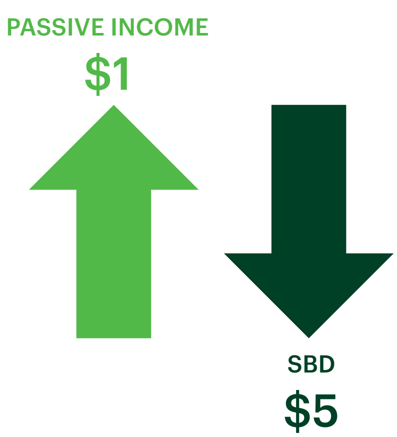
TD Wealth

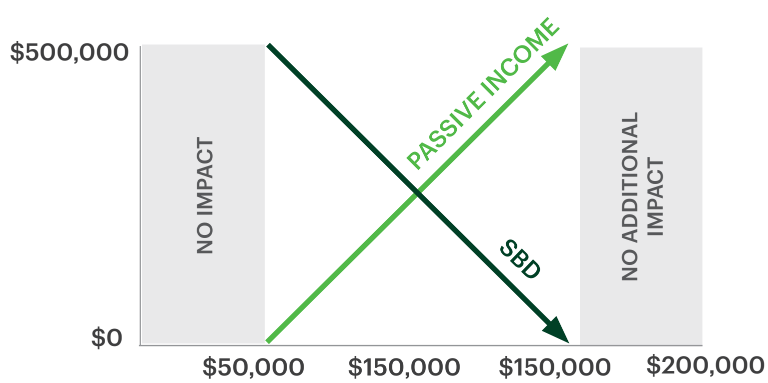
Are You Earning **Passive Investment Income** Inside Your Company?

What you need to know

From the 2019 tax year onward, certain Canadian Controlled Private Corporations (CCPCs) will have their small business deduction (SBD) reduced by $5.00 for every $1.00 of passive investment income that exceeds $50,000. The SBD allows a portion of a CCPC's active business income to be taxed at a lower rate up to a certain limit.

This is visually illustrated by the following:





A detailed numerical example:

Consider a corporation with active business income (e.g.: net sales income, net consulting fees, etc.) of $350,000 and passive income of $100,000. This would result in the corporation's SBD being reduced by $250,000 (computed as: $50,000 of passive income in excess of the $50,000 threshold = $50,000 x $5 for a reduction = $250,000 from the $500,000 limit). As a result, $250,000 of the corporation's $350,000 of active business income will be taxed at the small business corporate tax rates. The remaining $100,000 would be taxed at general corporate tax rates.

Before

Tax years before 2019

After

Tax years including 2019 and onward

Active Business Income: $350,000

Passive Income: $100,000

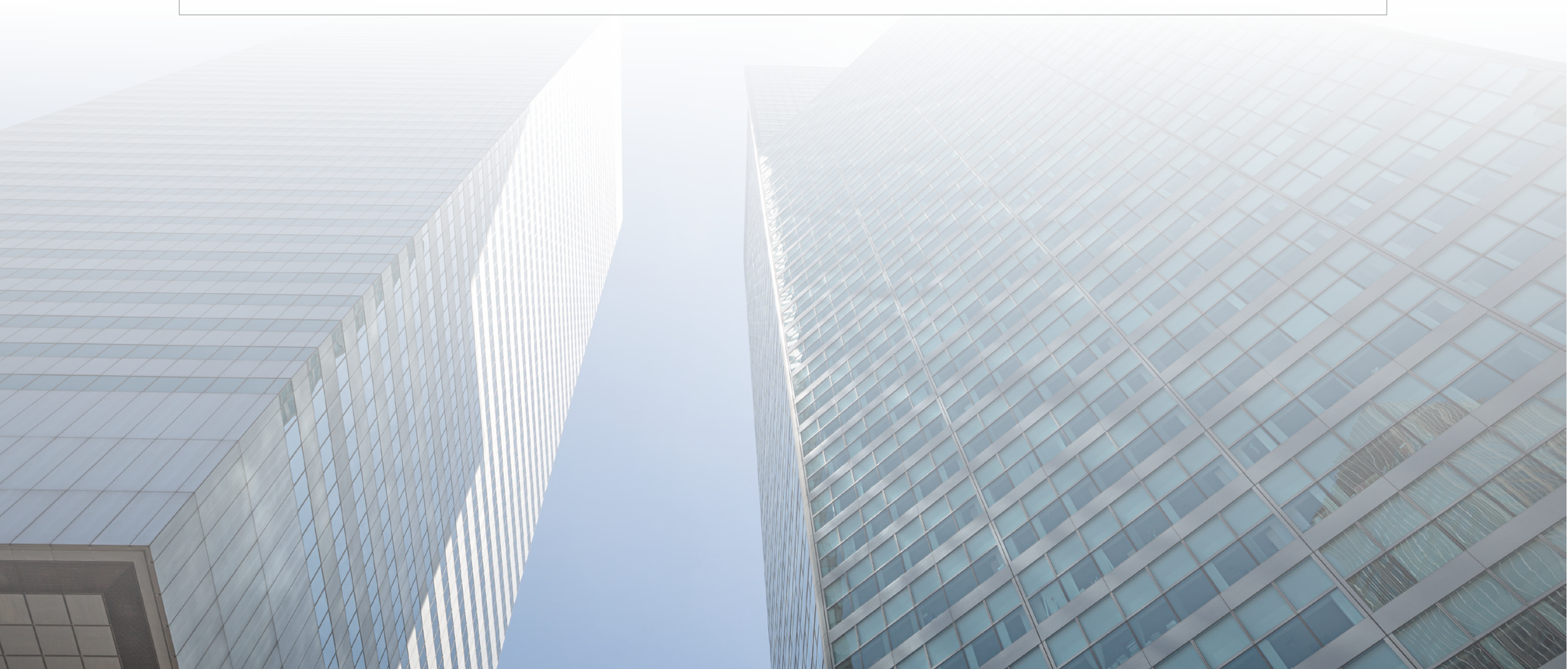
~$93,000
in taxes payable

(Assuming a small business tax rate of 12% and a 51% tax rate on passive income)

~$15,000
more in taxes

~$108,000
in taxes payable

(Assuming a small business tax rate of 12%, a general corporate tax rate of 27% on active business income in excess of the reduced SBD and a tax rate of 51% on passive income)



Impacted CCPCs	Non-impacted CCPCs
Canadian corporations (along with any "associated corporations" such as a holding company) that utilize the SBD and generate passive income above the $50,000 threshold. **Passive income** includes, but is not limited to, interest income, dividends, capital gains, and rental income.	**Investment holding companies** are not impacted as only active business income benefits from the SBD. A holding company typically does not generate active business income. **Corporations that only hold passive real estate** would not be affected unless the business is a larger operation with more than five full-time employees and has access to the SBD.

Potential planning opportunities to discuss with your tax advisor include:

- **Reducing your corporation(s) net investment income** through:
  - Generating expenses which may help reduce gross investment income such as interest expenses.
  - Utilizing deductions to reduce net income.
  - Reviewing the types of passive investments held inside your corporation (and its associated corporations, if any). For example, growth investments may generate less annual taxable income compared to interest or dividend paying investments.
- **Reviewing your Capital Dividend Account (CDA) balance** to determine whether a tax-free capital dividend can be paid.
- **Making charitable donations** through your corporation.
- **Reinvesting back into your business** by acquiring assets used in your day-to-day operations.
- **Funding a corporately owned life insurance policy.**
- **Funding an Individual Pension Plan** with corporate earnings that would otherwise have been directed towards passive investments.

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