

# COALITION FOR SMALL BUSINESS TAX FAIRNESS

[Example]

May 28, 2018

The Honourable Carole James  
Minister of Finance and Deputy Premier  
Room 153 Parliament Buildings  
Victoria BC V8V 1X4

## **Subject: Request for provincial assistance on the taxation of passive investment income**

Dear Minister James,

We are writing on behalf of the Coalition for Small Business Tax Fairness. Together, our organizations represent hundreds of thousands of independent businesses, professionals and taxpayers, across all sectors of the economy and all regions of the country that employ millions of Canadians. We are writing today to request your assistance on the taxation of passive investment income of Canadian-controlled private corporations.

As you may recall, the federal government proposed a series of historic changes to tax planning mechanisms used by private corporations in July 2017. Many provinces joined the small business community to express their concerns regarding the potentially negative impact of these changes on businesses in their communities. Following unprecedented pushback, the federal government abandoned some of the more harmful components of the proposed changes and made some adjustments to others. Despite a new approach outlined in the 2018 federal budget, we remain very concerned with changes relating to the tax treatment of passive investment income earned within Canadian-controlled private corporations (“CCPCs”).

The current business environment is becoming increasingly difficult for smaller firms. In addition to these tax changes, small business owners are facing payroll tax increases (CPP/QPP, EI), the implementation of carbon pricing measures and, in some provinces, increased labour costs. At the same time, there is added uncertainty over the prolonged renegotiation of NAFTA and significant tax reform in the U.S, which are raising questions about Canada’s ability to effectively compete on a global stage.

### **New Rules on Passive Investment Income**

As part of Budget 2018, the federal government proposed changes to the taxation of passive investment income in a corporation. According to the new rules, starting after 2018, businesses will start to lose access to the small business deduction once they earn more than \$50,000 in passive investment income in a year, and completely lose access once they earn more than \$150,000 per year. This means that businesses with more than \$150,000 in passive investment income will have to pay the general corporate tax rate on their active business income.

While the process is somewhat simpler than previous proposals, we feel it will unfairly penalize businesses that accumulate capital to protect the business against economic downturns, purchase property or for future investments in their business. With the previous federal proposal, it was promised that all existing passive investments would be “grandfathered”. However, the Budget 2018 proposal does not exclude existing passive investments from the new taxation regime. This will cause businesses with larger pools of passive investments to lose access to the small business tax rate on active business income starting in 2019. We also believe that small businesses will start to make business and investment decisions with a view to minimizing the impact of these new rules, with potentially negative long-term economic consequences.

## **Recommendations**

While other federal tax changes (including changes to income splitting rules for small businesses) automatically apply to provincial tax systems, we have confirmed that federal changes that will claw back the small business tax rate based on a CCPC’s passive investment income do not need to extend to the small business deduction provided by the provinces. In other words, the provinces can make their own decision on whether businesses can continue to access the provincial small business deduction, whether or not they have a stream of passive investment income.

While Prince Edward Island and Ontario have indicated that they will follow the federal government’s lead, other provinces and territories have not indicated whether they will do the same.

**In order to help protect businesses’ hard-earned investments, we are urging your government NOT to follow the federal government in limiting businesses’ access to the provincial small business deduction based on passive investment revenue. We urge the governments of PEI and Ontario to reconsider their decision on following the federal government’s lead.** In advance of the meeting of federal, provincial and territorial finance ministers in June, we encourage you to deliver a strong message to your colleagues and the federal government: Stand up for small businesses and support your local communities by taking a public stance against these proposals.

In addition, we would value your support in our ongoing efforts to encourage the federal government to do the following:

1. Immediately undertake an economic impact assessment of the package of proposed tax changes and delay implementation until this assessment is complete.
2. **On income splitting with family members:**
  - Postpone the application of the changes until, at the very earliest, January 1, 2019.
  - Consider, at a minimum, a full exemption for spouses from the new income splitting rules.
3. **On passive investment income in a corporation:**
  - Do not proceed with the proposed passive investment rules.
  - If determined to proceed, work with the Coalition and tax professionals to ensure that existing passive investments are not included in the formula to determine eligibility for the small business deduction going forward. We are committed to working with you to develop a way to grandfather past passive investments without adding significant new complexities to the system.

- Implement a more gradual “grind” in eliminating the benefit of the small business tax rate. For example, adjust the grind over \$50,000 of passive income to \$2.50 per \$1 of passive income (rather than \$5 per \$1 of passive income). This would mean that the Small Business Deduction is not ground down to nil until passive investment income reaches \$250,000.
  - Raise the threshold where passive investment income begins to affect a firm's access to the small business rate from \$50,000 to \$100,000 to exempt more small firms.
  - Index the \$50,000 and \$150,000 exemption limits to inflation to prevent small businesses from being subject to bracket creep on the taxation of their passive investment income in future years.
4. Undertake a comprehensive review of Canada's income tax system with a view to reducing complexity, thereby helping small business owners to better understand tax implications before making critical business decisions.

To ensure that small businesses in Canada can succeed, they need the support of all levels of government to help create a business environment that is fair for smaller firms and conducive to growth. If you have any questions or would like to meet to discuss our recommendations further, please feel free to reach out to any of the undersigned groups.

Sincerely,



Greg Pollock  
President and CEO, Advocis  
The Financial Advisor  
Association of Canada



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Association des  
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 Executive Director  
 Canadian Bison  
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 Hons.B.Comm., J.D.  
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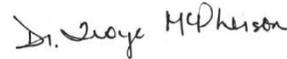

Edward Whalen, P.Eng.  
President & CEO  
Canadian Institute of Steel  
Construction




Gary Simonsen  
Chief Executive Officer  
Canadian Real Estate  
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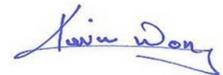
122,000 Realtors



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President  
Canadian Veterinary  
Medical Association



6 665 members



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Executive Director  
Canadian Water Quality  
Coalition



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Executive Director  
Chinese Business Chamber of  
Canada



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Coalition of Ontario  
Doctors



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President  
Conference for Advanced  
Life Underwriting



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Léopold Turgeon  
Président-directeur général  
Conseil québécois du  
commerce de détail



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Executive Director  
Electrical Contractors  
Association of Ontario



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Family Enterprise  
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Fédération des chambres  
de commerce du Québec



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Association



Ontario Real Estate  
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Resorts of Ontario

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Restaurants Canada



The voice of foodservice | La voix des services alimentaires

30 000 members



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Saskatchewan Stock Growers  
Association

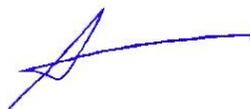


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**STOCK GROWERS**  
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President  
Western Canadian Wheat  
Growers Association

John Schmeiser  
CEO  
Western Equipment  
Dealers Association



800 members

Cc: Mr. Andrew Wilkinson, Q.C. Leader of the Official Opposition  
Mr. Bruce Ralston, Minister of Jobs, Trade and Technology