TAX NEWSLETTER

Spring 2017

An Independent Member Firm of
DFK Canada Inc. and DFK International

In This Issue...

Change in Tax Treatment of "Work in Progress" for Professionals

By Patricia Day, CPA, CA, CBV, TEP
GGFL Chartered Professional Accountants

Big-ticket items invariably attract the headlines at budget time, but at GGFL we comb through the small print to find measures that impact our clients.

The Federal Budget released on March 22, 2017 proposes changes to the tax treatment of "Work In Progress for Professionals." These changes could have a significant impact on tax bills for professionals. Tax legislation specifically includes Accountants, Chiropractors, Dentists, Lawyers, Medical Doctors, and Veterinarians as professionals.

Work in Progress (WIP) is the work that has been performed but not yet billed to clients. The value of WIP will vary according to the size of the practice. Those in partnerships need to be especially alert to this.

Prior to this latest budget, professionals could elect to not include any work in progress in taxable income until the work was billed. However, expenses related to that unbilled income could be deducted in the year they occurred. The Budget proposes to change this approach and will disallow the deduction of costs until the work is billed.

According to the Budget, WIP is to be included in taxable income (by excluding it from deductible expenses) at the lesser of cost and fair market value. Most professionals value WIP based on their billing rates. To value WIP at cost, include only amounts that have been expensed. This would include salary costs and fees paid for professional services, as well as disbursements such as courier charges. The costs would generally exclude any cost for the time of the owners of the business, unless they are paid professional fees that are expensed.

These changes will take effect for all fiscal years that begin after March 22, 2017. If your practice operates on a calendar year, that would be the year beginning January 1, 2018.

The Budget proposes implementation of this change over a two-year time frame. For the first year, 50% of the WIP must be included in income at year's end. In the second and subsequent years, 100% of the WIP must be included in income.

What you should consider:

- Are you carrying WIP on your books that will never be billed or will never be billed in total?
- Reviewing your WIP at year-end and making a supportable and reasonable adjustment to fair market value, where there is uncertainty, on a job-by-job basis.
- For professionals with contingency fees, CRA has announced that until the right to collect an amount is established, the amount is not receivable. In these cases, in valuing the WIP, no amount should be included for these jobs.

The Doctor’s Financial Lifecycle: Transitioning to Medical Practice—from Salaried to Self-Emplyed

By Hugh Faloon, CPA, CA, TEP & Donna Ho, CPA, CA
GGFL Chartered Professional Accountants

Becoming a doctor is no easy feat. You don’t need a bunch of accountants to tell you that. But, we can tell you a few things about the business side of your practice and help get you on the road to financial security.

We can help you navigate the tax issues that distinguish the salaried resident from the self-employed physician.

You should know about paying income tax installments, allowable business deductions, and filing returns. And, should you incorporate? Incorporation is an important professional decision for which you need specialized professional advice.

Taxes and the practicing physician

As a salaried medical resident, your employer is responsible for taking off the necessary taxes and payments for EI and CPP. You’re more likely to earn a refund after claiming all your tuition credits than you are to owe. Simply put, the salary you collect from your employer is the net amount, as opposed to the gross. None of that requires a great deal of expert know-how.

Working as a practising physician is an entirely different matter. In most cases, you will be self-employed.

As a self-employed physician, you will bill and receive income from OHIP. You will be responsible for paying your own taxes, quite likely as a member of the highest tax bracket. At this point, you may have exhausted all of your tuition credits against your resident salary; however, you will be able to deduct certain business expenses. In short, you need to manage your income to allow for tax payments, but you will have expenses that can be used to reduce your taxable income. You should have separate bank accounts for your personal spending, and for your business revenue and expenses to simplify accounting for your business.

Allowable tax deductions for self-employed physicians

As a rule, most expenses incurred are deductible if they are incurred to earn business income, are reasonable in the circumstances, and are allowed under the Income Tax Act (ITA).

The following are some common business expenses for physicians:

- Accounting and legal fees;
- Advertising and promotion;
- Meals and entertainment (50%);
- Annual license fees and professional dues;
- Interest on office loans and lease payments on equipment
- Professional development;
- Medical supplies;
- Salaries and employee benefits;
- Travel expenses;
- Automobile;
- Practice overhead insurance;
- Extended health insurance; and
- Malpractice insurance.

KEEP YOUR RECEIPTS for all of the above and any other expense you think might be business related.

Your accountant can help you understand eligible deductions based on your specific situation and help you maximize your deductions and minimize taxes.

Filing tax returns and paying the Canada Revenue Agency (CRA)

As a self-employed physician, your tax return **must be filed by June 15;** however, any **tax owing is due April 30.** As a resident, your tax return is due on April 30. No one is withholding your income tax at source, so the CRA requires quarterly installments due on the 15th of March, June, September, and December. The easiest way to pay your taxes is online, through your bank.

Set aside money for taxes owing and for future tax installments to avoid interest and penalties on insufficient or missed payments. It’s a good idea to open a separate bank account to save for taxes.

If you still have a large line of credit, and the limit does not decrease with payments, with proper planning, you could park your savings for taxes in the line of credit to reduce interest charges until the tax payments are due. Clear this with your bank.

We recommend meeting with an accountant before you transition into self-employment.

Get a Head Start on Your 2017 Personal Taxes

By Beth Porter, CPA, CA, CFP
Noseworthy Chapman Chartered Professional Accountants

Given that the personal tax deadline has just passed, it may seem odd to see an article regarding personal tax planning; however, there is no better time than now to plan for next year. As the old saying goes... the early bird gets the worm.

In the fast-paced world we live in today, we are all busy; however, it is important that you take time during the year to consider items that may be claimed as deductions or credits on your tax return to ensure you have the proper receipts and documentation in place for when tax time comes again. Failing to be proactive can cause you to pay more tax than you should. Also, accountants charge fees based on their time, so you will pay your accountant more if they have to contact you to request additional information that you have omitted, to obtain receipts or tax slips on your behalf, or if you have to make changes to your tax return after it has been completed because of additional information you have found.

Tax planning has to be done consistently throughout the year, not just in December before the end of the year and certainly not in March and April after the year has passed. Some of the most simple, yet best recommendations we can make are noted here for you.

Families and Seniors

Child care and camps: Keep receipts during the year for all amounts paid for eligible childcare which may include camps your children attend during the spring and summer breaks. However, fees for ancillary items such as clothing or equipment are not eligible.

Medical expenses: You can obtain an annual summary of all payments for prescription drugs from your pharmacy and dentist for all family members. However you may be missing amounts paid to other practitioners that are eligible medical expenses. The CRA has a complete listing available on their website that will tell you if amounts you pay to other practitioners such as a chiropractor, dietician, or psychologist can also be claimed based on your province of residence. The listing can be found at: http://www.cra-arc.gc.ca/tx/ndvdls/tpcs/ncm-tx/rtrn/cmpltng/ddctns/lns300-350/330-331/ampp-eng.html or by searching for "Authorized medical practitioners for the purposes of the medical expense tax credit" on CRA's website.

Disability Tax Credit: If you or a family member suffers from a severe and prolonged medical condition, an application can be made for the disability tax credit using Form T2201 which must be completed in part by your physician. This form can be submitted to the CRA at any time during the year and must be approved in advance in order to claim the credit on your tax return. In addition to the credit amount, approval by CRA may permit additional medical expenses to be claimed such as attendant care for the patient.

Home Accessibility Tax Credit: Seniors or those approved for the disability tax credit with mobility issues may be able to claim this new credit which was introduced in 2016 for costs of up to $10,000 related to making their home more accessible. Therefore, ensure all receipts for renovations or modifications to the home are retained if they are eligible for this credit. Some expenses that qualify for this credit may be eligible to be claimed a second time as a medical expense.

Sale of your home: New rules were announced in 2016 that require the sale of your principal residence to be disclosed on your tax return, even though the sale may not be taxable. Ensure your tax accountant is advised of any sales to ensure the disclosure is made and your tax exemption on your principal residence is allowed.

Purchase of a new home: If you purchase a new home during the year and have not been a homeowner in the previous four years, you may be eligible for a first time home buyers credit of $5,000. Ensure you keep documents to provide to your accountant which will verify your new home purchase.

Tuition and education: If you or a child attends a qualifying post-secondary institution in Canada, Form T2202A is required when determining the amount of eligible credits. For universities outside of Canada, Form TL11A must be completed by the foreign university. It may take time for the foreign university to provide the information so keep this in mind to ensure you have received it in time for your tax return to be completed. Also ensure that the currency of payment is noted on the form.

CPP pension sharing: Eligible retirees may make an election on their tax return to split up to 50% of eligible pension income with their spouse, however many do not realize that this does not extend to CPP benefits received during the year. In order to split CPP benefits, a joint application must be made with Service Canada for pension sharing so that the payments are actually split between the couple during the year. This may provide an additional income splitting opportunity which may lower the overall tax for the couple.

Investors

Gains and losses: If you have investments outside of a registered retirement or education savings plan or a tax-free

(continued on page 4)

Get a Head Start on Your 2017 Personal Taxes

(continued from page 3)

savings account, you need to report any gains and losses on these investments on your tax return. Depending on whether you are using a self-directed investment account or using an investment advisor, the information available in the form of an annual year end reporting package may differ. As such, the information required to prepare your return, such as the amount you originally paid for your investments, may not be easily determined. Even if you suffer losses on some investments, the silver lining is that these amounts may be used to offset tax on other gains. Keep all documentation related to your investment transactions to ensure your accountant has all the information they require in order to properly report these transactions on your tax return in the year they occur.

RRSP Contributions: Amounts you contribute to your RRSP must be supported by official receipts in order to claim a deduction on your return. These receipts are delivered during the months of January to March so it is important that you ensure you receive all of them and provide them to your accountant in order to make certain that the full deduction you are entitled to is claimed. Contributions made in the first 60 days of the year can be deducted on last year's return and should be reported on that tax return (ie a contribution made in January 2017 can be claimed on the 2016 tax return that you just filed).

Turning 71 during the year: If you are turning age 71 before the end of the calendar year, ensure you speak with your financial institution which holds your RRSP accounts as these must be rolled into an annuity or RRIF prior to December 31st otherwise the value of the plan will be deemed to be taxable income in your hands on that date.

<u>CRA Communication</u>

Notice of Assessment: After your tax return has been filed and you receive your Notice of Assessment, do not file it away with your tax return. If the assessment differs from what was filed, you need to speak with your accountant as a processing error could have been made and your time to object to the assessment is limited. If everything is fine, keep this assessment and place it with your information for next year so that your accountant can review it as it may contain other important information. Also, now would be a great time to provide your current year RRSP room to your financial advisor so they are aware of how much you can contribute to your plan this year. Waiting until February of the following calendar year to make your RRSP contributions to ensure you have a deduction to claim on your return isn't prudent from an investment standpoint; you should make your contributions as early in the year as possible to maximize your investment earnings.

CRA "My Account": By signing up for the CRA's "My Account" service, you will have access to a lot of information including assessments for your last ten years of tax filings, your RRSP and TFSA contribution room, as well as all payments including any instalments you make during the year. You should review this regularly and ensure all payments are reflected properly. If payments are not reflected in the appropriate instalment year, you may have to contact CRA in advance of filing your taxes to ensure this is corrected. Also, if you need copies of your Notice of Assessment at any time during the year for your bank or other lenders, you can easily obtain them through this service.

While this information may seem fairly simple, being organized and proactive is the best way to ensure you pay the least amount of tax possible. It also ensures that your accountant has all the required information and you are not paying them to organize and collect your financial data. Our team of advisors want to be able to provide you with advice and strategies that lower your overall tax burden and having your complete financial picture is the first step in that process.