Tax Talk
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Finance cost must-knows

Most expenses involve something tangible. Fuel, tires, a place to stay for the night – you get a real product or service in exchange for your hard-earned buck.

Then there are "soft" costs like interest, fees, and other charges on loans and lines of credit. They're folded into payments or tucked away at the bottom of statements where they might go unnoticed for a while. But there's nothing soft about them.

Financing costs are a major expense for owner/operators and small fleets. If you borrow money to run your business, here are four things you should remember about managing these expenses effectively:

It's easy to miss tax-deductible expenses

Any time you pay to borrow money, and that money is used to help you earn business income or provide working capital, that expense is tax-deductible. This includes interest you pay on the loan, the cost for the loan to be set up and managed, and any fees for legal, accounting, and bookkeeping services related to applying and completing loan documentation.

Loan-related expenses aren't like most business expenses. Interest and other fees may be amortized over the life of the loan and wrapped into monthly payments. Up-front administrative or documentation fees may be buried in the fine print. The paperwork can be onerous and complicated. It's easy to miss potential deductions.

Separate business and personal credit

Keep dedicated accounts so the expensing of service charges, overdraft charges, interest, and other fees is clear to you, to your accountant, and to any auditor who might review your return. (In a perfect world you would have separate credit cards and credit lines for business and personal use).

Your accountant can help you clarify precisely which borrowing expenses are business and which are personal. For instance, you might think your tax accounts (including personal tax, corporate tax, payroll source deductions, and GST account) are business-related. But CRA says you cannot deduct the interest charged to these accounts or any loans you may get from financial institutions to pay these amounts.

Also, any loans to buy RRSPs or fees charged within your RRSPs are not deductible.

When money is borrowed partly for business and partly for some other purpose, only the part of the expense that may reasonably be considered applicable to the business is deductible. Canada Revenue Agency (CRA) expects you to apportion a business-related percentage of related interest and charges.

If you mix business and personal debt, you'll have to calculate the proper business percentage each year. An auditor will want you to show that these percentages are valid. That may mean going back over years of statements to prove the business portion.

Catch mistakes in documents

Mathematical errors, incorrect interest rates, misspelled names, confusing guarantee terms, missing pages, illegible type – I'm amazed at the mistakes I see in loan documents.

No matter how eager you are to seal the deal, spec' the money with as much care as you do the truck. Review the documents with your accountant. Make sure the payments are properly amortized and the interest is calculated correctly.

Use loan expenses to your advantage

Here's an option in case you're having a low income year and are worried what your bank will say once they see your statements.

If you borrow money for the purpose of acquiring depreciable property (for example, your truck), you can add the interest paid and any other loan costs to your capital cost allowance of your asset rather than expensing them this year. You're not giving up the deduction, you're just expensing it over time.

> **Soft costs like interest and other loan-related fees pack an unexpected punch.**

Your income will be a little higher, but that's okay if it means keeping the bank manager happy. If you think this approach is right for you, talk to your accountant to make sure.

November is a big month for budgeting. You should have a solid handle on your income and expenses for this year, which you can use to project your numbers for 2015.

Hard costs may be easy to identify but soft costs like interest and other loan-related fees pack an unexpected punch. If you plan to borrow money to expand, add equipment, or just pay the monthly bills, take every opportunity to identify and control loan-related costs. Talk to your accountant about how to properly record and expense these items on your business statement.

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