Assante® WEALTH MANAGEMENT

CCPCs – Where are we now?

On July 18, 2017, the Department of Finance (Finance) released its discussion paper "Tax Planning Using Private Corporations," which included new proposed tax legislation that, if implemented, would fundamentally impact the taxation of Canadian Controlled Private Corporations (CCPCs) and their owners. While the tax planning community expected dialogue and had a sense as to the direction Finance was taking, it did not anticipate the complexity and significance of the proposed measures announced.

Between October 16 and 24, Canada's Prime Minister and Minister of Finance made a series of announcements that included a drop in the small business tax rate and changes to the July 18 tax proposals. Unfortunately, with the exception of the rate drop announcement, the ambiguity associated with these changes left tax and wealth planning communities and taxpayers with more questions than answers.

As mentioned, Finance announced that the small business tax rate will decrease from 10.5% to 10% on January 1, 2018, and to 9% on January 1, 2019. They also quietly announced an increase to the non-eligible dividend tax rate to ensure integration is upheld.

The Assante wealth planning team has been reviewing the proposed measures and additional announcements as they relate to income sprinkling and converting income into capital gains, as well as the methods being contemplated regarding passive investments held by a private corporation. We understand you may have many questions about the proposals and how it will impact you and your business.

We would like to emphasize that the proposed changes are draft and not yet enacted as law, and the October announcements and accompanying press releases are high level with no detailed legislation or notes. We believe the legislation that will ultimately be enacted is likely to differ significantly from the proposals, which creates a challenging planning environment that is in a state of flux. However, what is virtually certain is that significant change is coming.

The below table summarizes the original measures proposed on July 18 along with the corresponding announcements from October.

	July 18 Proposed Measures	October Announcements
Income sprinkling - Dividends	• Expanded tax on split income rules (previously known as 'kiddie tax') • 'Unreasonable' dividends paid to related individuals will be subject to the highest marginal tax rate	• Going ahead as proposed • Will provide more guidance on how to determine if a dividend is 'reasonable'
Income sprinkling - Lifetime capital gains exemption (LCGE)	• Minors would no longer be eligible to claim the LCGE • Gains that accrued while an individual was a minor would not be eligible for the LCGE • Trusts would no longer be able to claim the LCGE	• Cancelled, but to what extent is unclear – all or some
Converting income into capital gains	• Broadly worded measures effective immediately to eliminate 'surplus stripping,' which involves converting corporate distributions into capital gains (instead of other forms of income such as dividends or salaries that are taxed at higher rates) • New proposed measures would have eliminated the post-mortem 'pipeline' planning used by individuals with private company shares to avoid double taxation	• Cancelled for now, but we believe this will be revisited
Passive income	• No legislation was proposed, rather several methods were outlined and feedback was requested o Finance was concerned about the investing of after-tax profits in passive investments where the small business tax rate was used, resulting in a perceived unfair tax deferral o Indication of grandfathering existing passive assets	• Will proceed with tax measures that will be finalized and announced in Budget 2018 • New legislation will: o Exempt $50,000 of investment income annually from the new rules o Include a grandfathering rule for current passive assets held in a corporation • Great deal of uncertainty on what can be expected in Budget 2018
Tax rate changes	• None proposed	• Small business tax rate will decrease from 10.5% to 10% on January 1, 2018, and to 9% on January 1, 2019 • Federal top marginal tax rate on non-eligible dividends to increase from 26.3% in 2017 to 26.6% in 2018 and 27.6% in 2019

Assessing the impact

Individuals should review their private company share structures and compensation arrangements with their tax advisor in order to assess the impact of the proposed measures and determine if further action is necessary.

Below we have listed situations that may be affected by the proposed rules. Individuals falling within these scenarios may have planning opportunities available to them in the short term, such as increasing dividends in 2017, share restructuring and share reorganizations. If you fit within the list below, please contact your tax advisor as soon as possible.

Immediate priority (before end of 2017)

- Corporations which pay dividends to shareholders who are family members not directly involved in day-to-day business activities;
- Incorporated business owners in the process of selling their business or contemplating a sale;
- Canadian corporations (qualified small business corporations) with significant accrued growth and inactive shareholders (individuals or trust); and
- Individuals currently considering incorporating.

Moderate priority (early 2018)

- Corporations where related party shareholders own the same share class.

Low priority (during 2018)

- Corporations earning passive income through portfolio investments.

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