TAXTALK

CHANGES TO IMMEDIATE EXPENSING RULES

The immediate expensing rules were originally announced on April 19, 2021 to allow 100% write off in the year of purchase of up to $1.5 million of capital asset purchases per year. These rules finally received Royal Assent on June 23, 2022 which allowed Canada Revenue Agency ("CRA") to start assessing immediate expensing claims.

For Canadian controlled private corporations ("CCPCs"), property acquired and available for use from April 19, 2021 to December 31, 2023 qualify. These rules were also expanded to include unincorporated businesses operated by individuals and partnerships for property acquired and available for use from January 1, 2022 until December 31, 2024.

Associated businesses, including corporations, sole proprietorships and partnerships, will have to share the $1.5 million annual limit.

An Eligible Person or Partnership ("EPOP") includes:

- A CCPC:
- A Canadian resident individual: and
- A partnership of which all members are either Canadian resident individuals or CCPCs.

What property qualifies for immediate expensing?

Designated Immediate Expensing Property ("DIEP") generally includes all depreciable capital property, other than property included in Capital Cost Allowance ("CCA") classes 1 to 6, 14.1, 17, 47, 49 and 51. These classes generally are property with a long life such as buildings and unlimited term intangible property including goodwill.

The enhanced CCA deductions for manufacturing and processing equipment and the Accelerated Investment Incentive Property ("AIIP") that allows for a 1.5 increase in the normal CCA rate in the first year, will continue to be available subject to a phase-out period which will begin for the AIIP after 2023 and which will not impact the $1.5 million limit.

To be eligible as a DIEP, the property must meet one of the following conditions:

1. The property has not been used for any purpose before it was acquired by the eligible person and it is not a property for which CCA was claimed by any person or partnership before the property was acquired; or
2. The property was not transferred on a rollover basis or was not acquired from a non-arm's length party.

What are the limitations on deduction?

The maximum deduction is equal to the lesser of:

1. The immediate expensing limit for the taxation year is $1.5 million which must be allocated among the associated group and pro-rated for short taxation years;
2. The UCC of the DIEP before claiming any CCA deductions for the year; and
3. For sole proprietorships and partnerships, the income before claiming any CCA deductions for the year. Thus, a sole proprietorship or partnership cannot create a loss using immediate expensing.

Associated corporations, sole proprietorships and partnerships

The immediate expensing annual limit of $1.5 million must be shared amongst the all associated persons including CCPCs, sole proprietorships and partnerships. To determine this allocation, sole proprietorships and partnerships are deemed to be corporations when determining whether they are associated with other businesses.

Trade-ins and disposals

If a capital asset is bought and sold in the same taxation year the capital asset will not qualify as a DIEP. If a capital asset is purchased in a prior taxation year and is sold or traded-in in the current year the full gross purchase price is eligible for immediate expensing. A capital asset becomes a DIEP only in the year that it is purchased, thus the disposal of that capital asset in a subsequent taxation year is not considered a disposal of DIEP.

Class 10.1

The CCA recapture and terminal loss rules do not apply to passenger vehicles included in class 10.1 that have a cost in excess of $36,000 for taxation years after 2022. However, if the Class 10.1 vehicle has been designated as an immediate expensing property, then special rules apply so that the recapture rules will apply on a disposal of the vehicle.

Taxpayers will now be required to track when immediate expensing was claimed for each Class 10.1 vehicle in a previous year in order to determine if recapture will apply when the vehicle is sold. Such recapture will cause an unexpected income inclusion, since each Class 10.1 asset is included in a separate CCA pool and the cost of a new vehicle would not reduce the recapture in the old pool.

Other issues to consider when deciding to claim immediate expensing

Claiming CCA and immediate expensing are optional deductions. However, where the business is operated personally or in a partnership, immediate expensing cannot be claimed to create or increase a loss. It can only be used to reduce taxable income of the business to Nil.

In many cases an individual taxpayer would want to make use of the lowest tax brackets as well as all of their personal tax credits, so it may be better not to claim all of the available immediate expense deduction since a large deduction in the current year would mean a smaller deduction in a future year.

An immediate expensing deduction may save tax at a low tax rate in the current year, however, a lower deduction or recaptured CCA may result in higher income in future years taxed at a higher rate.

There is no ability to carryforward any of the unused $1.5 million limit that is not used in a particular year. Thus, the timing of capital asset purchases can be important to maximizing the use of this deduction.

A taxpayer can choose which CCA classes the immediate expensing is applied to. Therefore, choosing to immediately expense the eligible property acquisitions in CCA classes with the lowest rates first will maximize the overall CCA deduction for the year and quicken CCA deductions in later years.

As the $1.5 million limit needs to be shared by members of an associated group, the amount of taxable income and tax rates applicable to each member of the group, as well as the CCA classes of eligible property acquisitions, must be considered when determining an allocation.

The designation as immediate expensing property must be made within 12 months of the eligible entity's filing due date for the year to which the designation relates.

WE CAN HELP

Your MG advisor can help you review your personal or business tax situation and help you decide which steps you should take next.

Offices:

First Canadian Place
100 King Street West, Suite 5700
Toronto, Ontario M5X 1C7
Phone: 416-362-0515

1900 Minnesota Court, Suite 116
Mississauga, Ontario L5N 3C9
Phone: 905-451-4788
Fax: 905-451-3299

TaxTalk is prepared by our Tax Group (taxtalk@mgca.com). Please visit our web site at www.mgca.com.

McCarney Group LLP is an independent member of Morison KSi