CALU 2019 Pre-Budget Submission

Recommendations

That the federal government undertakes the following initiatives:

Quality Long-Term Care Support for Canadians

- Provide the new Minister of Seniors with a strong mandate to identify and develop solutions to deal with the long-term care funding issue;
- Convene a federal, provincial and territorial ministers joint committee to identify and develop a national approach for dealing with long-term care funding issues; and
- Hold a national symposium which includes stakeholder groups to discuss and debate seniors' issues and develop appropriate recommendations.

Implementation of a National Pharmacare Program

- Take a cautionary approach to funding a national pharmacare program, and that taxation of group life and health insurance premiums not be considered as a means of funding this program.

Taxation of Private Corporations and their Shareholders

- Only extend the pre-existing TOSI rules (which only applied to minors) to include adult children who are under the age of 25 in the year;
- In the absence of providing grandfathering for passive investments accumulated before 2019, modify the "claw-back" of the small business deduction to take effect on a more gradual basis;
- Undertake a review of the tax rules and CRA administrative practices for Employee Life and Health Trusts to ensure that family operated businesses, as well as those which rely on highly paid employees, are not adversely affected;
- Work in conjunction with provincial governments to restore tax integration across the provinces and territories in respect to all sources of income;
- Introduce changes to section 84.1 of the Income Tax Act to better accommodate intergenerational transfers of businesses while protecting the fairness of the tax system;
- Consider the integrated business/individual tax rates in both Canada and the U.S. in determining the competitiveness of the Canadian tax system as it applies to private corporations and their shareholders.

Overview

CALU is a national professional membership association of established financial advisors, accounting, legal, tax and actuarial professionals. For over 25 years, CALU has engaged in public policy advocacy on behalf of its members and the members of its sister organization, Advocis. CALU represents the interests of more than 13,000 insurance and financial advisors and in turn the interests of millions of Canadians.

Our submission focuses on three key issues which are of importance to Canadians and contributes to ensuring Canada's competitiveness.

Quality Long-Term Care Support for Canadians

In prior submissions CALU has highlighted the impending long-term care crisis in Canada. As Canadians live longer, they are more likely to be managing a chronic disease and will need some degree of long-term care support—in the home or in an institutional setting.
We believe the federal government needs to play a leadership role by working with the provinces and territories to find solutions to this critical issue. We recommend that the federal government undertake the following initiatives:

- Provide the new Minister of Seniors with a strong mandate to identify and develop solutions to deal with the long-term care funding issue;
- Convene a federal, provincial and territorial ministers joint committee to identify and develop a national approach for dealing with long-term care funding issues; and
- Hold a national symposium which includes stakeholder groups to discuss and debate seniors' issues and develop appropriate recommendations.

CALU supports federal and provincial initiatives that will provide meaningful sustainable solutions to this funding crisis. We are working within the financial services industry to explore initiatives that will educate Canadians on their funding obligations for long-term care, and in turn identify suitable investment and risk-based product solutions.

Implementation of a National Pharmacare Program

In Budget 2018, Finance Minister Bill Morneau announced the creation of an Advisory Council on the Implementation of National Pharmacare. Acknowledging that there are more than 10 million Canadians without extended health benefits, CALU welcomed the announcement in anticipation that a national approach to pharmacare could close this gap.

According to the Parliamentary Budget Officer's estimates, implementing a national pharmacare program could cost the federal government as much as $19.3 billion. Currently such costs are incurred by federal and provincial governments, private insurance plans and patients.

CALU is currently developing its position on a national pharmacare strategy and will be pleased to share its findings with the Finance Committee.

CALU recommends a cautionary approach to funding a national pharmacare program, and that taxation of group life and health insurance premiums not be considered as a means of funding this program.

Taxation of Private Corporations and their Shareholders

The small business community continues to be very concerned with recent tax measures which have negatively impacted the taxation of business and investment income.[1]

While CALU appreciates the government's response to concerns expressed during the consultation period relating to the Tax on Split Income (TOSI) and passive investment rules, we believe the federal government needs to make further changes as part of a commitment to undertake a more comprehensive review of the tax system governing private corporations. This would both give immediate reassurance to the small business community, while in the longer term ensuring that Canadian tax rules continue to be supportive of the growth of the small business sector in Canada.

We offer the following specific observations and recommendations as part of any such review process:

1. The TOSI Rules—as stated in CALU's prior submissions to the Minister of Finance,[2] are overreaching in effect, too complex and create an unnecessary compliance burden on small business owners. These rules also create an unfair bias against private corporations that are engaged in providing services vs. those that produce goods.

   We recommend these concerns be addressed, while still substantially achieving the government's goals, by only extending the pre-existing TOSI rules (which applied to minors) to include adult children who are under the age of 25 in the year.

2. The Passive Investment Rules — Some small business owners have accumulated passive investments in their corporation— to act as a "rainy day" fund; as a sinking fund for large capital expenditures; and/or to provide a source of retirement income to the business owners. As part of the October 2017 announcements relating to the taxation of private corporations, the Finance Minister announced that passive investments which were accumulated prior to finalizing these rules would be "grandfathered" from any new rules. The final rules effectively place limits on the amount of passive investment income that can be earned by a Canadian-controlled private corporation by limiting access to the small business deduction when such income exceeds $50,000 in a tax year. The result is that the equivalent of $3 million of passive investments (assuming a 5% return) would eliminate access to the SBD. No grandfathering was provided to exempt any existing passive investments in a Canadian-controlled private corporation when the new rules were effective. As a result, business owners who had already accumulated more than $3 million of passive investments (which was not to be impacted by the new rules) are now restricted from claiming the SBD.

   CALU recommends that in the absence of providing grandfathering for passive investments accumulated before 2019, that the "claw-back" of the SBD be further modified to take effect on a more gradual basis.[3]

[1] In particular, the recently enacted Tax on Split Income and passive investment rules.
[2] We would be pleased to provide copies of our submission to the Finance Committee upon request.
[3] Specifically, we are recommending that the SBD be reduced by $2.50 for every $1 of passive investment income, rather than the current SBD reduction of $5 for every $1 of passive investment income.

3. Health and Welfare Trusts (HWTs) — Small business owners may use an HWT as a vehicle to provide certain health and welfare benefits to employees (including the owner-manager). Budget 2018 proposes that an existing HWT must either be wound-up or converted to an Employee Life and Health Trust (ELHT) by the end of 2020. As noted in our recent submission to the Department of Finance[4], the rules governing ELHTs make them unsuitable for many small businesses, with the result that their only option will be to wind up the HWT. We believe this change, combined with certain interpretations issued by the Canada Revenue Agency (CRA), will make it difficult for small business owners to offer certain health and welfare benefits to more highly-paid employees on a similar tax basis as those applicable to larger employers.

   We recommend that as part of the process of establishing a workable framework for transitioning HWTs to ELHTs that a review of the tax rules and CRA administrative practices for ELHTs be undertaken to ensure that family operated businesses, as well as those which rely on highly paid employees, are not adversely affected.

4. Tax Integration — An important component of the Canadian tax system as it applies to small business owners is to ensure that the level of taxation on income earned by a private corporation (whether active or investment income) will be subject to tax at a combined effective rate upon distribution to a shareholder (as a dividend) as would be the case had that income been earned directly by the shareholder. However, depending on the type of income being earned and the province where the shareholder and private corporation reside, the current federal and provincial tax rules can penalize business owners who chose to establish a corporation to earn this income.[5]

   We recommend that the federal government work in conjunction with provincial governments to restore tax integration across the provinces and territories in respect to all sources of income.

5. Succession Planning for Small Business Owners — In October 2017 the Minister of Finance announced that the Government plans to "work with family businesses, including farming and fishing businesses, to make it more efficient, or less difficult, to hand down their businesses to the next generation". . . and that. . ." in the coming year, the Government will continue its outreach to farmers, fishers and other business owners to develop proposals to better accommodate intergenerational transfers of businesses while protecting the fairness of the tax system. CALU is very supportive of the government's review of these rules. As noted in CALU's submission to Finance on intergenerational transfers of family businesses[6], modifications should be made to section 84.1 of the Income Tax Act to ensure that business owners are not discouraged from transferring their businesses to family members because the tax treatment of the proceeds is less advantageous than selling the business to an arm's length third party.

   We recommend that the Department of Finance finalizes its review in 2018 and announces legislative changes in this area as part of its 2019 federal budget.

[4] We would be pleased to provide copies of our submission to the Finance Committee upon request.
[5] We can provide illustrative charts for various types of income and provincial tax rates upon request.
[6] We would be pleased to provide copies of our submission to the Finance Committee upon request.

6. U.S. Tax Changes —Changes to the U.S. Tax Code that became effective in 2018 have not only significantly reduced the rate of tax payable on corporate business income, but similarly reduced the tax rates applicable to income earned by certain individual taxpayers. As well, the top federal tax rate in the U.S. applies to income over US$500,000, in comparison to Canada where the top federal rate (and generally the top provincial tax rate) commences at approximately CDN$205,000. Depending on the state of residence, a business or individual taxpayer may now be significantly better off under the U.S. tax system.

   We recommend that the federal government consider the integrated business/individual tax rates in both Canada and the U.S. in determining the competitiveness of the Canadian tax system as it applies to private corporations and their shareholders.

Conclusion

Thank you for the opportunity to make this submission and we would greatly appreciate the opportunity to appear before the Finance Committee and discuss these matters as part of its pre-2019 budget consultation hearings.

Marty McConnell, Chair
Guy Legault, President