

# Business Matters

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## TAXATION

### Available for Use

**Operating an automobile for business and personal use has tax consequences.**

Purchasing or leasing an automobile in the company name and allowing employees to drive the automobile has tax consequences that may require owner-managers to add a taxable benefit to the employee's T4.

#### **CRA Definition of Automobile**

For there to be a taxable benefit, the employer must first determine whether the vehicle is an automobile under the *Income Tax Act*. The Canada Revenue Agency (CRA) defines an automobile as “a motor vehicle that is designed or adapted mainly to



carry individuals on highways and streets and has a seating capacity of not more than the driver and 8 passengers.”

This definition of an automobile [paraphrased from 248(1) from the *Income Tax Act*] does not include “a van, pick-up truck, or similar vehicle” that:

1. can seat no more than the driver and two passengers, and in the year it is acquired or leased is used primarily to transport goods or equipment in the course of business, or
2. in the year it is acquired or leased, is used 90% or more of the distance driven to transport goods, equipment, or passengers in the course of business; or
3. pick-up trucks that you bought or leased in the tax year that:
  - a) you used primarily to transport goods, equipment, or passengers in the course of earning or producing income
  - b) you used at a remote work location or at a special work site that is at least 30 kilometres away from any community having a population of at least 40,000.

### **Restrictions on Deductibility**

Vehicles that fall within this definition of an “automobile” are subject to a maximum capital cost allowance addition (available for future capital cost allowance) of \$30,000 plus HST. This limitation imposes a significant constraint on many business owners’ primary motivation for purchasing the vehicle in the corporate name. Vehicles such as king cab trucks that do not fall within the definition of “automobile” are not subject to such a restriction since they are considered necessary for the business and are not considered “luxury vehicles”. There are also restrictions imposed on leased automobiles. Generally, monthly lease costs for automobiles are restricted to \$800 plus HST.

### **Taxable Benefits**

In addition to the restrictions on the deductibility of annual depreciation (or leasing costs), users of such vehicles are also deemed to have received a taxable benefit from the corporation for the use of the vehicles for non-business purposes.

For example, assume an owner-manager purchases a high-end SUV in the company name but the owner-manager’s spouse uses it primarily (i.e., more than 50% of the use) for non-business purposes. Assume also that the base price of this vehicle is \$90,000 and the overall cost of owning the vehicle, once HST is added, is \$101,700. The standby charge to the employee is calculated at 2% per month of the total cost of the vehicle. Thus, the standby charge for the employee is calculated at \$101,700 at 2% (\$2,034) per month or \$24,408 per year. The standby charges would be reduced in cases where the vehicle is used primarily for business purposes and annual personal driving does not exceed 20,000 kilometres.

On top of the standby charge, an additional operating benefit of 26 cents per personal kilometre driven is taxable in the hands of the employee. In the case where the vehicle is primarily used for business purposes, the operating benefits could be reduced to 50% of the standby charges if the benefit results in an amount lower than otherwise calculated.

(Standby charges for a lease can be expensive as well. A monthly lease cost of \$1,350 over 84 months creates a standby charge for 12 months of \$10,800 plus an operating expense benefit as mentioned above.)

### **Owner-Manager’s Use of Vehicles**

Owner-managers may believe they are not subject to the available-for-use rules because they are shareholders of the corporation and not employees. The CRA has made it clear that owner-managers are subject to the same taxable benefit as employees as indicated by the CRA’s reference to archived IT63R5 *Benefits, Including Standby Charge for an Automobile, from the Personal Use of a Motor Vehicle Supplied by an Employer — After 1992*.

Paragraph 18 reads as follows:

#### Shareholder Benefit

18. The above guidelines may generally be applied to a shareholder of a corporation. Subsection 15(5) provides that, for the purpose of subsection 15(1), the value of the benefit to

be included in a shareholder's income when an automobile is made available to such a person (or to a person related to that person) by a corporation, whether or not resident or carrying on business in Canada, is calculated on the assumption that subsections 6(1), (1.1) and (2) apply with such modifications as are required in the circumstances, and as though the references therein to "employer" were read as references to "corporation."

### **Working from Personal Residence**

Many owner-managers may work from their principal residence and thus have access to the vehicle 24 hours a day. The question is: "Does the close proximity of the vehicle mean that it is available for personal use and therefore a taxable benefit must be added to the owner-manager's income at the end of the year?"

*CRA: There is no taxable benefit if the automobile is operated for business use only.*

#### **The Answer According to the CRA**

"An automobile is available to your employee if he or she has access to or control over the vehicle. It includes any part of the day, weekends and holidays during the calendar year." (This suggests that, since the vehicle is parked at the place of residence and is available 24 hours a day — 365 days a year, there is a taxable benefit.)

"If your employee does not use the company's automobile for any personal driving, there is no taxable benefit, even if the automobile is available to your employee for the entire year. This applies as long as the kilometres driven by your employee are in the course of his or her employment duties and the vehicle is returned to your (business) premises at the end of his or her work day." (This suggests that, if the owner-manager can establish that they do not use the vehicle for personal use at all and park it at the "corporation's" premises [also the owner-manager's principal residence] then there may not be a taxable benefit.)

### **Keep Detailed Records**

Convincing taxation authorities that the vehicle is not used for personal use will require due diligence and good record keeping since the CRA will take into consideration many factors when determining whether available-for-use benefits should be added to income.

The first line of defence is a complete log book. Record the odometer reading as at January 1 of and December 31 of each calendar year to establish the total annual distance the vehicle has been driven. Log each business trip taken plus a description of the purpose. Hypothetically, the number of kilometres driven for business trips and the total kilometres driven should be the same.

Although it is highly unlikely an owner-manager would purchase or lease an expensive "toy" and use it primarily for work purposes, the CRA may start to review the purchase of vehicles to ensure they are indeed "work vehicles." Additional calculations and circumstances will alter the available-for-use add-on, whether for a purchased or leased vehicle. But, as our hypothetical taxable benefit examples demonstrate, the additional taxable benefit will push the employee (i.e., owner-manager) into a higher tax bracket and thus bring closer scrutiny by the CRA.

### **Consult Your CPA**

Calculation of available-for-use benefits is complicated and may be somewhat offset by taxable deductions within the corporation. If your business is considering purchasing or leasing a vehicle that will be operated in the gray area between business and personal use, consult your CPA to ensure you understand the potential personal tax consequences.

## TECHNOLOGY

# It's a Bird, It's a Plane...No...It's 3D XPoint Technology

**The way you store your data is about to change.**

For the last 60 years, increasingly vast amounts of data have been stored primarily on magnetic hard disk drives (HDDs). Hard drives are capable of storing a huge amount of information, but they are mechanical devices and can be more delicate and a lot slower than more recent NAND (stands for negative-and logic gate) flash memory, which has no moving parts. NAND flash memory, sometimes called a solid state drive (SSD), has become ubiquitous as a storage medium since it is a compact, fast and fairly inexpensive alternative to the noisy hard drives currently used in computers, mobile phones, USB flash drives and memory cards, among other things.

While hard drives and NAND flash memory are great for data storage, mobile devices and computers also have a smaller amount of super-fast short-term memory called DRAM (dynamic random access memory). DRAM is quite a bit more expensive and, unlike your hard drive or SSD, the contents in memory are “volatile”, meaning whatever is stored disappears when you turn off your device.

But what if long-term storage could be as snappy as DRAM?

*The new technology does not use transistors.*

### “You Ain’t Seen Nothin’ Yet”

Sometime in 2017/2018, a new memory and storage technology called 3D XPoint (pronounced 3D cross point), developed by Intel and Micron, will hit the market. The new technology is different from both NAND flash memory and DRAM in that it does not use transistors; instead, it uses a three-dimensional checkerboard structure that allows each memory cell to be addressed individually. The ability to read and write



data in smaller increments is a huge advantage over flash memory, which is only able to store information in blocks of data.

### How Fast Is Fast?

What makes this new technology so incredible and likeable is that it allows the user to take stupendous amounts of stored data and treat it as if it were in active memory rather than in traditional storage such as a hard drive or SSD flash drive. 3D XPoint memory is expected to read data three times faster, write four times faster and use 30% less power than NAND flash memory. That means it is not only faster than your current SSD or flash storage, but will help manufacturers to stretch the battery life a bit further once it is available in laptops and mobile phones.

### How Much, You Ask?

We all know that those who purchase the newest technology pay the higher price and pave the way for those who wait for the technology to become mainstream. At the moment, a fixed price point has not been set in stone, but it has been suggested that 3D XPoint memory will cost about four or five times the current price of NAND flash drives.

## Do I Really Need 3D XPoint?

For most owner-managers, today's computers with their hard drive or SSD will be sufficient for everyday use. However, if your business applications require

rapid data storage and transmission, whether for extensive analysis, high-performance databases, or simply for fast storage of immense amounts of data, this new technology is a game changer that will undoubtedly be worth the cost.

## MONEYSAVER

### Penny-Pinching Pays

**Playing Scrooge is not just for Christmas any more.**

Even though penny-pinching is harder to do today without any pennies, the concept remains valid and is especially applicable to the expenses incurred by small businesses. Here are a few ideas to improve the bottom line.

#### Outsource

Employees require salaries and benefits as well as insurance, office space and equipment. Contracting out office tasks transfers these costs to a highly competitive third party and frees up your own premises for revenue-producing uses.

#### Negotiate with Suppliers

Contact your suppliers and see whether you can get a better deal. Far too often suppliers mechanically increase prices without recognizing the value of a long-term, reliable client. Why should rewards and discounts go to new clients while long-standing customers like yourself see costs go up? Call and make your pitch.

#### Use the Cloud

Using the Internet to send invoices and make and receive payments saves the cost of cheques, envelopes, letterhead and postage as well as the related labour. Further, cloud-based solutions for almost every manufacturing or accounting need are available for a reasonable "lease" rate. Such an approach reduces the cost of buying and installing software and assures you your cloud services will always have the latest updates.



#### Consider In-House Printers

Many businesses still need to print data to hard copy. Consider purchasing a laser or inkjet colour printer. Once templates for invoices, letterhead, or business cards have been installed, they can be printed as needed, thus eliminating large inventories of pre-printed forms. The templates can be adjusted for format changes or for staff and address changes.

*Face-to-face meetings are not always necessary.*

#### Meet with Telecommuting

For most business communication, a face-to-face meeting is not necessary. Virtual meetings will work if the number of participants is small, the meeting is kept short, and the agenda well planned. Establishing timelines, requesting daily updates and having access to work-in-process by the use of shared cloud facilities will ensure projects stay on time and on budget.

## Maintenance

How often are the premises cleaned? Perhaps reducing the frequency of cleaning or having staff empty their own waste baskets at the end of the day are options that will reduce costs without impacting the tidiness of the office.

## Go Paperless

Going paperless can be difficult for older employees used to paper trails. Paperless offices must establish a filing system suitable to everyone; this includes scanning every piece of paper that comes into the system and allocating it to the appropriate folder. Going paperless also means reviewing existing client files and purging data no longer required for taxation, legal or business purposes. This is the time to adopt standard records management practices for preserving, storing (onsite and offsite) and destroying documents. Scanning documents saves the cost of renting physical storage space, using employee time to file paper, and ultimately shredding and disposing of that paper.

## MANAGEMENT

# Life Is a Gamble

**An insurance plan today can support your business and family tomorrow.**

No one, with the possible exception of a professional gambler, expects to build a reserve of funds by gambling. Nevertheless, purchasing or not purchasing life insurance is a gamble in itself. If you buy life insurance, you only win if you die early because the insurance pays off your debts; if you don't purchase life insurance, you only win if you live a very long life and pay off your debts without having paid life insurance premiums. What you must decide is whether you want to gamble that you will live to pay off all your obligations, or take a more conservative position and accept that you might die younger and be willing to pay the insurance premiums to ensure that your debts will be paid off at your early death.

## Review the Cost of Your Premises

Signing a long-term lease may lock your business into a lease cost that will not be acceptable in the future. Look ahead and determine how your business will evolve over the next five years. If your strategic plan includes increasing or decreasing your space, consider signing shorter-term leases that allow an exit with, for example, three months' notice.

If you own your building but no longer need all the space, consider subletting. You might also think of selling or leasing the entire property and moving to a smaller space. Such a move would provide proceeds from the sale of the building or lease income while reducing your own rental costs.

## Think about Your Future

Taking an hour or so with your CPA to look at your current business model and associated costs will help you think about changes that will positively impact the bottom line and ensure that your business keeps on going.



## Factors to Consider

To understand why you would need to provide these funds, ask yourself: Will my spouse be able to pay for:

1. my funeral?
2. our home (including any outstanding mortgage) and way of life for the children?

3. outstanding credit card debt?
4. funds borrowed from the RRSP to put a down payment on the house?
5. the monthly mortgage/rental, utility and maintenance?
6. day care?
7. my personal income tax liability as an owner-manager if I have not repaid draws or have not deducted sufficient taxes at the source?
8. short-term loans from the company?
9. personal guarantees to financial institutions if there is no other source of income?
10. our children's future education or future medical costs should they currently have special needs or develop them in the unforeseeable future?
11. RRSPs, investments or TFSAs for the future needs of our family?
12. the capital gains tax (if) the second residence (e.g., a cottage) has to be sold?
13. an equalization of my estate? For example, the family cottage has been left to three survivors, but only one has a real interest in preserving it. What will happen to the cottage if that person does not have the financial means to pay out the two other survivors? Does that mean the property would have to be sold to meet the terms of the will? Should life insurance be purchased to provide a cash payout to the other two beneficiaries to prevent the sale of the property and therefore keep it in the family?

*Entrepreneurs should not defer purchasing life insurance.*

## What about Now?

Term life insurance provides coverage at a fixed premium for a limited period of time (i.e., the term). After the term expires, coverage at the previous rate is no longer guaranteed. Term insurance is usually the lowest-cost way to purchase a substantial death benefit.

Putting off purchasing life insurance is not an option entrepreneurs should consider because (in the event of your passing):

- your business associates will need cash flow to fill your vacancy
- life insurance becomes more expensive as you get older: your province of residence, your life style, the amount of the payout and your gender will impact the insurance premium; for a non-smoking 25-year-old man, for example, the yearly premium for \$600,000 of renewable five-year term life insurance may cost you \$600\* per year; however, as you age, the amount goes up: at age 46 (around \$900) and age 55 (around \$1,500); the problem with term life insurance is that, after the term expires, the policy has no value.  
*\*Please note that all amounts and calculations are generic estimates. Each individual's circumstances will impact the premium.*
- even if you paid an annual premium of \$1,500 (hypothetically) from age 25 to 55, the total cost of your premiums would be only \$45,000, but the payout would be \$600,000, which is an excellent return on your investment
- conversely, if you invest \$1,500 per year at 5% compounded annually for 30 years, you would have only about \$100,000 at age 55
- if you incur serious physical problems or develop a medical condition, you may not be able to purchase life insurance.

## Key-Person Insurance

Key-person insurance is paid for by the company, with the company as beneficiary. This type of insurance is designed to cover the consequences of losing an indispensable person such as the founder or owner who can no longer contribute to the business through death or disability. Funds will be available to keep the operation going while restructuring is taking place after your death.

Key-person insurance can provide funds to buy your share from your survivors without the business assuming additional debt. A key person payout can be used to back your personal guarantees on business loans as well as pay deferred taxes and other regulatory deductions.

## How Much Should You Buy?

How much insurance you need depends upon what you need to insure: self-employed earnings, current assets, debt, savings, cost of living, business and family structure, as well as the future needs of family and the business. To determine this amount, first put together a summary of the collective assets and debts of your business and your family unit along with details of the cost of your current life style and future expectations. Contact an insurance agent, discuss your situation and design a policy that will meet your needs.

## Something to Think about

Don't gamble with your future. Accidents and illness happen. Hope for the best but plan for the worst. Think about your business and family situation and what would happen if you were not there. Do not leave your survivors in jeopardy when you can take care of their futures today.

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