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Moneysaver

Don't Forget

As the old saying goes, "*It's hard to clear the swamp when you're worried about the alligators*."

With tough times problems that distract owner/managers from the fundamentals of running their businesses can cause decisions to be poorly thought out and create even greater difficulties for both the business and the entrepreneur.

Before making those important decisions, consider the following 10 "**Don't Forgets**":

1. **Suppliers:** At a time when cash flow is tight for everybody, forgetting a payment to a supplier may make creditors think you have cash flow problems. Because their concerns can easily translate into cash on delivery or a reduced credit limit for your business, make sure all invoices are paid on time. If you are having cash flow issues, contact your supplier, speak to someone in authority, let them know your problems and provide them with assurances and time frames for the payment of outstanding amounts.
2. **Business line of credit:** The cyclical nature of most businesses makes a line of credit essential. During a normal business cycle the line eases concerns about sufficient cash flow. Tapping your line of credit to its limit to pay creditors will certainly ease the current situation but may leave insufficient working capital to finance the next upturn in business.
3. **Financing business with personal credit cards:** Credit limits on credit cards issued to an owner for business purposes can often exceed those limits that would be granted personally or even the business's line of credit. The temptation to purchase supplies, pay off corporate debt, or take temporary cash loans to finance business operations is tempting but extremely expensive. Granted there are responsible

financial institutions that offer reasonable interest rates for outstanding amounts, but most still carry rates in the 17-to-29% range. The short-term benefit will be offset by the negative impact of having to carry a balance at high rates of interest; more cash will be withdrawn from the business to pay the cards, and profits will suffer as will personal credit ratings. Combining these factors with the fact that the credit cards are the holder's personal responsibility suggest that this is not a good business move.

4. **RRSPs:** You worked hard to build your business. You and your accountant devised business strategies to minimize both corporate and personal income taxes. Along the way you determined that to ensure reasonable retirement the proceeds from the ultimate sale of your business should be augmented with an RRSP strategy. Not only did this provide immediate personal tax relief but it built a nest egg with tax-deferred growth. Immediate cash flow needs for the business may tempt you to cash in RRSP funds. This action will create the following consequences.
   - In the first instance 20% will be withheld on withdrawals in excess of $5,000. Thus if the business needs $20,000, $25,000 will have to be cashed out.
   - The addition of these amounts to the income of the individual making the withdrawal will undoubtedly result in a higher income bracket and additional taxes at the end of the calendar year.
   - Certainly there is anticipation that the loan from the owner/manager will be repaid with interest by the company. However, should the corporation be unable to pay the loan for an extended period, the owner/manager loses growth within the RRSP.
   - Further, should the corporation be forced into bankruptcy the shareholder would probably not be a secured creditor and could forfeit the loan entirely.
5. **Personal guarantees:** Financial institutions often require business owners applying for a business loan, leases of premise or vehicles, or corporate credit cards, to sign not only as a representative of the corporation but also as an individual who will personally guarantee the loan or contract. Where there is more than one shareholder, such as a spouse or a business partner, there may be more than guarantor. Generally signing a contract as a representative of the corporation would restrict creditors to attaching only the assets of the corporation. Personal guarantees usually allow the creditor to seek a remedy against the guarantor if the primary debtor cannot fulfill the obligation. It may be advisable to review contracts to ensure that contractual obligations are met to avoid jeopardizing personal assets.
6. **Staff:** Meeting payroll is the largest responsibility of any owner/manager. Nevertheless, it may become necessary to lay off staff to cut costs. If this becomes inevitable, the challenge for owner/managers is to ensure employees are treated with respect and fairness. A staff meeting addressing the reality of the situation is a must. A frank discussion may reveal that a shorter work week, reduced wages, or reduced or shared benefit costs, may be the solution that saves jobs. On the other hand, if such solutions are impossible, holding out false hope will only exacerbate the situation while cash flow slips away and the very survival of the business comes into question. Various labour laws ensure that dismissed employees are entitled to employment insurance benefits and termination packages. Understanding corporate obligations and providing dismissed staff with timely settlements will lessen the difficulties of dealing with the remaining staff who suddenly find themselves worrying about their own survival. Your fair dealing with laid-off employees will have a positive effect on the employees who stay with you to move the company forward after the inevitable economic upturn.
7. **Customers:** Customers have a responsibility to pay on a timely basis but may not be able to meet their obligations as they did in the past. Certainly you are within your legal rights to demand payment but if your client is having difficulty consider:
   - negotiating repayment over an extended period of time,
   - accepting post dated cheques,
   - cancelling interest on overdue accounts,
   - arranging alternate forms of payments such as service or goods for past debt, or
   - providing inventory on a 50%-down-50%-credit basis.

   These may be solutions that will not only help the customer survive but create goodwill for the future. When the worst is over, people remember those who helped them and usually reciprocate by maintaining a business relationship.
8. **Government:** Concerns with suppliers, payroll, overhead and other immediate matters can take over an owner/manager's attention and obligations to the government can easily slip into the background. The consequences of forgetting to remit the required forms and funds as required can be catastrophic. Failure to remit will undoubtedly lead to interest and penalty charges. Continuing to be late will simply raise the penalties and interest. If filing is still not completed there is a high probability the business will be assessed based

on past performance. If previous years have been profitable, the estimated assessment will probably be higher than it should be. At this point it will be necessary either to pay the assessed amount or expend time and money to satisfy the authorities. If the letters and assessments are ignored, funds in the business bank account will be attached or the account will be frozen. In either case the ability to write cheques, make deposits and ultimately obtain credit could be severely compromised. Depending upon which regulatory ruling has been violated, directors and officers may be held personally accountable. This can result in personal liability and possibly criminal charges.

9. **Family:** We all work hard to provide for family. As entrepreneurs we may forget how difficult it is for family members to comprehend the concerns and responsibilities that drive us to work. Responsibility to maintain the business, to ensure that all employees take home a pay cheque and that suppliers and customers are taken care of are all prerequisites to ensuring that adequate resources are left over to maintain a roof over the family. Discussing the social and financial aspects of current business difficulties with family members and explaining the effect reduced business is having on funds normally available to support the family's life style can help them understand the need to reduce expectations as well as spending. If family members understand the concerns of the provider(s), they may reduce their demands and thereby ease the worrisome burden of providing carried by the self-employed.

10. **Keep your word:** Business may be business, but in the scheme of things businesses are run by entrepreneurs who base their firms' survival on the promises that other entrepreneurs have made to them. Entrepreneurs work within a community circle wherein the work performed depends upon the supplies, labour and capital provided by others within the circle. For those in larger communities the circle may be wider but in the end everyone within the circle knows someone who knows you and your business. As such, your word is your bond. Should you break that bond, good faith established over the years will disappear overnight. Thus, promises made are promises that must be kept. In trying times maintaining business integrity will ensure continuing support from those who know they can rely upon you. Such personal strength enhances the probability of business survival and a more prosperous growth when the business community enters once again on the path of recovery. ■

Taxation

Take Time for Taxes

Mid year is a good time to consider tax issues that may be important for next year's filing.

Joint Accounts—Spouses

Many couples have bank or investment accounts in both names so that each partner can carry out transactions. This way, difficulties can be avoided if the account is frozen because a sole signatory has become incapacitated or dies. Financial institutions may issue T3 or T5 slips in both names or in one name even though the account(s) may be held jointly. (The CRA does not require slips to be issued to both partners; the financial institution need only issue the forms to one individual.)

A question arises, however, at the time of personal income tax filing: who should report the income?

Regardless of whether the forms are issued in both names or to only one partner, tax rules require that income should be reported in proportion to the amount invested by each spouse or common-law partner in the account. Thus, if A has invested $20,000 and B has invested $30,000, income should be reported 2/5 by A and 3/5 by B.

Joint Accounts—Non-spouses or Common-law Partners

If two individuals hold an account in joint tenancy with the right of survivorship, the investment income reported on the slips should normally be reported equally between the named persons provided they are not spouses, common-law partners or parent/minor child.

Just because one or two names are on a slip does not mean the income must be split 50/50 or allocated 100% to one person. To ensure that income is allocated properly, make your chartered accountant aware of the income to be allocated to each party.

Interest Earned but Not Received

Suppose you purchase a $50,000 City of Victoria bond on July 1, 2009 that pays simple interest of 3% per annum and matures July 1, 2011. If held to maturity, you would receive a cheque for $53,000 of which $50,000 would be a return of capital and $3,000 in interest ($1,500 each year for two years). Since you did not receive the interest at the end of the first year, the interest "accrued" to the end of the second year.

Technically, you can report interest income when it is received (subject to the modification following) or when it is "receivable", i.e. when you are entitled to receive it, not when it accrues. However, even if you chose to ordinarily report the interest on the received basis, you cannot defer reporting it beyond the year in which each anniversary falls. In other words, interest accruing from July 1, 2009 to June 30, 2010 must be reported in 2010 and interest accruing from July 1, 2010 to June 30, 2011 must be reported in 2011. Notwithstanding these technical rules, if you chose to report the interest income at the end of each calendar year on the accrual basis (i.e. $750 in 2009, $1,500 in 2010 and $750 in 2011) because it will be taxed in a lower bracket, it is likely that this will be acceptable to the CRA.

Strip Bonds

Strip bonds are government or high-quality corporate bonds from which the interest-paying portion (coupon) has been "stripped" so that both the principal amount (residual) and the interest-paying portion can be discounted and sold separately. Each part is now a strip bond with a specific maturity date. If held to maturity, the difference between the purchase value and the maturity value is considered to be accrued interest and is taxed accordingly. Because strip bond prices fluctuate with interest rates as do conventional bonds, purchasers may have a capital loss or a capital gain if the strip is sold before maturity.

If, for example, you invested $50,000 in a strip bond, the accrued interest would be calculated by multiplying the purchase price by the yield to maturity. As discussed above, this accrual must be reported on the anniversary date and not on a calendar year basis. Thus if, as in our previous example, the yield to maturity is 3%, the first accrual amount would be $1,500 and would be reported as income in 2010 because the first anniversary date of the strip is 2010. If the strip is sold prior to maturity, the gain or loss is found by first calculating the accrued interest and reporting it as income, subtracting it from the proceeds of disposition, then calculating the capital gain or loss.

Worthless Securities

If you have suffered losses on speculative investments, keep in mind that you may be able to obtain some taxable benefit from a capital loss. If the value of the speculation seems to have been reduced to zero, the first order of business is to obtain assurance from your broker that the company is, in fact, defunct. The second is to locate the broker's confirmation slip stating the original purchase price plus brokerage fees to determine the adjusted cost base. This information will allow your chartered accountant to determine the capital loss. The capital loss can be netted against any capital gains from the sale of other investments to reduce capital gains.

If you do not have capital gains this year, take heart. If capital losses for any year are greater than capital gains in that year, the excess may be carried forward or back to a year in which there are capital gains that are not offset by the current year losses. Losses may be carried back three years, and carry forward indefinitely.

There are circumstances where the investment could be considered to have been acquired in an "adventure in the nature of trade". In such instances, a loss on disposition would be a fully deductible loss rather than a capital loss. However the loss can be taken only by disposing of the security. This possibility should also be discussed with your chartered accountant. ■

Unemployed or Living the Dream?

As the recession drags on, many individuals find themselves with a reduced work schedule, reduced benefits, fewer vacation days and, for the even less fortunate, no income.

Add to this mix the fact that fewer employers are offering employment, the prospect of immediate placement can be bleak.

Those fortunate enough to have received a reasonable severance package or to have pension plans or RRSP savings to draw on may have sufficient funds to sit out the recession — or start a business.

In fact, what might have begun as a crushing catastrophe may become the opportunity of a lifetime to realize a dream of doing what you always wanted to do: ***have a business built according to your own vision.***

The Three Basic Structures

There are three forms of business organization: sole proprietorship, partnership, and corporation. Since each has it own pluses and minuses, deciding which one is best for your purposes is an important first step.

Sole Proprietorship

In this form, you are the only owner and have direct control over all aspects of the business. The downside is that you will be subject to **unlimited liability** for breached contracts, torts, and insolvency. If the court awards the plaintiff damages, you could lose not only the assets of your business but also your personal assets such as your house, cottage, or car to satisfy the judgement. In addition, the principle of **vicarious liability** makes the sole proprietor responsible for the torts of employees committed while on company business. Much of these risks can be offset by insurance, however.

Since proprietors pay themselves by withdrawing capital rather than taking salaries or wages, they cannot make deductions at source for income tax, CPP or EI. Profit is added to the personal income from other sources of the proprietor and taxed at the personal marginal rate. Canada Pension premiums must be paid.

Because proprietors do not pay into EI they cannot collect benefits in the event the business fails and they cannot find other work.

It is possible to employ relatives such as a spouse at a level of compensation commensurate with their responsibilities. CPP contributions must be deducted and remitted along with the proprietor's share. EI premiums are not normally deducted and thus employment benefits cannot be claimed in the event of layoff. Proprietors would be advised to look into the requirements of paying Workers' Compensation premiums for employees, whether related or not, within their jurisdictions. A sole proprietorship ends with the death of the proprietor.

Partnership

This form has the advantage of shared work, investment, and rewards. Because shared responsibility can lead to conflict, a written partnership agreement should assign responsibilities, determine when all partners are required to make a decision and, of course, spell out what defines profit and how it will be shared. Since each partner is the agent of the others and has the power to bind all partners to a contract, each partner becomes liable for his or her own wrongful acts, those of their partners, and those of employees committed while working (vicarious liability.) Thus not only are the assets of the partnership at risk to satisfy a judgement, but also the personal wealth of all the partners regardless of which partner breached the contract or committed the tort.

Instead of taking salaries or wages, partners usually share profits and losses equally. Thus if a three person partnership share a net profit of $30,000, each partner would claim $10,000 as income. As in a sole proprietorship, this profit is added to any other income and the whole is taxed at the partner's marginal rate.

Each partner is required to pay Canada Pension premiums. Partners do not pay into EI and thus cannot collect benefits in the event the partnership dissolves and they cannot find work.

As with the sole proprietorship, partners can employ relatives. All partners should first be in agreement about this practice to avoid misunderstandings over perceived nepotism. CPP must be deducted from their wages and remitted along with the employer's matching share. EI premiums are not normally deducted and thus employment benefits cannot be claimed in the event of layoff. Workers' Compensation coverage may be a requirement within your provincial jurisdiction for partners or related parties. Ensure that coverage is in place if required. A partnership can be dissolved in a variety of ways including the death or insolvency of any partner.

Corporation

A corporation is a legal person distinct as an entity from its shareholder owners. As a legal person, a corporation can own assets, incur liabilities, enter into contracts, and generally carry on business through its agents, the employees. A shareholder can give up ownership by selling his or her shares. Unlike a partnership, the corporation does not have to be dissolved or initiate new agreements between owners if shares are sold. Naturally, shareholders should consider a shareholders' agreement to protect the rights and assets of the shareholders. Shareholders elect the board of directors which, in turn, hires the officers of the corporation. Shareholders would be advised to speak to their solicitors about the legal responsibilities assigned to shareholders who agree to become directors or officers.

Provided shareholders sign agreements as officers of the corporation and do not provide personal guarantees, in most situations **limited liability** will be assigned to shareholders. This limited liability is limited to the cost of shares in the corporation and protects personal assets from the corporation's creditors.

Corporations pay income taxes based on their taxable income. Depending upon the province of incorporation, both federal and provincial taxes may have to be filed. Individual shareholders are subject to taxes only if they receive remuneration from the company. (This is a complex area that should be discussed with your chartered accountant).

An incorporated business may hire employees that include shareholders' spouses and family members. The corporation will be required to withhold and remit income tax and CPP contributions from pay cheques as well as the corporation's matching share of CPP. Employment insurance premiums for employed shareholders, their spouses, and family members are not normally deducted and thus employment insurance benefits cannot be claimed if their jobs are terminated. Workers' Compensation premiums requirements should be reviewed to ensure local obligations are met.

Live Your Dream

Succeeding as an entrepreneur can be the most trying and yet the most rewarding of all of life's adventures. Understanding the business form best suited to your emerging needs combined with the helpful advice of a chartered accountant is the first step to ensuring a successful future for you and your family. ■

Technology

Where Did I Put My Cell?

Losing your cell phone can be almost as traumatic as losing a wallet or purse — perhaps more so for some.

Cellular telephones are not just for making calls any more; they have the potential to store a significant amount of information: the contact book feature on most devices can store hundreds of names; phone numbers; e-mail, business and residential addresses; and birthdays. Some owners even personalize their contacts by attaching a picture to each!

Many phones contain large internal and/or upgradeable storage capacity that enables the user to save documents, spreadsheets, correspondence, and any other form of data, thus turning the cell phone into a portable storage device like a USB flash memory stick.

The use of multiple bank accounts, credit cards, debit cards, membership information, and e-mail addresses must be secured by passwords, usually alpha numerics of a specific minimum length. Trying to remember one or two passwords may not be a problem for most of us but the need for more and more passwords has led some people to create lists of their passwords which, in turn, get stored on their cell phone! In fact, a recent survey found that more than 80 percent of users store addresses etc. on their cells while close to 25 percent store personal data as well as passwords, credit card numbers and other confidential information.

Because cell phones now store so much information, a misplaced phone is not only an inconvenience; it can also significantly impact your business and personal life.

If your cell is lost or stolen consider the following:

- Your name and address may be determined by doing a reverse look-up using your telephone number.
- Should the cell phone store passwords and credit card numbers, this information combined with names, address and telephone numbers create the opportunity for fraudulent purchases and identity theft.
- Your business data or that of a client could be compromised; stored passwords could be used to gain unauthorized access to your office or client servers or other online services.
- Your business could be held legally liable for failing to safeguard personal and confidential information as required under privacy legislation.

Proactive Defence

- Institute a policy as to what can be saved on company cell phones and ensure that staff are reminded of it regularly. Although all cell phones now include this simple feature, more than 40% of users do not set a password.
- Require that all cell phone users set a password on their device. These areas may be difficult to monitor in practice, but publishing and distributing guidelines will certainly ensure that staff are aware of the potential damage that can occur if security is taken lightly.
- All cell phones should be returned when an employee leaves the company or is terminated.
- The loss of any cell phone should be reported immediately to management and the wireless provider. The wireless provider may temporarily suspend the account to prevent unauthorized charges.
- If your business uses a cell phone for financial transactions, notify the financial institution(s) of any lost phone. Depending upon the security protocols in place, they should be able to disable access to your account.
- All cell phones should have a synchronization programme to allow rapid reconstruction of data. Not only will this allow business to continue as usual, but access to the data will allow management to determine the potential damage to the business and the clients should a cell phone be lost.
- Never leave a cell phone unattended. It only takes about two minutes for someone with the right software to access your cell phone and copy all of the data onto their laptop or other handheld device.
- Discarded cell phones should have their storage cards removed; internal memory should be cleared and restored to the factory defaults.

A lost cell phone with password protection makes it difficult for a good Samaritan to contact the owner. Consider attaching or writing in indelible pen an alternate telephone number on the outside of the telephone with the wording: “If found, call (number).” This may save the cost of replacing the phone and the potentially sensitive data stored.

The cell phone is primarily a communication device enabling people to be connected anytime, anywhere. It’s easy to forget that the cell phone has become a portable computer capable of processing business data, doing the banking or online shopping, and storing data essential to operations. Now that cell phones have taken root in our businesses, more than ever it is essential that management consider steps to ensure safeguarding business information. ■

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