2016 Year-End Tax Planning Tips for Self-Employed Persons and Corporate Business Owners

While the end of 2016 is approaching, there is still an opportunity for both self-employed persons and corporate business owners to review their financial situation with their TD Wealth advisor and explore year-end tax planning. Here are some of the year-end tax planning ideas a self-employed person or corporate business owner might want to explore.

Recent Changes and Updates:

Eligible Capital Property (ECP): As a result of changes announced in the 2016 Federal Budget, effective January 1, 2017, the eligible capital property (ECP) regime will be repealed and replaced with a new capital cost allowance (CCA) class (Class 14.1) with a 100% inclusion and a 5% annual depreciation rate.

Determine Compensation Mix: Salary and bonus are both considered earned income which is used to calculate your registered retirement savings plan (RRSP) contribution limit for the subsequent year. For 2016, you will need earned income of $144,500 to make the maximum RRSP contribution of $26,010 for 2017.

1. Self-employed Individuals

☐ **Pay salaries to family members**
Paying family members a salary or wages before December 31st for services they've provided to your business is a great income splitting opportunity. In order to support payments to family members, you should review the services family members provided in 2016 and determine the amount you can justify as reasonable compensation. While the family member would be taxed on their compensation payments, they may be in a lower marginal tax bracket than you and therefore pay little or no tax on this income. At the same time, your business should also be entitled to a deduction for tax purposes for the same amount.

☐ **Purchase capital assets**
If you're considering buying assets for use in your business in the near future, you may want to consider buying the assets and having them available for use in the business before December 31st in order for you to claim capital cost allowance (CCA) in 2016. On the other hand, if you delay buying assets until 2017, your claim for CCA is delayed to 2017.

☐ **Defer selling depreciable business assets**
If you are planning to sell depreciable business assets, you may want to consider delaying your sale until 2017. By delaying your sale of assets to next year, you can reduce your income by deducting CCA in 2016. In addition, if you previously claimed CCA on these assets and the sale may give rise to recaptured CCA (*i.e.*, treated as ordinary income in the year of sale), you can defer the tax on this ordinary income (recaptured CCA) to 2017.

☐ Accelerate deductible expenses

If you are looking to reduce taxable income in 2016, you might want to consider making certain business expenditures before December 31st in order to claim a business deduction for these expenses in 2016.

☐ Defer income

If you are able to put off receiving income until 2017, you may be able to defer the tax on that income for a full year. This may be accomplished if you postpone the completion of work or the issuance of final invoices.

2. Corporate Business Owners

☐ Pay reasonable salaries to family members

Income splitting can be achieved if you own a corporation and pay reasonable salary amounts to family members who have lower marginal tax rates than yours and who provide services to your corporation. Paying reasonable salary amounts before the end of 2016 should provide the corporation with a tax deduction for its taxation year and provide the family member with earned income that would create RRSP contribution room for him/her in 2017.

☐ Accrue salaries or bonuses

Your corporation may be able to accrue salaries and bonuses (make them payable) in order to deduct such amounts in computing the corporation’s income, but at the same time defer the actual payment of these amounts to the intended recipient (*i.e.*, you) for up to 179 days after the corporation’s fiscal year-end. By doing so, the corporation may be able to take a current deduction for these accrued amounts and you can defer the tax on the same amounts to next year if you receive them after December 31st. You might consider this strategy if your corporation’s tax rate is higher this year or your personal tax rate may be lower next year.

☐ Purchase assets for CCA

As described above for a self-employed individual, if your corporation has a calendar year-end and is also considering buying assets for use in its business in the near future, it may be a consideration for the corporation to buy those assets before December 31st in order to claim a deduction for CCA in computing its income for 2016.

☐ Defer selling depreciable business assets

Similar to the situation for self-employed individuals described above, if your corporation has a calendar year-end and is considering selling some of its depreciable business assets, delaying the sale until 2017 allows the corporation to claim a deduction for CCA this year and defer any recaptured CCA to a future year.

☐ Purchase an automobile from your corporation

If your corporation provides you with a car for your own use, the corporation is obligated to report a taxable employment benefit to you each year that this car is made available for your use. This taxable benefit would include: i) a standby charge; and ii) an operating cost benefit. You would pay tax on these taxable benefits when you file your 2016 personal income tax return. If the car owned by your corporation has declined in value, you may want to consider buying the car from the corporation before December 31st to minimize your taxable benefits in 2016 and possibly receive a tax-free car allowance from your corporation next year.

☐ Claim your lifetime capital gains exemption (LCGE)

The $824,176 (for 2016 and indexed for inflation) LCGE is available to shelter capital gains on the sale of qualifying small business corporation shares and qualified farm or fishing property (QFFP). For QFFP there is an additional lifetime exemption amount to effectively increase the LCGE for QFFP to $1 million. The LCGE for QFFP will stay at $1 million until the indexed amount of the base LCGE exceeds $1 million. At that time, the same LCGE limit, indexed to inflation, will apply to the all three types of property. You may want to trigger capital gains on this type of property before December 31st in order to claim your capital gains exemption. There may be strategies for you to consider when claiming your exemption without giving up control over this property. If you have cumulative net investment losses (CNIL) on December 31, 2016, you may not be able to claim your full capital gains exemption until your CNIL balance is zero. A CNIL arises when your investment expenses are greater than your investment income. Therefore, increasing your investment income (*i.e.*, earning interest or dividend income) helps lower your CNIL. You should consult with your professional tax advisor to determine the utility and consequences of claiming your capital gains exemption.

- ☐ **Claim an ABIL against other income**

An allowable business investment loss (ABIL) can arise where you invested in the shares of, or lent money to, a small business corporation (SBC) which later becomes insolvent or bankrupt. An ABIL is equal to 50% of the actual investment lost (*i.e.*, the investment in shares or a loan to a SBC) and as the business owner, you can use an ABIL to offset any type of income, such as employment, interest and dividend income as well as capital gains for a period of time. At the expiry of this time, any unused ABIL is treated as an ordinary capital loss and therefore can only be used to offset capital gains. In addition, your ABIL claim may be restricted if you have utilized any of your LCGE.

- ☐ **Ensure your corporation pays its final tax owing**

To minimize interest and penalty charges that may be imposed by the Canada Revenue Agency (CRA) on any final tax amounts owing (or deficient tax installments), you should ensure your corporation pays the balance of any income tax owed within two months (three months in the case of certain Canadian-controlled private corporations) of the corporation’s year-end.

- ☐ **Have your corporation donate before year-end**

Corporations are entitled to a deduction in computing their taxable income for charitable donations made during the year. If your corporation is considering a charitable donation this year, you should ensure the corporation makes the donation before its fiscal year-end.

- ☐ **Shareholder loans to your corporation**

If you have withdrawn or used money from your corporation during 2016 and while the corporation is indebted to you, consider treating the money you have withdrawn or used as if it were a repayment to you of your loan. Since loan repayments can be received by you tax-free, this may be better than treating the money as if it were taken by you as salary, bonus or dividends in 2016.

- ☐ **Shareholder loans from your company**

If you borrowed money from your corporation, be sure to repay the debt within one year after the end of the taxation year in which the loan was made, so that the outstanding amount is not taxed in your hands as income. Exceptions to this rule may apply depending on how you used the borrowed money and the type of your corporation. Therefore, speak with your professional tax advisor to determine how these rules may apply in your personal circumstances.

- ☐ **Employer gifts and awards to employees**

You may give an employee an unlimited number of non-cash gifts and awards with a combined total value of $500 or less annually. If the $500 limit is exceeded for non-cash gifts and awards, only the amount of gifts and awards in excess of the $500 is taxable to the employee.

Employers may want to consider making tax-free employee gifts and awards before December 31st.

- ☐ **Compare provincial/territorial tax rates**

A corporation’s year-end offers you the opportunity as owner to review both the tax and non-tax advantages (and disadvantages) of carrying on business in various provinces and territories in Canada. It is possible that you may uncover cost or tax savings by having your corporation carry on its business in another territory/jurisdiction in future years.

Since the tax and non-tax issues can be complex, you should speak with your corporation’s professional legal, accounting and tax advisors concerning these issues.

3. Businesses with Foreign Connections

☐ Plan your personal and your corporation's presence

As the end of 2016 approaches, you may want to review your personal and your corporation's obligations to file tax returns and pay taxes in a foreign jurisdiction. Since foreign jurisdiction business and tax issues can be complex, particularly where electronic or "e"-commerce is concerned, you should speak with your professional legal and tax advisors concerning these issues.

☐ File treaty-based returns

If either you or your corporation is conducting business in foreign jurisdictions, you or your corporation may be required to file treaty-based tax or information returns. Since foreign jurisdiction business and tax issues can be complex, you should speak with your professional legal and tax advisors concerning these issues, and possibly re-organize your business matters to minimize foreign reporting and tax obligations in future years.

☐ U.S. state and municipal tax

If you or your corporation is conducting business in the U.S., you should consider the tax filing and other reporting obligations with any states or municipalities in the U.S. You and your corporation may have state and municipal tax and other filing obligations even though there may not be any federal tax or filing obligation. Since U.S. state and municipal business and tax issues can be complex, you should speak with your professional legal, accounting and tax advisors concerning these issues, and possibly re-organizing your business matters to minimize U.S. state and municipal reporting and tax obligations in future years.

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