



## Income From a Business—Did You Know ... ?

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### Business Income

Individuals, professional corporations (i.e., corporations that carry on the professional practice of a doctor, dentist, lawyer, engineer, or accountant), and partnerships that carry on a business cannot defer the taxation of their business income by adopting a year-end other than the calendar year-end.

Taxpayers have until June 15 of each year to file their tax returns, although income tax must be paid by April 30. All unpaid tax as of April 30 will be subject to interest charges. However, no penalties will be imposed on taxpayers before the date at which such tax returns should have been filed.

#### *Adopting a December 31 year-end*

A taxpayer with a non-calendar fiscal year-end may change it to December 31. The income of the current year will include the net business income earned in the period ending in the calendar year on a date other than December 31 as well as the net business income earned from that time to December 31.

#### *Electing the alternative method*

A taxpayer with a non-calendar fiscal year-end may elect to keep it. Eligible taxpayers must adjust their business income according to the calendar year by calculating an additional income to be included in their income for the year. The additional income is an estimate of the business income calculated every year based on the income of the fiscal period that ended in that calendar year. The income is calculated as follows:

Business income based on an off-calendar fiscal period;

Plus additional income inclusion for the current taxation year calculated using the following formula:

$$A \times B \div C$$

Where

**A** = Business income earned during the off-calendar fiscal period ending in the calendar year;

**B** = The number of days during which the business was carried on after the end of the fiscal period and before the following January 1;

**C** = The number of days in the business's fiscal period ending in the calendar year;

minus additional income inclusion for the previous year.

For a taxpayer that carries on a business as a member of a partnership, the net business income is that determined after deducting the total of carrying charges and automobile operating expenses that are not deductible by the partnership but rather by the taxpayer.

If the business income includes an amount deemed to be a taxable capital gain, item A of the additional income calculation must be adjusted in order to exclude this amount.

A taxpayer may opt out of the alternative method and elect a December 31 year-end.

The opposite however, is not possible. A taxpayer who revokes the alternative method election and adopts a December 31 year-end can subtract from business income the additional income included in the preceding year's tax return.

A taxpayer who elects to maintain an off-calendar year-end or a taxpayer who revokes such an election must complete and sign Form T1139.

### Example: Alternative Method

In this example, an individual elects to use a non-calendar fiscal period of April 1 to March 31 to carry on his business. The 2009 additional business income inclusion for the stub period of April 1, 2009 to December 31, 2009, was \$150,000. The 2010 business income earned by the individual for the period of April 1, 2009 to March 31, 2010, was \$250,000. The business income to be included in the individual's 2010 calendar year would be calculated as follows:

Business income for 2010 fiscal year:

\$250,000

+ Additional business income for period of April 1, 2010, to December 31, 2010 ( $\$250,000 \times 275 \text{ days} \div 365 \text{ days}$ ):

\$188,356

- Additional business income for period of April 1, 2009, to December 31, 2009:

\$150,000

Business income to be included in 2010 calendar year:  
\$288,356

## Rental income

In the calculation of rental income, it should be noted that a rental loss cannot be created or increased by claiming capital cost allowance. If a taxpayer owns several rental properties, all rental income and losses from these properties must be combined to determine the net income from all such property for the purpose of calculating the capital cost allowance.

## Farm income and losses

All farmers are entitled to use the cash method of accounting. Moreover, a farmer may include in his income an amount for the livestock and inventory on hand at the end of the year. This amount must not exceed the fair market value of those assets and must be deducted in the computation of the following year's income.

When the result obtained using the cash method is a loss, a "mandatory inventory adjustment" must be calculated. This adjustment reduces the loss by an amount which

is the lesser of the cost and the fair market value of the inventory on hand at the end of the year. The adjustment calculated for a year may be deducted in the following year. Farm losses may be carried back three years and forward 20 years against income from any source.

### Restricted Farm Loss

When farming is not the major source of income of the taxpayer, the deductible farm loss in the year cannot exceed the lesser of:

- the net farm loss for the year;
- \$2,500 + 1/2 (net farm loss minus \$2,500); and
- \$8,750.

The portion of the loss that cannot be deducted in the year constitutes a restricted farm loss. It can be carried back three years and forward 20 years against farm income.

