Collins Barrow

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By [John Oakey]

How will the new Passive Investment Income rules actually affect CCPCs?

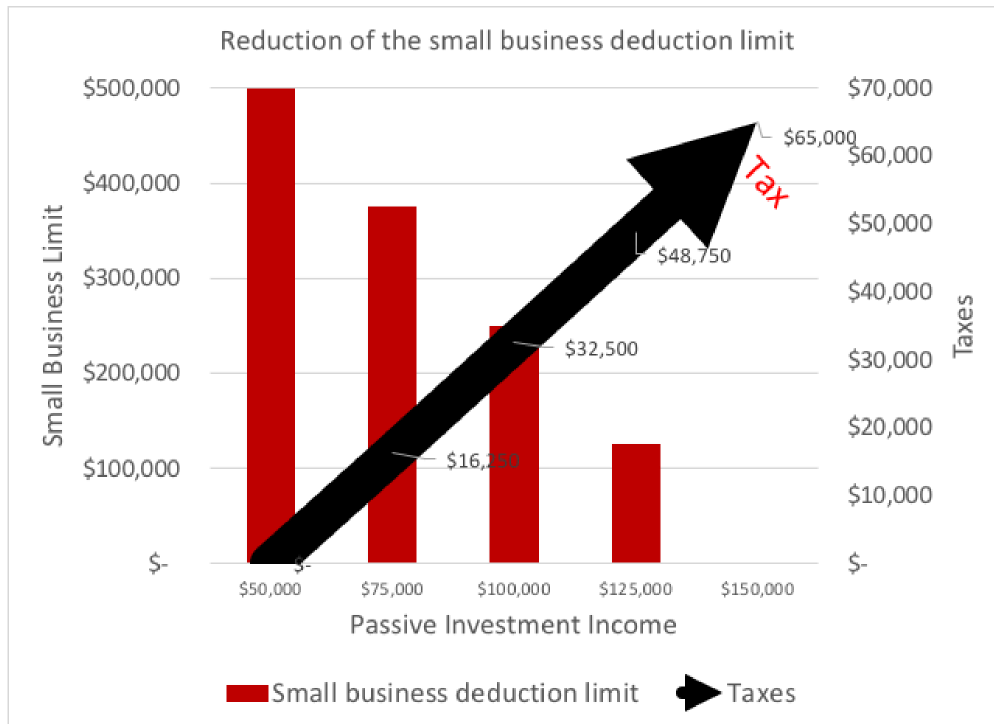
OTTAWA, ON – After months of public consultation, speculation and concern, the rules regarding Passive Investment Income have finally been unveiled. In today's 2018 Federal Budget release the government announced that passive investment income over a certain limit will now reduce a Canadian-controlled private corporation's (CCPC) small business deduction.

This isn't quite the news we were expecting. The corporate tax changes presented by the federal government for public consideration throughout 2017 were significantly more punitive, and would have resulted in a non-refundable tax burden. That said, for some high-net worth individuals and corporations, who are still actively working and have sizable corporate investments, this new regulation may cost a pretty penny.

Let's break down the changes:

As of 2019, if you're a CCPC with passive investment income exceeding $50,000, you will face a straight-line reduction of your $500,000 small business deduction. And once the CCPC hits $150,000 of passive investment income, you've lost that deduction all together.

What kind of financial loss could you be looking at? Say you are an incorporated Ontario professional with a $3 million dollar investment, which earns you a 5% rate of return annually (the rate of return assumed in the Budget). You bring in $150,000 of passive investment income, which essentially negates your entire $500,000 small business deduction. All of a sudden, your tax rate on that $500,000 of income jumps by 13%. Your tax burden has just increased by $65,000.



With that kind of tax hike, we expect some affected individuals and private companies will want to quickly consider alternative investment planning. Options might include the purchase of assets that increase in value over time (capital appreciation) but don't offer dividend payments in the present. Or, tax-exempt life insurance policies and contracts. Of course, these alternative options may also be accompanied by increased investment risk.

Whatever course of action you as a CCPC might choose, you'll have to decide soon, before the new rules come into effect on January 1, 2019. The new legislation even includes anti-avoidance provisions to ensure no loopholes are crafted (restructuring prior to the effective date, for instance, in an effort to delay the rules by a year could earn you unwanted attention).

Consult with your financial advisor to calculate the potential impacts of these new rules on your business and plan around them.

Meet the Author

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