

Tax Change Proposals Could Have Serious Effects

By Ivana Karac

On July 18 a shocking announcement was made by Finance Minister Bill Morneau regarding major changes proposed for the taxation of small businesses and private corporations. The announcement has resulted in a backlash, with several petitions being circulated to stop, delay and/or revise the proposed changes, including an official House of Commons E-Petition.

So what's all the fuss about? The details of the proposed changes are outlined here.

Income Splitting, effective January 1, 2018: The proposed changes are meant to close the loopholes used by a large and growing number of businesses, such as the practice of reducing overall tax rates paid by families running small businesses. Business owners pay dividends or salaries to spouses and children in a lower tax bracket than themselves, even if those family members are not actively involved in the business. The proposed changes will require the payment to family members be "reasonable," which is a term that is not yet well defined. It is possible that the involvement in the business and the capital contribution by the individual in question will bear significant weight in the determination of whether the payment is reasonable. Payment of dividends to these individuals will result taxation at the highest marginal tax rate if deemed not reasonable.

Capital Gains Exemption, effective January 1, 2018: The capital gains exemption is the amount of tax-free gain that each Canadian is entitled to from the sale of qualified small business shares. Previously, each family member owning shares in the business was entitled to this lifetime exemption, of approximately \$835,000. Proposed rules

restrict the availability of the capital gains exemption to some family members and also introduce the flexible allocation of the gain to family members based on this "reasonable" approach.

Other proposed changes include converting income into capital gains for certain complex transactions and increasing tax rates for corporations with passive assets, such as rental properties and stocks, which is not yet in draft legislation.

Justin Trudeau's attitude and comments on the proposed changes seem to indicate that these changes are coming, whether we like it or not: "We're doing more for the people who need it, and less for the people who don't. That's the commitment we made to Canadians and will continue to make to Canadians ... I will make no apologies for this approach."

To discuss your options, or if you would like to receive a quarterly tax newsletter, please contact Ivana Karac at 519-746-7220 / Ivana.Karac@flkcpa.com.



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