CC&C Professional Corporation
CHARTERED PROFESSIONAL ACCOUNTANTS

Tax Integration Zone

The impact of high personal and corporate tax rates

The combined Federal and Ontario personal tax rates are at 53% for 2017 on taxable income over $$220,000. The Ontario corporate tax rates on the first $500,000 of taxable income are just under 16%. The difference in these personal and corporate rates is the "Integration Zone". We can help design your personal and corporate cash flow requirements within the tax compliance rules.

Income taxes are a large part of family owned business cash flow and affect both the financing and available cash for the employee owner shareholders. Small businesses are usually financed from a combination of sources including shareholder investments, retained earnings and bank borrowings. In Ontario and Canada, the combined effect of all payroll, HST and income tax installments is a monthly cash commitment that must be met. CRA's current collection's policy is to seize funds in available bank accounts, on arbitrary assessments, that may or may not have been communicated. CRA considers payroll and HST withholdings as “trust” funds and makes the business responsible for their collection and remittance, regardless of the business environment or other cash flow demands. Your banker will not understand or sympathize with you when the CRA Third Party demand garnishees your bank account and in fact will look at you as a poor business person and question your current credit arrangements.

Planning to minimize and delay the payment of taxes is NOT illegal and failure to do this planning using the available tax deferral techniques does indicate poor business management. Let's change your tax management!

In Canada, there has been a rise of left-leaning federal and provincial governments. The policy of borrowing short term and the temptation to increase tax rates has become the new political philosophy. The tables below show the reversal of historical tax rate decreases both personally and corporately over ten years.

Ontario Top Marginal Personal Tax Rates on Income

	1996	2014	2016
Ontario - All Income	52.92%	49.53%	53.53%
Ontario – Capital Gains			26.76%
Ontario – Dividends			45.30%

Federal and Ontario Corporate Rates

	1996	2014	2016
Ontario General	44.62%	26.50%	26.50%
Ontario CCPC Rate			15.0%
Ontario Investment Rate			50.0%

A quick review of the above tables reveals two obvious observations. In the span of two years, Canada has managed to reverse course on personal tax rates and bring us back to personal tax rates that are higher than they were 20 years ago! The second observation is that corporate rate varies depending on the type of income. However, the low corporate rate tax rate that Canada has used favorably to attract business and capital may be short-lived given the new US administration's commitment to dramatically reduce US corporate rates.

The collection of HST tax in Canada does give our Federal and Provincial government an advantage over our southern neighbor but it cannot be pushed higher without affecting the economy's ability to grow. The net effect of HST is to essentially tax the net earnings of our businesses and it sometimes gets forgotten in tax planning because of the "refundable" nature of the calculations.

The consistent message from the Federal and Ontario Liberal government is that the rich need to "…pay a little bit more". Apparently your rich, if you make $220,000 (Ontario) of personal income. But what if you have a lot of monetary and "sweat" capital at risk, in order to make such income? Are you still rich? Small business entrepreneurs are special people. They often risk much of their livelihood and wealth to chase their business goals and create jobs and strive get a decent rate of return on their time and money investments. Is such risk worth taking if they are subjected to high personal and corporate rates that reduce their overall rates of return?

Enough of the background …… how do we use the "Tax Integration Zone" concept to plan to minimize our income tax costs.

The concept of active business income is beyond the scope of this blog post but if you "actively" earn income in a company in Canada (as opposed to earn investment of dividend income) the Canadian Controlled Private Corporation (CCPC) rate of tax on the first $500,000 of taxable income is 15%. An annual tax cost of $75,000.

If you had this much income taxed at personal tax rates in Ontario the total personal tax cost would be $230,000. This is an average rate of 46% remembering that average rates are always lower than marginal rates.

The difference between the CCPC rate and the personal tax cost on the same amount of taxable income ($230,000 less $75,000) or $155,000, is the "tax integration zone" that we reference. This is a simplistic analysis but demonstrates the dramatic advantage given to small business rates for businesses in Ontario.

Incorporation of your business involves legal as well as income tax matters and is a major decision that should only be undertaken with legal and accounting advise.

There is a myriad of other tax issues that must be brought into your corporate and personal tax plan and cover areas such as:

- Income splitting with family employees;
- RRSP, RESP and TFSA investing for tax deferral and retirement planning;
- Dividend payments to distribute after tax corporate income and trigger refundable tax at the corporate level; and
- Timing on payment of salaries to match personal tax credits and other personal deductions.

The utilization of the taxes saved from using tax integration can help your business preserve cash and build an investment fund to help meet future cash requirements.

CC&C
Professional Corporation
CHARTERED PROFESSIONAL ACCOUNTANTS