# A Business Owner's Tax Saving Strategies in Uncertain Times

Sheila and her husband Ray are small business owners. Like many small business owners they are concerned about the survival of their business given the current volatile economy. The couple has approached their financial advisor to ensure they fully understand the measures being implemented by governments as part of the economic response to the covid19 pandemic. They have also asked their advisor for other tax saving strategies for their business in the current market. Here are some strategies open to them.

## 1. Utilizing Government Programs

On March 25, 2020, the federal government passed the COVID-19 Emergency Response Act, aimed at stabilizing the economy and supporting Canadians. Since then, additional announcements were made with respect to the federal government's COVID-19 Economic Response Plan. All provinces have also implemented significant measures to help businesses and individuals. Sheila and Ray might want to consider the following:

i. The Canada Emergency Wage Subsidy which will cover 75% of payroll costs for three months retroactive to March 15th for eligible employers whose revenues decrease by specified percentages in March, April or May 2020. Organizations that don't qualify may still qualify for the previously announced 10% Temporary Wage Subsidy.

ii. The work-sharing program has been extended to 76 weeks from 38. It offers employment insurance for employees whose hours have been reduced. Business owners may consider the program to protect current cash on hand while keeping skilled employees ready to go when the economy normalizes.

iii. Apply for newly available low interest or no interest loans and look for debt servicing relief. The Canada Emergency Business Account offers bank loans of up to $40,000 - interest free for the first year - for small businesses who paid between $20,000 and $1,500,000 total payroll in 2019. Up to $10,000 may be waived for repayment.

iv. Cease remittances to the CRA. Tax becoming payable on or after March 18 is deferred to September 1 without interest or penalties[1]. GST payment and customs duties are extended to June 30. Certain federal tax filing deadlines have been extended[2]. Provincial tax filing deadlines and payment deadlines have also been deferred. File as early as possible if a refund is expected.

For more details on the federal and provincial programs read:

COVID-19 Economic Response Plan and Federal & Provincial Economic Response to COVID-19

v. Sheila and Ray may also want to consider working with their bank for relief on mortgage payments, their credit card company for interest relief, their landlord for rent relief and their insurer for temporary changes to auto and workspace policies. They should be reviewing their insurance and determining if there is any coverage they do not need on a short term basis. Also consider utility bill and property tax relief offered by service providers and municipal jurisdictions.

vi. If Sheila and Ray are working from home, they should be able to claim home office deductions on their 2020 tax returns. If they have employees working from home, those employees may also be able to claim home office expenses. One of the requirements for an employee to claim home office expenses is the employer must complete and sign Form T2200.

vii. Revisit other tax credits or incentives such as Scientific Research and Experimental Development (SR&ED) which may provide a refund or investment tax credit, particularly as businesses innovate to respond to the crisis.

[1] This payment extension provides relief for December 31st year end Canadian controlled private corporations (CCPCs) who generate less than $500,000 of active business income as taxes owing 2019 would otherwise be due on March 31, 2020. It provides no relief for corporations with December 31 year-ends earning only passive income (i.e. not active business income) as 2019 taxes owing were due by February 29, 2020. There is relief for all corporate taxpayers for tax instalments due after March 18, 2020 for the 2020 tax year. For self-employed taxpayers and individual taxpayers including personal trusts, the payment deadline for 2019 tax payable and 2020 tax instalments coming due after March 18, has been extended to September 1, 2020.

[2] The personal tax filing deadline has been extended to June 1, 2020. For self-employed individuals, the filing deadline remains at June 15, 2020. Tax payments for 2019 are also extended to September 1, 2020. For trusts, the filing deadline which would otherwise be March 30, 2020 is extended to May 1, 2020. There will be no interest or penalties charged during the deadline extension (with the exception of trusts which will be dealt with on a case by case basis).

## 2. Protect Captal Dividend Account ("CDA") Balances

One of Sheila and Ray' s corporations has a large CDA balance. The company has experienced some capital losses over the last two months which have not yet been realized. As a realized capital loss erodes a company's CDA balance they should consider having the company pay each of them a tax-free capital dividend prior triggering any capital losses.

## 3. Consider Previously Refunded Dividend Tax on Hand

Carrying back capital losses can have implications on Refundable Dividend Tax on Hand ("RDTOH"). If Ray and Sheila carry back corporate capital losses to apply against prior year capital gains of the corporation, previously received RDTOH may have to be repaid, reducing their expected refund from the losses carried back.

## 4. Address Passive Investment Income Rules

Sheila and Ray's group of companies are earning both passive and active income. They have been reluctant to address the passive investment income rules for fear that triggering large capital gains will impact the small business tax rate on their active business income. Now may be a good time to reallocate corporate investment holdings to more tax efficient options such as corporate class mutual funds, investments with ROC distributions, or potentially moving passive capital outside the corporate structure. Corporate class mutual funds distribute only capital gains and dividends. Capital gains are taxed more efficiently than other forms of income. T-class mutual funds distribute ROC which is not immediately taxable. ROC reduces the cost base of the investment, triggering tax at capital gains rates when the cost base becomes negative or when investment is sold. Capital gains and ROC mitigate erosion of small business limit within corporate structures.

## 5. Consider an Estate Freeze

The global pause on non-essential economic activity has depressed the valuations of many active businesses, including Sheila and Ray's. An estate freeze could limit future capital gains in their estate. Post-freeze growth (and related capital gain) is transferred to the next generation, either directly or through a family trust. If current valuations are sufficient to fund Sheila and Ray's lifestyle, and they anticipate growth over time, an estate freeze can effectively transition assets to the next generation on a tax deferred basis now, and limiting the future tax liability in their estate to current depressed values. This strategy can also apply to non-business assets such as a portfolio of publicly traded securities and can be an effective probate mitigation tool.

For business owners operating active businesses through Canadian controlled private corporations ("CCPCs"), an estate freeze can generate additional tax savings on future sale of the business by extending the Lifetime Capital Gain Exemption ("LCGE") to family members brought into the business through the freeze process. The LCGE represents approximately $220,000 of tax savings per taxpayer, depending on the province. Strict ownership and use criteria must be met to claim the exemption, but it is designed to exempt capital gains on disposition of qualified Canadian businesses[3]. There could also be other income splitting opportunities prior to the sale, such as paying dividends to lower income family members. The rules related to tax on split income ("TOSI") must be reviewed before dividends are paid.

Business owners who previously triggered an estate freeze may consider a refreeze. Where an estate freeze has been done in the past, the preferred shares issued are revalued at the current, lower, market value. This would allow the business owner to take advantage of tax relief inherent because of the current economy. The corporation's share structure must be reviewed if considering a refreeze.

Business objectives, cash flow and long-term goals take priority over short-term tax savings. However for Sheila and Ray, who have worked so hard to build up their business, proper planning today can help it  survive the current market and continue to flourish in the future.can help it survive the current market and continue to flourish in the future.

[3] For 2020, The LCGE is $883,984 on for qualified small business corporation shares and $1,000,000 for qualified farming or fishing property including shares of qualified family farm or fishing corporations.

## IMPORTANT DISCLAIMERS



Published April 20, 2020

CI Investments

2 Queen Street East, Twentieth Floor, Toronto, Ontario M5C 3G7 I **www.ci.com**

| **Head Office / Toronto** | **Calgary** | **Montreal** | **Vancouver** | **Client Services** |
|---|---|---|---|---|
| 416-364-1145 | 403-205-4396 | 514-875-0090 | 604-681-3346 | 1-800-792-9355 |
| 1-800-268-9374 | 1-800-776-9027 | 1-800-268-1602 | 1-800-665-6994 | |

20-04-0554_E (04/20)