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Tax Tip

“Work-In-Progress — Professionals”

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Work-in-progress (“WIP”) represents time/cost incurred by professionals for performing services, which has not been invoiced to their clients. Prior to the March 22, 2017 budget, professionals could file an election to allow them to defer WIP until the point in time when the work was completed and invoiced. The deferral benefit allowed professionals to match revenue recognition to the payment of taxes. Certain professionals, such as actuaries, architects and engineers, could not make this election. ***This election will no longer be available.***

The March 22, 2017 budget announced that every professional must include year-end WIP into income at the lower of cost or fair market value, effective for taxation years commencing after March 21, 2017. This legislative change will apply to most professionals who work in Canada. Some examples of professionals include accountants, lawyers, medical doctors, dentists, veterinarians and chiropractors. This budget proposal was subsequently updated by the Department of Finance in the draft legislation released on September 8, 2017 and approved December 14, 2017

What has changed?

- As previously noted, WIP incurred by professionals will now need to be included in income at the lower of cost or fair market value. As there is no legislative guidance to help determine the cost of unbilled WIP, professionals judgement must

be exercised (i.e. employee salaries, supplies used and a reasonable allocation of overhead costs).

- The new legislation provides a five-year transitional relief period. For 2018 and future years, for purposes of calculating the WIP income inclusion, WIP must be reported for tax purposes as follows:
 - ◇ 2018 – 20% of the lower of cost or fair market value of unbilled WIP
 - ◇ 2019 – 40% of the lower of cost or fair market value of unbilled WIP
 - ◇ 2020 – 60% of the lower of cost or fair market value of unbilled WIP
 - ◇ 2021 – 80% of the lower of cost or fair market value of unbilled WIP
 - ◇ 2022 – 100% of the lower of cost or fair market value of unbilled WIP
- The above noted transitional relief will only be available where the taxpayer elects to exclude WIP in computing income in the last taxation year that begins before March 22, 2017 (i.e. December 31, 2017 taxation years for most professionals).

