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CHARTERED PROFESSIONAL ACCOUNTANTS

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the newsletter of Prentice Yates & Clark

Tax Benefits for the Self-Employed

There are many tax advantages for self-employed Canadians who work from home and hire family members in their business.

The December holiday season is a time for home and family. This year, if you are self-employed, you may want to consider incorporating home and family into your business to create tax benefits for both the business and the family. Consider the following opportunities to reduce your taxable income and thus increase the amount of money left over to support your family.

Individuals in a 40% tax bracket save $40 on every $100 spent.

Hiring Family Members

If your business needs employees, why not hire your children or your spouse? Of course, the job must correspond to their abilities and the pay be reasonable in terms of the going market rate for such skills. It is usually more beneficial for a sole proprietor to pay family members rather than a third party for the same work. Suppose, for example, you pay one of your children or your spouse $5,000 per year for performing a task and they have no other income. Because the $5,000 is less than their personal exemption ($11,327 for 2015) they will not have to pay any income tax on the earned amount. Further, the payment is deductible from your self-employed income. If, as sole proprietor, you are in a 40% tax bracket, the $5,000 paid to the family member effectively saves $2,000 on your self-employed income while providing $5,000 of tax-free income to the family member.

If, for example, you are paying $5,000 per year for your child's tuition and the child was not paid from your business, you are effectively paying in after-tax dollars. That means you will have to earn $8,350 (40% of $8,350 = $3,340) in order to clear the $5,000 ($8,350 - $3,340 = $5,010) needed to pay for your child's education.

Home Office

You are allowed to deduct at-home expenses if you meet **one** of the following conditions:

1. You do more than 50% of your work at home.
2. The work space is used only to earn income and for meeting customers or clients. You cannot deduct at-home expenses if you are just using your kitchen table to do the work.

Home Maintenance Expenses

You can write off a portion of your home maintenance expenses such as heating, home insurance, electricity and cleaning supplies. A percentage of property taxes and mortgage interest can also be deducted.

Capital Cost Allowance

CRA also allows the deduction of a percentage of the capital cost allowance on the cost of the house or outbuildings. However, since there are tax consequences after the principal residence is sold, discuss this option with your CPA tax advisor before claiming the expense.

Allowable Write-Off

The method of determining the percentage of allowable write-off must be determined on the basis of the space used by each particular business. Some sole proprietorships may only

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Holiday Donations

In lieu of seasonal gifts to individual clients, Prentice Yates & Clark made donations to the following charities:

Homeward Family Shelter
Kehilla Residential Programme
St. Clare's Multifaith
St. Hilda's Towers Foundation
Society of Saint Vincent de Paul

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need a 10 x 10 office to conduct their business; others may need a larger office or perhaps even outbuildings for additional office space or storage. The most common calculation method, however, is to take the square footage of used space as a percentage of the total usable space.

Losses

If, for instance, profit before the application of home expenses was $7,000 and the at-home expenses were $8,000, you cannot claim a $1,000 loss. Your taxable income from the business will be nil but the $1,000 that was not applied can be carried forward to the following taxation year and applied against that year's income. If your business has a loss of $8,000, you cannot increase the loss by the application of at-home expenses. These losses would be carried forward from year to year as well.

To claim business expenses, retain all receipts.

Business Expenses

The expenses listed below are normally common to all businesses. In order to claim any of these, however, make sure they are incurred to earn income and that all receipts are retained:

- accounting and legal fees
- advertising expenses
- business taxes, fees, licences and dues
- insurance expenses
- interest and bank charges
- maintenance and repairs
- meals and entertainment
- office expenses
- salaries, including employer's contributions
- motor vehicle expenses

There may be limitations to deductibility within each category. Seek the advice of a CPA tax advisor before making any claims.

Credit Cards

Interest on credit card balances incurred for business expenses is deductible. But, if business purchases are made with a personal credit card, the CRA will most likely disallow the interest expense because the interest applicable to outstanding business balances cannot be separated from the interest charged on personal balances.

Business Bank Accounts and Business Loans

Business bank accounts allow bank charges to be easily identified as business expenses; deposits and withdrawals can be more readily traced back to suppliers, customers or owner's withdrawals or contributions. Separating business accounts from personal accounts minimizes the confusion when processing year-end tax information or when preparing for a CRA audit.

Loan Interest

Loan interest for vehicles and equipment is also a deductible expense. Make sure the transaction is transparent so you can establish that the principal went into a business bank account. If the loan is from relatives, make sure proper documentation establishes the date of the loan, the interest rate and the repayment terms.

Mortgages

Should you need to increase your mortgage to provide operational funds for the business, separate clearly in your records the mortgage for the principal residence from the funds for your business. The date the additional funds are deposited into the business account establishes the break. Your CPA tax advisor will thus be able to calculate separately the loan interest attributable to the business and that attributable to your personal residence.

Limitations of Do It Yourself Software

Certainly you may choose to complete your tax return by yourself. "Do it yourself" software can tell you how to fill in the blanks and can do the calculations accurately; however, it cannot analyze the data to determine whether it has been entered correctly or whether you have obtained the maximum tax benefit. Hiring a CPA tax advisor will be your best tax deductible expenditure. Not only will your CPA ensure accurate tax results, but also suggest additional measures you should make this year and in future years to minimize your income tax liability. ♦

Virtual Offices

Virtual offices reduce costs significantly for certain types of business.

Offices are familiar places that serve practical functions: the site where employees work, a location to meet with clients, and a centralized storage space for paper files. Historically, many service-based businesses (e.g., insurance, accounting, research, finance or sales) were able to maintain bricks-and-mortar offices because they had the critical mass needed to justify the cost and overhead of commercial space.

Office Alternatives

The definition of workplace has changed considerably and continues to evolve because the nearly ubiquitous availability of portable tools and technology has profoundly changed the way we can work. The Internet is required for most kinds of work. WiFi and cellular network coverage mean Internet access is available nearly everywhere. Similarly, the portability of computers makes working from an airport, coffee shop or even a park possible. Laptops under three pounds with long battery life are readily available. You may even be able to work using just a mobile device such as a tablet, which can weigh less than a pound.

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Virtual Offices - continued

What Is a Virtual Office?

Virtual offices and office sharing are ways for small businesses to avoid the costs associated with traditional office space. Overhead such as rent, liability insurance, maintenance and cleaning services is no longer an unavoidable cost of doing business when the only space needed is the amount required for you and your laptop. In its simplest form, a virtual office provides a business mailing address and mail handling, and telephone answering services.

Virtual office services can be purchased separately or, more typically, bundled in with the cost of the virtual office. Naturally, a greater number of services will result in a higher fee, but you still only pay for what you need. This cost is often lower than the cost of maintaining a full-time staff member, especially when you do not require a high volume of administrative work. Simple virtual office companies that provide only a mail service may charge as little as $30 per month. If a dedicated number and live call answering is required, costs may rise to $70 or more. Office Sharing

Office sharing (or co-working) services can provide a physical office space to suit your needs. These services can offer all the benefits of your own bricks-and-mortar office space without the costs associated with maintaining that space once you no longer need it. Virtual office and office sharing companies may offer services such as:

- business address for mail and delivery
- mail receipt and forwarding
- reception services to receive your calls
- access to a desk, office or collaborative workspace
- use of conference and meeting rooms
- office administration services such as data entry, faxing or photocopying
- equipment and space necessary for presentations
- catering, lunch, and coffee
- secure storage areas
- phone, Internet and WiFi

The larger virtual office companies have expanded to all the major metropolitan areas. Many provide the ability to book an office or service anywhere your business may carry you. If you have to make a presentation or meet with associates in a strange city, the virtual office company may be able to provide audiovisual equipment or find you space in a hotel.

Productivity and use of time improve.

Virtual Office

There are many benefits to having a virtual office. Productivity improves. Time formerly used to travel can now be used to work. Billable hours increase as a percentage of the number of hours worked each week. Other benefits are also important:

- Capital asset expenditures are minimal.
- Overhead and carrying costs are almost non-existent.
- Daily travel costs are significantly reduced.
- The bottom line improves now that more hours generate revenue.

There are potential downsides to a virtual office as well:

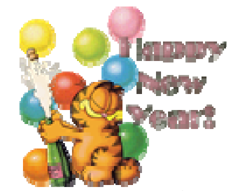
- A 9-5 routine in your home office can suffer from distractions.
- Work-life balance can become a tricky juggling act.
- Clients cannot just “pop by” quite as easily.
- Less interaction with people can lead to “social starvation”.

Even though these negatives may seem to some a deterrent, to others they may be a selling point. Some people may see less social interaction as an alleviation of distraction, and others may find the flexibility of working from home a life-improving benefit.

Lower Costs and Better Service

The new world of entrepreneurs views virtual offices as an opportunity to provide better service to their clients without the need for administrative overhead and the stress that accompanies it.

Although virtual offices may not be a good fit for all service businesses, there is a growing number of companies that no longer require an office to present to their clients as a symbol of their success and prestige. A service business that seldom has clients “dropping in” or has clients and associates around the world may be better suited to a virtual office, not only to reduce costs but also to improve the bottom line. ♦



Happy New Year!

The end of the year is a good time to review long-term investments and mortgages.

New Year’s resolutions. So easy to make, so hard to keep. According to a Nielsen survey, the most common resolution for 2015 was to keep fit. A resolution to spend less money and save more was only the fourth most popular after lose weight, and enjoy life to the fullest. As we are about to enter 2016, perhaps we should all resolve to pay more attention to spending and saving and the effect on our investment portfolios and mortgages in the coming year.

Review Your Investment Portfolio

- Start with investments outside the RRSP or RRIF.
- Calculate the gain or loss between the end of 2014 and the end of 2015.
- Review your statements for the entire year.
- Calculate investment fees paid.
- Identify withdrawals or contributions.
- Net your gains against your losses.
- Calculate the percentage return on investment after deducting the cost of fees paid to your broker, financial advisor or mutual fund manager.
- Using this rate of return and a compound interest table, assume a constant rate of growth and calculate what the investments could be worth by the time you want to cash them in.
- Calculate the potential future value assuming:
    a) a regular annual capital infusion
    b) no capital infusion.

Using different rates of return, calculate how much additional capital must be saved and invested to meet your investment goal

Review Your RRSP

For self-employed persons and those not in pension plans, the RRSP probably represents the principal source of retirement funds. As such, the capital gains and income generation should be monitored closely. Perform the exercise mentioned above on your RRSP portfolio to determine whether the future value of your RRSP investments will be sufficient when you can no longer contribute and have to roll the RRSP into a RRIF in the year you turn 71.

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Happy New Year! - continued

If you discover the calculated rate of return on the RRSP and your current level of contributions will not meet your investment goals, discuss the various options available to you with your investment advisor. Perhaps you will need to restructure the balance between equities and interest-bearing securities, increase the risk or increase your contributions. Keep in mind, however, that higher rates of return usually bring a higher risk of a loss.

Now is also the time to review your RRSP contribution limit to determine any unused amount. Do not forget that unused annual contribution amounts are carried forward. If you find a fairly large balance of accumulated contribution room, you and your advisor may be able to develop a strategy to meet your investment/retirement goals.

Funds can be withdrawn from a RRIF into a trading account or a TFSA.

Review Your RRIF

If you have already rolled your RRSP into your RRIF, review the RRIF portfolio using the procedure outlined above. There is a mandatory withdrawal rate based on a predetermined percentage. (This information is available from CRA or from your investment advisor.) Review the current value and rate of return. Remember that the withdrawal rate simply determines the portion of the RRIF that must be deregistered each year and brought into taxable income. It does not mean you have to sell that portion of your portfolio every year. In a self-directed plan, for instance, the taxable amount can be transferred in kind into a trading account and thus remain part of your total investment portfolio for future use.

Instead of having a trading account to receive the securities withdrawn from your RRIF, you could move them into a Tax-Free Savings Account (TFSA) if you have the room. Future capital gains and income within the TFSA are not taxable.

Review Your Mortgage

Reviewing your mortgage should be part of any New Year's resolution. Look at the current balance and determine when the mortgage will be completely paid off at the current payment rate. Ideally, your mortgage should be fully paid before retirement so you do not retire still having to withdraw funds from your RRSP or RRIF to meet mortgage payments. Review the mortgage agreement and identify any lump sums that can be paid to reduce the remaining balance owing. Use an amortization table to calculate the number of years by which the life of the mortgage can be shortened by doing any or all of the following:

a) finding a better interest rate
b) changing the payment frequency from monthly to weekly, or
c) making a lump sum payment.

Work with Your CPA

Whether projecting income within your investment or retirement portfolios or calculating a strategy to reduce your mortgage, amortization tables will help you with those calculations. Work with your CPA to provide unbiased feedback on the choices available to you in your particular circumstances. The decisions you make now will impact not only your lifestyle but personal income taxes in the future.

Inside PYC

Congratulations to **Wendy Duncan, Manager, Finance & Administration, Stoney Creek Community Homes Inc.** Ms. Duncan won the draw for the Niagara Presents gift basket courtesy of Prentice Yates & Clark at the recent ONPHA Conference and Trade Show.

Congratulations to Viola Bardhoshi, Manager, in reaching the 10 year milestone of service at PYC. Viola received her Chartered Accountant designation in 2008 while articling at PYC.

Congratulations to Sanjay Kiran who recently completed all the requirements for his designations as a Chartered Professional Accountant, Certified Management Accountant.

Congratulations to Aria Afshar and Garry Gatti for successfully completing the CPA Common Final Examination (CFE). Aria and Garry continue to accumulate work experience toward their designation as a Chartered Professional Accountant.

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