Canadian Federation of Apartment Associations
Fédération Canadienne Des Associations De Propriétaires Immobiliers

1600 Carling Ave., Suite 640
Ottawa, Ontario K1Z 1G3
Tel. 613-235-0101 Fax 613-238-0101

October 2, 2017 **BY EMAIL**

Dear Minister Morneau:

Re: the proposed corporate tax reforms

The Canadian Federation of Apartment Associations ("CFAA") represents the owners and managers of close to one million residential rental suites in Canada, through 11 associations across Canada and direct landlord memberships. The private rental housing sector provides close to four million rental homes for nine million Canadians of all ages, incomes and situations. The rental homes range from 850,000 apartments in high-rise buildings, through 1,800,000 apartments in buildings under five storeys to some 525,000 rented single family homes.

Among our 10,000 landlord members, close to 3,000 own or operate their rental properties through corporations. In addition, among our 1,200 supplier members, close to 1,000 operate them through corporations. As a result we represent the owners and operators of 4,000 corporations, the vast majority of which are Canadian Controlled Private Corporations (CCPCs).

Rental housing is an industry with low barriers to entry, and as such it is very competitive with low profit margins. Some members of the public see landlords as rich because they focus on the market value of the building, but in fact most landlords begin with relatively little equity and build it up over years as they in sequence pay down their mortgages, and run them up to pay for major repairs.

This is to provide our input on the proposed corporate tax reforms.

We recognize that the proposed changes do not affect rental owners who hold their properties in their own names or the name of themselves and their spouse. That covers a great many small landlords.

We also recognize that the proposed changes are said not to affect family trusts.

General comments

CFAA is opposed to the apparent intention to prevent income splitting among family members. We suggest that the relatively small amount of additional revenue is not worth the disruption and disincentive effects that such a change will cause.

CFAA is also opposed to treating 2nd generation income differently than the first generation of real estate income. Such a program would require complicated tracking, and waste resources and time to do that tracking. As with inventory, for any changes in holdings there would be legitimate arguments about whether to use LIFO or FIFO.

As well as tracking first generation income and second generation income, it will be necessary to track third and subsequent generation income. Once the "super-tax" is applied to the second generation income, any initial advantage will have been removed, and there would be no justification for applying the “super-tax” to the third and subsequent generation income.

Detailed comments on the Consultation Questions (page 54)

Taxing corporate passive income in a way “that is more fair for Canadians.”

1. what approach would be preferable in order to improve the fairness of the tax system with respect to passive income?
    a. CFAA answer: Along with any changes to the taxation of corporate passive income, rental housing income should be recognized as active business income, due to the work involved in operating rental housing.
2. If you prefer the apportionment or elective methods described in this paper, what criteria or broad considerations should the Government consider in selecting a method?
    a. CFAA answer: Make sure one or more simple options are available, as well as a precise option for those who wish to do the necessary tracking.
3. Regarding the tax treatment of corporations mostly engaged in passive investments, are there considerations that you would like to bring to the Government’s attention?
    a. CFAA answer: Yes, leave them out of any reformed rules, by setting a test for the proportion of investment funding they can receive which is active business income. That proportion could be 10% or 20% for example.
4. What would be the appropriate scope of the new tax regime with respect to capital gains? What criteria should be used by the Government in making this determination?
    a. CFAA answer: there are valid reasons for treating capital gains as they are treated now. Capital gains are measured in current dollars so that much of what appears to be capital gains is merely an adjustment for inflation. In addition, capital gains tend to occur when capital is at risk, and taking risks is good for the economy. Attached is the paper CFAA submitted in the Spring regarding capital gains treatment.
5. Are there key transition issues that you would like to bring to the Government’s attention?
    a. CFAA answer: That issue will depend on the rules that are brought out. The government should not reach back. It will be hard enough to track what proportion of investments comes from active business income vs passive income going forward. No one should be forced to untangle it going back in time.

6. Is there any reason why any aspects of the new rules should not apply to private corporations other than Canadian-controlled private corporations?
    a. CFAA answer: Yes, publicly traded corporations should be left out of the reformed rules. Since publicly traded corporations are open for investment by salaried people (who can take advantage of any preference such corporation may benefit from, if indeed there is any) there is no valid or even arguable reason to bring them within these proposed new rules.

Comments specific to rental housing

We believe there are four main groups of rental housing providers who will be affected by the changes to one degree or another. They are set out below along with the impacts as we understand those impacts.

Group by form of title and type of initial income	**Impact of the proposed new rules**	**Comments**
Corp (of fewer than 6 FT employees) receiving rental income The situation of many investors.	Little direct impact because they are already paying the “passive rate”	Rental housing income should be treated as active business income due to the work involved in operating rental housing.
Corp (of more than 5 FT employees) receiving rental income. The situation of many mid-size and large investors who self-manage.	They get the active business tax rate on their first generation income. If they reinvest in new rental buildings or improvements to get more revenue from existing buildings, the new “2nd generation” income will still be active business income (taxed at the active business rate but not the small business rate)	To avoid disincentives to these landlords and to rental housing supply, it is critical that the 2nd generation” income still be treated as active business income, **as it is now.**
Management corp performing rental management and getting some income at the small business rate	On income reinvested in rental property they would have to pay the increased tax on “2nd generation” income, even though they are already paying the full tax rate on passive income (of close to 50%)	To avoid harm to these landlords and to rental housing supply, it is critical that the “2nd generation” income still be treated as ordinary passive income, and not taxed at the new high rate. It would be even better if such income could be accepted as active business income, as it is now for corporations with more than 5 employees.

Corp whose main business is other than real estate, which invests surplus income in real estate. This sector is non-trivial since numerous companies in the trades buy rental housing to keep their employees working during the slow season. Examples are electricians, plumbers and roofers.	Their real estate income will be hit by the higher tax on "2nd generation income"	If the proposals go ahead, this may be the category which faces the worst change in its position. A tax rate of 73% would deter businesses from making any investment in rental housing, which will reduce the supply, with negative effects on maintenance, availability and affordability

Conclusion

CFAA would be pleased to meet with you or your officials to seek to address any serious problems which they can point to, in a better way which does not decrease the merits of investing in rental housing.

Yours truly,

John Dickie

President, CFAA

cc: LandlordBC, Manufactured Home Park Owners Alliance of BC (MHPOABC), Saskatchewan Landlord Association Inc. (SKLA), Professional Property Manager's Association of Manitoba (PPMA), London Property Management Association (LPMA), Waterloo Regional Apartment Management Association (WRAMA), Hamilton & District Apartment Association (HDAA), Federation of Rental-housing Providers of Ontario (FRPO), Greater Toronto Apartment Association (GTAA), Eastern Ontario Landlord Association (EOLO), and the Investment Property Owners Association of Nova Scotia (IPOANS)