

something that would make a very, very difficult situation—and in some cases even create a hardship—for small businesses, is certainly hard for many of us on this side of the House to understand.

Having said, that, I would like the minister to indicate to us how many corporations he feels are getting out of this income tax net at the present time without this section being passed. How serious a problem is this of dividends going from small business concerns to other corporations, and does the minister feel there is a leak that should be plugged, such as he is proposing in clause 32?

Mr. Chrétien: Mr. Chairman, we do not have the numbers of the corporations that use this route to avoid paying their normal share of the tax burden. We do see the danger of this situation arising and we merely wish to make sure that it is not abused. Of course, we have done some very positive things for small businesses in the last while, and it would not serve any good purpose to permit some big corporations to abuse or use that route to obtain some benefits which are not necessarily in the best interests of small businesses.

What we want to do, Mr. Chairman, is to have the small entrepreneurs expand, and we have many new measures for this. I would like to congratulate my colleague the Minister of State (Small Business), who has done a very good job since taking over that portfolio, to communicate with small businesses and to perform a series of things that have been accepted by the small business community in Canada. I had the pleasure the other day of meeting the president of the Canadian Federation of Small Business, Mr. Bulloch, and he was telling me that they have made more progress in the last one and a half years than has been made with the government in years. The crocodile tears of the hon. member for York-Simcoe are unwarranted because under the present government, and especially under the leadership of my colleague the Minister of State (Small Business), we have made a lot of progress.

To give a technical explanation, I will read the statement. The small business deduction permits a Canadian controlled private corporation to pay a reduced rate of corporate income tax of up to \$150,000 of active business income earned in Canada in each year, until the corporation has accumulated \$750,000 of active business income. The technical mechanism that keeps track of the business income accumulated by the corporation for the purpose of the \$750,000 test is referred to as the cumulative deduction account, CDA. The CDA is increased by active business income earned and is reduced by dividends paid out of such income.

Bill C-56 will restrict the deductions for dividends paid in computing the CDA in certain circumstances. Let me explain why. Prior to April 10, 1978 the tax system permitted dividends paid by one private corporation to another to be received free of the 25 per cent part IV tax which normally applies to such dividends, provided that the recipient corporation owns more than 10 per cent of the equity of the payor and that the recipient and companies associated with it have not yet accumulated \$750,000 of active business income.

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This technical structure had two serious defects. First, it frustrated corporate joint ventures involving medium and large sized private corporations. This was highly undesirable and the source of numerous representations. Secondly, it provided a mechanism whereby shareholders of many small Canadian companies could recognize their holdings and, in effect, multiply the amount qualifying for the low rate of tax. These reorganizations involving the use of holding companies could be used to multiply the amount of income subject to a low rate of tax so that, in extreme cases, the \$750,000 limit might effectively be increased to a \$7.5 million limit. Then, of course, it is not any longer small business.

● (1532)

This was clearly inappropriate. The government moved to solve both these problems. First, subclause 42(2) will facilitate joint ventures involving medium and large sized private corporations. Then, in order to check the abuse that already existed and the further abuse that would be possible as the result of subclause 42(2), the government proposed clause 32.

Clause 32 would restrict the deduction for dividends paid in computing the CDA. In effect, the payor corporation or, if the payor is a member of a corporate group, the group, can deduct in computing its CDA only those dividends on which the recipient pays income tax. This is appropriate. It prevents the game that was being played by certain taxpayers prior to April 10 whereby they organized their holdings to facilitate payment of exempt intercorporate dividends to reduce the CDA. It prevents the multiplication of the amount qualifying for the low rate of tax through the use of holding companies.

A number of representations were received by my officials to the effect that clause 32 would produce an unduly harsh result where dividend income flows through a private holding company. Subclause 42(1) should resolve any difficulties in this regard. It allows a private corporation in receipt of a taxable dividend to elect to pay the refundable part IV tax, with the result that the dividends will reduce the payor corporation's CDA.

Mr. Stevens: Mr. Chairman, I think it is very clear from the remarks of the minister that he is trying to cope with something when he does not know the size of the problem. This is typical of this government's actions. They set up a provision allowing small businesses to have the advantage of relatively low income tax up to \$125,000 per year or a cumulative amount of \$750,000, and then panic when they find that some small businessmen actually take advantage of this. I asked the minister in how many situations this had become a problem and he said he could not put a number on it. Reading his prepared text, he said several times that he had many representations on it.

My question to the minister is very simple. If he cannot tell us how many situations are actually involved in this type of payment of a small business corporation dividend to another corporation, could he indicate why he has not at least left an opening so that if a dividend is paid from a small business corporation to another corporation which, in turn, pays a