COALITION FOR SMALL BUSINESS TAX FAIRNESS

November 20, 2017

The Honourable Bill Morneau
Minister of Finance
Finance Canada
90 Elgin
Ottawa, Ontario K1A 0G5

Subject: Coalition for Small Business Tax Fairness feedback on revised tax proposals

Dear Minister Morneau,

Since we last wrote, the **Coalition for Small Business Tax Fairness** has further grown in size and now represents close to 80 business associations. 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 provide feedback on revisions to the proposed tax changes announced during Small Business Week.

Our Coalition welcomes the federal government's decision to reinstate its promise to reduce the small business corporate tax rate from 10.5% to 9% by 2019. This decision will pump hundreds of millions of dollars back into the small business community, helping them create more jobs and grow the economy.

As for the amendments to the July tax proposals, we are encouraged to see some of the major concerns addressed in full or in part. We are particularly pleased that the government has listened to the concerns of business owners by stepping back from the measures relating to the conversion of income into capital gains. These rules would have made it more costly for small business owners — including farmers and fishers — to sell or transfer their business to their children.

We are also pleased that your government has begun to recognize the important role passive investments can play in the life of a business and its owner(s).

While we thank you for making progress on the items noted above, we remain very concerned by the remaining proposals that appear to be moving ahead. We find it quite concerning that the Department of Finance was able to parse through 21,000 written submissions in just under two weeks. We question whether the largest set of tax changes in over 40 years was given its due diligence in such a short period of time. In fact, tax practitioners are still reviewing the revised announcements from your government and are of the view that more details are urgently needed.

While we continue to review the revised proposals, we raise the following concerns and recommendations relating to the income sprinkling and passive investment proposals.

Income Sprinkling Rules

The rules that will penalize business owners for paying dividends and other forms of income to adult family members remain a significant concern. The proposed changes do not reflect the many formal and informal ways family members participate in the business, especially when it comes to the participation of spouses. However, the government says it will still move ahead with requiring a "reasonableness test" for family members to ensure that they are making a “meaningful contribution” to the business before allowing them to share income with that family member.

While it was implied that the process will be simplified and more targeted, no further details have been provided and time is quickly running out as the changes are set to take effect January 1, 2018. **We urge you to provide these details as soon as possible and allow time for stakeholder input to help minimize any unintended consequences.** Given the key role spouses (including common law partners) often have in a business that cannot always be clearly quantified, we would also **recommend that the federal government consider at a minimum an exemption for spouses from the new sprinkling rules. In addition, the Coalition recommends that the federal government postpone the implementation of the changes until, at the very least, January 1, 2019.** As the burden of proof and compliance remains on the business owner, the delay would help ensure that the business community is fully aware and provided with sufficient time to implement required fixes to existing business structures.

Passive Investments

As noted, we are pleased that the federal government made changes to begin to recognize the importance of permitting some passive investment (and resulting income), however, we believe the amendments will be inadequate for many— particularly for those businesses saving for larger investments, innovations or expansion. While the $50,000 annual threshold will be helpful for small businesses that want to remain small, it will be insufficient for those who are saving to grow and create more business opportunities.

Canada already has a dearth of medium-sized businesses and the $50,000 annual income threshold may be insufficient to help businesses looking to get to the next level. In addition, an amount of $1 million will provide an owner with an annual annuity of between $34,000 and $54,000. After a lifetime of taking risks and building a business, this would amount to less than a teacher’s pension in most provinces.

In addition, we believe most small businesses will continue to be saddled with additional complexity and compliance costs despite the $50,000 allowance for passive investment income. For example, the acquisition of a passive real estate investment for $100,000 could result in a significant one-time gain on a future sale that would put the business over the $50,000 annual limit. Alternatively, over an extended period of time, even nominal growth in passive investments could result in passive income exceeding $50,000 per year on recurring basis. We therefore think that the government’s statement that the $50,000 allowance will result in a vast majority of small businesses not being impacted is incorrect.

We therefore recommend that the government drop the passive investment rules until a full economic impact assessment has been completed and an approach has been developed that will ensure there are no unintended consequences.

We understand that proposed legislation on passive investments is to be brought forward in federal budget 2018 and we want to ensure we take the time to get this right. The Coalition is seeking more clarity about how this change will be implemented, including whether the threshold will be indexed to inflation and whether any unused income can be carried forward over time, similar to TFSA/RRSP rules.

Intergenerational Transfers

We are pleased your government has expressed an openness to making it easier and less costly to transfer a business to the next generation. Two private members' bills — from NDP MP Guy Caron (Bill C-274) and Liberal MP Emmanuel Dubourg (Bill C-691) —proposed amendments to a section of the Income Tax Act which currently makes it easier to sell a family business to a third party than to a family member. In Canada, when an individual sells their business to a family member, the difference between the sale price and the price originally paid is considered a dividend. If the individual sells the business to an unrelated person, it is considered a capital gain. This difference in the Income Tax Act discourages the transfer of a business to a family member because the transaction does not benefit from the lifetime capital gains exemption and is, therefore, more heavily taxed. Both these bills try to address this flaw in the tax system.

As previously stated, **we stand ready to work with the government on finding solutions to ensure that intergenerational transfers of small businesses are easier and less costly, while, at the same time, maintaining the integrity of the tax system**.

Conclusion and Recommendations

Given the complexity of these proposals, more analysis and consultation is needed to fully understand the effect on the small business community. We look forward to working with the government to continue to find solutions that do not negatively affect the small business community's ability to grow and prosper. We therefore **recommend:**

1. Immediately undertake an economic impact assessment of the package of proposed changes and delay implementing any tax changes until this assessment is complete.
2. On **income sprinkling**:
   - Postpone the implementation of the changes until, at the very least, January 1, 2019.
   - Consider, at a minimum, a full exemption for spousal income and dividends from the new income sprinkling rules.
3. On **passive investment**:
   - Do not proceed with the proposed passive investment rules.
4. Look at ways to make **intergenerational transfers** easier and less costly for business owners.
   - Implement changes to make intergenerational transfers tax neutral compared to arm's length sales.

5. Undertake a comprehensive review of Canada's income tax system.

Please do not hesitate to reach out to any of the undersigned groups and sectoral associations should you have any questions or comments about the contents of this letter. We remain committed to working with you.

Sincerely,

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

13,000 members

Leah Olson
President
Agricultural Manufacturers of Canada

Andy Brooks
CEO
Alberta Roadbuilders & Heavy Construction Association

1,000 members

Luc Bélanger
CEO
Association des professionnels de la construction et de l'habitation du Québec

John D. Gamble, CET, P.Eng.
President & CEO
Association of Consulting Engineering Companies

Alan Rowell, MFA, DFA-Tax Services Specialist
Director
Association of Tax and Accounting Professionals

187 members

Caroline De Guire, M.Sc. Écon.
CEO
Association québécoise des informaticiennes et informaticiens indépendants

1,500 members

Jean Thiffault
President
Association québecoise des pharmaciens propriétaires

John Reid
CEO
Canadian Advanced Technology Alliance

Liz Robertson
Executive Director
Canadian Association of Farm Advisors

400 members

Mary Blair
Managing Director
Canadian Association of Management Consultants

2,500 members

Dr. Michael Dennis
President
Canadian Association of Optometrists

4,800 members

Dr. Emil Lee, President
Canadian Association of Radiologists

2,182 members

Kerry Simmons, Q.C.
President
Canadian Bar Association

36,000 members

Terry Kremeniuk
Executive Director
Canadian Bison Association

550 members

Perrin Beatty
President and Chief Executive Officer
Canadian Chamber of Commerce

200,000 members

Michael Atkinson
President
Canadian Construction Association

20,000 members

Dr. Larry Levin
President
Canadian Dental Association

John Dickie,
President of the Canadian Federation of Apartment Associations

11,200 rental owners, rental managers and rental industry suppliers

Dan Kelly
President and CEO
Canadian Federation of Independent Business

109,000 members

Lorraine McLachlan
President & Chief Executive Officer
Canadian Franchise Association

750 Corporate members representing 40,000+ franchised outlets

Kevin Lee, Chief Executive Officer
Canadian Home Builders' Association

8,500 members

Keith Costello, BADM, MBA-Strategy
President & Chief Executive Officer
Canadian Institute of Financial Planners

8,000 members

Ralph Suppa, CAE,
President & General Manager
Canadian Institute of Plumbing and Heating

260 members

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

Christopher White
President & CEO
Canadian Meat Council – conseil des viandes du Canada

52 Regular Members and over 92 Associate Members

Dr. Laurent Marcoux
President
Canadian Medical Association

85,943 members

Samantha Gale
Executive Director
Canadian Mortgage Brokers Association

5,000 members

Perry Eisenschmid
Chief Executive Officer
Canadian Pharmacists Association

Bob Brunet, CAE, BComm
Executive Director
Canadian Roofing Contractors' Association

400 members

Aaron Wudrick, Federal Director
Canadian Taxpayers Federation

123,000 supporters

Dr. Troye McPherson
President
Canadian Veterinary Medical Association

6,665 members

Kevin Wong, CAE, MBA
Executive Director
Canadian Water Quality Coalition

208 members

Sean Hu
Executive Director
Chinese Business Chamber of Canada

1,300 members

James Swan, MD, FRCPC
Coalition of Ontario Doctors

2,450 members

Guy Legault
President
Conference for Advanced Life Underwriting

670 members

Bill Brushett
President and CEO
Family Enterprise Xchange

Stéphane Forget, MBA
Président-directeur général
Fédération des chambres de commerce du Québec

139 Chambers and
50,000 businesses

Sandra Kegie
Executive Director
Federation of Mutual Fund Dealers

Jaye Hooper, Chair of the Federation of Ontario Law Associations

8,500 members

Mark Brock
Chair
Grain Farmers of Ontario

28,000 members

Iain J.S. Black
President and CEO
Greater Vancouver Board of Trade

5,200 members

Warren Heeley
President
Heating, Refrigeration and Air Conditioning Institute of Canada

Nancy Allan
Executive Director
Independent Financial Brokers of Canada

3,500 members

Jeff Wachman
President
Institute of Advanced
Financial Planners

Richard McKeagan, Chief
Executive Officer
Mechanical Contractors
Association of Canada

900 members

Terrance Oakey
President
Merit Canada

3500 members

Mark Prieditis, MD, FRCPC
President
Ontario Association of
Radiologists

1,400 members

Keith Currie
President
Ontario Federation of
Agriculture

37,000 members

Dr. Shawn Whatley,
President
Ontario Medical Association

43,493 members

Ettore Cardarelli
President
Ontario Real Estate
Association

Tony Elenis
President & CEO
Ontario Restaurant Hotel
and Motel Association

11,000 members

Robert Dalton, Executive
Director
Opticians Association of
Canada

3,979 members

Doug Bedard, Chair

Georgina Blanas, Executive
Director
Private Capital Markets
Association of Canada

Membership 500

Sean Reid
Vice President
Progressive Contractors
Association of Canada

180 members

Richard Darveau
President & CEO
Quebec Hardware and
Building Supply Association
1,000 members

Grace Sammut
Executive Director
Resorts of Ontario

Shanna Munro
President and CEO
Restaurants Canada
30,000 members

Shane Jahnke
Saskatchewan Stock
Growers Association
600 members

Levi Wood
President
Western Canadian Wheat
Growers Association

John Schmeiser
CEO
Western Equipment Dealers
Association
800 members

cc: Mr. Alexandre Boulerice, NDP Member of Parliament for Rosemont-La Petite Patrie, Finance Critic
Senator Percy Mockler, Chair of the Senate Committee on National Finance
The Honourable Pierre Poilievre, Conservative Member of Parliament for Carleton, Shadow Minister of Finance and National Capital Commission
The Honourable Wayne Easter, Liberal Member of Parliament for Malpeque, Chair of the Standing Committee on Finance
The Right Honourable Justin Trudeau, Prime Minister of Canada