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WealthHealth

A monthly financial service
specifically for Physicians



Proposed Legislation Likely to Increase Taxes of Canadian Physicians as Soon as 2018

On July 18th, federal Finance Minister Bill Morneau announced proposed changes to the income tax regime that, if implemented, are likely to increase the tax bill of Canadian physicians who are incorporated as a private corporation. An overview follows of the three main changes as contemplated.

Currently, owners of private corporations who draw salary income/dividends from their businesses may reallocate some of that income in the form of salary or dividends to family members who earn less and are therefore taxed at a lower personal rate than the principal shareholder. The principal shareholder will then pay more taxes.

INCREASED SCRUTINY ON INCOME SPRINKLING

Morneau intends to apply a “reasonableness test” – yet to be defined – that sets new limits on the amount of income that may be redistributed to family members. This change will greatly reduce the ability of the principal shareholder to split income among family members with little involvement in the day-to-day activities of the business, and will be particularly strict with regard to children under the age of 25.

CONVERTING REGULAR INCOME INTO CAPITAL GAINS

Owners of private corporations have the ability to convert regular business income into capital gains, rather than taking that income from the corporation in the form of a dividend. Dividends are taxed at a higher rate than capital gains. This is often done in a complex set of steps involving the sale of shares to another company related to the shareholder or another shareholder. Morneau proposes to end these opportunities.

If you are considering selling your corporation or passing it on to the next generation, please consult with your financial advisor and your tax lawyer before the end of the year.

PASSIVE INVESTMENT PORTFOLIOS HELD WITHIN A PRIVATE CORPORATION

At present, when a corporation generates income, it is eligible for a pretty attractive rate of tax (about 15%, but varies by province) on the first \$500,000 of active federal business income.

If the business does not need all of this income for its operation, it is common to leave the rest inside the corporation to invest – perhaps in a portfolio earning passive income. For example, you may hold stocks, real estate and other financial products within a private corporation and income earned on those products is taxed at the lower corporate rate, thus giving the owner of the private corporation significant tax deferral advantages.

Morneau has stated that they find this “unfair,” but has not stated how he intends to reduce a shareholder's ability to invest excess corporate

earnings in a passive portfolio, only that the federal government anticipates much greater tax revenues from changes to this rule and offers a few options.

We do not think there is a need for changes to this, taxes are already high here and when you may use in the form of dividends later, we see this simply as a tax grab. The Canadian Medical Association has prepared an excellent FAQ on this issue: <https://www.cma.ca/Assets/assets-library/document/en/advocacy/cma-faqs-en.pdf>

These three proposals, which were signalled in the March 2017 federal budget, would apply to the 2018 tax year and subsequent tax years.

Once the federal government clarifies these highly complex proposals, we recommend that you consult with your professional financial advisor and your tax advisor to see how these changes may affect your taxes and what may be done to minimize the impact on your income.

In the interim, the government has invited feedback from Canadians by no later than October 2, 2017. We feel strongly that people should contribute their voices to these issues. If you are concerned about the fairness of these proposals, like your CMAN team, make your views known immediately to your professional association, Prime Minister Justin Trudeau, Finance Minister Bill Morneau, and your federal representative.



Raising Children in a Wealthy Household: What You Should Know

Every parent wants to raise happy and successful children, but as any parent knows this is not always easy. When parenting takes place in a higher net worth environment there are some unique challenges in how the children will deal with this wealth. CMAN will offer some insights on the topic in next month's WealthHealth.



Innovative Life Insurance Strategies for Estate Planning

Welcome to a world of higher personal and corporate taxes on investment income. Tax rates are increasing for personal income, capital gains and dividends on income over \$200,000. CMAN has information that help you optimize your tax scenario through tax-exempt life insurance strategies.



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