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### Agenda

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- ▶ What is work in progress
- ▶ Old rules
- ▶ Old rules : election
- ▶ New rules
- ▶ Example
- ▶ Planning
- ▶ Valuation
- ▶ Implications

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## What is work in progress

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- Work in progress is partly finished services which are in the process of completion.
- Work in progress is identified as inventory in the ITA.
- Subject to inventory valuation rules per ITA.
- Work in progress must be included in taxable income

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## Old rules

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- Work in progress must be included in income of the taxpayer.
- Taxpayer can elect to exclude work in progress from income from a designated professional business.
- Designated professional business: accountant, dentist, lawyer, medical doctor, veterinarian, chiropractor.
- Taxpayer may be an individual or a corporation.

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## Old rules: election

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- Where the taxpayer is a partnership, the election must be made only by the partnership (executed on behalf of all partners) and the election is deemed made by all partners.
- Due when filing return of income for the year for which the election is made.
- No special form for the election. Made by attaching a letter to the return of income or clearly indicated in the financial statements submitted with the return.
- Election apply to following years, unless election is revoked, with the concurrence of the Minister.

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## New rules

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- Election to exclude work in progress from income is eliminated for taxation year beginning after March 21, 2017.
- Transitional measure available, 5 years phase-out:
  - 80% at the end of the first taxation year
  - 60% at the end of the second taxation year
  - 40% at the end of the third taxation year
  - 20% at the end of the fourth taxation year

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### Example

- ProfCorp has a December 31 year end.
- ProfCorp made an election not to include WIP in income in a previous taxation year.
- ProfCorp has \$350,000 of WIP on December 31, 2018.
- ProfCorp has \$400,000 of WIP on December 31, 2019.
- ProfCorp has \$375,000 of WIP on December 31, 2020.
- ProfCorp has \$425,000 of WIP on December 31, 2021.
- ProfCorp has \$450,000 of WIP on December 31, 2022.



### Example

	2018	2019	2020	2021	2022
WIP	\$350,000	\$400,000	\$375,000	\$425,000	\$450,000
20%	\$70,000				
40%		\$160,000			
60%			\$225,000		
80%				\$340,000	
100%					\$450,000
Included in revenue prior year	\$0	\$70,000	\$160,000	\$225,000	\$340,000
Taxable this year	\$70,000	\$90,000	\$65,000	\$115,000	\$110,000



### Example

- Taxed in total on \$450,000
- For any following years, any variation will be included in income.



### Planning

- Structure of the business
- Maybe no need to include work in progress in income for contingency-fee arrangement
- Can choose valuation method for work in progress.



## Valuation

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- Each item valued at the lower of cost and fair market value or valuation of the entire inventory at its fair market value.
- Valuation must be done at the end of each taxation year.

## Valuation

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- What is included in cost:
  - Labour
  - Overhead
- What method for overhead:
  - Variable costs only
  - Variable and fixe costs

## Implications

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- Planning on cash flow – taxes are paid before work in done or billed
- Consider interim billing to recover cash flow
- Valuation of work in progress
- Change in partners

## Questions?

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