Fall Economic Update Highlight: Deductions on Equipment Purchases

By Chris Duncan

On November 21, 2018, the federal Minister of Finance announced the fall economic statement that included several measures to improve competitiveness for Canadian businesses.

One of the most highlighted measures is a full write-off of machinery and equipment used in the manufacturing and processing of goods. This measure is targeted toward improving Canada's manufacturing sector in a time when industry players may be eyeing tax changes south of the border as an opportunity to relocate.

Unfortunately for contractors, logging is specifically identified in Canada's *Income Tax Act* as not being in the manufacturing category. Unfortunately, this means the 100 per cent deduction is not available for logging equipment.

However, a second accelerated investment incentive was also announced as a measure to support all sectors and types of businesses across the economy. For capital assets purchased after November 20, 2018, this measure suspends the half-year rule normally applied to depreciation for tax. Instead, 1.5 times the full rate of depreciation will be available.

For example, prior to the incentive, a capital asset in Class 10—which has a rate of 30 per cent and under which most logging equipment falls—would be eligible for a depreciation rate of 15 per cent of the cost of the asset in the year it is purchased; this is due to the half-year rule. Under the new incentive, the contractor will be able to claim 45 per cent depreciation in the first year, or 1.5 times the rate normally eligible in the first year of an asset purchase.

The incentive does not change the total amount that can be claimed for depreciation over the asset's useful life. In fact, the deduction will eventually be offset by smaller deductions at the end of the asset's life; the end result is more value upfront.

Under the new incentive, the contractor will be able to claim 45 per cent depreciation in the first year, or 1.5 times the rate normally eligible in the first year of an asset purchase.

This incentive, which became available November 20, 2018, will begin to phase out in 2023, and will end in 2027. For assets purchased in the phase-out period during 2024–2027 that are normally subject to the half-year rule, the rule will be suspended. For example, logging equipment in Class 10 will have a 30 per cent depreciation rate for tax in year one.

The following is an example of a Class 10 Log Loader with a purchase price of $600,000, financed at 6%:

This incentive makes purchasing rather than leasing equipment more favourable in year one if you understand in the later years you will have less deduction for tax. This could just be the incentive you need to go get a new piece of equipment. As always, before deciding which option is best for you, talk to your advisor.

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	Deductions for tax purposes: year one	
	Old Rules 15%	New Rules 45%
Capital Cost Allowance	$90,000	$270,000
Interest Expense	$36,000	$36,000
Total deductions	$126,000	$306,000
Tax savings at small business rate*	$15,120	$36,720
Tax savings over small business rate**	$34,020	$82,620

*Tax rate for 2018 for active business income up to $500,000 in BC is 12%
**Tax rate for 2018 for active business income in excess of $500,000 in BC is 27%