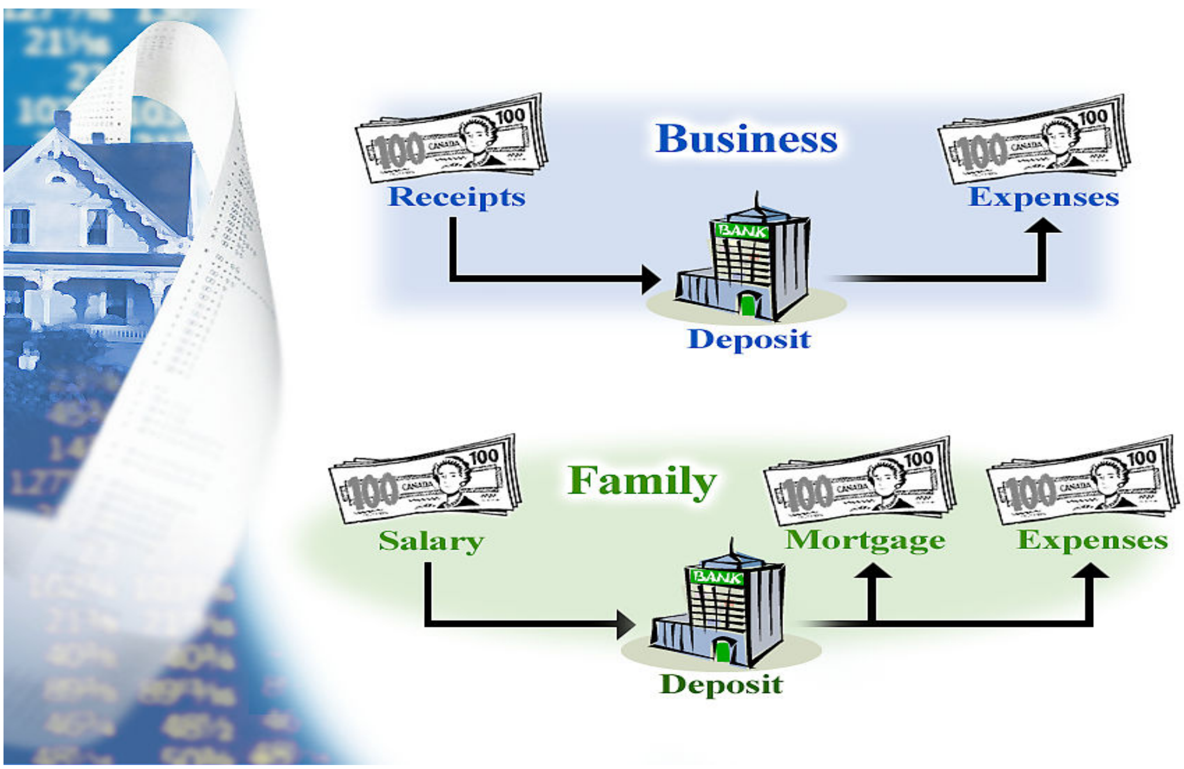
The Cash Flow Dam

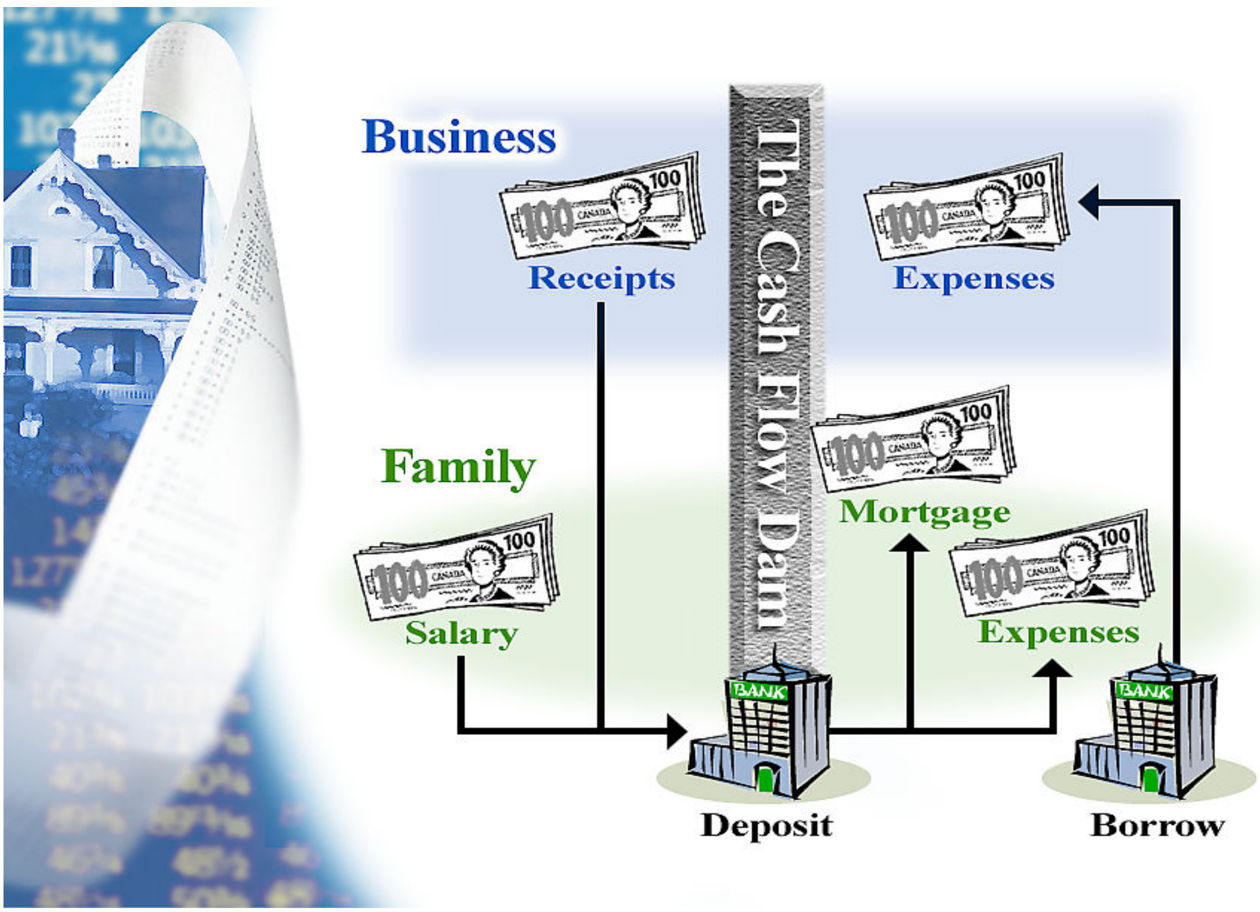
"Typically" for anyone who has a house mortgage and in addition runs an unincorporated business or owns a rental property the "business banking" is kept separate from the household banking as shown here.



The Cash Flow Dam-Implemented

Here is an accelerator for anyone who has a house mortgage and in addition runs an unincorporated business or owns a rental property.

This illustrates putting a dam between income and expenses of our business. Borrow the money from the bank under our "Smith Manoeuvre" readvanceable mortgage in order to pay the expenses of the business.



The Cash "Flow" Dam

A Backgrounder

You live in your own house with a mortgage that does not yield tax-deductible interest. You also own one or more rental units, which are operated as an unincorporated business.

We will rely on the tax fact that money borrowed personally to invest in a business in order to generate income gives rise to deductible interest on that loan.

Further, nothing in the tax act says that you have to pay company expenses with revenue generated by the unincorporated business. You may pay your expenses with borrowed money.

Being unincorporated means that for tax purposes, you and your rental business are the same person. Your accountant will total your annual rental revenues, subtract company expenses and the difference, the profit, will be added to your other personal income for the calendar year.

Ok. The tax act allows us as Canadians to deduct the interest carrying costs on personally borrowed funds to personally invest in a business opportunity that has a realistic expectation of profitability. (For ever since I can remember we have relied on this fact when we purchase rental properties).

Now, if you own one or more income producing properties you are essentially running an unincorporated business and by being unincorporated means that for tax purposes, you and your rental business are one and the same. (This does not work for incorporated businesses because unlike unincorporated entities, an incorporated business is essentially considered another person for tax purposes.)

What typically happens is that at the end of the year, you (or your accountant) total up the rental income you received, subtract from that the "company" expenses and the difference – your profit, is added together with your other personal income and taxes owing are calculated accordingly.

Now, if you want to reduce or eliminate your mortgages you are going to have to either dig pretty deep or talk to your friendly banker. In all probability, you will be having a chat with your banker. The banks solution is very typical. Switch from monthly payments to bi-weekly payments accelerated. This suggestion makes you use more of your hard earned after tax dollars to make overpayments on your mortgage. While on the surface this is OK, it is still a fact that you are having to give up more of your after tax money from your wallet!

Now, none of this will be new to you – and in fact, may have been your strategy up to this point.

But the following is going to be new – brand new to you. This is where it gets to be fun and profitable for you!

Rest assured that there is nothing in the tax act that says that you MUST pay your unincorporated company expenses (the mortgage) from the revenue generated by your income property (your unincorporated company).

Did you know that you can pay your expenses with borrowed money?

And why would you want to do this?

Why to pay down your principal residence (non deductible) mortgage quicker of course.

How can we do this?

Use the cash flow available from your renters.

This amount will be equal to the expense of your company for the month. This amount will be applied against your first mortgage (the non deductible one on your principal residence). (Note: If you take a monthly draw, this draw is not classified as business expense).

Furthermore, capital expenses (the cost of that new fridge, or new roof) as well as the operating costs (utilities, etc). are eligible and qualify for the tax deductible interest treatment if these expenses are paid with borrowed money.

Here are the mechanics of it all:

1. First off, at the end of each month, total up all of the qualifying expenses that directly relate to your rental business. (Remember to be precise and to keep good records.)

2. Then, write a cheque against your "Investment (LOC) Line of Credit" for that very same amount. (The "Investment (LOC) Line of Credit" will be the one registered against your principal residence). On the check "memo" line, write *"Business Expenses"* and make it payable to your business and pay your rental mortgage and expenses with this money. Deposit this check in the account where your rental mortgage is drawn from.

3. The next step is to write a cheque from the business payable to yourself for the total amount of the expenses. On the check "memo" line, write *"Re: Business Expenses".*

4. Now, deposit that cheque into your personal chequing account. From that account you will be paying down your first mortgage by the same amount. This will be another payment over and above your regular monthly mortgage payment.

(**Note:** Some banks will not accept monthly lump sum overpayments so put the money in a separate savings account. Pay out that account on the date your lender allows for the annual "penalty free" overpayment.)

Cash "Flow" Dam – Rental Properties – ***Flow Chart***

"Investment" LOC	1- Pay "Bus. Expense"	Mortgage & Expenses
Principal Residence	**Business Account**	**Rental Property**
Mortgage	2- "Draw" Re: Bus. Expenses	Rental Income

Summary

The Cash Flow Dam requires no new money and no new resources of any kind from the taxpayer. The benefits are free, and accrue as a result of reorganizing finances, just like wealthy people do.

Mark Huber, CFP is also author of - "The UnCanadian Way" series of reports, Ebooks, audios and videos…

Check out the full library of resources here at:

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About the Author

Mark Huber is a proud Canadian living with his wife in scenic Richmond, British Columbia, Canada.

For over 22 years, Mark has worked in the financial services industry. The focus of Mark's financial planning advisory practice is focused exclusively to British Columbian (BC) Canada residents.

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-The End-