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Canadian Tax Alert

Planning in light of uncertainty

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Since the July 18, 2017 Department of Finance announcement, the tax landscape faced by private companies in Canada has been filled with questions and uncertainty. While some proposed measures have been abandoned and others clarified, many still require further details to provide meaningful direction.

This Canadian Tax Alert aims to help private companies navigate and plan despite the uncertainty, by highlighting areas to consider going forward, including discussions to have with your Deloitte tax advisor.

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Action to be taken before the end of 2017

Legislation with respect to limitations on "income sprinkling" is expected to take effect on January 1, 2018, leaving payments in 2017 unaffected. To the extent that individuals will be subject to "tax on split income" under the new rules in 2018, accelerating future payments and maximizing current payments in 2017 should be considered. Further, as personal tax rates on non-eligible dividends are expected to increase in 2018 as a consequence of the decrease in the small business tax rate, a further benefit may result from accelerating dividend payments into 2017.

Planning for future family income

Where family members will be subject to tax on split income in 2018, there may be other methods of compensating those family members in the future. New tax structures and compensation models should be considered for 2018 and beyond.

Structuring passive investment holdings

Given what we know of the passive investment proposals, thought should be given now to optimizing grandfathering and the de minimis elements of any new legislation before changes take effect, likely in 2018. Caution should be exercised in this area, as there has been no draft legislation released, and significant uncertainty remains regarding what the ultimate impact may be and how grandfathering rules might be developed and applied.

Revisit estate plans and wills

With all the changes to private company taxation, any wills drafted and estate tax modeling done in the past should be revisited in light of both the current changes (income sprinkling and passive investments) as well as expected changes to capital gains after the year-long consultation period. In addition, anticipated tax liabilities on death should be recalculated to allow for insurance updates or adjustments to other financial reserves. Any private company shares held in an estate could be affected, so care should be taken to keep shareholder death implications in mind when preparing new wills and undertaking other planning, including the drafting of shareholder agreements.

Capital gains and capital dividend accounts

Although proposals related to capital gains have been abandoned for the moment, the details of the original proposals as well as the announcement of a one-year consultation period in this area give us a lens into what to anticipate from the Department of Finance in the future. With this in mind, reviewing opportunities to plan capital gain transactions now may make sense. Private companies should also consider accessing capital dividend account balances and other tax-preferred balances over the next year, as they may be affected by future changes.

Be prepared

These changes will likely be accompanied by new compliance and reporting requirements. We anticipate this in the short term for related-party payments and passive investment pools. Over the long term, capital gains and capital dividend account reporting may also be affected. Anticipating how the changes may impact your business and ensuring that your tax team is prepared to respond will make the transition easier and lower your overall risk.

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We are still awaiting new proposals, draft legislation and enactment of the announced rules; this could happen in various stages between now and the next year or more. It will be important for companies and their shareholders to continue monitor their situation and to put plans in place as new details emerge.

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