<u>October 30, 2017</u>

The consultation period for the July 18, 2017 draft legislation and consultation paper ended on October 2, 2017. After reviewing the submissions, Finance Minister Bill Morneau released five separate news releases, and on October 24, 2017, the fall economic provided some additional information on these measures. Unfortunately, there remains a great deal of ambiguity, and as such, we still cannot recommend taking significant actions in response to the proposed changes at this time.

New Announcement – Reduction of Small Business Tax Rate - Department of Finance announced that it intends to lower the Federal small business tax rate by 0.5% on January 1, 2018 and an additional 1.0% on January 1, 2019. The personal tax rate on dividends paid from this income will be increased to offset this savings in the corporation.

Income Sprinkling - The proposed rules limit the tax savings available to business owners paying dividends or other income to family members on or after January 1, 2018. The government has announced that they intend to go forward with the rules but has also confirmed the need to "simplify" the proposed measures. They have not clarified which portion of the rules they intend to simplify, nor whether the effective date will remain the same. If this impacts your corporation, you should consider paying more dividends to family members in 2017 as your ability to do so in 2018 may be restricted. We recommend using caution when doing this, however, as the legislation details and effective date remain uncertain.

Capital Gains Exemption (CGE) - The government has announced that it does not intend to proceed with the measures to limit the ability of certain shareholders to claim the Capital Gains Exemption. It is unclear whether they intend to remove all or only part of the legislation contained in the July 18 proposal.

Investment Income Earned in an Active Corporation - In response to the submissions, the government has announced that the new rules will only apply to increase the tax on passive income in an active corporation in excess of $50,000 per year (5% rate of return on $1,000,000 investment). They have also confirmed that these rules will apply on a "go-forward-basis" but have not provided clarity on how the past earnings or investments of a company will be grandfathered. There has still been no draft legislation released detailing how the Department of Finance intends to enact these changes. We expect these measures to be released in the 2018 Federal budget in March.

Converting Income to Capital Gains - These rules targeted a specific type of transaction but had broad unintended (and possibly retroactive) consequences to the payment of capital dividends as well as to transfers of a business to family members during life or on death. On October 19, 2017, the Department of Finance announced that it did not intend to move forward with these measures as originally drafted. We expect that new legislation may be presented with a more targeted focus on the specific transaction Finance seeks to limit.