before implementation.
4. That the Federal Government complete a detailed financial and economic analysis on the impacts of the proposed changes as they relate to family-owned businesses. ill Rate Ratio between 0.75-2.0. Retain the phase-in tax tool for managing volatility.

Notable Advocacy Win:

In response to heated criticism from the business community, Minister Morneau and Prime Minister Justin Trudeau announced during Small Business Week back in October that significant amendments to the earlier proposed tax measures would be made:

5. The federal portion of the small business rate on the first $500,000 of active income is scheduled to decrease from its current 10.5% to 9% by 2019.

6. The effective tax rate on non-eligible dividend income will increase to maintain what the CRA refers to as the ‘integration' of the personal and business income tax system. As a result, the increased rate applied to non-eligible dividends will at least partially offset the gains in take-home income from the rate cut.

7. The federal government announced that it was abandoning its plan to curtail the conversion of income to capital gains.

8. The federal government also announced that it would be moving ahead with some of the more controversial measures, albeit scaled back. For example, a proposed measure meant to discourage the accumulation of passive income in a CCPC will go ahead, but a new threshold will allow for $50,000 in income annually to be exempt from the new, higher tax.

9. The proposed measure to curtail income splitting for family members not

deemed by the CRA as active in the business will move forward. After business groups voiced concerns about the subjective nature of applying the reasonableness test to the contributions of family members, along with the added compliance costs the measure would create, Minister Morneau stated that this measure would be simplified further.

10. While the federal government will move forward with the simplified rules to limit income sprinkling using CCPCs, they have promised that the new rules would not impact businesses to the extent that there are clear and meaningful contributions by spouses, children, and other family members. The Chamber believes that this measure should still be scrapped, or at very least, an exemption be made for spouses.

History:

Letters to Federal Minister of Finance 2017 (including Petition results)
Letter to Premier 2017
Issue in Focus: Taxation: Proposed Changes to the Taxation of Private Corporations in Canada Report 2017
Letter to Federal Minister of Finance 2018