



The Fair Tax Plan a Federal Fairy Tale ?

In Finance Minister Bill Morneau's July 2017 letter to all Canadians introducing the Fair Tax Plan he states: "And it starts by making sure that we all pay our fair share of taxes – with no exceptions." We don't think that exposing Canadian small business owners to tax rates of 93% or more is fair, and we trust that Canadians would agree.

The measures in the Fair Tax Plan do not just impact the "1%" high income earners. In fact, the Fair Tax Plan affects all Canadian small business owners, which, according to the Federal Government's own statistics, comprised over 97% of Canadian businesses in 2015 and include restaurant owners, franchisees, real estate agents, plumbing contractors and a broad range of other small businesses and yes self employed chartered professional accountants..

The mere proposal of these changes has already created turmoil in the Canadian private business owner tax system into turmoil, and, unfortunately, the Federal Government and the Department of Finance do not seem to appreciate and possibly do not understand the extent of the damage that the proposed Fair Tax Plan will cause to Canadian business owners, employees of their businesses, and the economy as a whole.

Combined with rising business costs including labour costs, among other things, the interaction of the changes in the Fair Tax Plan (some of which took effect as of July 18, 2017) will: (a) undermine retirement and succession planning in ways that are often retroactive, punitive and could result in an effective confiscation of a small business owner's property; (b) burden estates with double or more levels of taxation; (c) negatively distort the market for private business owners seeking to sell their businesses, including in ways that may effectively take away their capital gains exemptions; and (d) create a new crushing compliance burden for any person or entity carrying on anything but a public or foreign business. The result is that many businesses will likely close and take with them the jobs they had created for the people whom the Liberal Government is trying to help.

There are some policy measures in the Fair Tax Plan that are fair and difficult to argue against, such as curbing planning that can allow the capital gains exemption to be enjoyed by taxpayers in ways far beyond the intent of the legislation. However, there are better ways to address such issues than through the wide net of the Fair Tax Plan. Some may suspect that we are exaggerating the impact of the Fair Tax Plan. To them, we would ask if a tax system that can confiscate the hard-earned income of a business owner at a tax rate of over 93% is fair? This could be the result if the Fair Tax Plan is implemented.

How do we get to 93% you ask? Here is a quick summary:

- Combined corporate and Personal Tax Rates as salary reach 53% on taxable income over 53%
- Not included are HST and Commodity taxes at the consumer level are 13% in most provinces
- Not included are Municipal and Education taxes are at least 3% of property values in most regional jurisdictions

See the detailed example of the current corporate and personal tax and estate tax rates and how the Proposed Fair Tax Changes will affect a corporate small business in Ontario for 2018 and following years.

	Current	Fair Tax
Active business income	750,000	750,000
Tax @ 15%	(112,500)	(112,500)
Net available for investment	<u>637,500</u>	<u>637,500</u>
Investment income	450,000	450,000
Tax @ 50.17%	(225,750)	(225,750)
Net after tax on investment income	<u>224,250</u>	<u>224,250</u>
Total income earned	1,200,000	1,200,000
Total taxes paid by Gardenco	(338,250)	(338,250)
RDTOH balance	138,000	-
Net assets in Gardenco	<u>999,750</u>	<u>861,750</u>
<i>Effective Gardenco tax rate</i>	<i>28.19%</i>	<i>28.19%</i>
Justice - Tax on Death		
Value of shares on death	999,750	861,750
Tax @ 26.76%	(267,581)	-
Tax @ 45.30%	-	(390,410)
RDTOH balance*	(138,000)	-
Net value available to Justice's heirs	<u>594,169</u>	<u>471,340</u>
Total income earned	1,200,000	1,200,000
Total taxes paid by Gardenco & Justice	(605,831)	(728,660)
Net value available to Justice's heirs	<u>594,169</u>	<u>471,340</u>
<i>Effective Gardenco + Justice tax rate</i>	<i>50.49%</i>	<i>60.72%</i>
Estate - Tax to Remove Funds from Gardenco		
Value of shares on death	999,750	861,750
Tax at 45.30%	-	(390,410)
Net assets available to fund Justice's tax on death and his heirs	<u>999,750</u>	<u>471,340</u>
Total income earned	1,200,000	1,200,000
Total taxes paid by Gardenco, Justice and estate	(605,831)	(1,119,069)
Net after tax cash available for heirs	<u>594,169</u>	<u>80,931</u>
<i>Effective tax rate</i>	<i>50.49%</i>	<i>93.26%</i>

The above noted is a technical calculation however this is how we have been dealing with small business taxes for owner managed business and how the Federal government is punishing all of us in this group to get a few situations where they see abuse.

In conclusion the individual proposals in the Fair Tax Plan are extremely complicated and their complexity increases as the interactions between the proposals and the rest of the Income Tax Act are considered. The Department of Finance has invited Canadians to provide comments and allowed only 75 days to do so (October 2 deadline). Given that these proposals collectively are perhaps the most transformational changes in over 50 years of tax law, this amount of time to respond is wholly inadequate. Regardless of the time provided for comments, as illustrated in the examples in the Annexes to this article, we believe that there is no way to work with the Fair Tax Plan and that it should simply be abandoned before any of it is enacted into law. Even though our proposal is to abandon the Fair Tax Plan, there are elements of the Canadian income tax system that do need to be improved and made more fair for all Canadian taxpayers. Hopefully, the Liberal Government will restart the process of making those changes by first better-defining its legitimate tax objectives and then spending time to properly consult with the tax community and affected constituents. We believe that it is possible to build a legislative plan that will be fair to all Canadians and will ensure the ongoing success of our economy. With what we know today of the Fair Tax Plan, it seems very likely that it will materially harm the Canadian economy. We can only imagine what other tax implications will be discovered once the greater tax community has had the time to fully review and understand the interaction of the proposed changes being made by the Fair Tax Plan with the rest of the Act. Provided the Fair Tax is abandoned.

Call us for your comments and remember they still have 7% to get after you pass away !.

