Weekly Updates Issue # 633

1. Weekly Markets Changes

[September 29, 2017]

S&P TSX	S&P 500	Dow Jones	NASDAQ	CAD/USD	Gold	WTI Crude
15,634.94 +180.7 +1.17%	2,519.36 +17.14 +0.68%	22,405.09 +136.8 +0.61%	6,495.96 +47.49 +0.74%	$0.8013 -0.91c -1.12%	$1,279.75 -17.75 -1.37%	$51.67 +1.01 +1.99%

2. Domestic growth takes a break in July

[September 29, 2017] Statistics Canada says the economy took a pause in July, the first month in 2017 that showed no growth.

The Ottawa-based agency says gross domestic product was unchanged from a month previous, at 0% growth in July compared with June (which marked the eighth month in a row of GDP growth).

Goods-producing industries saw a contraction of 0.5% in July while service industries had overall growth of 0.2%.

The oil and gas subsector shrank 1.8%, with declines in both conventional and non-conventional production.

The manufacturing sector also fell 0.4% overall, mostly because of declines in motor vehicle manufacturing and parts.

Growth in services was led by wholesale trade, which was up 2%, the highest monthly gain since September 2014.

3. Toronto, Vancouver could face housing bubble

[September 29, 2017] Toronto has topped the list of major global cities most at risk of a housing bubble with Vancouver ranking fourth, according to a report by UBS Group AB.

It's the first time Toronto has cracked the annual rankings compiled for the UBS Global Real Estate Bubble Index, where other top five bubble-risk cities include Stockholm, Munich and Sydney.
The Swiss-based global financial services company says the bubble risk in all of these cities has increased significantly over the last five years, where house prices have climbed by almost 50% on average since 2011.
In Toronto, Munich and Sydney prices rose more than 10% in the last year alone, where the fear of missing out on further appreciation predominates among homebuyers.
In Canada, a large part of the negative impact of higher purchase prices on affordability was cushioned by low mortgage rates.
While Toronto and Vancouver's house prices have moved in rough lockstep where the depreciation of the Canadian dollar effectively buffered them against economic headwinds, UBS says a strengthening loonie and further interest rate hikes would "end the party" for Toronto.

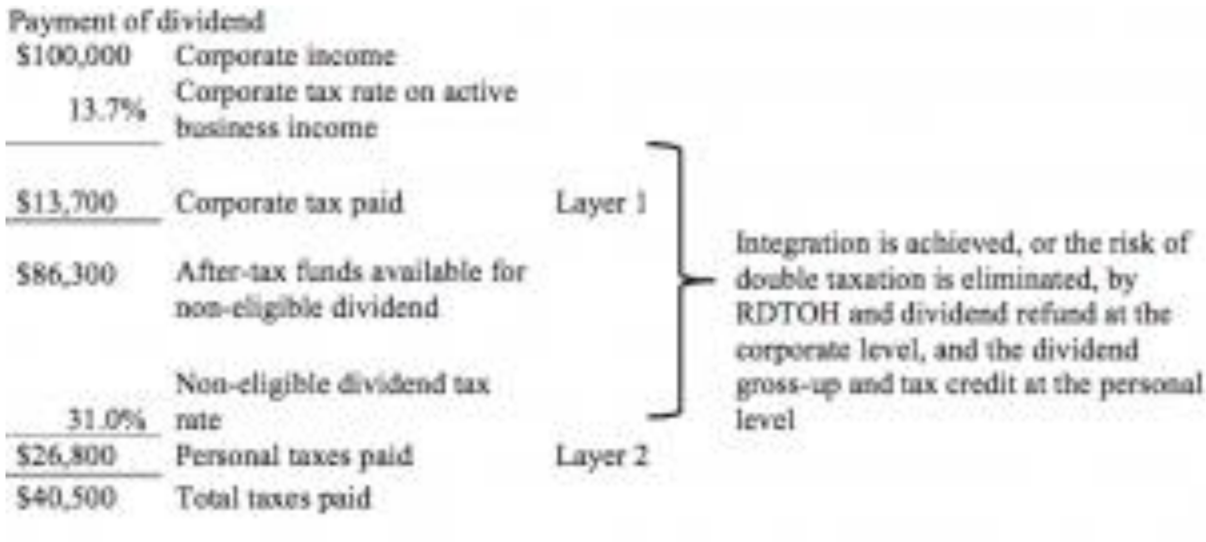
4. Problems with Finance's passive investing proposals

[September 29, 2017] Finance says Canadians who hold passive investments in private corporations get an unfair tax advantage. That view is problematic.
For this second issue highlighted in its July 18 tax proposal, Finance didn't provide draft tax legislation or set an implementation date. Instead, Finance outlined concerns with the current passive income tax measures, proposed alternate methods to address its concerns, and requested key stakeholders and taxpayers to comment on the proposed methods by October 2.
Let's take a deeper look.

Current measures

Integration is a fundamental principle of Canadian income taxation. In brief, the cumulative total of taxes paid on a dollar of income earned first by a corporation and then paid to an individual as a dividend should equal the tax paid by an individual who earned the same income directly.
Currently, several tax provisions or accounts help achieve integration, such as the Refundable Dividend Tax on Hand account (RDTOH) for private corporations and the dividend gross-up and tax credit for individuals. These prevent double taxation, whereby the same income is taxed twice, which is different than being subject to two intergrated tax layers. See Table 1.

Table 1: Two integrated tax layers



Another example is the Capital Dividend Account (CDA). To preserve tax-preferred treatment on certain types of receipts, such as the 50% non-taxable portion of capital gains or the tax-free portion of a life insurance payout by a private corporation to shareholders, the corporation uses the CDA and pays out tax-free capital dividends.

Without the CDA, a corporation would have to pay a regular dividend to its shareholders to distribute the 50% non-taxable portion of capital gains or tax-free life insurance, which would be taxable in the shareholders' hands. That wouldn't be fair: the shareholders would pay more tax on these receipts than individuals who had received these receipts directly.

Finance's concerns

Finance says current tax measures and the principle of integration on income are insufficient, as they don't account for the source of passive investments generating such income. Note the distinction here between investments and income. Finance wants to take a step back and apply integration to the original source generating the passive investments. Specifically, Finance wants to focus on whether passive investments are sourced from cheaper after-tax corporate dollars or more expensive after-tax personal or corporate dollars.

For example, Finance says private corporations, particularly those with more favourably taxed active business income, benefit from a significant tax deferral advantage when after-tax dollars are invested in passive investments at the corporate level. Finance is concerned that this deferral provides an incentive for private corporations to become personal savings vehicles — and that's not fair, it says.

The average combined tax rate (as of June 30, 2017) for a corporation earning $100,000 of active business income is 13.7%, whereas the average combined tax rate for an individual earning regular income is 26.7%. The corporation would have an additional \$13,000 (\$100,000 × (26.7% − 13.7%)) to invest annually on an after-tax basis. However, when passive corporate investments are liquidated, and, on an after-tax basis, paid out by the corporation, a second layer of income tax — personal — is incurred by the business owner. Hence, tax is deferred, not saved, on corporate passive investments.

For subsequent passive income earned on such investments, an individual investor will be subject to only one layer of tax — personal — as opposed to a corporate investor, who is subject to two layers — corporate and personal, as shown in Table 1. Given the existing punitive tax treatment of passive interest income left in a corporation of 51.7% (average combined tax rate), most tax advisors immediately declare and pay dividends to move such income into the hands of shareholders. Thus, there's generally minimal or no deferral or tax savings generated on corporate passive income.

Finance's proposed alternatives

Despite these existing disincentives for corporate passive income, Finance is proposing to move integration up one level — where the passive assets are generated. To do so, Finance proposes that Canadian-controlled private corporations elect to use one of the following methods for taxing their passive income:

Method	Effect on corporation	Effect on shareholder		Considerations
		Individual	Corporation	
Deferred taxation on general active business income	Tax passive investment income at top combined marginal personal tax rate, with removal of RDTOH	Non-eligible dividends are the only type of dividend	Non-eligible dividends are the only type of dividend	No distinction between eligible and non-eligible dividends received from passive corporate investments Non-taxable portion of capital gains wouldn't flow through to CDA, meaning the entire capital gain would be a taxable dividend in the shareholder's hands
Deferred taxation by apportionment method on passive income	Apportion passive income by tracking three pools of capital:	There could be eligible, non-eligible	There could be eligible, non-eligible,	The corporation would deduct the amount of dividend

		income subject to active/small business tax rate, income subject to general tax rate and amounts contributed by shareholder on an after-tax personal rate. Corporate tax rate would determine nature of shareholder dividend	or tax-free dividends	or tax-free dividends	from its designated pool Non-taxable portion of capital gains wouldn't flow through to CDA (as above)
Deferred taxation by elective method	Default	Tax passive investment income at top combined marginal personal tax rate, with removal of RDTOH	Non-eligible dividends are the only type of dividend	Non-eligible dividends are the only type of dividend	No distinction in how corporate income is taxed Assumes passive assets are purchased with earnings at active/small business rate Assumes no shareholder contributions are used to purchase passive assets Non-taxable portion of capital gains wouldn't flow through to CDA (as above)
	Elective	Subject passive income to additional refundable taxes. Further, the non-refundable tax rate would equal the top combined marginal personal tax rate. No income would be eligible for active/small business rate	Eligible dividends are the only type of dividend	Eligible dividends are the only type of dividend	No distinction in how corporate income is taxed Assumes passive assets are purchased with earnings at general rate Assumes no shareholder contributions are used to purchase passive assets Non-taxable portion of capital gains

					wouldn’t flow through to CDA (as above)
Holdco election		Considers all income passive income, subject to top combined marginal personal tax rate using refundable tax system, like current RDTOH regime	Eligible dividends are the only type of dividend	An additional refundable tax would bridge the gap between corporate tax rate and top combined marginal personal tax rate	Assumes passive assets are purchased with after-tax personal dollars Non-taxable portion of capital gains wouldn’t flow through to CDA (as above)

You’ve probably heard of the potential 70%+ tax rate reported on passive income using these proposed methods. That can indeed happen.

In brief, this tax rate occurs when $10 of interest is subject to 50% corporate tax (equal to the average top combined marginal personal rate) and the remaining after-tax $5 is paid out to the shareholder in the form of a non-eligible dividend where it is taxed at 20% on average. The 20% tax rate can vary dramatically depending on the individual’s province and respective marginal tax rate. Simply put, integration doesn’t occur under the proposals, as no adjustment is made to corporate tax paid on the interest and when paid out as a dividend to the individual shareholder. See the above chart, specifically “Deferred taxation on general active business income” and “Default,” under the Elective method.

Finance intends that any tax measures subsequently introduced will apply to passive investments on a go-forward basis, and it asked stakeholders and taxpayers to submit recommendations during the consultation period on how to grandfather or preserve the tax treatment of existing passive investments.

Carson Consultants Corporation (CCC)

Consider this example of how passive income is treated now versus under the proposals:

Aja Carson, a 53-year-old divorcee with no dependants, incorporated her oil and gas resource engineering consulting practice, CCC, more than 15 years ago. When additional assistance is needed to meet clients’ demands, CCC uses outside contractors.

Over the years, CCC has set aside, withdrawn and replenished funds for anticipated capital needs or to help carry expenses when receivables aren’t paid on a timely basis or during an economic downturn, as recently experienced. CCC currently has $1.2 million invested in a diversified conservative portfolio to meet these needs.

What Aja Carson and CCC should know

Though Finance hasn't yet provided proposed tax legislation or an implementation date for such, the following points should be highlighted and discussed now with Aja Carson and clients like her.

General points

Complexity leads to costs — The proposed methods are complex and few business owners have time or expertise to assess their passive investments and provide the relevant income information to be compliant. This burden will fall to their tax advisors, thus increasing the associated costs of compliance (preparing corporate tax returns). How will Finance explain such cost increases to business owners?

Genuine corporate savings incur a cost — Finance hasn't distinguished between the various uses for accumulating passive investments in the corporation. Such uses include future growth; capital assets, such as equipment, buildings or farmland; an operations cushion in an economic downturn; or business owner retirement. Growth and expansion aren't linear, and unplanned events can become opportunities if a business owner has passive investments on hand. With little savings, what are the chances a business manufacturer can approach a bank or credit union to extend a mortgage to acquire a warehouse? Saving corporately, for whatever reason, will be a lot more expensive tax-wise.

Dividends affect retirement savings — Where business owners pay themselves dividends, they don't generate RRSP contribution room, as dividends aren't considered earned income for RRSP purposes. The proposed methods severely compromise business owners needing flexibility in saving for both corporate growth and retirement. Sure, they can always pay themselves a salary; however, there are numerous other considerations when contemplating salary versus dividends.

Double standards — Many business owners save for retirement in their corporations because of the aforementioned flexibility concerns. Yet passive income earned in an RRSP is subject to tax only upon redemption, whereas passive income earned in a corporation is never sheltered from tax. In addition, when anyone is paid a salary and makes RRSP contributions, and subsequently converts the RRSP to an RRIF or other similar retirement income stream, the eligible pension income can be split with their spouse. Yet, Finance with their proposed tax measures wants to eliminate spousal income splitting for private corporations.

Choosing a method today — Finance's proposed methods require that a corporation elect a method to track its passive assets, and/or income from such, to determine the tax treatment of passive income on a go-forward basis. How many business owners have the knowledge or expertise to make such a decision, and can forecast which method will be in their best interests in five, 10 or 20 years? Times and circumstances change, not to mention tax legislation.

Capital gains are penalized — Finance will no longer add the 50% non-taxable portion of a capital gain to a private corporation's CDA. In brief, integration of capital gains will be severely compromised, and capital gains will be taxed at a much higher combined tax rate than if they had been reported personally.

Specific points for Aja Carson to address with a tax advisor

Corporate reorganization may be needed — Should a corporate reorganization be considered, as CCC has $1.2 million in passive investments? Would the creation of a holding company, or perhaps a butterfly transaction, be prudent to separate CCC's existing passive assets from its active, ongoing operations? Such steps would make it easier to preserve the grandfathering of existing passive investments, allow for a separate election to be made by the new holding company, and ease future tax compliance associated with the passive investments. On the downside, if the passive assets are needed by CCC to fund capital expansion or maintain operations in an economic downturn, a corporate loan between the two corporations will be required, which introduces its own associated issues.

Plan for future passive investments — Once Finance has drafted and implemented its new tax measures for passive investments, what should CCC's tax advisors consider when accumulating new passive investments in CCC? Undoubtedly, the new tax measures will impact the quantum and nature of Carson's compensation, as well as how CCC accommodates future growth or cash flow needs.

Canadian small businesses that don't fund future growth with after-tax earnings each year will be penalized with higher corporate income tax rates on passive income. They'll also likely incur additional compliance costs due to the complexity of reporting passive investments and income in future.

Finance has expressed the following objectives for its tax regime on passive investments held in corporations:

1. Preserve the intent of the lower tax rates on active business income earned by corporations, which encourages growth and job creation.
2. Eliminate the tax-assisted financial advantages of investing passively through a private corporation.

3. Limit, to the extent possible, the complexity of any new tax rules.

Finance's proposed methods address only the second objective, achieving it at the cost of the other two. In an effort to capture those taxpayers Finance says are unjustly advantaged, Finance penalizes those who genuinely drive Canada's economy. Many Canadians are employed by Canadian private corporations, purchase goods and services from them, and provide goods and services to them. That means all Canadians will be impacted by these proposed tax measures.

Admittedly, there are private corporations and respective shareholders that benefit unjustly from current tax measures. Tax reform is needed. However, what I have outlined in this and previous articles is that, in their current form, the proposed measures and methods are too broad, impacting all private corporations. They don't exclusively capture high-income-earning Canadians.

Finance has also failed to provide adequate consultation and sufficient time for corporations to consider restructuring. Finance recognized the increase in private corporations more than 10 years ago. Over that time, they drafted and considered various tax measures for private corporations. The current government had at least 21 months to consider Finance's proposed measures before announcing them. Yet, Finance allowed stakeholders and taxpayers only 75 days to research, consider and comment on the proposed measures and methods outlined in its July 18 tax proposal.

Private corporations that incorporated years ago, with appropriate authorized share classes and shares that were issued onside with historical corporate and tax legislation, may now be offside and require major restructuring, which in turn requires the time and attention of sophisticated corporate legal and tax advisors, which will be costly.

Advisors should reach out to private corporation clients and provide them with information on their passive investments. Clients should also be prompted to reach out to their tax advisors to consider Finance's proposed methods and determine what alternatives they might have. Your value proposition lies in being proactive, and delivering timely information, as clients might have only a short time to react before the tax measures become law.

5. Canada should lower corporate taxes to stay competitive with U.S.: MEI

[September 28, 2017] While the U.S. President has just reiterated his intention to reduce corporate taxes, Canadian Finance Minister Bill Morneau wants to raise taxes for entrepreneurs.

Ottawa would be better off focusing on Canada's tax competitiveness with its neighbour, for example by adopting a proportional tax rate of 10.5% for all corporate earnings, argues a report published today by the MEI.

President Trump is looking to lower the federal corporate tax rate in the U.S. from 35% down to 20%. If such a reform were adopted, Canada's tax competitiveness would be substantially reduced, says the report. Indeed, the highest combined (federal and provincial) marginal corporate tax rate in Canada is currently 31%.

"If Trump goes ahead with this reform, and Ottawa sits on its hands, there will be serious consequences for Canada's corporations, and especially for its workers, who would suffer a large part of the negative effects since investment and the demand for labour in Canada would decrease," explains Mathieu Bédard, Economist at the MEI and author of the publication.

Indeed, even a more modest reduction in tax rates than the one advocated by Trump would generate an effect similar to an increase in tax rates in Canada, since it would increase our relative tax burden, notes the report.

In order to protect workers, Ottawa could abolish its top income tax rate of 15% and maintain only the lower rate of 10.5%, which currently applies exclusively to small firms, writes Bédard. This would bring Canadian policy more in line with the proposed reform in the U.S., and would help preserve Canada's tax competitiveness.

"Actually, Ottawa has an interest in taking the lead and adopting such a measure, regardless of what happens with American tax reform," adds Bédard. "The introduction of a proportional corporate tax would promote business growth, whereas the existence of multiple (i.e., progressive) rates of taxation tends to discourage it."

Michel Kelly-Gagnon, president and CEO of the MEI, notes, "The federal government has committed itself to adding tens of billions of dollars to the debt over the coming years in order to 'stimulate' the Canadian economy. It should instead reduce corporate taxes and introduce proportional taxation, since this would achieve its goal without saddling Canadians with more debt."

6. Show discernment with dividends

[September 28, 2017] If you're like most investors, dividend growth puts a smile on your face and a spring in your step.

"Investors love dividend growth, as it typically signals the business is robust enough and profits are healthy enough to increase returns," says Craig Jerusalim, portfolio manager at CIBC Asset Management.

Investors could find research to support this view. Previous empirical evidence shows "companies that grow their dividends consistently outperform non-payers, cutters and non-growers," he points out. "But there are lots of holes in that analysis."

For instance, a myopic focus on dividend growth can lead to suboptimal outcomes, "especially when companies sacrifice investing in their ongoing operations, overextend their leverage or manipulate payout ratios just to deliver dividend growth," says Jerusalim.

In fact, many solid companies that could pay dividends choose not to, he explains, naming Spin Master, Berkshire Hathaway and Shopify. Instead, they pursue growth opportunities or invest retained earnings on investors' behalf.

For these reasons, Jerusalim focuses on the more holistic metric of total shareholder yield, which incorporates dividends and dividend growth potential, as well as net share repurchases and net debt reductions — "all the asset allocation options available to a management team," he says, adding that these are divided by market capitalization to calculate total shareholder yield. "A higher number suggests higher shareholder value, [which] should result in higher stock prices over time."

Jerusalim lists the key characteristics of such companies:

- defensible and sustainable competitive moods;
- strong business models;
- prudent balance sheets; and
- disciplined management teams.

For example, management should exhibit "an unwavering focus on optimizing returns on invested capital, such that they mak[e] the best asset allocation decision," he says.

Sometimes that means increasing dividends, but it can also mean buying back shares or investing in growth or making other creative acquisitions.

Says Jerusalim: "Occasionally, we find great companies like CN Rail, Magna or Intact Financial that are able to successfully do all the above."

7. Tax measures hurt modest business owners: coalition

[September 27, 2017] The Coalition for Small Business Tax Fairness has written a new letter to Finance Minister Bill Morneau with professional analysis confirming that Ottawa's tax proposals will affect middle-class business owners.

"It is the farmers, mom-and-pop shops, and entrepreneurs, who invested everything into their businesses, that will be most affected by these changes,

instead of targeting the real problem," says Perrin Beatty, president and CEO of the Canadian Chamber of Commerce, in a release.
The government claims the proposals won't affect business owners with incomes under $150,000. Tax practitioners disagree.
One of the new rules introduced would restrict small business owners from sharing income with family members. Tax practitioners say this can affect business owners with incomes as modest as $50,000. Also, as two-thirds of Canadian incorporated businesses are majority-owned by men, the restrictions on sharing income with a spouse are likely to remove a disproportionately higher number of women from benefiting from their family's business.
The government also proposes changes that would discourage small business owners from holding passive investments in the incorporated company. According to tax practitioners, business owners retain business earnings in the corporation to safeguard against economic downturns, secure bank financing and invest in other startups.
In its letter, the coalition says tax practitioners are "united in the view" that the proposed changes would result in higher combined corporate and personal taxes for business owners across the board, and in many cases, small business owners would incur tax rates far greater than what an employee with a similar level of income would pay.
The coalition, which has doubled in size since August 31, is asking the federal government to review the analyses of tax professionals across the country, take the proposals off the table and launch meaningful consultations with the business community to address any shortcomings in tax policy.

8. Opinion: Minister Morneau, your analysis is incomplete

[September 26, 2017] On September 5, the Globe and Mail published an op-ed by Finance Minister Bill Morneau titled "Tax changes are about leveling the playing field." He wrote that he wants to make the middle class equal to business owners from a taxation point of view. As his government has repeatedly stated, it is concerned about "the ability of high-net-worth individuals to use private corporations to inappropriately reduce or defer tax."
Why is his analysis incomplete?

- Logically speaking, the majority of owners of the 1.1 million small businesses in Canada must be in the middle class, since there are 17 million tax filers in Canada (only 170,000 can be in the 1%).

- Business owners take significant risks with respect to starting their enterprises. They're also responsible for contributing 100% of funds toward their retirement and benefits.
- Conversely, civil servants face no such risk. Fairly compensated civil servants receive benefits and pensions that are far greater than can be accumulated by the majority of incorporated business owners and professionals, as we'll see.

Any reasonable analysis of Minister Morneau's conception of equality must include a comparison between an incorporated professional and a career civil servant. We have done such a comparison below, contrasting Bob, a dedicated civil servant, to Cheryl, an equally committed doctor. The results are both surprising and telling.

The playing field

First, let's provide some context. According to Statistics Canada, as of December 2015, there are 1.17 million employer businesses in Canada, of which 1.14 million (97.9%) are considered small businesses (defined as having 100 employees or fewer). These small businesses collectively employ 8.2 million Canadians, or 70.5% of the private workforce.

Minister Morneau states in his op-ed that "over the past 15 years […] the number of private corporations has increased by 50%." He attributes this increase to a greater number of small business owners, entrepreneurs (plumbers, farmers, electricians, etc.) and professionals (accountants, doctors, dentists, lawyers, etc.) incorporating, and implies that this is unsustainable and unfair.

Yet the federal government's own "Benefits of federal incorporation" website states: "Business corporations are taxed separately from their shareholders. The corporate tax rate is generally lower than the individual tax rate. In some cases, incorporation offers some fiscal benefits." Minister Morneau, how can you imply that incorporated Canadians are tax cheats, when the government encourages them to do so?

Morneau's proposals also take aim at passive investments, even though the Income Tax Act already taxes passive investment income equally to regular income when withdrawn from a company; this is called tax integration.

Unfair comparison

The Department of Finance's July 18 proposals compared "ordinary" Canadians to those who have incorporated. We propose a fairer comparison: ordinary Canadians to civil servants.

According to Statistics Canada, there are 3.6 million public sector employees in Canada. The ones who work full time generally enjoy guaranteed salaries, group benefits, paid sick leave and paid vacations. Such civil servants also receive generous defined benefit pension plans at retirement.

Consider a comparison of these further areas:

	Incorporated individuals	**Employees**	**Civil servants**
Salary	Not guaranteed	Guaranteed	Guaranteed
Work week	Not fixed; coud be up to 60 to 70 hours per week	40 hours per week, on average	40 hours per week
Group benefits	Potentially; if so, paid for through own corporation	Potentially; if so, paid for by employee and employer	Yes; paid by government
Paid parental leave	None (unless paid into through EI)	Up to one year	Up to one year
Paid sick days	None	Yes	Yes
Paid vacation	None	Yes	Yes
Retirement pension	Potentially; if so, paid for through own contributions (e.g., IPP)	Potentially; if so, paid for by employee and employer	Defined benefit plan, paid for by taxpayers

Civil servant pensions provide guaranteed, indexed income based on the average of their highest-paid five consecutive working years. Unlike with an RRSP, TFSA or corporate investment portfolio, those with indexed defined benefit plans don't have to concern themselves with market volatility, portfolio risk, asset allocation or management fees.

Civil servant versus incorporated doctor

Let's now compare the retirement incomes of Bob, a career civil servant with Cheryl, an incorporated physician.

Bob graduates from university at age 25 and begins working in the civil service with a starting salary of $40,000 plus benefits. During his career, he enjoys a guaranteed salary, 40-hour work week, group benefits, paid sick leave, paid parental leave, paid vacation days and an indexed DB pension plan. Bob is both dedicated and ambitious and decides to get his MBA. His employer (in Bob's case, the federal government) supports this decision and pays for more than half the tuition. With his newfound credentials, his salary will increase at a faster rate (as it should), leading to a significantly higher long-term pension benefit.

Now let's explore his pension in more detail.
Bob works his way up to more senior positions and finishes his career as an associate deputy minister at age 60 with a final salary of $200,000. After a 35-year career, Bob's DB pension will provide him $133,000 per year indexed to inflation. That makes the present value of Bob's pension $3.3 million.
If Bob had tried to build an RRSP account worth $3.3 million during his 35 years of civil service (assuming he earned a 4% return after inflation and fees), he would have needed to make deposits equivalent to 50% of his salary. That amount is far more than he could deposit under today's regulations, where the maximum contribution rate for RRSPs is 18% of salary to a limit of $26,010 for 2017.
In 2007, the government announced that pension splitting would be allowed. As a result, when Bob retires he can split his pension with his spouse (or common-law partner). If they have no other income at retirement, they will have a joint tax bill in the range of $26,000 (or 20% of $133,000). This ability to income split (which one could refer to as income sprinkling) is one of the benefits Minister Morneau wishes to now eliminate for incorporated individuals, but not civil servants.
Now let's compare Bob's lifetime compensation (working years plus retirement) to that of his friend Cheryl, a physician.
Cheryl graduates at 25 from medical school. After a year of residency, she is able to earn an income as a family physician.
Once she starts her practice, she will work 60 to 70 hours a week and be on call five days a month. Her medical practice will gross $350,000 per year, she will employ two staff who each earn $50,000 ($100,000), rent office space ($25,000), pay expenses ($10,000), provide group benefits ($8,000), and pay malpractice insurance ($5,000). She will take a salary of $144,000 to maximize her RRSP contribution of $26,000 per year. That leaves her with net income in her medical practice of $58,000 before tax, or $49,000 after tax in Ontario. As she plans on having two children, the funds saved in the corporation for the first four years will be used over the next five years as she works part-time to help raise her young family. She returns to full-time work at age 39 and is now able to add her corporate savings to her RRSP funds.
By age 60, Cheryl's RRSP account will be worth just over $1.5 million, assuming she earns 4% after inflation and fees. Note that there is no guarantee she can consistently generate this kind of return, whereas Bob's pension returns are fully guaranteed by the government.
The only way for Cheryl to accumulate a pension somewhat close to that of Bob is to save money in a corporate investment account. She cannot save the funds necessary to equal Bob's pension because she does not make enough

money, but she could save $50,000 per year. Her medical corporation will pay a tax rate of 50.17% on this investment income, which is the current tax rate before proposed changes.

If Cheryl earns the same rate of return as in her RRSP, less the tax she pays from age 39 to 60, she will have about $1.4 million in her corporation and $1.5 million in her RRSP. When she withdraws the funds from her corporation during retirement, she will pay a dividend tax. If the new proposals are passed, Cheryl's tax rate on her passive income earned in her medical corporation will ultimately be 71% (combined corporate and personal tax in Ontario) when she starts to receive them at retirement, compared to Bob's 20%.

There are a few other factors that must also be considered in this comparison. First, Cheryl funds 100% of her RRSP, disability, critical illness, life insurance and any health benefits she and her family require. Second, Bob has an opportunity for salary increases over his lifetime — at minimum, at the level of inflation, but in his case considerably higher because of his MBA. In contrast, most physicians' fees decrease in real terms.

Perhaps most important, however, is that this analysis shows that Cheryl's current savings plan (RRSP and corporate investment plan) will result in a substantially smaller retirement nest egg than Bob. This is in addition to bearing the burden of investment, volatility and business risk.

Conclusion

We have no issue with the total compensation enjoyed by civil servants. Instead, we're arguing that we should return to the original narrative Minister Morneau used to describe the unfair advantage incorporated professionals and business owners have over other Canadians. The real issue here is that Minister Morneau is only looking at half of the picture; with all due respect, his analysis is incomplete.

We ask that he consider not only the benefits incorporated people accrue during their working years but also how they are able to able to plan for retirement compared to employees and civil servants.

In our opinion, the existing system is not only fair, but plays out far better for the 3.6 million government employees than it does for the 1.1 million small business owners.

9. Pre-retirees relying on homes to fund retirement

[September 26, 2017] Many Ontarians are overestimating their ability to finance their retirement using their homes, according to a study by the OSC. In fact, 45% of pre-retired Ontario homeowners are relying on the value of their home increasing to fund their retirement.

Further, homeowners without any retirement savings or plan are among those most likely to be counting on the continued appreciation of their homes.

"Owning a home is not a substitute for retirement planning," says Tyler Fleming, director of the Investor Office of the Ontario Securities Commission. "Research like our study is key to improving our understanding of investor needs and issues."

The survey also finds substantial gender differences. For example, women aged 55 and older are more stressed when it comes to retirement planning.

The top financial concerns for a quarter of Ontarians aged 45+ are retirement-related, including having enough money for retirement, planning and saving for retirement, and maintaining quality of life in retirement.

Apart of the concerns about retirement, these people express concerns about having enough money to pay for the cost-of-living today (13%), paying off or managing debt levels (10%) and investment performance, growth and protecting capital (9%). Just 11% say they don't have any financial concerns.

Additionally, nearly three-quarters of pre-retirees (73%) own their home; 38% with a mortgage and 37% without a mortgage.

The investment savings profile of this group is as follows:

- 38% have no investments;
- 21% have an investment portfolio less than $100,000;
- 25% have an investment portfolio between $100,000 and less than $500,000;
- 11% have an investment portfolio of $500,000 or more; and
- 5% would not disclose the size of their investment portfolio.

About the survey: The survey was conducted online among a representative sample of 1,516 Ontarians, 45 years or older, between May 9 and 16, 2017.

10. Will Toronto add new vacancy tax on rental properties?

[September 26, 2017] The Toronto Real Estate Board is urging the city to exercise caution regarding a possible vacant home tax.

The board says it's worried there is not enough data or evidence to support the idea that a vacancy tax would increase the supply of rental housing.

It urged the city of Toronto to take a measured approach to help avoid any unintended consequences for the housing market and property owners.

The board also raised the issue of private property rights and the administrative challenges.

The Ontario government moved earlier this year to cool the Toronto housing market, including the imposition to a foreign buyer tax and other changes.

The move followed the introduction of a tax on foreign homebuyers in the Vancouver region last year. The City of Vancouver also imposed a tax on vacant homes.

Have a nice and fruitful week!