Trowbridge Haywood
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WEALTH PARTNERS

New Rules For Private Company Taxation

Trowbridge Unabridged – The Quest for Clarity

Our first issue of *"TH-ink"* outlined the July 18 tax change proposal for private corporations from the feds and our hope for October clarity after the "consultation period".

This week, Finance Minister Morneau (or is it "More? No!") let us know that Justin and he want to make nice with small business owners and incorporated professionals before getting tarred and feathered.

So… it appears they were "just kidding" about some aspects of their party pooping plans. At least for now……,

This backtracking provides a "temporary reprieve" for sprinklers and pipe-liners who have been using and abusing these nifty ploys in their resolve to pay less tax. That's less tax now *and* when they croak or "shuffle off the mortal coil" to quote my euphemistically inclined partner, Michael Haywood.

Notably, the brutal intention to go after corporate "passive income" seems to be undeterred with only the first $50,000 safe from Ottawa's grasping tentacles. That amount barely covers the club dues and bar bills of most of our corporate clients.

I'm sure Haywood's legally trained eye for detail will let us know what I've missed or misunderstood.

Over to you Michael….

The Haywood Summation – Odd Government Policy

I have a few things I could add. **First, being able to plan one's affairs again is good.** Most, but not all, the uncertainty is now gone. And, the current state of the proposals is vastly better than the first draft.

The simplest item is the proposal to eliminate capital gains exclusions for family members. This seemed to me to radically misunderstand the nature of business families, so it is good to see this proposal dropped altogether. One down.

The second simplest to describe is the income splitting proposal. Paying dividends to shareholding family members will be possible only if it is "reasonable" having regard to their contributions to the business. The Department of Finance is still working on what the test for that will be, but assures us that they understand it will need to be more objective and easier to administer than their first effort. Without seeing the test, I would say the jury is out on this one. Other commentators have pointed out that adding a lot of complexity to an area where there was minimal abuse seems like odd policy.

Perhaps the best news for our industry and clients with corporate owned life insurance is that **the Department is dropping entirely their proposal to change the taxation of capital gains.** This was by far the most technical of the changes, and the one where almost all tax practitioners said the Department had a point. The problem the government wanted to cure was that clever people had been converting other types of income into capital gains with increasing frequency for the past few years. That was met with a terribly drafted cure. It caught valid estate planning steps that would have seen every shareholder in a private company facing potential double tax. It put into doubt whether a capital dividend could ever be paid. The government immediately said that was not the intent, but words mean what they say, and who knows how a court would have interpreted the language if it had been enacted. The proposals are gone entirely, with clear commentary that they are not coming back. The original problem still exists, and clever people can still convert ordinary income into capital gains, so I expect the Department to think up a new way to catch that, which is likely justified. Next time I expect a narrow change. Only good news on this one.

Bob's comments on the fourth item – passive investments in a corporation - are spot on. With a $50,000 annual income limit, this is still a serious limitation. Here are two more observations. First, what about capital gains? Would you hold revenue property in a corporation? The annual income threshold might not be an issue (depending on the value of the property), but what about when the company sells the asset? Isn't that likely to generate income far above the threshold? There are still lots of problems with this change.

This one, too, is surprising as government policy. I like the statement by John D Rockefeller: *"I think it is a man's duty to make all the money he can, keep all that he can and give away all that he can."* That is becoming harder. Sure, all current retained earnings will be grandfathered (somehow – we don't have the legislation yet). Many of our clients are rich, and are being treated very kindly. All your existing corporate wealth is fine. But if you are in the camp that wants to become rich, well it just got a lot tougher. **I just find creating the two camps is very odd public policy.** And it is not all good news for those with wealth. Adding to the corporate pot is now a significant challenge. I will add that it certainly solidifies corporate life insurance as an attractive asset.