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YEAR-END PLANNING

Start looking now for year-end savings and…

Trim your tax bill

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Attention taxpayers! Time is running out on year-end tax planning opportunities – but there are still a few weeks left to implement these tax-saving strategies.

So, while you're making up your holiday gift list, also take some time to think about year-end planning and trimming your 2012 tax bill.

Here are some tips for those of you who own businesses, and for employees.

For business people

File a Tax Return

Many new businesses experience start-up losses in the first few years of their existence.

Still, you should file a return for each year. That's because your business's loss can be used to reduce income from other sources in the current year, or it can be carried back three years and forward twenty years. And that income can be from any source – be it the business itself, from employment or even from investment income.

But to claim the loss, you must file a tax return for the year.

The year-end for an individual who is a sole proprietor or an active partner in a partnership created since 1995 is December 31. Self-employed taxpayers and their spouses (if not separated) have until June 15 to file a return, although any taxes owing must be paid by April 30.

Lower Your Tax Instalments

If you pay taxes on an instalment basis, you've probably received several notices from CanRev informing you how much those instalments should be. But if your income has gone down in the last few years, think twice before you send in your cheque.

CanRev's instalment calculations are based partly on your income tax position from two years ago, and partly on last year's.

Instead of using CanRev's method, you are legally entitled to base your instalments on last year's tax position, or even on the current year's estimated position, if it is lower.

But be careful with the latter: penalties may apply if you underestimate your taxes and your instalments turn out to be lower than what the other two options required.

If your income has gone down in the last couple of years, using one of the other two options can mean that you could reduce your quarterly instalments without suffering interest penalties. But if you under-install, CanRev will start to charge you interest; the current rate is five per cent.

However, this rate is compounded daily – and worse still, it's non-deductible. So this is an expensive way to enhance your cash position. For seriously delinquent instalments, there is a 50 per cent interest surcharge slapped on.

If, during the year, it becomes apparent that you have paid more instalments than necessary, you might consider deliberately not following the instalment schedule by paying defi-

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cient or late instalments. This, in fact, is quite "legal."

By the way, if you've over-installed or have paid early, CanRev gives you what's known as an "offset" or "contra-interest" credit.

Basically, the rule works as if you had deposited the instalment in a bank account and earned interest (at CanRev's prescribed rates – currently three per cent for individuals and one per cent for businesses).

This credit can then be applied against interest penalties on deficient or late instalments.

The flip side of this, of course, is that you can reduce interest charges on a late or deficient tax instalment by overpaying other instalments, or paying them before their due date.

Deductions

Deductions for most normal business expenses are based on whether the expense has been incurred by year end, rather than whether the item has actually been paid for, e.g., office supplies, auto and other repairs, etc.

Exceptions include compound interest charges (regular 'simple' business interest that can be expensed when payable), site investigation and utility service connection charges, and disability-related equipment and building modifications.

Consider accelerating purchases of equipment, capital and other expenditures before year end. Examples include equipment and auto purchases (and repairs for the latter), to name just a few. Half of the normal depreciation can be claimed this year; next year, you claim the full depreciation rate.

Note: even though the depreciation rules restrict the write-off on capital purchases, you can claim a full GST credit for the year of purchase. So if you buy before the end of the year, the credit will allow you to reduce the GST you owe.

If you "accrue" a salary to family members (this must be reasonable in relation to the business service they perform) you can claim a deduction as long as you actually pay the expense within 179 days of your business' year. This may allow the recipient to defer tax on the amount until next year.

For employees

Reducing your source deductions:

For employees, one unlikely source of cash could be the source deductions withheld on your paycheque. Many people regularly get tax refunds because of deductions like support payments or carrying charges on investments (see box below).

If you're one of them, call the payroll division of your local tax office. Tell them you want to apply for a reduction of source deductions under section 153(1.1) of the Income Tax Act (if you cite the section number, they'll know you mean business). They'll send you a form and ask you for some info to back up your application. If you do, they'll probably cut your withholding so you can pocket the money. Most tax offices are quite cooperative when it comes to this procedure.

According to CanRev, there is no specific minimum amount below which they will not consider an application. Technically, you are supposed to show that, without a reduction, you're a hardship case. However, Revenue Canada seems to be pretty easy on this requirement.

One item that may get you a source-deduction slash is an early 2013 RRSP contribution. Contributing early in the year also means your earnings will compound on a tax-sheltered basis sooner rather than later.

Warning: if you are basing your application on a shelter, questionable deduction or other aggressive tax planning, an application for reduced source deductions could bring unwanted scrutiny. Better to leave well enough alone.

Other Tips:

✓ If possible, you should defer the receipt of employment income if your tax bracket will be lower in 2013.

✓ Employees are entitled to claim tax depreciation called

Other Expenses May Qualify

In addition to carrying charges and support payments, you can reduce the amount of income withheld at source based on a number of other expenses that qualify as deductions or credits. These include child-care expenses, alimony, employment expenses, interest expenses on investment loans, charitable donations, medical expenses and rental losses.

Capital Cost Allowance (CCA) on automobiles, aircraft and musical instruments, depending on the circumstances. If you're entitled to deduct CCA and you're considering purchasing a new asset, you should do so prior to the end of the year.

This will accelerate capital cost allowance claims by one year. The asset must actually be available for your use to qualify for a CCA claim.

✓ Reduce "operating cost" tax. If personal use of a company-owned car is less than 50 per cent, consider notifying your employer by December 31 if you want the taxable operating-cost benefit based on one half of the standby charge (less any reimbursements you paid).

Other ways of reducing your operating benefit include reimbursing your employer for operating costs, reimbursing your employer for 100 per cent of the personal-use portion of actual operating costs, and minimizing your personal driving.

✓ Reduce "standby charge" tax on autos. Standby charges are calculated using the vehicle's original cost. After a few years when the vehicle is worth less, consider buying it from your employer to avoid the high standby charge.

Alternatively, have your employer sell the automobile and repurchase it or lease it back – or choose a less expensive car. ❒