Belliveau Veinotte Inc.
CHARTERED PROFESSIONAL ACCOUNTANTS
Member of The AC Group of Independent Accounting Firms

PO Box 29
11 Dominion St
Bridgewater NS B4V 2W6
Canada

Tel: 902-543-4278
Fax: 902-543-1818
bridgewater@bvca.ca

www.bvca.ca

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Department of Finance
140 O'Connor St #19
Ottawa, ON
K1A 0G5

By Email: fin.consultation.fin@canada.ca

RE: Proposed Changes to the Income Tax Act

We are writing in regards to the proposed changes to the Income Tax Act as outlined in the Department of Finance's consultation paper date July 18, 2017. We understand you have likely had the opportunity to speak with many of your constituents regarding their thoughts and opinions on these proposed changes, but as you know, these proposed changes are extremely complex and many Canadians lack an understanding of the practical application and implication of these changes. As a firm with extensive experience in both tax legislation and advising small business owners, we have analysed and evaluated these proposed changes and feel an obligation to provide you with this submission outlining our concerns.

We understand your initial thought upon receiving this submission may be that it is unnecessarily long; however, we can assure you it will be worth your investment of time to review in its entirety. We suspect the majority of submissions you have received to date provide numerous qualitative reasons why these proposed changes are offensive to small business owners (which for the record, are valid in our opinion), but you have likely not received any quantitative analysis of their impact. Our firm has dedicated countless hours to reviewing, interpreting, analysing and quantifying the impact of these proposed changes, which has built the foundation of this submission. Further, although we believe the current system already provides "fairness", we have provided various additional options for your consideration.

Below, we have outlined our analysis with respect to each of the proposed changes, including both our quantitative analysis supported by qualitative explanations. We have also addressed Finance’s claim that business owners making $150,000 and under will not be impacted by these changes as our analysis of Income Sprinkling, Educational Assistance and Passive Investments within a corporation are all based on income levels far less than $150,000. You will note many of the proposed tax changes overlap with one another, so we have built this overlap into our analysis to ensure you, and hopefully Finance, can understand the practical implications. We understand these calculations are extremely complex, so we welcome any questions or concerns you may have. Further, we will gladly provide the working papers to support our calculations in the event you wish to have a copy.

"Income Sprinkling"

Analysis

The current tax system allows for a corporation to be structured in such a manner that allows for the corporation to distribute its earnings among family members, including spouses and children. Finance believes this provides small business owners with an "unfair" advantage because employees do not have the ability to do the same. Firstly, we would note our previous government did allow spouses to income split through the family tax cut, but our current government decided to take this benefit away. Further, our current tax system does allow for pensioners to income split and actually allows employees to income split with children to a certain degree, which has been discussed below under "Educational Assistance".

In reviewing numerous articles regarding the topic of income splitting, including those prepared by Finance, we note a common trend in these examples. The level of income being discussed is commonly in excess of $200,000, being the top 1% of Canadians, but these proposed changes are not isolated to these income levels. In fact, these proposed changes will impact all small business owners at all income levels. Therefore, in quantifying the impact removal of income sprinkling would have, we have prepared our analysis using more modest and common examples of income levels.

We will first address Finance's claim that the proposed tax changes will not impact small business owners making under $150,000. Schedule A outlines a situation where a family business earns $80,000 and pays $10,800 in corporate tax, leaving $69,200 to be distributed out to the family. Under current tax law, the income is distributed by way of dividends equally between the two spouses such that each spouse pays $2,116 in tax, or $4,232 in aggregate. Total corporate and personal tax is $15,032. Removing the ability to split the income will result in the single spouse paying personal tax of $10,759 and total combined tax of $21,559. This is a difference of $6,527 in additional tax for this family, which we would suggest will cause financial hardship for a family with income at this level. We argue that additional tax will be incurred at all income levels, even those below $150,000.

We have heard arguments from Mr. Morneau that the business owner can offset this increase in tax by maximizing RRSP and TFSA contributions. We would suggest this is very unlikely in that most families at this income level cannot afford to do so, whether they are an employee or a small business owner. Should a family at this income level be fortunate enough to have excess cash, contributing it to the RRSP would restrict access to the cash and create additional financial hardship should the business owner require cash for operations. We have elaborated on this point even further under the "Passive Investments within a Corporation" section below.

We believe that looking at examples of income and tax comparisons between an employee and an incorporated business person for a single year is misleading. In most cases, a real life situation would be one where business owners typically make less than the average employee in the start-up years and will eventually make more than the employee in later years. Schedule A-1 contains an example that compares an employee to a small business owner with and without income splitting through their working careers up to retirement. We have used annual income levels that result in both the employee and the business owner making the same amount of money throughout there working career but at varying income levels during this period. The example also uses equal contributions to a Registered Retirement Savings Plan (RRSP) to ensure we are comparing "apples to apples".

It is no secret that income sprinkling does provide tax savings to small business owners, in some cases on a large scale. In reference to Appendix A1, you will note the small business owner in our analysis receives $220,000 more cash available for personal consumption than the employee. To ensure our analysis remains unbiased, we have assumed the small business owner would invest this additional cash, thus gaining a rate of return equal to 5% on the investment. Although these investments would be held outside of an RRSP and therefore the investment income and growth would attract personal tax, we have not accounted for these personal taxes as it is unnecessary to illustrate our point. However, factoring this in would only deplete the investment balance, creating an even larger variance. You will note in Appendix A1 that even with income splitting, the small business owner ends up having $279,320 less in retirement savings.

Without income splitting, the business owner does pay $21,700 more in income tax but has a $22,000 advantage in net cash flow. (This is a combination of not paying into EI and corporate tax savings on the employer's portion of the CPP payments). At an initial glance, one would think this has resulted in a fairly equal tax situation, considering the difference is relatively small for a lifetime of equal income. There are, however, a couple of underlying issues that result in an inequality and hardship to the business owner. First, the $22,000 of additional cash flow relates almost entirely to not contributing to EI. Accordingly, this $22,000 is all the business owner has to cover lack of business earnings, sickness and/or parental leave.

Due to the timing issue of when small business owners start to earn higher incomes, the small business owner has substantially less cash available for business use in the earlier years. In our example, throughout the first 18 years, the business owner receives substantially less cash than the employee on an annual basis. By the end of year 18, the business has received $108,000 less cash than the employee. It's the early years that are critical for small business success. Income splitting helps to alleviate this cash flow issue, providing the business owner with reduced taxes while business income is lower.

The third underlying issue relates to the amount of cash available for retirement. Without income splitting, the small business owner's savings at retirement are only 48% of what the employee has available to them. Our example assumes the employee's contribution is matched by his/her employer. We acknowledge that many employees do not benefit from an employer contribution; however, there are many that do. With this understanding, we would like to address under no circumstance does the business owner ever receive a pension or employer funded contribution to an RRSP. In our example, the variance in the value of the RRSP is a result of the small business owner not having an employer match their contributions. As a result, the RRSP generates less investment income and market growth due to having less principal invested. Income splitting and the corporate tax deferral are two ways to help the business owner bridge this gap.

We also acknowledge that some business owners are fortunate enough to build a business that has value by the time they are ready for retirement. However, in a majority of cases, businesses have no value and cannot be sold. We note that doctors would be included in the latter group.

We have assumed in our example the business can be sold as a means of closing the gap in the savings values. As a firm with experience in valuation of businesses, we have prepared a simplistic overview of the valuation as follows: The annual maintainable after-tax earnings of the business must first be determined. This is completed by adjusting the pre-tax earnings for a market value management salary to the owner (as a purchaser is only willing to pay for the earnings over and above what they feel would be a reasonable wage to have someone manage the business for them) and then subtracting off corporate taxes which would be due. Based on our experiences, businesses of this size would generally attract a multiple of 3 to 5 times maintainable after-tax earnings at best, leaving a midpoint valuation of approximately $227,000. This is $52,000 short of funding the RRSP gap in the case of income splitting and $300,000 short in the case of no income splitting. To completely close the GAP with no income splitting, a multiple of 9 times would be required, which is double the fair market value and impossible to attain.

We recognize the shortfall of pension funds available to the small business owner is largely a result of not having someone match their retirement savings. Further, we recognize the small business owner knew this when starting the business and also recognize it is not Finance's responsibility to fund a small business owner’s pension. However, Finance is completely changing the playing field that existed when the decision was made to become self-employed; a playing field that historically has always provided an opportunity to save for retirement.

We believe it is Finance's responsibility to ensure Canada's economy remains sustainable. While Government spending can stimulate an economy, it alone cannot create a sustainable economy. Our economic growth and way to maintaining a sustainable economy is on the back of the private sector, largely being the small business owners who will be impacted by these proposed changes.

While some Canadians are entrepreneurs at heart and will persevere regardless of our tax system, many need to have incentive in order to make the leap. If the proposed changes are enacted as proposed, the only incentive remaining for entrepreneurs is increased income potential if (and that's a big IF) their business idea becomes a success. Further, many spouses forgo their career aspirations to manage the family responsibilities while their spouse is working 70+ hours per week on average to develop the business. In many cases, a family unit would be unable to even attempt to start a business without the ability to income split with their spouse.

While you may or may not agree, we strongly feel these proposed changes will deter numerous Canadians from taking the leap to opening their own business, ultimately having a drastic negative impact on our economy in addition to our country being unable to retain top talent.

Suggestions

Our current Government has taken the approach the way to "fairness" for the middle class is by taxing a large segment of the middle class higher. We ask our Government why it feels the necessity to achieve this so called "fairness" through a tax increase, as opposed to providing the entire population of Canada the ability to income split. In most family units where one spouse earns significantly higher income than the other spouse, that family unit is making sacrifices to allow that to occur, whether it is an employee or a small business owner. Is it so bad to create an environment where it is possible for one spouse to work less and have sufficient time to raise a family, much like the way our historical economy functioned prior to all the tax hikes?

We suggest our tax system be adjusted to allow for joint spousal filings where two spouses would pool their income together and pay tax as a family unit, thus essentially resulting in income splitting / averaging. This would require changes to the existing marginal tax brackets and non-refundable tax credits, the easiest adjustment of which would be to double each since there would then be two taxpayers.

We understand our suggested approach would result in reduced tax revenues, but a reduction in tax revenues results in an increase of cash flow to tax payer’s pockets, which would inevitably stimulate the economy as opposed to the current deflation the entire business community is feeling.

Educational Assistance

Analysis

In discussing income sprinkling above, you will note our comments were largely based on income splitting with spouses. Next, we'd like to address income splitting with children, the largest use of which is to fund a child's post-secondary education.

Firstly, you should note while our Government is suggesting income splitting with children should not be permitted, employees are already income splitting with their children through the use of Registered Education Savings Plans (RESP). Employees contribute to an RESP using their after tax dollars received from employment. The Canada Education Savings Grant (CESG) contributions and any investment income and / or market growth within the RESP are taxed in the hands of the child upon their receipt of the funds, assuming they attend a post-secondary educational institution. Since these amounts were generated through a contribution by the parent, we would argue by definition that the result is income splitting.

We recognize that the target of the proposed tax changes on income sprinkling to children is to a much greater extent than being achieved above. Further, while we can appreciate Finance's concern to some degree, the legislation as proposed will prevent a small business owner from being able to fund their child's education through the use of corporate funds. We recognize at a high level view it appears the small business owner is receiving a benefit due to allowing their child to pay the personal tax on the dividend received, which is much lower than the parent's personal tax would be. However, as outlined in the attached Appendix B, elimination of income splitting does not result in more revenue for the Government. In fact the opposite is true.

Appendix B assumes an employee uses an RESP and a small business owner uses corporate investing and subsequently allocates the corporate funds to the Child. We have prepared an analysis of the results under the current tax regime as well as under the two proposed changes to passive income. Under the current tax regime, the small business owner does require less pre-tax earnings to fund the investment than the employee (assuming the investment can be funded evenly over the 18 years). In many cases, the small business owner may not be able to fund the investment evenly, resulting in higher contribution requirements to offset the lost growth; however, we wanted to provide similar scenarios for the purpose of this analysis. You will note under all scenarios the investment balance at the time the child reaches age 18 is approximately $50,000.

Under the employee-RESP scenario, the employee requires $50,236 of pre-tax income to yield $50,000 in the RESP. Factoring Government RESP grants, the government collects a net amount of $10,800. Under the corporate-current regime scenario, $46,873 of pre-tax corporate income is required to net $50,000 of investments within the corporation. Although the corporate cash requirement is less than the personal cash requirement, the net tax cost to the taxpayer is within $600. Given there is less than a $600 difference under these scenarios, one could argue that the two are actually quite fair. Implementation of the proposals on passive income will create a situation that is not fair. Under Proposal A (small business deduction survives but loss of refundable taxes), the pre-tax corporate income required to net $50,000 in the RESP is $51,066, however, the net tax cost to the taxpayer is $15,977, almost $5,200 more than the employee-RESP option. Under Proposal B (loss of small business deduction but refundable taxes survive), the cash required to fund the $50,000 RESP is $58,761 and the tax cost to the tax payer is $23,252, almost $12,500 more than the employee-RESP option. Clearly, the changes result in an unfair burden in the corporate setting.

There are two primary reasons why this is the case. Firstly, the employee is accessing the benefit of the CESG whereas the small business owner is not. Secondly, the employee's child has the future benefit of the education tax credits, but the small business owner's child does not. You may not be aware, but our tax system currently requires a taxpayer to fully utilize their tuition tax credits before they are permitted to utilize the dividend tax credit. As a result, the child's education tax credits will be fully used as a result of receiving the dividends.

In the event the proposed changes did not allow for allocation to the Child, both the corporate earnings required and the taxes collected paid would be even higher. We understand Finance's position may be the small business owner should simply use an RESP instead, but we see two potential flaws in this logic. Firstly, RESP's only work if there is an ability to fund evenly over time, as the maximum annual grant is based on $2,500 of contributions. Small business owner's income is volatile and they may not be able to contribute each year, but perhaps would be able to fund a larger lump sum in the good years. However, in doing so, they cannot access the full extent of the grant like an employee may be able to.

Secondly, numerous taxpayers have designed a plan to fund their child's post-secondary education based on the tax legislation currently in place. Assume a small business owner currently has $50,000 in their corporation put aside to fund their 17 year old child's post-secondary education, beginning next year. If the small business owner is unable to distribute these funds to their child during 2018, they will need to distribute the funds to themselves either during 2017 or 2018, incurring $15,900 of personal tax based on the business owner's current personal income level within our analysis at Appendix B. Even if the residual cash of $34,100 were invested in an RESP, no CESG would be received based on the current rules. Does it seem fair to you that an employee's child will still have their $50,000 after the proposed changes, but the small business owner's child may only have $34,100, even though both have completed adequate planning?

Further, as advisors to small business owner's, we can assure you with certainty that if the proposed changes to passive investments and income sprinkling are enacted, there will be a large uptake in the use of RESP's as that will certainly be our advice. Has Finance ensured the CESG program has sufficient funds to support this uptake?

Suggestions

Although our current tax system does allow for income sprinkling for the purposes of educational assistance, it does also allow for income sprinkling to children for other purposes even though they are not actively involved in the business. While we do not agree with Finance's view on eliminating this, we do respectfully understand their concern. As such, we have outlined two possible suggestions for consideration as opposed to the proposed changes.

Firstly, we strongly feel that small business owners should not be deprived of the ability to use corporate money to fund their child's post-secondary education. As such, one suggestion would be an amendment to the current proposed legislation to ensure that dividends can continue to be paid to adult children, so long as those funds are being utilized for post-secondary education.

Secondly, if our Government is insistent on enacting the proposed changes, we strongly suggest the governing legislation surrounding the CESG program be amended to remove the annual maximum grant threshold of $500 and the specific limitations for access to the grant where the child is 16 or 17. At a minimum, this would at least allow small business owners who currently have corporate money put aside to access the maximum CESG benefit. If the proposed legislation is enacted and no changes are made to the CESG program, we feel it would be absolutely punitive to small business owners as they would not be able to access the historical CESG grants that would have been available to them had they contributed to the RESP all along.

Accrued Capital Gain during Trust Ownership

Analysis

The proposed legislation aims to ensure that any capital gain accrued during the time the shares were held by a trust (except for a few specific types of trust not widely used) will no longer be eligible for the Capital Gains Exemption (CGE). Based on our analysis of Finance's comments, these proposed changes are designed to address small business owners who are multiplying the CGE across a wide variety of family members, thus incurring significantly less tax on the sale of their business. However, the proposed legislation has a much broader impact than just stopping this type of planning.

Although trusts are widely used for income splitting and multiplication of the capital gains exemption, they are also used for many other purposes. These include creditor protection, estate planning, business succession planning and purification of an operating company to ensure it can continue to even qualify for the CGE. We could write an entire paper on the importance of each of these particular items; however, given the length of our paper as it is, we want Finance to understand that the proposed changes will capture more than just stopping the multiplication of the CGE.

If the proposed legislation were enacted as drafted, the ability to facilitate many of these important aspects would be lost, resulting in further punitive measures against small business owners. Unfortunately each of these areas is highly technical and difficult to quantify, so we have not provided a quantitative analysis related to these given the narrow timeframe at hand. However, we would certainly be open to providing further comments and analysis on this particular area if a reasonable timeframe could be provided to do so.

We do want to talk about the impact of subsection 55(2) of the Income Tax Act (Canada)(the “Act”). Without the use of trust, purification of operating companies to ensure they qualify for the CGE is impossible unless all excess cash was removed from the corporate level, resulting in substantial personal taxes that could jeopardize the very existence of the business. Currently, to purify an operating company and stay within the rules of subsection 55(2) of the Act, Trusts are used to flow excess cash from the operating company to a holding company. This cash may be required for future expansion, funding cash shortfalls, business down turns, etc., but keeping it in the operating company can cause the company to go offside for CGE purposes. Implementation of this change would wipe out the ability for many families to use any CGE. We believe the intent of Finance is stopping the abuse in the use of the capital gains exemption; for example, allocating an $800,000 capital gain to a young child; not to eliminate entirely.

Suggestions

If Finance's concern is with respect to the multiplication of the CGE, we suggest Finance redraft the proposed legislation to ensure shares held by a trust can continue to qualify for the CGE, but perhaps require the recipient of the proceeds on sale to have been impacted or involved in the business for a reasonable period of time. Lack of a salary from a business does not mean the family member did not contribute. Some businesses simply cannot afford to pay a salary. Even if spouses and children are not actually involved in the day to day business, it would absolutely unfair to say those people did not contribute to the value of the business. These are the people who make the sacrifices (be it risk, lack of family time, etc.) which allowed the business to succeed and they should absolutely be entitled to a share of the proceeds if that is what the family decides. We understand it may be that the gain is fully offset by the CGE, but this a lifetime exemption that every Canadian has entitlement to use only once in their lifetime. Is it so bad for the person actually receiving the proceeds not to pay tax on gain? At a minimum, spouses and children should be eligible to claim the CGE on shares held by a trust provided the proceeds on sale are actually distributed to them, for their use. We do agree that income allocated to a spouse or child should belong to that spouse or child and should not be "gifted" back to the principal.

Another suggestion would be to impose a limitation by family members to use the exemption based on the gain accrued during their lifetime as compared to the total length of time the shares were held by the trust. For example, we agree that use a newborn child's capital gain exemption is rather aggressive. It does; however, fall within the existing tax rules. Limiting the use of the CGE based on the ratio described above would create a substantial overall reduction in the multiplication of the exemption where the gain was incurred while the family member wasn't even alive. For example, assume a parent wishes to allocate a gain to a 1 month old and assume the trust held the shares for 20 years (or 240 months). In this case the ratio would be 1/240 x CGE limit. In the case of a 15 year old, the ratio would be 180/240 x CGE limit.

Finally, should the government continue with the changes that include the family trust changes, we suggest that the deemed disposition (in this case) be exempt from Alternative Minimum Tax (AMT). With no cash coming in from an actual sale, AMT will create cash flow issues for many businesses but not likely for the top 1%. We recognize that AMT is recoverable; however, it doesn't resolve the cash flow issue of paying the AMT in the first place.

Passive Investments within a Corporation

Analysis

Although the consultation paper indicates Finance's concern with passive investments within a corporation, Finance has not provided draft legislation on their intended approach, rather provided two different possible approaches. As there is obvious uncertainty as to how the proposed changes would be implemented, we have prepared our analysis under both proposed approaches.

The first approach is to remove access to the small business deduction on any corporate income invested in passive assets (IE - stocks, bonds, GIC's, rental properties, etc.), but leave the other components of the current tax regime for passive income in tact. In short, this means the following would be true (and yes, this is where it begins to bit more technical, but stay with us). Please note the rates discussed below are based on Nova Scotia 2017 tax rates:

1. Tax rate on Corporate income under the $500,000 small business limit used for passive investing would increase from 13.50% to 31%;
2. The initial corporate tax rate on passive investment income will remain at 54.67%, of which 30.67% is added to the Refundable Dividend Tax on Hand (RDTOH) account of the Corporation;
3. The RDTOH becomes refundable at the time of paying a taxable dividend. The maximum refund is equal to the lesser of 38.33% of the taxable dividend and the balance of the RDTOH account at the time of paying the dividend;
4. If the Corporation receives a capital gain, the 50% non-taxable portion of the capital gain is added to the Capital Dividend Account (CDA). The balance of CDA can be distributed to shareholders on a tax

free basis (NOTE - If an individual received a capital gain, 50% would not be taxable. The purpose of this CDA account is to ensure the 50% non-taxable portion can be flowed out to the shareholders tax free, putting them in an equal position to the individual).

The second approach is to allow continued access to the small business deduction on any corporate income invested in passive assets, but remove the current tax regime of RDTOH and CDA. In short, this means the following would be true. Please note the rates discussed below are based on Nova Scotia 2017 tax rates:

1. Tax rate on Corporate income under the $500,000 small business limit used for passive investment would remain at 13.50%;
2. The corporate tax rate on passive investment income would remain at 54.67%, but no portion of this would become refundable;
3. The above concept of CDA created on passive investments would be removed;

Before reviewing the actual calculations, it is important to understand a distinct difference between an employee and small business owner. Since an employee's income remains relatively consistent and can often be forecasted, RRSP's are often the chosen investment vehicle due to the tax deduction and deferred tax on income and growth. If a small business owners income was structured the same, an RRSP would be their choice of investment as well; however, income of a small business owner often fluctuates from year to year.

Small business owner's income is volatile at best, not to mention it is important for any small business owner to hold a "nest egg" for a future downturn in the economy, growth opportunity, or normal capital reinvestments. As a result, small business owners will often not utilize RRSP's because this essentially locks their money away. In order to access money from an RRSP, you must pay tax on the withdrawal, thus reducing the amount available for use. Further, RRSP room is not replenished upon withdrawal, meaning the withdrawals by the small business owner reduces their ability to have that tax free growth an employee enjoys. Although this all sounds very negative for small business owners, there has never been a huge concern due to the lower corporate tax rates that our government now wants to take away.

To quantify the impact of these proposed changes, we have prepared an analysis which compares an employee contributing to his/her RRSP investment to an equivalent corporate investment under the current tax regime as well as Proposal A and Proposal B. To ensure the scenarios are comparable to one another, we have assumed equal income between the employee and small business owner over all years, even though we know this would never occur as noted above. Again, you will note we have used a more modest estimate of $70,000 in annual income (given 2/3 of small business owners make less than $73,000 per year) and have assumed an investment contribution of 10% ($7,000) in all cases.

Appendix C contains 4 different tables that reflect the various implications of investing corporately as opposed to inside an RRSP. Table 1 outlines the advantage of compounding tax-free growth inside the RRSP compared to corporate investments where the income is taxed as it is earned inside the company up to the age of retirement (65). Table 2 outlines the same concept through retirement. Personal and corporate taxes are noted in both Table 1 and Table 2. Table 3 summarizes the personal taxes that will be paid as the various investment portfolios are drawn upon throughout retirement for personal use. Table 4 outlines the total taxes paid (personal and corporate) as both totals and as percentages of the pre-tax investment, income and growth. Table 4 also highlights the length of time the plans can be drawn upon and the timing of when income taxes are actually paid. Below we provide a more detailed explanation of each table.

Table 1 and Table 2 - The first item to note is the employee pays no personal tax before contributing to the RRSP, but the small business owner has less capital to invest, due to having to pay corporate tax before making the investment contributions. As a result of having less principal to invest, even though the earnings were identical, the small business owner generates substantially less investment income. Further, the small business owner must pay tax on investment income as it is generated, whereas the employee's RRSP investment income continues to be invested on a tax-deferred basis. As a result, the business owner once again has less principal, resulting in less market growth.

Table 3 - As a result of the reduced principal invested all the way along, the value of the investments in the corporation are much lower than the value of the RRSP. As a result, the amount of after tax cash flow received by the small business owner throughout retirement, even under the current regime, is only 54% of that received through and RRSP, even though they earned the exact same amount of money and same rate of return. As if the small business owner is not already at enough of a disadvantage, the proposed changes by our Government could reduce this even further to being only 40 - 41% of that received through an RRSP.

Table 4 - In reference to the combined tax paid in comparison to pre-tax amounts invested, we will highlight the small business owner is paying 3.61% less than an employee under the current regime. However, the small business owner is paying their tax as the income is earned whereas the employee is not paying any tax until retirement. The time value of money would surely outweigh this, not to the mention the huge disadvantage already prevalent for small business owners. At this point you may be wondering why small business owners invest corporately based on our analysis, but we've already addressed this in the fifth preceding paragraph.

Based on our analysis, you will also note if each of the employee and the small business owner wish to have the same income throughout retirement (which would be "fair" right?), the small business owner will certainly run out of retirement funds first. In reference to the age when the small business owners plan is fully depleted (between 79 and 83), I think it would be fair to say this is a common age for seniors to begin looking for assisted living care. Based on how Canada currently calculates funding for these types of living arrangements, the reduced retirement income will create a further strain on our Government to contribute towards the senior living accommodations. We find it troublesome that our Government appears to be concerned about Canadians having sufficient income throughout retirement, yet they propose legislation that severely inhibits the retirement plans of small business owners.

CRA Concern

The final point we would like to make is not actually concerning the punitive treatment to small business owners, but rather a tax revenue concern we are unsure that our government has considered. We assume that the government is hopeful these proposed changes will result in an increase tax revenues; however, have they considered the timing of the tax revenues? With the proposed tax changes on passive investments within corporations, it appears that small business owners will be forced to utilize RRSP's. Accordingly, there will be drastic change in the timing of the collection of tax revenue. Please refer to Appendix D for an illustration.

According to Statistics Canada, there were 1,144,000 small businesses within Canada as at December 2015. Further, we would hazard a guess that at least 50% of these small business owners would have a spouse or child actively involved in the business. This would equate to 1,716,000 people involved in the operation of SME's in Canada. Now let's assume that 30% of these people (500,000) begin using RRSP's instead of corporate investing. The $7,000 that was previously invested at the corporate level will now be paid out as a salary and contributed to an RRSP. This will result in lost tax revenue at the corporate level of $910 per person, or $455,000,000, nationally each year. We acknowledge that is only a deferral but it is a substantial deferral that would not be lost if the changes to passive investing at the corporate level was not changed.

No additional personal tax revenue will be received since the additional salary is going straight into an RRSP. Further, the principal will now be invested inside an RRSP instead of the corporation, meaning no annual corporate taxes will be paid on the annual income and / or growth, thus resulting in even more lost corporate tax revenue. The Government will not realize personal tax revenue from the RRSP until such time as the taxpayer withdraws the funds.

The length of time it will take before the timing corrects itself depends on the age of the taxpayer, but in some cases, it could take 40+ years (IE - a taxpayer who is currently 25 and doesn't withdraw from the RRSP until 65). Now we recognize that over the long-term, the Government will collect more tax from the RRSP then they will from the corporate investing, but how does our Government intend to finance this lost tax revenue until the timing issue corrects itself?

Suggestions – Passive Income

Based on various comments made by Finance, it appears the primary cause for concern is the ability for a small business owner to invest an unlimited amount of earnings corporately, paying only the corporate tax rate, whereas an employee will pay personal tax on all of their earnings except for contributions to an RRSP. If our interpretation is correct, why is Finance closing the door on corporate investing completely?

Perhaps Finance should consider something similar to an RRSP, but for a corporation. We see two potential alternatives as to how such a regime could be introduced. We have outlined an overview of the alternatives, but a more in depth analysis would be required, which we would be pleased to consult on further:

1. Similar to an individual, the corporation could contribute to a corporate RSP (CRSP) and receive a deduction against its corporate income for the contribution. However, any withdrawals from the CRSP would be taxed as active business income. The CRSP limit would be cumulative, similar to that of an individual, and could be calculated as follows:

    a) Prior year unused CRSP limit plus the lesser of:
        i. (Maximum CRSP limit for the respective year + Recovery of lost maximum limit*)
        ii. Current year earnings x 18%

    *Recovery of lost maximum limit - In each year where the corporate earnings were less than the amount needed for maximum CRSP, the difference between the maximum CRSP limit and the actual CRSP limit created could be added to this pool. If earnings in a subsequent year exceed the amount required to maximum CRSP limit in that year, the excess earnings could be utilized to generate additional CRSP room up to a maximum of this pool's balance. Although this isn't something available to individuals, it would be necessary in a corporate setting due to the volatility of earnings (A corporation can easily go from $100,000 of income to a loss year-over-year).

2. Another alternative would be to limit the amount of corporate income annually which can be utilized for passive investment purposes. Unlike the CRSP scenario as noted above, the annual limit under this regime would need to exceed the annual RRSP limit available to an individual. The rationale is that the corporation would still be subject to tax before investing the funds and would continue to be subject to tax on the investment income and growth (as illustrated in Appendix C). Further, because

of the loss in principal due to tax, a small business owner needs to be able to invest more income in order to remain "equal" in retirement.

We would need to complete further analysis to determine an equivalent amount to account for these items, but would suggest the annual limit would need to be a minimum of $50,000. Again, to allow for a corporation's volatility in earnings, the annual limit would need to accumulate regardless of actual corporate income.

Corporate Integration

Analysis

Canada's tax system includes the concept of corporate Integration, which essentially means the after tax cash flow of a dollar earned through a corporation and fully distributed to its shareholder should be identical to that earned by an individual. Under the current tax regime, our system is the closest to perfect integration for corporate income under $500,000 as it has ever been. However, our current system continues to allow for excessive tax for corporate income over $500,000 and for passive investment income inside a corporation. Please refer to Appendix E which illustrates corporate Integration at the top marginal tax bracket in Nova Scotia.

The effective tax rate for active corporate income under $500,000 is 54.13% for income earned through a corporation vs. 54.00% for an individual. This is essentially near perfect integration. However, for active corporate income over $500,000 and for passive investment income, the combined tax rates are 59.69% and 61.02% respectively. These amounts exceed the individual's top marginal rate by 5.69% and 7.02%, respectively. These are based on the top marginal tax rates, meaning we are talking about the top 1% of Canadians, but how is it fair that a small business owner can pay a higher rate of tax than the top marginal personal tax rate ?

Now again, Finance may argue the business owner could avoid this flaw in corporate Integration by paying all corporate income out as a salary, but this would fail to recognize that corporate income is calculated on an accrual basis, not a cash basis. Therefore, just because a corporation has $700,000 of corporate taxable income, does not mean the corporation has $700,000 of cash available to pay out a salary. As a result, it is virtually impossible for a business owner to pay out 100% of their corporate income as a salary, leaving at least a portion subject to these excessive rates.

BUT, as if the above is not already punitive enough, our government has proposed that one of the options to deal with passive investments within corporations may be to remove the concepts of RDTOH and CDA (as discussed under passive investments above). In doing so, the combined tax rate on passive income within a corporation would climb to 75.96%, exceeding an individual's maximum tax rate by 21.96%. This is clearly punitive tax treatment towards small business owners and is absolutely offensive tax policy.

Suggestions

As noted above, the combined taxes for active corporate income over $500,000 and passive investment income within a corporation already result in punitive taxation to small business owners (at both the top marginal bracket as illustrated above and throughout the marginal brackets).

To correct for corporate Integration on active corporate income over $500,000, the dividend gross up and dividend tax credit regime for eligible dividends requires adjustments at both the Federal and Provincial levels. We have not prepared the calculations to determine the necessary adjustments (though we could), we do want to bring this to your attention.

To correct for corporate Integration on passive investment income within a corporation, an entirely new dividend regime would need to be created. Currently, the dividends paid by a corporation as a result of after tax passive investment income are ineligible dividends, for which the dividend gross up and dividend tax credits are based on corporate Integration on active corporate income under $500,000. This creates issues for corporate integration since the corporate tax rates between active corporate income under $500,000 and passive investment income are different. In order to correct this, we would suggest the following changes to our tax system would be required. These changes are necessary regardless of whether the proposed changes for passive investments within a corporation are enacted or not as punitive taxation is already occurring:

1. Create yet another corporate pooled account balance called Passive Rate Income Pool (PRIP);
2. The after tax of all passive investment income earned by a corporation would be added to PRIP;
3. If the refundable tax regime remains in place, any dividend refund the corporation would receive as a result of paying a dividend would be added to the PRIP immediately before the dividend was paid;
4. When paying a dividend, the corporation would declare the dividend as a "Passive Dividend", thus reducing the PRIP. The dividend gross-up and dividend tax credit would be calculated to ensure the combined tax rate after distribution to the individual shareholder was equal to maximum individual tax rate, thus achieving perfect corporate integration.

If the government is truly concerned about creating tax fairness by increasing tax on the wealthy business owners (“the 1%”), why not simply increase the tax rate on active business income in excess of $500,000? Adding 1-2% to these taxpayers would likely achieve the desired tax revenue and target the 1% that the government wishes to target. The other changes would not be required as they do not target the 1%. We acknowledge that the dividend tax credit system would need to be adjusted to ensure integration is maintained but, overall, this would be a more effective approach, easier and would target the intended tax payers.

Changes to Section 84.1 of the Income Tax Act (Canada) (ITA)

Analysis - Deceased Taxpayers

We apologize in advance for this next analysis being technically complex, but unfortunately the analysis outlined below must be understood to comprehend the punitive nature of the resulting taxation.

When a person passes away, they are deemed to dispose of everything they own for fair market value, including shares of a private corporation. As a result, significant income taxes typically arise and the capital gains exemption cannot be used to shelter these gains from tax. When the cash is paid out of the company by way of a dividend to the estate or the individual beneficiaries, additional taxes are incurred at the personal level. This situation is often referred to as double taxation. A third level of tax often arises on the liquidation of the underlying assets of the company as these assets typically have inherent taxable gains.

There is currently an alleviating provision under subsection 164(6) of the ITA where the assets of the company are liquidated within the first taxation year of the estate, resulting in dividends being paid to estate. In this case, a capital loss arises on the shares which is carried back to offset the capital gain resulting from the deemed disposition, thus bringing the tax on the deemed disposition to NIL. As a result, the only tax paid is the tax on the dividends to the estate and tax on the liquidation of the corporate assets.

Another common method is referred to as the "pipeline". To accomplish the pipeline, the estate completes various transactions which ultimately results in a promissory note (equal to the fair market value of the shares of the company at the time of death) due to from the company to the estate. As a result, cash of the company equal to the promissory note can be paid to the estate on a tax free basis over a period of time. The result of the pipeline planning is the total tax paid is the tax paid on the capital gain on the deemed disposition of the shares on death. Since the current tax rates on capital gains are lower than current tax rates on dividends, the pipeline will generally result in less taxes being paid overall.

If the proposed changes to Section 84.1 of the ITA were enacted, the pipeline transaction would no longer be available, meaning the only method of mitigating double taxation would be to liquidate the assets of the company within the first taxation year of the estate. Although this may seem like a viable option, it often takes much longer than the first taxation year of the estate to liquidate the assets of the company. Further, these planning opportunities are not widely known to the general public and it is not uncommon for a mourning executor to wait over a year before even contacting an advisor who would be aware of the opportunity. In the event the assets are not liquidated within the first year, double taxation would result. The impact of this double taxation has been illustrated in Appendix F and Appendix F1.

In preparing this analysis, we started with an individual owning an RRSP worth $1,000,000 at the time of their passing. In Appendix F, we calculated the equivalent corporate investment at the time of passing under each scenario. The concept of how we determined the equivalent corporate investment is the same as the logic outlined above for passive investments within a corporation.

We have prepared an analysis of the taxes which would be paid under each of the scenarios outlined in Appendix F1. We understand the pipeline plan under the current tax regime does provide some favourable results, but there has been an immense amount of jurisprudence on this specific transaction which outlines very specific items which must occur to ensure one does not fall into the current Section 84.1. As a result, the pipeline transaction is not widely used due to it requiring a specific fact set in order to be applicable. However, we expect this may be Finance's target with the proposed revisions to Section 84.1.

If Finance's intention is to prevent the pipeline transaction from occurring, the impact of this needs to be understood by Finance, which is the purpose of Appendix F. Since the loss carry back under 164(6) is only available during the first taxation year of the estate, the assets of the company can often not be liquidated in time to access this benefit. Reasons why this may not be possible range from extended periods of mourning, disagreements between family members, or even estate litigation in some circumstances.

You will note that even under our current tax regime, the combined income tax rate can reach 72.89% where no loss carry back under 164(6) is available. You may be questioning how such a high rate of tax can occur, and the answer would simply be double taxation as we've highlighted above. However, you will note under each of Proposal A and Proposal B this combined tax rate can climb even higher to 83.27% and 75.66% respectively. Given the Income Tax Act is generally drafted to prevent double taxation; it is difficult to comprehend how Finance considers these changes fair tax policy.

Further, it should not be lost on Finance that even with the loss carry back under 164(6), combined tax rates under Proposal A and Proposal B can reach 62.43% and 75.66% respectively, both of which exceed the maximum personal income tax rate of 54% in Nova Scotia.

Suggestions - Deceased Taxpayers

If Finance is insistent on the proposed tax changes to Section 84.1, it will be necessary to expand the provisions under 164(6) to ensure the loss carry back is available beyond the first taxation year of the estate. Otherwise, double taxation will begin to occur within our tax system, which we surely hope is not the intent.

Analysis - Related Business Purchasers

When an unrelated purchaser acquires shares of a corporation, a common tax planning technique is to have the purchaser incorporate a separate corporation (Holdco) to acquire the shares. The benefit in doing so is that if the purchaser is borrowing funds to purchase the shares, the loan payments related to principal can be paid with after-tax corporate dollars (only 13.5% tax paid) vs. after-tax personal dollars (between 23.87% and 54%). In the event the purchase is funded with the purchaser's personal funds, the use of Holdco allows them to extract the amount of their investment from Holdco over time without incurring any personal taxes, which is fair given the money they provided to the Holdco was after tax personal cash.

The Income Tax Act has a long-standing provision to prevent certain tax benefits achieved through share transactions between related persons. Where a vendor and purchaser are related, the adjusted cost base (ACB) of the purchaser is categorized between "soft ACB" and "hard ACB". The soft ACB is equal to the LCGE claimed by the vendor and the hard ACB is equal to the total ACB less the soft ACB. If the purchaser chooses to transfer the acquired shares to a separate corporation after acquiring them, the aggregate of the non-share consideration received is limited to the hard ACB or a deemed dividend will arise. As a result, if a related purchaser wanted to use a Holdco, the amount of debt the Holdco could assume or value of promissory note the Holdco could issue to the purchaser would be equal to the hard ACB. To simplify, a parent cannot sell his/her shares to a child's corporation, whether the parent utilized the capital gains exemption or not. However, a parent can sell to an unrelated person's company and can also utilize the capital gains exemption.

Under the proposed legislation, Finance has suggested that *all* ACB received as a result of a purchase from a related party will be soft ACB. As a result, if the purchaser chose to transfer the acquired shares to a separate corporation after acquiring them, the receipt of any non-share consideration would result in a deemed dividend.

If these changes are enacted, a related purchaser would no longer be able to use a Holdco for the purposes of repaying debt corporately or extracting cash tax free since no hard ACB exists, even though the vendor did not use the CGE. Further, we would highlight that this concept of soft ACB only applies to related persons, so if the purchaser were unrelated to the vendor, the entire ACB is considered hard and Holdco could issue non-share consideration (IE - assume debt or issue a promissory note) for the full ACB, even with the use of the CGE. As a result, these changes would put a related purchaser at a significant disadvantage, thus greatly impacting the ability to move small businesses down the family line, even in situations though these transactions are completed at fair market value. These amendments further increase the disadvantage to a related buyer, creating a further motivation to sell to an unrelated person. This could potentially allow for industry consolidation, which is not a step in the right direction for our economy.

Suggestions - Related Business Purchasers

Many related party purchases occur at true fair market value and Finance needs to recognize this to ensure family owned business are not sold to unrelated purchasers solely because an issue within our tax system. Where transactions can be supported as fair market value, Section 84.1 should not apply in any way, including the current application to create "soft" ACB for the portion of the gain sheltered by a related person.

Conclusion

It is our hope that the above submission provides you with an in depth overview of both the current tax system and how the proposed tax changes will impact small business owners. After having time to digest this material, we are even more hopeful that you will be able to see how the results are not only negative, but actually punitive in many cases. Further, we hope that you will give some thought to our suggestions as we feel they are fairly representing taxpayers, but also allowing Finance to accomplish what has been stated as their objective without destructing the entire small business community in the process.

We would also like to inform you that it is our intention to also forward a copy of this submission to every Member of Parliament across the country and directly to the Department of Finance. Further, we will be making this submission a public document via our website, social media, and perhaps the news. As such, feel free to discuss this particular document with your fellow members while in Ottawa.

If you have any questions, concerns or comments regarding this submission, we request that you to contact us directly so we can address them accordingly. We feel consultation on these changes is of the upmost importance to our Country and we will make it a priority to ensure we are available for further clarification via telephone or in person.

Yours truly,

Belliveau Veinotte Inc.

Paul MacNeil, CPA CMA CBV
Partner - Tax & Business Valuation
(902) 543-7805 ext. 148
pmacneil@bvca.ca

Jason Conrad, CPA CA
Tax Manager
(902) 444-8068 ext 104
jconrad@bvca.ca

Appendix A
Income Splitting
Impact on $80,000 family income

Facts and Assumptions

1) A small business generates $80,000 of annual corporate income

2) The principal's spouse is not actively involved in the business as they manage the family while the principal is working extensive hours to try and grow the business

3) Under the current tax regime, all dividends are split 50/50 between the principal and their spouse

4) Under the proprosed changes to income sprinkling, there would be no ability to income split with the principal's spouse

5) All below calculations are based on 2017 Nova Scotia Tax rates

Calculations

	Current	**Proposed**
Corporate earnings	80,000	80,000
Less: Corporate taxes	(10,800)	(10,800)
After tax cash available for dividends	**69,200**	**69,200**
Dividends to Principal	34,600	69,200
Less: Personal tax on dividends	(2,116)	(10,759)
After-tax cash flow	**32,484**	**58,441**
Dividends to Principal's spouse	34,600	-
Less: Personal tax on dividends	(2,116)	-
After-tax cash flow	**32,484**	**-**
Aggregate after tax cash flow	**64,968**	**58,441**

Appendix A1
Income Splitting
Calculation of Taxes Paid - Employee vs. Business Owner

Facts and Assumptions

1) An employee begins their career at age 25 earning a salary of $40,000 and receives annual raises equal to 3% of their salary

2) The employee's employer provides a company pension plan whereby the company will match (dollar for dollar) their employees RRSP contributions to a maximum of 6% of the employees income

3) To maximize their retirement income, the employee contributes the maximum 6% to their RRSP and their employer matches this 6% (IE - 12% total)

4) The business principal starts their own business at age 25. The business generates the following net incomes throughout the principal's working career

- Age 25 to Age 29 inclusive - $30,000
- Age 30 to 34 inclusive - Income from Age 29 + annual increases of $1,500
- Age 35 to 39 inclusive - Income from Age 34 + annual increases of $2,500
- Age 40 to 44 inclusive - Income from Age 39 + annual increases of $4,000
- Age 45 to 49 inclusive - Income from Age 44 + annual increases of $5,000
- Age 50 to 65 inclusive - Income from Age 49 + annual increases of $2.530

5) The business principal takes 1/3 of the company's net income as salary to ensure they generate RRSP room equal to 6% of the annual net company earnings. All earnings after paying corporate tax is distributed via a dividend

6) The business principal contributes annually to their RRSP, the amount being equal to 6% of the company's annual earnings

7) Average annual growth within all savings plans are assumed to be 5%

8) At age 65, the business principal intends to sell their business, the proceeds of which will be used for retirement. Based on our experience, many businesses never have any value due to the business being so reliant on the principal, but in the event a business is transferrable, a business of this size would generally attract a multiple of 3 to 5 times; or an average of 4.

9) All below calculations are based on 2017 Nova Scotia Tax rates

Calculations

	Total earnings age 25 - 65	Cash available for personal consumption	Advantage (disadvantage of business owner)	Corporate taxes paid age 25 - 65	Personal taxes paid age 25 - 65	Combined taxes paid age 25 - 65	Combined taxes paid as % of Total Earnings	Jobs created
Employee	3,147,000	2,071,000	-	-	753,300	753,300	23.94%	No
Business Owner - Dividends split 50/ 50 with Spouse	3,147,000	2,291,000	220,000	277,100	299,900	577,000	18.33%	Yes
Business Owner - No income splitting	3,147,000	2,094,000	23,000	277,100	497,900	775,000	24.63%	Yes

	Additional cash flow over Employee	Growth which could be earned on savings	FMV of savings	Employee / Business Owner Contributions to RRSP	Employer Contributions to RRSP	Growth in RRSP Plan	FMV of pension / RRSP @ age 65	Total FMV of retirement savings	Advantage (disadvantage of business owner)
Employee	-	-	-	188,790	188,790	638,500	1,016,080	1,016,080	-
Business Owner - Income splitting	220,000	52,870	272,870	188,790	-	275,100	463,890	736,760	(279,320)
Business Owner - No income splitting	23,000	2,380	25,380	188,790	-	275,100	463,890	489,270	(526,810)

	Potential value of business (If saleable)	
Annualized business earnings at Age 65	135,480	
Less: Reasonable wage for management of the business	(70,000)	
Maintainable pre-tax earnings of the business	65,480	
Less: Corporate taxes	(8,840)	
Maintainable afte-tax earnings of the business	56,640	A
Estimated achievable multiple	4	
Estimated value of business	**226,561**	
Required value of business to compensate for pension variance - With Income Splitting	**279,320**	B
Implied multiple required **(B / A)**	**5**	
Required value of business to compensate for pension variance - Without Income Splitting	**526,810**	B
Implied multiple required **(B / A)**	**9**	

Appendix B
Educational Assistance - Children
Comparison of Government revenues between Employee and Business Owner

Facts and Assumptions

1) Employee earns an annual salary of $70,000

2) Business owners corporation has annualized net income of $70,000

3) Employees target balance for an RESP in the year their child turns age 18 is $50,000

4) Business owners target is to have $50,000 of corporate funds available to fund their childs post education in the year their child turns 18

5) The RESP and corporate funds will be paid out to the child evenly over 4 years, being $12,500 each year

6) Assume the portion of the Child's annual tuition which will qualify for the education tax credit is equal to $6,250

7) Assume the Child has income equal to the basic federal exemption in each year they receive the funds

8) Federal government provides funding to the RESP equal to 20% of the employees contributions

9) All investments (RESP or otherwise) grow at 3% annually

10) The post secondary education tax credit regime continues as it currently applies

11) The below reference to "Proposal A" assumes the following proposed legislation for passive investing is passed - Continued access to the small business deduction for passive investing, but removal of the refundable tax regime and Capital Dividend Account

12) The below reference to "Proposal B" assumes the following proposed legislation for passive investing is passed - No access to the small business deduction for passive investing, but continued use of the refundable tax regime and Capital Dividend Account

	Individual	**Corporation (Current)**	**Corporation (Proposal A)**	**Corporation (Proposal B)**
Taxable earnings required to fund the investment	50,236	46,873	51,066	58,761
Less: Personal taxes paid before funding investment	(18,673)	-	-	-
Less: Corporate taxes paid before funding investment	-	(6,328)	(6,894)	(18,216)
Net funds invested by Individual / Corporation	31,563	40,545	44,172	40,545
Net Government contributions	6,313	-	-	-
Total funds invested	37,876	40,545	44,172	40,545
Growth in investment from Child's birth to age 18	12,132	12,453	12,869	12,453
Less: Tax paid on investment growth	-	(2,989)	(7,036)	(2,989)
Balance of investment when Child reaches age 18	**50,008**	**50,009**	**50,006**	**50,009**
Taxes paid before funding investment	18,673	6,328	6,894	18,216
Taxes paid on investment growth	-	2,989	7,036	2,989
Personal taxes paid by Child on receipt of funds	4,388	2,048	2,048	2,048
Total taxes collected by Government	23,061	11,364	15,977	23,252
Less: CSEG received	(6,313)	-	-	-
Less: Future benefit of education tax credit	(5,948)	-	-	-
Tax cost to family (net of CSEG)	**10,800**	**11,364**	**15,977**	**23,252**

Appendix C
Impact of Proposed Changes to Passive Investments inside a Corporation

Facts and Assumptions

1) To ensure these calculations are comparing like items, assume the following

- Employee earns an annual salary from Age 25 to 64 inclusive and retires upon reaching Age 6!
- Employee contributes $7,000 annually to an RRSP from Age 25 to 64 Inclusive
- A business generates $70,000 of taxable inomce from the Principals Age 25 to 64 inclusive and retires upon reaching Age 6!

- To ensure the business owner and the employee have the identical personal after-tax cash flow throughout their working careers, the business only retains $7,000 of its income annually for the purpose of investing

2) Assumed annual investment income and market growth are 2% and 3% respectively

3) Beginning at age 65, each taxpayer wishes to receive $34,125 of annual after-tax cash flow

4) The below reference to "Proposed A" assumes the proposed changes to remove access to the Small Business Deduction, but retain the refundable tax and capital dividend regimes, are passed as legislation

5) The below reference to "Proposed B" assumes the proposed changes to continue access to the Small Business Deduction, but remove the refundable tax and capital dividend regimes, are passed as legislation

6) All below calculations are based on 2017 Nova Scotia Tax rates

Calculations

Table 1 - Summary of Investment, growth and tax incurred on growth, up to retirement

	A	B	C	D	E	F	G (C + D +E + F)
	Taxable income used for investing	Tax paid prior to investing	Principal Invested	Aggregate Investment Income Generated Prior to Retirement	Aggregate Market Growth Prior to retirement	Tax paid on Investment Income & Market Growth prior to retirement	Net value of investment at time of retirement
RRSP	280,000	-	280,000	234,695	352,043	-	866,738
Corporate Investment - Current Regime	280,000	(37,800)	242,200	169,796	254,693	(92,827)	573,862
Corporate Investment - Proposed A	280,000	(86,800)	193,200	135,444	203,166	(74,047)	457,763
Corporate Investment - Proposed B	280,000	(37,800)	242,200	169,796	254,693	(92,827)	573,862

Table 2 - Summary of Investment, growth and tax incurred on growth during retirement

	G	H	I	J	K (G + H + I + J)
	Net value of investment at time of retirement	Aggregate Investment Income & Market Growth generated throughout retirement	Tax paid on Investment Income & Market Growth through retirement	Refund of corporate taxes previously paid	Aggregate Funds available throughout retirement
RRSP	866,738	1,011,844	-	-	1,878,582
Corporate Investment - Current Regime	573,862	264,121	(170,697)	147,838	815,123
Corporate Investment - Proposed A	457,763	166,047	(119,080)	108,274	613,004
Corporate Investment - Proposed B	573,862	245,088	(163,413)	-	655,536

Table 3 - Total Withdrawals, Tax incurred to Withdraw & After tax cash flow

	K	L	K + L	
	Aggregate amount received by Taxpayer throughout retirement	Personal Taxes	Net after tax cash flow to Taxpayer	% of after tax cash compared to RRSP
RRSP	1,878,582	(657,504)	1,221,079	100.00%
Corporate Investment - Current Regime	815,123	(150,553)	664,570	54.42%
Corporate Investment - Proposed A	613,005	(114,202)	498,803	40.85%
Corporate Investment - Proposed B	655,537	(162,180)	493,357	40.40%

Table 4 - Calculation of Combined Tax Rate and Timing of Tax Collections

	(A + D + E + H)	(B + F + I + J +L)					
	Aggregate of Pre-tax Prinicipal, Investment Income and Market Growth	Combined taxes paid	Combined Tax as a % of Aggregate Pre-tax amounts	Age when plan is fully depleted	Age when corporate taxes on principal invested are paid	Age when tax on Investment Income & Market Growth are paid	Age when Personal taxes are paid
RRSP	1,878,582	657,504	35.00%	100	N/A	N/A	65-100
Corporate Investment - Current Regime	968,610	304,039	31.39%	83	25-65	25-83	65-83
Corporate Investment - Proposed A	784,657	285,855	36.43%	79	25-65	25-79	65-79
Corporate Investment - Proposed B	949,577	456,220	48.04%	79	25-65	25-79	65-79

Appendix D
Lost Tax Revenue - Change to RRSP from PassiveCorporate Investments

Facts and Assumptions

1) As a result of the proposed changes, lets assume of the $1.144M SME's in Canada (per 2015 Statistics Canada), 500,000 of these SME owners change their investment strategy from Corporate investing, to RRSP's

2) Further, prior to switching to RRSP investing, assume each of these Canadians were investing in the manner outlined in Appendix C

3) Further, assume the average taxpayer's working life to be 40 years, suggesting this transition would take 40 years to correct itself

Calculations

	Corporate Income being Invested	Less: Corporate taxes which would be due	Number of Canadians to use RRSP investing instead of Corporate	Annual Reduction in Corporate taxes collected
Corporate Investing - Current Regime	7,000	910	500,000	455,000,000

Appendix E
Tax Integration at Top Marginal Personal Tax Rate

Facts and Assumptions

1) 2017 Corporate tax rates (Nova Scotia)

- Under Small Business Limit	13.50%
- Over Small Business Limit	31.00%
- Passive Investment Income	54.67%
- Refundable Portion of tax on Passive Investment Income	30.67%

2) 2017 Personal Top Marginal tax rates (Nova Scotia)

- Employment Income	54.00%
- Ineligible dividends (as percentage of actual dividend)	46.97%
- Eligible dividends (as percentage of actual dividend)	41.58%

3) The below reference to "Proposed" assumes the Government legislates the proposed changes to remove the current refundable tax regime

4) The below calculations assume the taxpayers income already exceeds $202,800 (IE - in the top 1% of Canadians)

5) All below calculations are based on 2017 Nova Scotia Tax rates

Calculations

	Employee
Incremental employment income	100,000
Less: Personal Income Tax	(54,000)
After tax cash received by employee	**46,000**
Effective combined tax rate	**54.00%**

	Active Income under Small Business Limit	Active Income over Small Business Limit	Passive Investment Income (Current)	Passive Investment Income (Proposed)
Corporate Income	100,000	100,000	100,000	100,000
Less: Corporate Income Tax	(13,500)	(31,000)	(54,670)	(54,670)
Cash remaining for payment of dividend	86,500	69,000	45,330	45,330
Corporate tax refund received on payment dividend	-	-	28,178	-
Total actual dividend to shareholder	86,500	69,000	73,508	45,330
Less: Personal Income Tax on dividend	(40,629)	(28,690)	(34,527)	(21,292)
After tax cash flow received by shareholder	**45,871**	**40,310**	**38,981**	**24,038**
Effective combined tax rate	**54.13%**	**59.69%**	**61.02%**	**75.96%**

Appendix F
Impact of Proposed Changes to Section 84.1

Facts and Assumptions

1) The below calculations are based off of a $1,000,000 RRSP at the time of passing (comprised of $400,000 of principal investment, $300,000 of investment income generated, and $300,000 of market growth generated)

2) Each of the below scenario's involving a corporation have been adjusted from the $1,000,000 RRSP value to account for corporate taxes paid throughout the duration of the investment. As a result of the reduction in principal invested due to the payment of corporate taxes, the investment income and market growth are less than that of the RRSP. This ensures the below analysis is comparing two "like" examples, as each scenario contemplates a $400,000 pre-tax investment.

3) The equity growth is deferred until the investment is liquidated after the time of passing

4) The below reference to "Proposed A" assumed the proposed legislation for passive investments is passed to allow claim of the small business rate, but removal of the refundable tax and capital dividend regimes

5) The below reference to "Proposed B" assumed the proposed legislation for passive investments is passed to not allow claim of the small business rate, but the current regime of refundable tax and capital dividend will remain

6) All below calculations are based on 2017 Nova Scotia Tax rates

Calculations

	A		B	C		D	E	B + D + E	A + C + E		
Scenario	**Aggregate investment before tax**	**Less: Tax required to be paid prior to investing**	**Funds available to invest**	**Aggregate investment income earned before tax**	**Less: Net tax paid on investment income**	**After tax investment income retained**	**Equity growth**	**Calculated value at time of Passing**	**Total pre-tax investments**	**Lost investment growth due to taxes paid**	**Equivalent investment if taxes had not been paid**
RRSP	400,000	-	400,000	300,000	-	300,000	300,000	1,000,000	1,000,000	-	1,000,000
Corporate investment with 164(6) loss carryback - CURRENT	400,000	(54,000)	346,000	259,500	(62,280)	197,220	232,809	776,029	892,309	107,691	1,000,000
Corporate investment with pipeline - CURRENT	400,000	(54,000)	346,000	259,500	(62,280)	197,220	232,809	776,029	892,309	107,691	1,000,000
Corporate investment with no 164(6) loss carryback - CURRENT	400,000	(54,000)	346,000	259,500	(62,280)	197,220	232,809	776,029	892,309	107,691	1,000,000
Corporate investment with 164(6) loss carryback - PROPOSED A	400,000	(54,000)	346,000	259,500	(141,869)	117,631	198,699	662,331	858,199	141,801	1,000,000
Corporate investment with no 164(6) loss carryback - PROPOSED A	400,000	(54,000)	346,000	259,500	(141,869)	117,631	198,699	662,331	858,199	141,801	1,000,000
Corporate investment with 164(6) loss carryback - PROPOSED B	400,000	(124,000)	276,000	207,000	(49,680)	157,320	185,709	619,029	792,709	207,291	1,000,000
Corporate investment with no 164(6) loss carryback - PROPOSED B	400,000	(124,000)	276,000	207,000	(49,680)	157,320	185,709	619,029	792,709	207,291	1,000,000

Appendix F1
Impact of Proposed Changes to Section 84.1

Facts and Assumptions

1) The below reference to "Proposed A" assumed the proposed legislation for passive investments is passed to allow claim of the small business rate, but removal of the refundable tax and capital dividend regimes

2) The below reference to "Proposed B" assumed the proposed legislation for passive investments is passed to not allow claim of the small business rate, but the current regime of refundable tax and capital dividend will remain

3) The below calculations assume the deceased individual and the estate are paying tax at the top marginal tax rate

4) All below calculations are based on 2017 Nova Scotia Tax rates

Calculations

	A	B	C	D	A + B + C + D				
Scenario	**Total value at time of Passing (Table F)**	**Less: Corporate taxes**	**Less: Trust taxes paid**	**Less: Personal taxes paid**	**Net cash flow to estate / beneficiaries**	**Advantage (disadvantage) over RRSP**	**Total pre-tax investments (Table F)**	**Cash retained as % of total pre-tax investments**	**Combined income tax rate paid throughout duration of investment**
RRSP	1,000,000	-	-	(540,000)	460,000	-	1,000,000	46.00%	54.00%
Corporate investment with 164(6) loss carryback - CURRENT	776,029	(27,937)	(296,704)	(31,429)	419,959	(40,041)	892,309	47.06%	52.94%
Corporate investment with pipeline - CURRENT	776,029	(63,638)	-	(209,528)	502,863	42,863	892,309	56.36%	43.64%
Corporate investment with no 164(6) loss carryback - CURRENT	776,029	(27,937)	(296,704)	(209,528)	241,860	(218,140)	892,309	27.11%	72.89%
Corporate investment with 164(6) loss carryback - PROPOSED A	662,331	(54,314)	(285,585)	-	322,431	(137,569)	858,199	37.57%	62.43%
Corporate investment with no 164(6) loss carryback - PROPOSED A	662,331	(54,314)	(285,585)	(178,829)	143,602	(316,398)	858,199	16.73%	83.27%
Corporate investment with 164(6) loss carryback - PROPOSED B	619,029	(22,285)	(236,677)	-	360,067	(99,933)	792,709	45.42%	54.58%
Corporate investment with no 164(6) loss carryback - PROPOSED B	619,029	(22,285)	(236,677)	(167,138)	192,929	(267,071)	792,709	24.34%	75.66%