



31 August 2017

Matt DeCoursey, MP, Fredericton  
494 Queen Street (Main Office), Suite 300  
Fredericton, New Brunswick E3B 1B6

Dear Mr DeCoursey:

**Re: Proposed Private Corporation Tax Planning Changes**

We are writing to express our members' concerns with the tax policy changes proposed in the document titled "Tax Planning Using Private Corporations" released by the federal Department of Finance on 18 July 2017. In fact, this matter is of such serious concern to our members that all members of our board asked to sign this letter individually - something that we have rarely done throughout our history.

Our overarching concern is that the document and related communications do not demonstrate a nuanced understanding of the fundamental differences between being self-employed and being an employee- the comparisons included in the discussion document are not apples-to-apples, but rather apples-to-Tuesdays. This letter outlines our concerns that have been shared with us by our members, we expect you to share them with your colleagues in Ottawa as the voice for our region. The three specific proposals that are giving our members the most concern are:

1. **Income Sprinkling:** Described by the Department of Finance as a "loophole," income sprinkling has been the legitimate basis of corporate tax planning for decades in Canada and across the world. It hardly needs to be said that this system was created by the federal government and at least tacitly approved by successive governments throughout the years. Moreover, it is a recognition that the risk assumed by entrepreneurs is borne by all members of the family unit. It is also recognition that family members make tangible contributions to the success of a business without being on the payroll. The change could have unintentional impacts on the spouse working at home, which in some cases are women. We recommend that the proposed taxation changes and potential impacts be viewed through a gender lens. With the ambiguity of the term "reasonable contribution" introduced on page 24, spousal or other family member efforts towards the business could be devalued if the proposed changes are implemented. We fear that entrepreneurs will end up spending more time on administration and compliance instead of growing their business and creating jobs. It is concerning that civil servants will be tasked with determining how much an individual is contributing to a business - what is their worth. We also recommend a cost benefit analysis be done on this initiative.
2. **Succession planning:** Proposed tax reform regarding the lifetime capital gains exemption is attacking family succession planning. Under the current proposal family businesses will face



double taxation if the family business is to be sold or transferred to a family member. With over 70% of businesses expected to change hands in the next decade, tax changes will severely impact the ability for succession to occur. The unintended consequences will be that many small businesses will close when third party purchasers are not available.

- 3. Investment income:** The proposed legislation on investment income will significantly impact a business owners' ability to save for expansion and to weather economic downturn. Many entrepreneurs also provide capital for entrepreneurs with new ideas - this may be challenging under the new system with fewer dollars to invest in new and innovative startups. The extremely punitive proposed taxation on these funds will result in significant economic impacts on small business sustainability and growth. There are well thought out public policy reasons for treating investment income differently. Business owners use these funds in lieu of maternity leave, sick time, vacation pay, retirement planning and many other benefits that employees receive. This income is also meant to protect the business (and jobs) during economic downturns or slow times for the business. It is what owners have to fall back on instead of EI eligibility that employees receive. The example of the fictionalized "Jonah" and "Susan" are not in remotely similar situations and serves to pit employees against entrepreneurs. An entrepreneur bears the risk, stress and rewards that comes along with owning a business. These changes could unintentionally create barriers for entrepreneurs. The same entrepreneurs that are the backbone of the Canadian economy accounting for some 1.17 million businesses in 2015, of which 97.9% were small business.

While there are many ways wealth is created, in one of its simplest forms, those prepared to assume risks are rewarded for taking the risks by way of financial gain. For example, the entrepreneur who decides to risk their own capital and spend their time, without any assurance of payment, is taking more of a risk than someone who works for salary. These risk-takers are sometimes financially rewarded. They're the ones we call successful. They're the ones who built a business from the ground up to become what it is today. Most that take that risk never see the rewards.

Taking risk is so fundamental to wealth creation that it's the way most businesses begin. In the process, they often create jobs for others, benefits for society and tax revenue to support the social support systems we provide for citizens. Over the years this risk taking has become recognized as having great value for society. In order to encourage people to take the necessary risks, successive governments have built a tax structure designed to help compensate these people for the risks taken.

Perhaps even more telling is the information not included in the document. Has an economic impact study been conducted on the proposed changes? Has government evaluated the increased compliance burden and financial cost to small businesses? Has government evaluated the increased cost and administration for CRA? How will the proposed changes be managed? Some of the language is vague and subject to interpretation. For example, implementing a "reasonableness" test. Has the benefit to the Canadian taxpayer been evaluated against the potential job loss and business failures this will result



in once these measures are implemented? Small businesses are the middle class, and are the employer of the middle class. Who will employ the middle class once many small businesses no longer exist? Has the potential ripple economic effect of these proposed changes been considered or evaluated?

Small businesses will be required to make the Atlantic Growth Strategy a success, a priority of this government. How will this strategy be executed upon if entrepreneurs are discouraged by these recent tax changes? Escalating costs involved with operating a business was already a growing concern for our members, many of whom feel that they are under attack from multiple levels of government.

The Federal Government asserts they value the contribution that small businesses and entrepreneurs make to the Canadian economy. However, this appears to be quite literally untrue given the lack of credit attributed to the risk entrepreneurs assume when starting a business as well as the financial disadvantages of owning a business. As discussed, these include employer-contributed pension plan, Canada Pension Plan, employer-contributed health or dental benefits, maternity leave, vacation pay, sick time, and the Employment Insurance safety net.

Our members also believe the language chosen in the document portrays the government's true valuation of the contributions of small business. Our members take offense to the tone of the document, implying that entrepreneurs avoid paying their "fair share" of tax due to taking advantage of "loopholes". These "loopholes" are simply the corporate tax system that has been set up and accepted by federal governments for decades. To now suggest that the users of the system are avoiding paying their fair share is, at best, disingenuous - politics at its worst.

The short, 75-day consultation period does not allow time for necessarily comprehensive discussion and for stakeholders to determine the impacts of the proposed changes. This is exacerbated by releasing the consultation document in the dead of summer when it is widely understood that feedback is more difficult to obtain. Furthermore, Minister Morneau has stated that "we will not change our minds," in reference to the proposals. Our members take these as a clear signs that this is a consultation in name only.

When businesses lose, so does the middle class. Business owners that are affected by these changes will, quite logically, take steps to protect their livelihood, their retirement, their rainy day fund. This will mean fewer jobs, fewer hours for employees, less disposable income for charities and community organizations - putting further pressure on the country's social safety nets. Small business owners are the engines of our communities - these proposed changes will hurt their ability to contribute and disincentivize the next generation of entrepreneurs - not a "fair" outcome for anyone.

Is the system as it is currently designed perfect? Unlikely. Are there provisions in the current set of tax structures that could be improved upon? Probably. Should we continue to encourage those willing to take risks to create wealth in our economy? Absolutely! We need to be careful that in the politically



popular hunt to stamp out the advantages of the “wealthy” (i.e. the ones who create wealth and pay the bulk of the taxes in society) we don’t irreparably harm the imperfect but relatively competitive system we currently have. If the purpose of these changes are to provide “fairness” to the middle class, don’t forget that the vast majority of small business owners fall into this category.

Thank you,

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cc: Perrin Beatty, President and CEO, Canadian Chamber of Commerce  
cc: Sheri Sommerville, CEO, Atlantic Chamber of Commerce