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# Cost Estimate of Election Campaign Proposal

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| Publication date: | 2019-09-24 |
| Short title: | Passive Investment Income Reversal |
| Description: | This policy would reverse two Budget 2018 changes to the taxation of passive investment income of Canadian Controlled Private Corporations (CCPCs). It would restore full access to the small business tax rate for corporations earning more than $50,000 in passive investment income in a given year. It would also restore full access to refundable taxes for corporations on the distribution of eligible dividends. |
| Operating line(s): | Corporate income tax |

Data sources:

| Variable | Source |
|---|---|
| Passive investment income | 2015 T2 corporate income tax return |
| Taxable dividends | 2015 T2 corporate income tax return |
| Refundable taxes | 2015 T2 corporate income tax return |
| Household property income | PBO economic projection |
| Corporate profits | PBO economic projection |

Estimation and projection method:

Our estimate is based on corporate tax data from the 2015 reference year. We assume that the proposed policy changes take affect on April 1, 2020.

*Business Limit*

We estimated each corporation’s passive investment income by adding their property income, taxable capital gains and portfolio dividends. As per Budget 2018 guidelines, we excluded capital gains related to active business investments.

We estimated the business limit (that is, the maximum amount of taxable income eligible for the small business tax rate) for corporations with over $50,000 in passive investment income under the Budget 2018 changes. We then estimated an alternative business limit which would restore full access to the small business tax rate consistent with rules prior to Budget 2018. The difference in tax payable under these changes to the business limit is our estimate of the federal revenue impact. We assumed that this estimate grows at the same rate as corporate profits.

We identified connected corporations and assumed that passive investment income is aggregated and evaluated at the group level.

*Refundability of Taxes on Investment Income*

We estimated each corporation's potential pool of refundable dividend tax on hand. Based on Budget 2018 policy changes, refunds from this account are restricted primarily to the payment of non-eligible and portfolio dividends.

We then recalculated the size of the refund when allowing refundable taxes to be obtained upon the distribution of eligible dividends, thus removing the Budget 2018 restriction.

We assumed that corporate behaviour concerning dividend payouts remains the same as in the 2015 base year. We assumed that this estimate grows at the same rate as household property income.

Uncertainty assessment:

This estimate has high uncertainty. It depends on discretionary corporate behaviour such as whether to pay dividends or retain earnings as well as evolving changes to corporate structures.

Moreover, until corporate tax data for 2018 and 2019 become available, it is not possible to analyze potential tax planning in response to the Budget 2018 changes.

## Cost of proposed measure

| $ millions | 2019-2020 | 2020-2021 | 2021-2022 | 2022-2023 | 2023-2024 | 2024-2025 | 2025-2026 | 2026-2027 | 2027-2028 | 2028-2029 |
|---|---|---|---|---|---|---|---|---|---|---|
| Total cost | - | 500 | 537 | 562 | 583 | 603 | 622 | 643 | 664 | 688 |

Notes:
Estimates are presented on an accruals basis as would appear in the budget and public accounts.
Positive numbers subtract from the budgetary balance, negative numbers contribute to the budget balance.
"-" = PBO does not expect a financial cost