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TAXATION

Tax Changes for 2018/19

Whether you prepare the return yourself or have them prepared by your CPA, it's almost time for all Canadians to be gathering their paperwork together for their 2018 personal tax returns. So, what changes for 2018 might affect your business? And, what other tax changes are coming into effect in 2019?

Changes Affecting Canadian-Controlled Private Corporations

The federal small business tax rate decreased to 10% as of January 1, 2018, and by a further one percent to 9% as of January 1, 2019. The personal tax rate for ineligible dividends increased to offset those decreases in order to maintain "integration" – the concept that the tax burden for income earned by an individual personally should approximate the combined corporate and personal tax paid if that income was earned through a corporation and then paid out as a dividend to the individual.

Ineligible dividends are those that are paid out of corporate income that has benefitted from preferential tax treatment, either through:

- the reduced small business tax rate noted above, or
- the refundable dividend tax treatment for certain investment income earned in private corporations

Changes to the Tax on Split Income (TOSI) Rules

Possibly the most significant tax changes are those affecting the shareholders of private corporations.

The TOSI rules were first introduced in 1999. They were developed in order to limit the benefit of tax structures that mainly aimed to reduce a family's overall tax burden by splitting income with minor children.

The 2017 federal budget identified similar concerns with income split between adult family members, and new rules were introduced that became effective January 1, 2018. These new rules are complex, but essentially they extend the TOSI rules to adult family members. Some sources of income are exempt from the TOSI rules, with different exemptions applying to those between 18 and 24 years old from those that apply to Canadians 25 or older.

Excluded business

Income from an excluded business will not be subject to the TOSI rules for individuals between 18 and 24 years old. The excluded business rules focus on the individual's contribution to the business and require that the individual has been actively involved in the business on a regular, continuous and substantial basis. Income for adults in this age group would also be excluded if it is under a specific amount, which is calculated using a legislatively-prescribed rate applied to the value of the assets that the individual has contributed to the business.

Excluded shares

In addition to the excluded business exception, Canadians 25 years and older have additional exceptions for both of the following:

- income from excluded shares, which apply where the individual owns more than ten percent of a non-services-based company
- a "reasonable" return based on the contributions of the individual. These contributions may be financial (capital contributed), based on one or both of:
  - the work that he or she does (after considering any remuneration they already receive for that work)
  - risks that he or she has assumed

There is an additional exception for spouses over 65 years old.

Changes to Taxation of Passive Income

In addition to the changes just discussed – and which affect the shareholders of private corporations – there are also changes, effective for taxation years beginning after 2018, to the taxation of passive income earned within a Canadian-controlled private corporation (also known as a "CCPC").

These rules are designed to limit the deferral advantage available to these private corporations, since they invest income that has been taxed at the low small business rate passive investments are subject to. In contrast, individuals who earn income personally would pay higher tax, and therefore would have less after-tax income to invest.

These changes to taxation of passive income reduce the access to the small business tax rate by $5 for every $1 of "adjusted aggregate investment income" above $50,000. They are also very complex, especially since some provinces, such as Ontario, have announced that they will not parallel the new federal passive income rules.

Other Changes

The new year brought in **increased Canada Pension Plan (CPP) contributions** designed to fund the enhanced CPP benefits in the future. However, a slight offset to those higher CPP rates exists and will be noted, as the Employment Insurance contribution rates have decreased. For more information, please see **www.canada.ca/en/services/benefits/publicpensions/cpp/cpp-enhancement.html**

The federal government's new **carbon pricing mechanism** will also come into effect in those provinces that do not have a carbon pricing mechanism of their own. This will result in increased costs for fossil fuels and the services that they support starting in April 2019, with a direct rebate to consumers to offset some of those cost increases.

Other than the changes discussed above to the tax rate for ineligible dividends, no changes are coming to the personal tax rates for other sources of income: salary, capital gains, and eligible dividends (generally those from public companies). The tax brackets and personal credit amounts are adjusted for inflation.

The **public transit tax credit** was eliminated as of July 1, 2017, so you might notice this credit disappearing completely for 2018 when you prepare or review your tax return. Also new for 2019: low-income workers can qualify for an increase in the **Canada Workers Benefit**. However, they will not receive the extra money until 2020.

In summary, while there were relatively few changes to the tax rules in 2018/19, those changes that were introduced for private corporations and their shareholders are complex and may have a significant impact on those affected. **To see if these changes affect you or your business, it's worth meeting with your CPA**.

MANAGEMENT

The SCARF Model: Brain-Based Ideas for Collaborating With Others

In 2008, after interviewing researchers in neuroscience and psychology, Dr. David Rock summarized his findings in a model of behavior based on three basic principles: people treat emotional or social threats with the same level of intensity as physical threats and rewards; people's ability to make good decisions and collaborate is weakened when they are in a threatened state; and threat response in people is more common than reward response and often needs to be carefully managed in social interactions.

While none of this is news to anyone having worked with challenging projects, clients or employees, Rock's research led him to create the acronym SCARF to explain the five basic triggers that cause someone to react with a defensive or threat-based emotional reaction:

- **Status** – When someone feels more or less important than another, they will either act emotionally defensive or collaboratively, depending on how they are presented with information about their own actions.
- **Certainty** – When someone feels that they can reliably predict and control themselves and their environment, they will act with less defensiveness when presented with a challenge.
- **Autonomy** – Generally, people react badly when they feel they are not autonomously able to control their own decisions and choices.
- **Relatedness** – When someone can relate or find "common ground" with another person, they will generally be less defensive, because they believe the other person to be like them in outlook and choices.
- **Fairness** – Depending on the person's perception of the level of fairness, they will create a negative or cooperative response to a decision made around but not *with* them.

Essentially, your subconscious reacts to the world in an "approach and avoid" pattern you aren't really aware is operating under the surface: you will naturally avoid things that feel threatening or bad (such as a dark alley or an overly obnoxious colleague) and will move toward or feel an affinity with things that you associate with positive feelings (such as a warm, sunny café table or a sales associate with a genuine smile).

These are subconscious activities that have kept us as humans alive for millennia. And if you are mindful of this threat/reward activity in your daily interactions, you can have a more positive experience in working with people.

What Are *Your* Response Triggers?

First things first though: you need to become more aware of your own threat and reward responses. If you aren't aware of your own response triggers, you won't be able to mindfully approach others with offers to collaborate or instruct. To become aware, you need to consider the last five interactions you had with people that were good, and five that were less than ideal.

In thinking about these interactions, consider what was good about them and what was not so great. You may want to record your thoughts for further reflection. Ask yourself the following questions:

1. What actually happened that needed your response?
2. How did you feel about the interaction as a whole experience?
3. How did you feel in the moment where "it" went wrong?
4. How did you feel in the moment where "it" was a good experience?
5. In hindsight, which of the five triggers did you react to: status, certainty, autonomy, relatedness, or fairness?

When you finish thinking about your five to ten experiences, you will begin to see patterns in your own behaviors. Being mindful of your own reactions and behaviors will help you think of the other person you're working with from a more distanced perspective. The old adage, "walk a mile in their shoes," is an appropriate one.

For example, approaching someone to collaborate or correct their work with the idea that your own beliefs and reactions are the same as theirs can lead you into trouble. It would be a good idea to begin by examining how each of you likes to communicate and working with the other person on their terms rather than your own.

Breaking Down SCARF Reactions – and *What* Triggered Them

Status

If you felt your status was threatened, was it because you believed your words and actions should have carried more weight or impression with your colleague? Did you feel that you were being dismissed or overlooked?

People will feel threatened if their status is not acknowledged and they believe they are either equal to or above the current situation or group or feel less equal to those with whom they are collaborating. You can put people at ease by acknowledging their external status, reputation, or experience with the task at hand.

Certainty

If you felt uncertain about how your work, conversation, or project would go, did you feel less committed to the work? Were you comforted or disillusioned by the commitment of others to the task at hand?

People may be less committed and therefore less likely to contribute fully to the project if they don't know:

- where a project begins or ends
- how important the work is with respect to the larger stakeholders or organizational plans
- where their own place is in the project

Consider using agendas, milestones, responsibility charts and regular reporting on projects to help everyone feel that their work is acknowledged, accepted, and being used.

Autonomy

If you felt like you were not being listened to, not being respected for your time or activities, or were being "railroaded" into a decision, did you react by being less attached to the work and decisions? Or, did you increase your intensity with your communication?

People will feel threatened if they do not believe that they have the ability to make their own decisions or that their choices or "votes" are not being considered in the final work product or plan. You can help people feel that they are able to contribute on their own by acknowledging the work done, recording votes, and listening carefully to those who are disagreeing.

Relatedness

Did you feel as if the other person just didn't understand you – or that they were so understanding that you felt they were just mimicking you? Then you were experiencing a flight response in relatedness.

People need to feel trust in order to fully commit to collaboration and development. Without trust, there can be no real sharing or vulnerability when it comes to working together on tough negotiations or over long hours. You can increase trust in your collaborative work by making yourself vulnerable or open to discussing your own concerns and ideas.

Fairness

If you felt as if the interactions you were having with your collaborator were shallow, disingenuous, or unfair, how quickly did you want to get away from the situation or person altogether?

People's sense of fairness isn't always at the same level and it is important to discuss what "fair" means to all parties concerned. Having open conversations up-front about responsibilities, timelines, and work levels will help to build trust and a sense of fair play that allows all parties to work together in a more collaborative environment.

Learn more

If you are interested in learning more about the SCARF model or brain-based techniques for collaboration and influence, you should visit the **Neuroleadership Institute** website or consider purchasing Dr. David Rock's book, ***Your Brain at Work***.

WEALTH MANAGEMENT

Will I or Won't I?

You've met with your lawyer and drafted your last will and testament. Congratulations – you are doing better than half of your fellow Canadians! But drafting your will should never be a "one and done" exercise. It's generally best practice to review your will every three to five years, to make sure that it still does what you want it to do. Certain life events should also trigger a review of your will. What are some of those? Read on to learn more …

Changes in Your Relationships

Significant changes in your relationships or family situation should trigger a review. Examples of these changes include:

- One of your beneficiaries has passed away.
- You have had a falling out with a beneficiary, executor or guardian named in the will.
- Maybe you designated a portion of your estate to a favorite cause, but now you've identified a different charity that will be a better fit for your legacy.

Marriage

In most provinces, your current will is automatically revoked when you get married, but there are some exceptions to this general rule. For example, if the will contains an "in contemplation of marriage" clause that identifies your future spouse by name, that will would not automatically be revoked. If your will is revoked and you do not make a new one, when you die you will be considered to have died "intestate," and your estate will be distributed according to the succession laws in the province where you live.

It is worth noting that these laws vary widely between the provinces, including whether or not they cover common-law spouses. The provincial family law legislation may also interact with the succession laws to provide additional options for the surviving spouse – so reviewing your will when you get married is an absolute must!

Divorce

The impact of a divorce on your will also depends on your province of residence. In some jurisdictions, the entire will is revoked, while in others only those provisions relating to your former spouse are revoked. If you are legally married, separation from your spouse will generally not have an impact on your will. The impact of a separation for common-law spouses varies from province to province, so you should consider making a new will whenever a legal marriage or a common-law relationship ends.

New additions to your family

The birth or adoption of a child is another event that should trigger an update of your will. In addition to selecting a guardian for your minor children, you may want to establish a trust to hold the property for those children until they reach a specific age. You should review these sections periodically to ensure, for example, that the person whom you have selected as the guardian still has the time, interest and ability to devote to looking after your children.

And, if your will was to establish a trust for your children until age 25, as you see your children grow is that still the right age? Or are they mature enough that they could handle their inheritance at, say, 18 – or maybe not until they are 30 years old? You should also consider whether your will should be updated when the youngest of the children reach maturity, finish post-secondary education, or get married or divorced as well.

Changes in Your Assets

In addition to major changes in your relationships, significant changes in your assets should also trigger a review of your will.

The need to review may arise through **changes in the relative value of your assets**. For example, if you plan to leave your home to one child, the family business to a second child and your investment portfolio to the third child, and the relative value of those assets has changed, you may want to change the terms of the will to be fair to all of your beneficiaries. Another factor that may affect the value of the assets could be changes to Canadian tax legislation, or international tax legislation if you own any foreign assets.

When you review your will after a significant life event or change in your assets, it is also important to **review the named beneficiaries** for your Registered Pension Plan, Registered Retirement Savings Plans, Tax-Free Savings Account and life insurance policies, to make sure that these reflect your current situation and wishes.

It’s also a good time to review your **powers of attorney**, which name someone to act on your behalf if you are unable to. There are two kinds of power of attorney: one for property, naming the person who can make decisions about your financial affairs; and one for personal care, naming the person who can make decisions about your healthcare, housing and other aspects of your personal life.

Finally, as noted above, the laws governing family law, wills and estates are provincial, rather than federal, so **if you move between provinces** it’s time to review your will and other related documents.

Your CPA Can Help

In addition to consulting with your lawyer, reviewing your estate plan with your CPA will help give you peace of mind that your estate will be distributed in the most efficient and effective way possible, in accordance with your wishes.

MANAGEMENT

Strategies to Help Businesses Comply with Canadian Privacy Laws

Privacy and data security are becoming an area of significant concern for both businesses and individuals. It is important you understand the laws and your obligations in this area to reduce and mitigate risks.

Overview of the Privacy Regime in Canada

The *Personal Information Protection and Electronic Documents Act*, SC 2000, c 5 (PIPEDA) is Canada's federal privacy law for private sector businesses. It sets out the ground rules for how businesses must handle personal information.

PIPEDA requires businesses to obtain a person's consent when they collect, use or disclose personal information in the course of a commercial activity.

Commercial activity is defined as "any particular transaction, act, or conduct, or any regular course of conduct that is of a commercial character, including the selling, bartering or leasing of donor, membership or other fundraising lists" [**s.2(1)**]. What constitutes commercial activity depends on the facts. For example, a court-appointed trustee-in-bankruptcy who collects personal information to administer a bankruptcy was found to engage in commercial activity because it received remuneration for administering the bankruptcy [PIPEDA case summary 2006-336]. Similarly, a non-profit daycare that was subsidized by a municipal government was found to engage in commercial activity because it received payment for child care services [PIPEDA case summary 2005-309].

Some organizations may be exempt from PIPEDA in provinces that have enacted their own privacy legislation that is substantially similar to PIPEDA. To date, Quebec, Alberta and B.C. have enacted provincial privacy legislation that is deemed substantially similar to PIPEDA. Nevertheless, PIPEDA continues to apply to international and inter-provincial transfers of personal information by private-sector businesses in those provinces.

Personal Information

Personal information is defined as "information about an identifiable individual" [**s.2(1)**]. This includes both factual and subjective information about a person. Factual personal information includes information such as a person's name, address, phone number, email address, ID numbers, and more sensitive information such as credit card information and financial information. Subjective personal information includes information such as a person's opinions, evaluations and comments. Canadian courts have interpreted personal information so broadly that it also includes information that does not alone identify an individual but when combined with other information, does identify an individual.

PIPEDA's 10 Fair Information Principles

Businesses subject to PIPEDA must follow a code for the protection of personal information. The code consists of 10 fair information principles that are set out in Schedule 1 of PIPEDA.

In addition to requirements around how to collect personal information, the fair information principles require businesses to appoint a chief privacy officer who is responsible for the business' compliance with PIPEDA, make their personal information handling policies publicly available, and allow individuals access to their personal information.

The fair information principles also require businesses to adopt security safeguards appropriate to the sensitivity of the information. For example, more robust security measures must be put in place to protect sensitive personal information such as financial information and medical records whereas less stringent security measures may be adopted to protect basic personal information such as name and email address.

Compliance Strategies for Businesses

The following six strategies will help businesses comply with their obligations under PIPEDA.

Develop a privacy policy and post it on your website. Businesses should develop a comprehensive privacy policy that sets out in detail what personal information it collects, why it collects it, how it uses it and to whom it discloses it. This privacy policy should also address other items such as what security measures are in place to protect the personal information and whether the information is transferred across borders. The privacy policy is an outward public-facing document that informs your clients and customers about how you manage their personal information.

Develop a privacy management program and train your employees. A privacy management program is an internal “how to” manual for businesses and their employees. It sets out in detail the policies, practices and procedures the business must adopt in order to comply with its privacy policy. In addition, businesses should train their employees on their privacy management program.

Develop a data breach response plan that complies with PIPEDA’s new breach reporting requirements. On November 1, 2018, PIPEDA’s new mandatory breach recording and record-keeping requirements came into effect. These new provisions impose requirements on businesses to keep track of every “breach of security safeguards” and report significant ones to the Office of the Privacy Commissioner of Canada and individuals affected by the breach. In order to comply with these requirements, businesses should develop a data breach response plan, which acts as the company’s “playbook” in the event of a data breach.

Adopt appropriate security measures and ensure data security is up-to-date. Businesses should adopt security measures that are appropriate to the sensitivity of the personal information. Businesses should also ensure that all data security is up-to-date. This may include, for example, ensuring all critical security patches are applied as soon as possible or within a reasonable period of time.

Obtain express consent whenever you can. While PIPEDA allows businesses to rely on an individual’s implied consent to the collection, use and disclosure of personal information in appropriate circumstances, businesses should nevertheless obtain an individual’s express, written consent where possible and maintain a record of that consent in order to avoid any ambiguity in the consent process.

Conduct a periodic review of your personal information handling practices and policies. Businesses should review their privacy policies and personal information handling practices annually to ensure they are up-to-date or make any amendments as necessary.

In the age where privacy breaches are splashed across the media, it is important for businesses, both big and small, to ensure they have appropriate privacy practices in place. This not only complies with the law but also demonstrates to clients and customers that you care about the personal data they entrust you with.