CAPITAL COST ALLOWANCE

- For accounting purposes we depreciate depreciable capital properties such as property, plant and equipment, furniture, and fixtures using various methods (straight line, declining balance, or units of production)
- For tax purposes, the amortization of depreciable capital properties are done through **Capital Cost Allowance**
- Assets are pooled into different CCA classes which have different CCA rates (for instance building goes into class 1) – please see the **CCA Classes Chart**
- Because the accounting amortization and the capital cost allowance are not the same, we need to add back the accounting amortization to accounting income and deduct the capital cost allowance in arriving at net income for tax purposes (division b).

Do businesses have to take Capital Cost Allowance (CCA)?

- There is a formula to calculate the "**maximum amount of CCA**" to be deducted; however, a taxpayer can choose to deduct anywhere between $0 to the maximum CCA
- CCA is a **discretionary expense**, a taxpayer can choose to deduct the max CCA or not
- A situation where taking the max CCA is not advisable is where you have a loss before CCA or with just a portion of the CCA; do not increase a loss with CCA because the Undepreciated Capital Cost (UCC) balance never expires while non-capital losses expire in 20 years.

CCA Formula:

Undepreciated Cost of Capital (UCC) Opening		$ xxx
add: Additions subject to half year rule	xxx	
less: Disposals in classes subject to half year rule	(xxx)	
Net additions subject to 1/2 year rule		xxx
Balance before CCA		xxx
add: Additions **not** subject to the half year rule		xxx
less: Disposals in classes not subject to half year rule		(xxx)
less: 50% of net additions subject to 1/2 year rule		(xxx)
Balance before CCA		xxx
CCA %		x%
CCA Claimed		**$XXX**

Additions and The half year rule:

- The half year rule **applies** to most CCA classes
  - In the first year only **50%** of the cost of the asset gets added to the CCA class
  - In essence, in the first year of acquisition most assets are only depreciated at 50% of its total cost.

- ½ year rule applies to **"net purchases"** in the year of acquisition; net purchases is the difference between additions and disposals. When the "net purchases in classes subject to the half year rule" is positive, we deduct 50% of it from the CCA class in the first year

- However, if the net purchases is negative (i.e. in a year where your disposal > additions) the full amount (100%) gets deducted rather than 50%
  - If purchases is $20,000 and disposals is $30,000; then the full $10,000 gets deducted from the CCA balance.

- Some classes are not subject to the half year – please see our CCA Chart
  - Some assets in class 12 (tools, utensils, and kitchen stuff) are not subject to ½ year rule
  - Class 14 not subject to ½ year rule
  - Class 52 not subject to ½ year rule

Shortened taxation year

- CCA needs to be prorated for shortened tax years (with less than 365 days)
  - Max CCA calculated * (# of days in tax year/365)

Disposal of assets in a CCA class:

- In the year of disposal deduct from the CCA Class, the lesser of:
  a) The original cost; or
  b) The proceeds of disposition

CCA Recapture

- CCA recapture occurs whenever a disposal causes a negative UCC balance
  - In essence, this means that in the past we took excess CCA and we must recapture the amount back into income
- CCA recapture = Business Income (also considered active business income)
- When a disposal occurs the amount we deduct from the UCC balance is the lesser of: original cost **or** the actual proceeds

Example of CCA Recapture:

- Opening UCC balance = 10,000
- An asset in this class is disposed for $15,000
- The original cost of this asset = $20,000
- Assume no additions

UCC opening		$10,000
additions	-	
disposals	15,000	
lesser of		
a) original cost = 20,000		
b) proceeds = 15,000		
net additions		(15,000)
UCC balance before CCA		$ (5,000)
CCA Recapture		**$ (5,000)**

Conceptually you can think of it like this:

- The asset was purchased for $20,000 but sold for $15,000; therefore, in reality the asset only depreciated in value by $5,000
- However, we took CCA of $10,000 ($5,000 in excess); therefore, this $5,000 is the CCA recap that we need to show as income.

Capital Losses on Depreciable Capital Properties

- Depreciable properties **cannot have capital losses** (since they already get a CCA deduction)
  - Therefore, in the above case although the asset is sold for ($15,000) less than the cost($20,000), you cannot claim a capital loss
- However, depreciable properties can have capital gains if sold for above the original cost and 50% of the gain is taxable

Terminal Loss

Terminal losses occur when **all** of the following 3 are met:

1. An asset in a CCA class is disposed
2. There is no other assets remaining in the CCA class after that asset is disposed
3. After the disposal, the UCC balance > 0

- Conceptually, this means that we did not take enough CCA and we take a terminal loss (a deduction) when the asset is disposed.
- Terminal loss is a **deduction** in arriving at business income

Example of Terminal Loss:

- Opening UCC = $10,000
- Original Cost = $20,000
- Proceeds of Disposition = $8,000
- Suppose no additions this year
- Suppose this asset is an equipment in class 43 and suppose this is the only asset in this class; and no other assets remain in the class after disposal

Terminal Loss = 10,000 – lesser of (8,000 or 20,000) = $2,000

Again, there will be no capital loss because capital losses on depreciable capital assets is not allowed for tax purposes.