TMFD Financial

Helping dentists build wealth

January/February 2018 VOLUME 14, NUMBER 1

2018 Tax Changes

Dr. Russell Changes Tactics under the Proposed New Tax Rules

Sterilization SOS Plan

2018 TAX CHANGES

Back in July 2017, while we may have been enjoying a summer activity like a round of golf, or a blockbuster movie, the federal government was unveiling a blockbuster of their own – a feature promising massive changes to our tax system.

The announcement made by Finance Minister Bill Morneau intended to fulfill a Liberal promise to combat perceived unfair tax practices by small business owners, including dentists and other medical professionals. The proposed tax changes were wide sweeping, with a focus on "income sprinkling", corporate investment income, limiting the use of the Lifetime Capital Gains Exemption (LCGE), and ending the practice of converting dividends to lower-taxed capital gains. All new rules were to be effective no later than January 1, 2018, leaving little time to plan, and with minimal detail.

Dentists and other medical professionals found themselves in the direct line-of-fire under these proposals, and the changes sparked tremendous negative feedback from business owners and the tax planning community. The Department of Finance received over 21,000 submissions during the 75-day feedback period. In reaction to the pushback, Mr. Morneau stated that the government had listened to Canadians, and that some proposed changes would be scrapped (albeit with the potential to be revisited later). However, "income sprinkling" and corporate investments would still be targeted.

To reduce the sting, existing corporate investments would be grandfathered, and new investment income up to $50,000 per year would not be subject to higher tax rates. Further, the corporate tax rate for small business would be reduced in 2018, and again in 2019. Still, there was very little detail regarding implementation of the new rules.

The Latest Announcement

Just two weeks before the end of the year, the government published an extensive set of new and complex rules for guidance on "income sprinkling". The provisions included new exemptions for adult family members who work at least 20 hours a week for the business, and for adults age 25 and older who own 10 percent or more of a corporation that is not a professional corporation. Another exemption applied to dividend payments to a spouse in cases where the owner is 65 or older, which was meant to provide a form of pension income splitting for seniors.

While the latest announcements proposed to make the rules fairer, to comply will require a high degree of complexity and judgment. Critics say it will be difficult for CRA to enforce the new rules, and that challenges to them will burden the courts.

IN THIS ISSUE

Our Senior VP of Advisory Services, Chris Molloy, considers the impact of the new tax rules on retirement readiness for a dentist near the end of his career. And Meghan Savoie, our Practice Management Coach, addresses the recent focus on sterilization protocols and how this affects your practice.

How Should You Go Forward?

From 2018 onward, dividends to family members may still be possible if they are considered "reasonable". Under the new guidelines, "reasonable" is based on the contribution of labour (i.e. work), capital (i.e. investment), or risk (i.e. co-signing loans). Alternatively, payment of salary should be considered instead of dividends. Either way, dentists are advised to document the duties performed and the hours worked in the practice to justify the compensation. And to comply with the investment rules, it's advisable to establish separate investment accounts, to delineate between the grandfathered assets and new assets.

Overall, we believe the proposals were ill-conceived, have been poorly introduced, and fail to provide adequate guidance in a timely manner. Further announcements are expected in the 2018 Federal Budget regarding corporate investments, making it difficult for tax advisors to plan effectively. Ideally, the government should delay the implementation of these changes until 2019, or scrap them altogether for a more comprehensive review of the tax system.

In the meantime, if you have further questions about how to address the new guidelines, or simply require a second opinion, please contact TMFD Financial for a complimentary meeting at info@tmfd.ca.

MIKE LAKHANI B.Comm, FCCA, CPA, CGA, CFP, R.F.P.
Mike is the CEO & Founder of TMFD Financial, formerly Tax Matters for Dentists. Since 1987, Mike has been providing expertise in tax planning, accounting and personal financial planning to dental clients. He has created a 'Multi-Family Office' for dentists geared to align their dental practices with their personal lives. With accessible, seasoned professionals all under one roof, each client's unique needs are considered with regard to tax planning, accounting, cash management, practice issues, retirement planning, structured portfolios, estate planning and insurance.

**All tax and accounting services provided by TMFD Professional Corporation, Chartered Professional Accountants*

DR. RUSSELL CHANGES TACTICS UNDER THE PROPOSED NEW TAX RULES

All dentists have been forced to reflect upon how the proposed new tax changes will impact their methods of compensation and saving for the future.

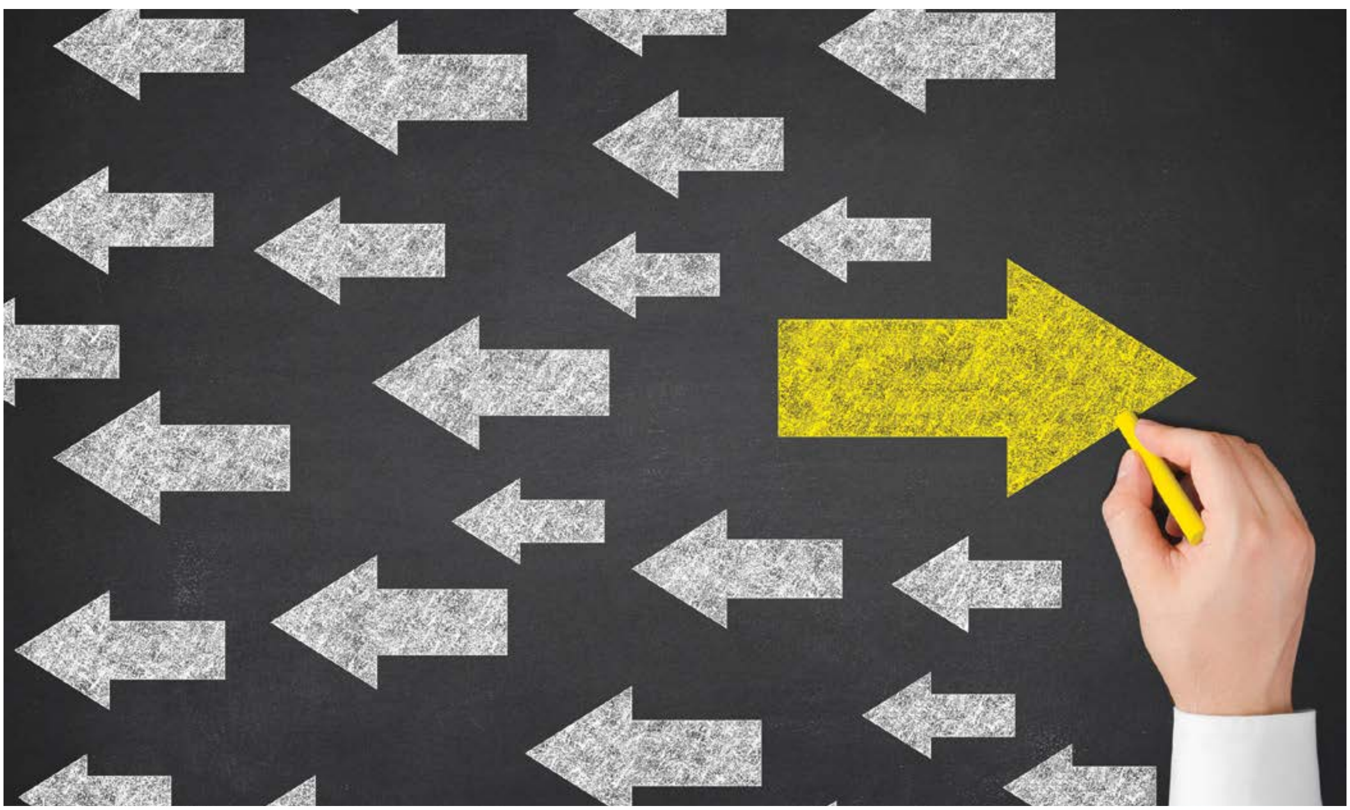
In an attempt to shine some light on possible outcomes, let's look at the case of Dr. Oliver Russell (name changed) who is firmly established in the community and has built a successful practice. At 60, Dr. Russell is thankful for the years of support provided by his wife Sandra (age 59) and for their two sons, who have both graduated and are working in their chosen fields.

Dr. Russell prefers to focus on the dentistry in the practice, while Sandra is responsible for managing payroll and coordinating the bookkeeping with the accountant's office each month. This sharing of duties has served them well for many years, and after a lengthy career, the couple has turned their attention toward retirement. Dr. Russell is prepared to work up to five more years but wants guidance and advice, particularly in light of the expected tax changes in 2018.

Profile

Dr. Russell's dental practice operates through a Professional Corporation. He and Sandra are both 'growth' shareholders and have been receiving dividends as their sole source of compensation. Their

The proposed new tax changes threaten current compensation structures and future savings within a Professional Corporation.



**All tax and accounting services provided by TMFD Professional Corporation, Chartered Professional Accountants*

two sons are 'income' shareholders but have not received any dividends since they are both employed full-time. Over the years, Dr. Russell has accumulated significant savings in the company, intended to supplement retirement income.

The proposed new tax changes threaten their current compensation structure and future savings within the company.

Opportunity

The new rules indicate that Sandra can receive 'reasonable' dividends only if she has contributed labour, capital, or risk to the business. Sandra works less than 20 hours per week, has not invested significant capital in the business, nor co-signed any previous business loans (which have been long paid-off).

Therefore, it's advised that she not receive any dividends, else pay tax at the top rate. Instead, her compensation should be based on a salary reflecting the duties and contribution of her labour to the practice.

The new rules will also apply a much higher tax on corporate investment income, except income from existing assets, which is grandfathered. Dr. Russell is relieved to learn the existing savings would be exempt from the higher tax rates. The rules also permit up to $50,000 per year of additional investment income (or approximately 5% income from a $1 million portfolio) before much higher tax rates apply. He is equally relieved that he could continue to save for retirement through his Professional Corporation. However, the portfolio would need to be monitored regularly, and managed in a manner to minimize future tax liability. Dr. Russell would prefer not to be burdened with this extra task but has accepted it knowing the proposed new rules could have been harsher.

Solution

Sandra, while no longer receiving dividends, should instead earn a salary of $40,000 per year, deemed reasonable for her duties towards payroll and coordinating the bookkeeping with the accounting office.

Dr. Russell has decided he'd also switch from dividend income to salary, in the amount of $150,000 per year, since this would allow

NET WORTH	Current Value	Annual Deposits	Future Value 5 Years (1)
RRSP	$ 900,000	n/a	$ 1,150,000
IPP	–	$ 50,000	$ 280,000
TFSA	$ 100,000	$ 11,000	$ 190,000
Corporate Savings	$ 500,000	$ 100,000	$ 1,190,000
Dental Practice/Proceeds of Sale	$ 1,250,000	n/a	$ 1,380,000
Liquid Assets	$ 2,750,000		$ 4,190,000
Home	$ 1,250,000		$ 1,380,000
Total Net Worth	**$ 4,000,000**		**$ 5,570,000**

(1) Assume 5% net annual growth for RRSP, IPP, TFSA & Corporate Savings;
Assume 2% net annual growth for Dental Pratice & Home

**All tax and accounting services provided by TMFD Professional Corporation, Chartered Professional Accountants*

him to benefit from Canada Pension Plan (CPP) and RRSP contributions. Further, Dr. Russell favours an Individual Pension Plan (IPP) over RRSP's for himself and Sandra because of the accelerated contribution limits.

With increased salary charged to the business, Dr. Russell should remain aware of Employer Health Tax (EHT). For all staff salaries (including owners), EHT premium will be required for salaries exceeding $450,000 (Ontario 2018). In this situation, total salary just touches the threshold meaning no tax would be payable; however, Dr. Russell will be required to register for EHT once combined salaries exceed this amount.

Although there is long-term risk to higher tax rates as he continues to save within the company, the new rules on corporate investment income do not pose an immediate threat. If Dr. Russell saves $100,000 per year within the company over the next five years, it seems unlikely the higher tax rates will apply since investment income should remain under $50,000.

Results

With these salaries, the Russells will be able to support their lifestyle expenses of $132,000 per year, including maximizing TFSA contributions of $11,000 per year. To maintain the same retirement lifestyle, they'll need to accumulate total savings of $3.3 million. Based on savings and growth over the next five years, this target could be easily exceeded, reaching over $4 million (see table).

RETIREMENT INCOME	Projected Cash Flow (2)
RRIF	$ 46,000
Annuity	$ 11,000
TFSA	$ 8,000
Dividends from Invest Co.	$ 48,000
Withdrawals from Savings	$ 55,000
CPP & OAS	$ 28,000
Cash Flow Before Tax	$ 196,000
Income Tax(3)	-$ 28,000
Cash Flow After Tax	$ 168,000
Target	$ 132,000
Surplus	$ 36,000

(2) Assume sustainable 4% withdrawal rate over 25 years, 5% annual growth and 2% inflation
(3) Tax calculated at current rates using assumptions for eligible/non-eligible dividends, capital gains, and pension income splitting.

Once retired, the proceeds of the IPP could be used to purchase life annuities. The annuities, CPP and Old Age Security, would provide guaranteed lifetime income and generate about 20% of their retirement income – enough to cover home expenses and food.

For tax planning, the current retirement income splitting rules allow RRIF and annuity income to be shared. Under the proposed new tax rules, the Russells could also share dividend income after age 65 from the investment holding company.

There's no doubt the proposed new tax rules mean many dentists will have to change the tactics of their compensation and savings strategies. However, every situation is different and must be evaluated on its own merits. For a complimentary meeting, please contact us at info@tmfd.ca.

CHRIS MOLLOY B.A.Sc., CFP
Chris is Senior VP, Advisory Services at TMFD Financial. Chris has over 20 years of experience at TMFD Financial working in the Ontario area. Chris specializes in tax, estate and investment planning for dentists and dental specialists. For a complimentary initial consultation with our team, we can be reached at info@tmfd.ca or by toll-free at (844) 311-8633.

**All tax and accounting services provided by TMFD Professional Corporation, Chartered Professional Accountants*

STERILIZATION SOS PLAN

Infection control protocols received plenty of attention in both the dental industry and the media in 2017. These are not new standards, however, many practitioners in the industry have been implementing the current protocols improperly. This article is designed to provide you, the dental professional, with a better understanding of the required criteria for best practices to navigate sterilization procedures.

Wrapped or Unwrapped?

The answer is: all instruments are to be wrapped to ensure sterilization. Instruments are not to touch the borders of the sterile pouch, and the pouch is not to be opened until time of use. If the package has lost integrity (integrity loss due to an instrument piercing through the packaging), the contents are no longer considered sterile, and must be reprocessed. If a package is released from the sterilizer and the pouch remains wet, then the instruments are to be removed from that pouch and repackaged for reprocessing. Why? Any pouch that is removed from the sterilizer that is wet is not considered sterile due to the possibility of wicking, which will contaminate the sterile instruments.

When in Doubt

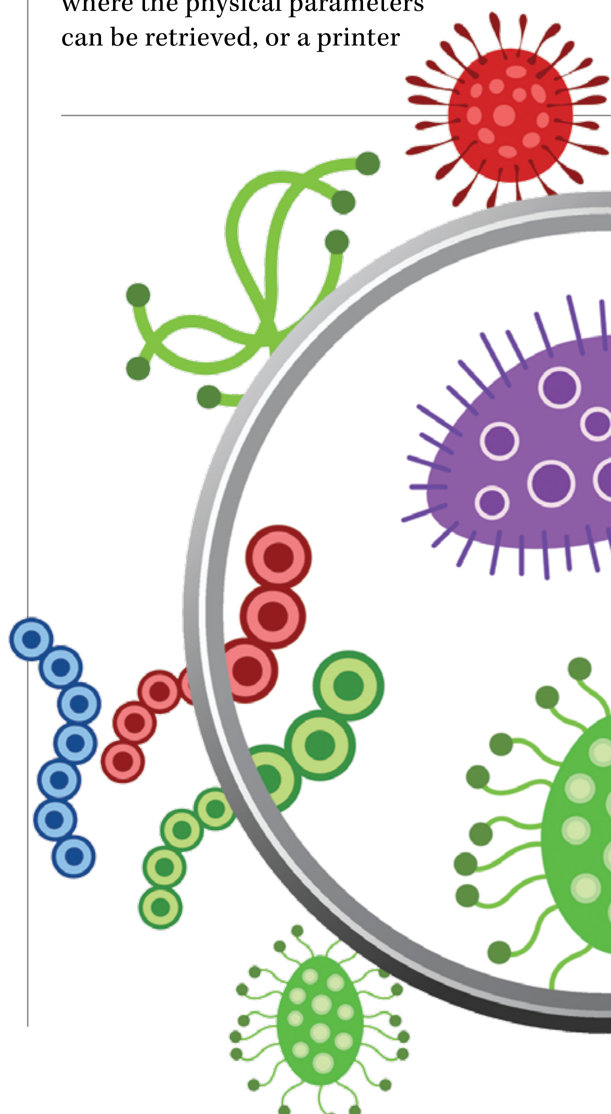
There seems to be a lot of confusion regarding how many instruments are allowed in each sterile pouch. The answer: always default to manufacturer's instructions. This will give you an exact maximum capacity for the pouches that your office uses, and will answer any other questions you might have regarding storage, maintenance, and performance requirements. We encourage you to keep a copy of each product manufacturer's instructions located in your office's *Infection Prevention and Control Manual*.

In addition to the maximum capacity for each sterile pouch, be aware of manufacturer's instructions for reprocessing instruments. The best example of this is the overlapping of instruments. Many owners and team members have this concern, and therefore, purchase cassettes. It can't be stressed enough – always confirm with your manufacturer's instructions that you are reprocessing your instruments to the best practice standards!

Test All Parameters

Of utmost importance is the testing of sterilizers for biological, chemical, and physical parameters. Biological, or "spore" tests, are required to be completed daily for each sterilizer, as well as a control run to ensure that the most harmful microbes are being eliminated through sterilization. The same applies to chemical indicators. For best practice, a Class 5 chemical indicator is to be placed in each sterile pouch, as well as a control in each load to ensure that the instruments are reaching a proper sterility level. The only exception from Class 5 occurs when instruments are being held in quarantine until the results of the biological indicator have been released.

Every sterilizer is required to have, at the very least, a USB port where the physical parameters can be retrieved, or a printer



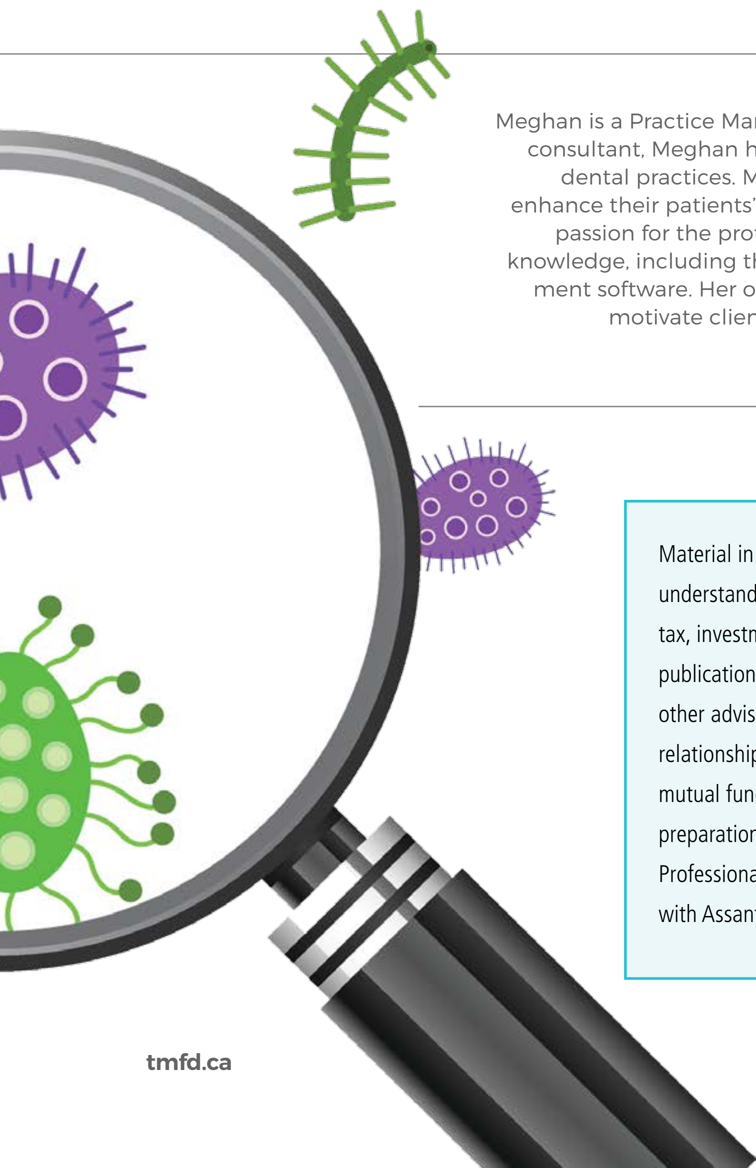
2017 has been a stressful year for the dental industry concerning infection control.

where the physical parameters will be printed and saved at the end of each workday. The minimum packaging requirement is a Class 4 internal indicator, recorded and verified physical parameters from a USB, or printer port connected to the sterilizer. It is vital that all three of these tests are completed and documented correctly, to ensure that your instruments are at an acceptable level to perform procedures on the public.

We acknowledge that 2017 has been a stressful year for the dental industry concerning infection control. Many professionals find the best practice standard has not been as simple as they may have thought. Fortunately, the regulatory bodies have provided us with checklists for dental settings as a resource to ensure we have the required standards in place.

If you need to implement an *Infection Prevention and Control Manual* in your practice or have any other questions, I look forward to hearing from you at meghan@tmfd.ca

MEGHAN SAVOIE RDH
Meghan is a Practice Management Coach with TMFD Financial. As a dental consultant, Meghan has expertise in the clinical and business aspects of dental practices. Meghan is passionate about working with clients to enhance their patients' experience, and overall practice performance. Her passion for the profession is evident and she continues to expand her knowledge, including the use of technology and dental practice management software. Her organization skills, energy, and positive attitude will motivate clients and their team members to achieve their goals.



TMFD Financial

Helping dentists build wealth

- Tax* and Financial Planning
- Incorporation and Practice Transition
- Practice Management
- Payroll and Accounting*
- Insurance Planning
- Retirement Planning
- Wealth Management
- Estate Planning

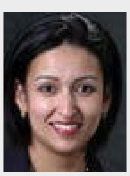
For over 30 years, TMFD Financial has been providing dentists and dental specialists with complete tax* and financial solutions. We work with new graduates, associates, established dentists and dentists transitioning or in retirement. We are proud to be leaders in the industry, but our client's satisfaction is our truest measure of success. To all of our clients,

"THANK YOU FOR PLACING YOUR TRUST IN US."

**All tax and accounting services provided by TMFD Professional Corporation, Chartered Professional Accountants*

Dr. Arthur Johnston, D.D.S. (Successfully Retired)

I have been in the private practice of dentistry for well over 30 years. I have had a very good accountant, a very capable financial planner, insurance agents that advise me well, and lawyers to give advice when necessary. Although each of these advisors did their best for me, they each worked in isolation and none were able to see the big picture. I needed someone to successfully integrate all the pieces of the financial puzzle. Mike Lakhani and his team have done an incredible job of analyzing, integrating, and managing my personal and corporate needs, and have made possible a much better bottom line than I have ever enjoyed before.



Dr. Sara Syed, B.Sc. (Hons), D.M.D. (Ottawa)

Mike Lakhani and his team listen and act on my individual needs rather than using a "one size fits all" method. They take a comprehensive approach to financial planning that includes tax planning, education, investment planning, insurance needs, estate planning and structuring, and debt reduction. Prior to working with the Lakhani team, I had to rely on multiple specialists and it consumed a lot of my time. Now, Mike and his team serve as a kind of CFO for my business and personal finances. Their integrated service frees up my time to do the things I really enjoy, such as practicing dentistry and spending time with my family.

Dr. Neil Gajjar, BSc, D.D.S. (Mississauga)

I find the unique approach that Mike has developed to integrate all of my bookkeeping, corporate filings, and wealth management needs the key to capturing tax savings opportunities that simply would not be apparent otherwise. The background preparation work undertaken by Mike and his team at TMFD directly resulted in real corporate and personal tax savings. I am now moving confidently through a well-planned strategy. I highly recommend Mike as your one source provider to manage all your tax, corporate and personal financial affairs.

Book your complimentary consultation today | www.tmfd.ca | info@tmfd.ca | (844) 311-8633