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Do you know that the small business tax rate is no longer available for Specified Corporate Income (“SCI”)?

2016’s Budget measure introduced the SCI rules to prevent the multiplication of the small business deduction (“SBD”) for unassociated corporations. Under the new SCI rules that are effective for **taxation years beginning after March 21, 2016**, Active Business Income (“ABI”) earned by a Canadian Controlled Private Corporation (“CCPC”) from the provision of property or services to a private corporation will be excluded from eligible ABI where certain conditions are met, unless a specific exception for associated corporations are met, or the private corporation is allowed (and willing) to assign part or all of its SBD limit to the CCPC.

Income that is ineligible for the SBD under these rules will be taxed at the general corporate tax rate.

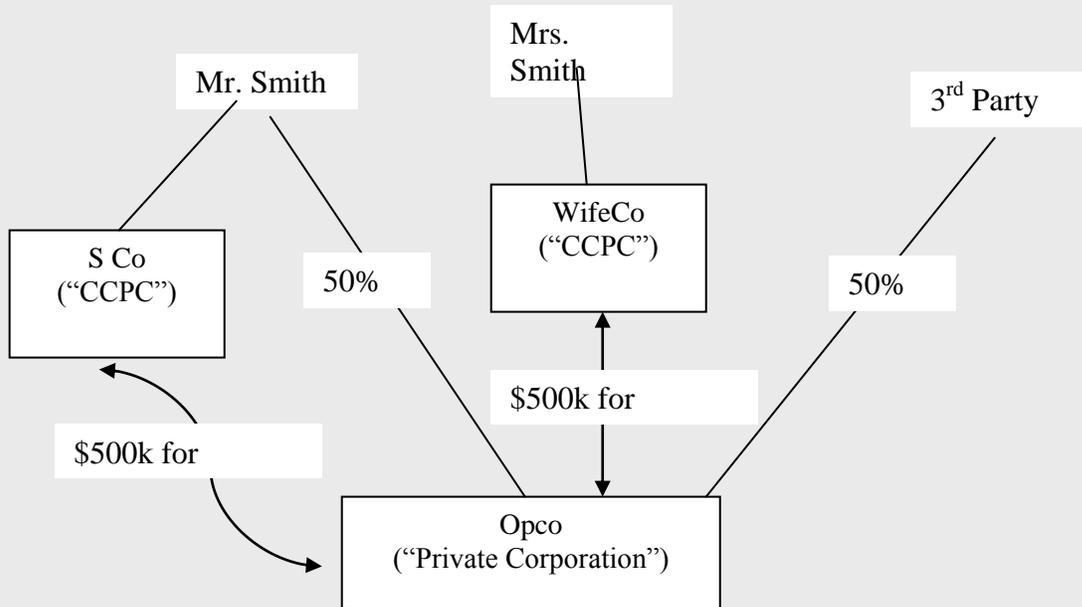
What would be caught?

The tax rules set out that income from an active business for the year earned by a CCPC from the provision of property or services (directly or indirectly, in any manner whatever) to a private corporation may be ineligible for the SBD if:

- At any time in the year, the corporation (or one of its shareholders) or a person who does not deal at arm’s length with the corporation (or one of its shareholders) holds a direct or indirect interest in the private corporation, **and**
- All or substantially all of the corporation’s income for the year from an active business is not from the provision of property or services to:
 - Persons (other than the private corporation) with which the corporation deals at arm’s length, or
 - Partnerships with which the corporation deals at arm’s length, other than a partnership in which a person that does not deal at arm’s length with the corporation holds a direct or indirect interest.

In general terms, if all or substantially all of a corporation’s ABI is earned from arm’s length sources, these rules should not be a concern. However, if all of the conditions above are met, it will be necessary to determine if the income is ineligible for the SBD or if an exception applies.

Example



S Co and WifeCo's active business income ("ABI") from providing services to the Opco will be **ineligible** for the small business deduction because one of its shareholders or a person who does not deal at arm's length with such a shareholder has a direct or indirect interest in the private corporation.

This ineligibility will not apply if all or substantially all of its ABI is earned from providing services or property to arm's length persons other than the private corporation. However, Opco can make a designation to assign all or a portion of its unused business limit to one or more CCPCs that are ineligible for the small business deduction.

Exception to the SCI rules:

The exception will apply where:

- A CCPC is earning ABI from the provision of property or services to an associated corporation, and
- That associated corporation is deducting those amounts from its own income that is *generally* unrestricted ABI¹.

It is also important to know that there is one overriding limit built into these rules. The amount of SCI of the CCPC may be determined by the Minister, based on what the Minister determines to be reasonable in the circumstances. This is effectively an anti-avoidance rule that provides the Minister with ultimate control over the SCI determination, likely to nullify planning used to escape the SCI rules and which the Minister deems inappropriate.

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The publication cannot be relied upon to cover specific situations without obtaining specific professional advice. Please contact I&A to discuss these matters in the context of your particular circumstance.

¹ S.125(10)