

COMMON QUESTIONS: TAXATION OF ASSETS

Q: (This question was raised at a recent meeting of home-based businesses): What difference does it make if I write off a computer in one year or over three years? It is going to get written off anyway, right?

Taxation laws most often give the advantage to government tax departments. In Canada, that agency is the Canada Revenue Agency (CRA). The answer proposed to the business owner was three-fold:

A: You may not be in business three years from now, so if you took the full write-off the first year, you would have the tax write-off, and CRA might have received no tax revenues from you before you went out of business.

A: The life of a computer is more than one year. Thus, it is reasonable that the computer be "expensed" over its lifetime. This helps government gain a steady stream of taxation revenues.

A: An important principle of accounting is "Matching Expenses With Revenue". You will likely use the computer over a number of years to gain income in each of those years. The expense incurred to use the computer would thus be applied over that same relative timeframe.

Q: What is the difference between "Depreciation", "Amortization" and "Capital Cost Allowance"?

A: There is actually no difference between "Depreciation", "Amortization" and "Capital Cost Allowance". They denote the same thing. Tax guidelines do not allow big-ticket items to be completely expensed in the same year they are purchased. Big-ticket items are written off (expensed) slowly over a number of years and at a specific rate each year. Expensing these big-ticket items over a number of years is called "depreciation" "amortization" or "capital cost allowance".

Q: What items are the "big-ticket" items that I need to depreciate slowly over a number of years?

A: Each country sets guidelines regarding what large purchases need to be depreciated instead of being expensed in the year of purchase. This includes computer software, whether or not it is an intrinsic part of the computer. The basic threshold in Canada has remained at \$200. for many years, regardless of the type of item purchased. Anything costing more than \$200. (including Provincial Sales Tax but not including GST) must be depreciated over time.

The second criteria after cost is that the item must also be useful for more than one year. Say you are in the construction industry and purchase several \$500-dollar electric drills each year because they either get trashed or stolen or lost. These items should be expensed 100% in the year of purchase and should not be depreciated over time. Tax preparation software is a purchase that could reasonably be expensed in the year it is purchased because you need to buy the new version of the tax software every year. Take heed, however, that Canada Revenue Agency (CRA) expects you to depreciate your software 50% in the year of purchase and 50% in the next fiscal year. The result is expensing the software over 12 months, albeit in separate fiscal years.

Q: Where can I find the "classes" for assets and the rate they depreciate at?

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A: The 17 most common asset "classes" and rates for depreciating them are listed in the Canada Revenue Agency (CRA) booklet "Business And Professional Income". Go to the CRA website <http://www.cra-arc.gc.ca> and search for "T4002".

To find the complete list to go the Justice Canada website <http://laws.justice.gc.ca/en/> and search for "part xi capital cost allowance" (use the quotation marks). You will have the option to search either the CONSOLIDATED REGULATIONS or CONSOLIDATED STATUTES. Be sure to select CONSOLIDATED REGULATIONS. You can also paste this link in your browser: <http://laws.justice.gc.ca/en/i-3.3/c.r.c.-c.945/135982.html> to bring up the exact section the Consolidated Regulations of Canada.

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