



*Business & tax tips for successful financial planning*

## Hidden problems when small business expands

### Plan ahead for the eventual economic slowdown:

- Cash-flow management is critical. Did you consider rising interest costs in the future?
- Draft a long-term business plan today. How will your business expand?
- Hire good employees.
- Look for the warning signs.

By Terence Chan

Over the last few years, Canada has been enjoying low inflation and interest rates. Led by a red hot economy in Alberta, many business sectors across the country are booming, and unemployment remains low. Behind the scenes, however, some experts are wary of the inevitable slowdown. As a shrewd business owner, you should plan ahead and examine your business to see if it is able to survive an economic downturn. Oversights today maybe be concealed by healthy profit margins, but they will have greater consequences when the economy weakens.

The most common oversight is cash-flow management. This can be a fatal mistake. During good years, generating sales and collecting receivables are often easy. The focus of the owner manager is on how to expand. Customers delaying payment? They will pay eventually. Limited cash to pay operating expenses? We can delay payments to our suppliers as well. No funds for expansion?

Banks are competing to give us low-interest loans.

Problems arise when the economy starts to slow down. Suppliers feel the cash crunch and are more reluctant to allow customers to delay payments. Customers take more time to pay because of their own cash-flow issues. At the same time, the company's bank loans still need to be repaid. Interest costs rise on existing loans and the cash required for previously-committed expansion creates added pressure. Businesses often fail, not because they are doing poorly, but because of cash constraints.

Cash-flow projections should be done on a regular basis.

Another common mistake is the absence of a long-term business plan. The emphasis for most small businesses is to increase sales in the near future. There is very often no plan about the longer-term direction of the company. Without a view of the bigger

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## Do you need to file a U.S. income tax return?

By Kevyn Nightingale

It could be said that Canada and the United States are the closest neighbours in the entire world. There is more cross border trade between our two countries than between any other pair. There are more border crossings than between any other pair. Most of us speak the same language, and share similar culture. The differences within

regions of each country are often greater than the differences between the countries themselves.

As a resident of Canada, you may have to file a U.S. tax return, and not even know it. You probably need to file a US return if you:

- were a U.S. citizen;

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## Missing out? The CRA SR&ED program

By Michael Fromstein

The CRA's Scientific Research and Experimental Development (SR&ED) program is essentially free money. They pay your company for activities you need to do in order to stay competitive or meet your customers' needs.

Is your company:

- Developing a new product or improving an existing one?
- Developing a new manufacturing process or modifying an existing one?
- Producing large early production runs that

are either scrapped, recycled or sold at a discount?

Does your company:

- Have a technical staff, either educated or with industry experience?
- Conduct R&D but not submit claims?
- Conduct R&D but had past claims rejected?
- Conduct R&D but think the claim would be too small to be worthwhile?

If you answered YES to any of the above questions then speak to your SF representative today about this program.



SR&ED tax credits are available to innovations big and small

## Business expenditure: Is it deductible?

By Doug Robinson

There are two overriding tests that all expenditures must meet in order to be deductible for business purposes:

- Was the expenditure made for the purpose of earning taxable income?
- Was the expenditure reasonable in the circumstances?

If the expenditure was not made to earn taxable income, no deduction is permitted.

The second test is both a question of purpose and amount. If it is not reasonable that the expenditure be made at all then no deduction will be permitted. If such an expenditure is reasonable but the amount is excessive it is possible that a reduced amount may be allowed.

If an expenditure meets these two tests, it does not necessarily mean it is deductible. There are other rules to consider. However, if these two tests are not met then the other rules will not matter.



To deduct, business expenditures should at least be reasonable

## Child care expenses

If you enroll your child in daycare, summer camp, boarding school, or a sports school, you may be able to claim your expenses for these activities on your income tax return. To qualify, you must have incurred the expenses in order to work or attend school. When there are two parents, the parent with the lower net income usually has to make the claim.

If your child is under the age of seven and you qualify, you may be able to claim up to \$7,000 a year. For each child over the age of seven but under the age of 16, you may be able to claim up to \$4,000. There is no age limit for a disabled child and you may be able to claim up to \$10,000.

## Corporate income planning

Corporate taxpayers subject to the small business rate may wish to defer income until after 2006 in order to benefit from changes to the tax system in 2007.

The federal small business threshold increases from \$300,000 to \$400,000 in 2007. The federal rate drops from 13.12% to 11.5% in 2008, and to 11% by 2009.

Corporations taxed at the general rate may wish to defer income to benefit from future federal rate reductions from 22.12% to 18.5%. There are also changes in several provinces.

## Children's fitness tax credit for 2007

By Doug Robinson

The children's fitness tax credit will allow parents to claim a maximum of \$500 per year for eligible fees paid for each child who is under 16 at any time during the year. The Department of Finance has indicated that, in order to qualify for the tax credit, a program must be:

- ongoing, lasting either a minimum of eight weeks duration with a minimum of one session per week or, in the case of children's camps, five consecutive days;
- supervised;
- suitable for children; and
- substantially all of the activities must include a significant amount of physical activity that contributes to cardio-respiratory endurance plus one or more

of: muscular strength, muscular endurance, flexibility, or balance.

The year in which the tax credit can be claimed is determined by the date when the fees are paid, not when the activity takes place.

Starting in 2007, you should receive a receipt from organizations providing eligible programs of physical activity. The organizations will determine what part of the fee qualifies for the tax credit.

You will need to keep the receipts issued by the organizations that deliver the programs. You will not need to submit receipts when you file your tax return, but you must keep them in case the CRA asks for them when verifying your claim. Receipts should be kept for six years.



Save the receipts from your children's organized sports programs

## Goods not so good

By Doug Robinson

If your company sells, buys or transfers goods to a related party outside Canada you should know that you may not be able to use the same transfer price for both customs and income tax purposes. The CRA has "clarified" that the Canada Border Services Agency (CBSA) uses a valuation method for customs purposes that differs from that used by the CRA for income tax purposes. It

is unlikely that the two valuation methods will yield the same result. It should also be noted that the foreign jurisdiction may not use either of the methods used by the Canadian government agencies. It is important that the basis of valuation for both income tax purposes and customs purposes as well as for foreign reporting purposes be documented in the company files.

## Do you need to file a U.S. tax return?

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- had a "green card";
- spent a lot of time in the U.S. over the past three years;
- earned rent from U.S. property;
- received U.S. gambling winnings;
- worked in the U.S.;
- owned an interest in a partnership that operated in the States, or
- died owning U.S. property (okay, it would be your executor, but you get the idea)

There can be substantial penalties if you fail to file a U.S. tax return, even if you owe no tax.



### Who needs to file?

Visit our website for more details:

[www.ustax.ca](http://www.ustax.ca)

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## Pension income splitting

By Kevyn Nightingale

When the Harper government proposed a controversial tax on income trusts last Halloween, it also introduced a Tax Fairness Plan aimed to bring tax relief to Canadian seniors. The proposal would allow individuals aged 65 years or over to split certain types of pension income with their spouses. Individuals under the age of 65 limited to splitting only their registered pension plan (RPP) income.

Splitting income will allow many pensioners to pay lower rates of tax. This will be the case for couples where one spouse is in a lower tax bracket than the other.

Pensioners over 65 will be able to split income that is eligible for the pension income credit. This includes income from RPP, RRSP annuity, locked-in RRIF (LIF), or deferred profit sharing plan (DPSP) annuity.

Some types of pension income do not qualify, such as Old Age Security, Canada/Quebec Pension Plan, Retirement Compensations Arrangements and lump-sum RRSP withdrawals.



*Pensioners may be able to split income with their spouse under a new proposal.*

## Hidden problems of an expanding owner-managed business

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picture over a longer time frame, a change in the economy quickly reveals the company's deficiencies.

When the times are good, a company is operating at full capacity and staff are working overtime to meet the demand, many problems can be overlooked. However, when sales drop and costs increase, the lack of direction is more visible and problematic.

Yet another area that business owners often overlook is good staffing. A hot economy often presents staffing difficulties, but the importance of training staff and keeping good employees cannot be over emphasized. Again, in a hot economy, customers may be willing to compromise (a bit). But when demand drops and competition inten-

sifies, a good corporate team may often make the difference between survival and failure.

Planning for the future is critical, because corrections are easier to make today than when the business is struggling. Every business has degrees of exposure. It may be cash-flow problems, too-rapid growth, oversized debt, or a drain of customers. Whatever the signs may be, it never hurts to revisit your business plan periodically. Consider the future - call your SF advisor today.



*Business is booming now, but will your company be ready when the economy slows down?*