

THE Quarterly Dividend

Vol. 22 No. 4 Your guide to income tax & financial planning

FAST TRACK



Should You Collect CPP Before Reaching 65?

Mary has been working at the bank for over twenty-five years and thought about retiring in the Fall after her sixty-second birthday. She has done her "homework" and contacted the CPP authorities to find out how much her CPP payments

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Conversation Etiquette

Conventional wisdom is at a loss in trying to explain the increase in popularity of social media in our society and the decrease in actual face-to-face conversation between people. Perhaps it can best be summed up as “real-life” communication has simply become annoying. Here are a few examples where conversation between two parties has deteriorated to such an extent that at least one of them must have wished he had conducted his end of the conversation from the safety of his cellphone rather than face to face.

- A. The person in the conversation insists on finishing your sentences for you. Does he really know in advance what you want to say? Are you really that predictable? You have been talking in complete sentences since you were a child. You are capable of expressing your own thoughts in your own words. Perhaps your message will surprise him;
- B. The person with whom you are talking is so interested in what he has to say that he does not listen to what you are trying to convey to him? Do you find that he is just allowing you to talk for a minute or so, so he can catch his breath and then continue imparting his wisdom to you? Do you find that he asks a lot of rhetorical questions that he does not really want you to answer, but would rather immediately answer himself? Does he “like to hear himself talk”?
- C. The person with whom you are conversing has expressed the need for some advice. However, in reality, he has already made up his mind long before and is just asking your opinion to confirm what he had been thinking all along. Do you ever wonder why he even bothered to consult you in the first place? Was the opinion you offered not in agreement with what he wanted to hear? Why was he so insistent on pressing his point of view on you? Was it simply to justify his preconceived notion? When you ask someone for their thoughts on a matter, choose someone who might actually disagree with you. Someone who

can point out ideas that you may not have thought about yourself. Someone who looks at things differently from you. Otherwise you will be stuck with “yes men” who will couch their “advice” in such a way that they present you only what they know you want to hear;

- D. The person with whom you are discussing a matter wants your input immediately and will not allow you time to properly consider the situation at hand before giving an answer. Has anyone ever asked you for “advice” and not been receptive to the notion that you might need some time to consider the situation at hand before providing an answer? Do they not understand that a “serious” question demands some thought before a cogent response can be presented? If the matter is strictly confirming some fact, for example, it might be easy to give a quick “yes” or “no”. But a question of substance will require some thought and maybe some research even if the person supplying the “answer” has encountered the same question many times before. No two situations are exactly alike and the differences between them may be subtle. Allow your advisor some reasonable amount of time to get back to you;
- E. Have you ever asked for advice from someone and after hearing what they had to say, regretted going to them in the first place? Wasn’t it clear from the outset that they did not know the “answer” and could not contribute constructively to the matter at hand? Did it not bug you that they just did not admit right from the start that they had “no idea” about the matter? It is okay not to know the answer to a question that has been put to you. If you want, you can try to figure it out “on the fly” by applying “logic” and attempting to come up with an answer. But in no case should you bluff an answer to a serious question. If you do, you will not be honest with them or yourself. If you must approach a situation that way, couch your response with such qualifiers as “perhaps” or “maybe”. Advise the

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will be under two different scenarios. If she decides to collect her CPP after she becomes 62, she will receive \$694 per month (indexed for inflation) as long as she lives. Alternatively, she can wait until she reaches 65 and becomes entitled to a monthly pension of \$828.

What should she do, assuming she does not "need" the money right now and can afford to wait the extra time before she collects the additional \$134/month "down the road"? Mary is in the lowest income tax bracket and will remain so whatever decision she makes.

To help her decide what she might want to do, she should compare the cash flows associated with each option and determine which one is preferable.

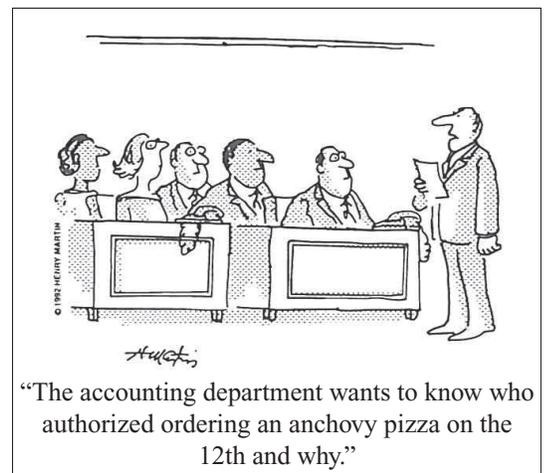
If she starts to collect her CPP in October, 2013 she will have a thirty-six month "headstart" over the payments she will receive by waiting until

other party to seek a "second opinion" from someone who has greater expertise in the matter;

- F. Have you ever asked for advice from someone and the answer you received "was all over the map"? First they answered one part of the question, and then without finishing their thoughts about that subject, went on to something else. And before that topic had been fully addressed, they skipped back to the first topic or onto something else again. Is it too much to ask that the first question be answered first, then the second, and so on? If you're going to skip around, tell the listener what you are doing so he can put all the pieces together and ultimately figure out what you were intending to say;
- G. Have you ever been in a conversation with a person who insists on interrupting you constantly before you have a chance to finish your sentence? This is different from (a) above because in this situation the "listener" is not finishing your sentence for you, he is basically telling you that he is not interested in even hearing what you might have to say;
- H. Have you ever been in a conversation with a person who insists he is correct about a certain matter, but is really mistaken? The best course of action is to explain patiently and in a non-threatening way where and why he has been incorrect. You can point out, tactfully, where he has "gone wrong". When he ultimately realizes that you are correct, he will, hopefully, acknowledge the truth without resenting the fact that he has been corrected. He might even thank you;
- I. Have you ever been in a conversation with some one that is being conducted within earshot of an other party, and this "third wheel" insists on joining the conversation, uninvited, as if he/she were a part of it to begin with? Have you had to endure when he/she makes inappropriate remarks because he/she does not know what the conversation has been about up to that time? Have you been forced to listen to his/her "wisdom" when it has not being requested. One particular example is when two couples have joined each other for dinner and the wives (for example) are talking to each other and the two husbands are conducting their own separate conversation. You can bet that sometime during the two parallel conversations one of the spouses will leave his/her conversation to join the other one that is taking place immediately beside him/her. In many cases, this is done to "correct" his/her own spouse and add details to the conversation that have no doubt been "omitted". It is as if the participant in one

conversation does not feel that his partner can carry on a dialogue on his own without additional input; and

- J. Have you ever been in a conversation with some one, usually on the telephone but sometimes in person, who is chewing gum or eating their lunch while conversing with you? Sometimes you can not even understand what they were saying. Wasn't that the point of having the conversation in the first place?
- K. Have you ever been in a telephone conversation where the other party is forever putting you on "hold" because they have to answer a second line? This takes all the "momentum" out of the conversation as you have to continually go back and re-iterate what has been said up to that point to make sure each of you is at the same place in the conversation. Once or twice is okay but any more than that, arrange to chat with each other at a time when neither of you will be constantly interrupted; and
- L. Have you ever been in a telephone conversation where the person on the other end of the phone has someone else with them who insists on distracting the person with whom you are trying to conduct your conversation? This may be because this additional person feels left out of the conversation his/her friend is enjoying or simply wants to hear what is going on and wishes to "contribute". This forces the person with whom you would like to be speaking privately to continually be drawn away from your conversation. It is incumbent upon this person to remind his/her friend that he/she is in the middle of a conversation and "nothing can be so important that it cannot wait until after he/she finishes the conversation in which he/she is engaged".





Financial Statement Analysis 101

2016. This translates into \$24984 (\$694/month for 36 months).

Without getting into sophisticated analyses considering the time value of money, etc. and recognizing that waiting will provide an additional sum of \$134/month, it will take her 186.50 months to "catch up" (\$24984 divided by \$134). This translates into fifteen and one-half years of \$828 payments before she will be in exactly the same situation under both scenarios. After that she will be "ahead" for the rest of her life.

If Mary is in good health and believes she will live to the age of 80 and beyond then waiting may make sense. If she attains the age of 90, for example, she will have collected \$16080 more in her lifetime than she would have otherwise.

On the other hand, anything can happen over the course of fifteen and one half years and perhaps it is better to start

Every financial statement tells a story but unlike books found in your local library the reader is never told in advance if the contents of the information presented belong in the fiction or non-fiction section of the building. While this is less of a challenge when the financial statements have been audited, it is still best to remember that the information you are given has been prepared by the company and will therefore convey their circumstances in their most favourable light.

This makes it all the more important to read the statements and their accompanying notes with a skeptical eye and to never take anything at "face value".

Take the time to "drill down" below the surface and determine what is really going on as best you can.

Here is a very basic set of financial statements and some sample questions that a reader might ask. Asking the right questions is only part of the job. The other is securing the answers you want and need to continue your analysis. The answer to one question may lead you to another and from there to still another. Do not be intimidated by what you discover. The only way to assess the believability of the information is to understand what has been presented and then make up your own mind based upon the research you have conducted.



Account	F/S Item Balance Sheet	"Drill Down" to Determine
	\$	
Cash	36,000	if company overstated its assets, understated its liabilities to show a stronger financial position than is warranted
A/R	120,000	content of "reconciling items"
Inventory	18,000	what percentage are collectible and how long it will take if items are saleable or obsolete; valuation
Prepaid Exp	3,000	if calculated correctly; typically rent, insurance
	<u>177,000</u>	
Equipment	98,000	if it is in good condition; how long is it expected to last
Acc Amort	(46,000)	if the cost has been spread out over too long a time frame
	<u>52,000</u>	
	<u>229,000</u>	
Bank loan	30,000	if operating line or financing inventory, equipment
A/P	140,000	what percentage are due now and which can "wait"
Corp I/T	6,000	if current income is \$NIL these must be owing from last year
	<u>176,000</u>	
Sh Advances	22,000	if owners are using the company for personal expenses
	<u>198,000</u>	
Sh Capital	5,000	if shareholders with whom you are dealing have sufficient authority
R/E	26,000	if prior years' financial statements are consistent with current figures
	<u>31,000</u>	
	<u>229,000</u>	
	Income Statement	
Revenue	720,000	if company "padded" its figures to show enhanced revenues and reduced expenses; numbers are reasonable
Cost of sales	240,000	if sales show actual transactions not those that are "expected"
Gross margin	<u>480,000</u>	if historical cost of sales percentage has been maintained
Expenses		
Salaries	358,000	if payroll includes "non essential" employees
Operating Exp	84,000	if only business related expenses have been recognized
Admin Exp	26,000	if this is a "catch-all" for items not belonging somewhere else
Amortization	12,000	if assets' costs have been spread out over too long a timeframe
	<u>480,000</u>	
Net inc for year	<u>NIL</u>	if company really has a loss and how it can be exactly "NIL"



Employee Stock Purchase Plans vs. Employee Stock Option Plans

collecting earlier. Mary does not need to look only at these two options before deciding what she may want to do. Her maximum pension "kicks in" at age 70 and so she could conceivably wait these additional eight years. This time frame is much shorter than the fifteen and one-half years considered above and gives her the maximum pension for the rest of her life.

Finally, she could begin to draw her pension at any age along the way. She could decide to start collecting when she finishes her working career. This will give her some additional income to replace what she is giving up by leaving her job.

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Compensation of employees working in public companies often includes more than their take-home pay from the salaries they earn, health benefits the company may offer and the opportunity to contribute to the company's pension plan. It might also allow the employee the right to acquire shares of the corporation itself either currently or at some time in the future at a favourable price without the incurrence of transaction fees.

Employee stock purchase plans: These allow the employee to purchase shares of the enterprise once per year at a particular price that is set out by agreement between him and the company.

For example, Harvey has been accorded the right to purchase a certain maximum number of shares in the company for which he works based upon the weighted average of the company's share price on the Toronto Stock Exchange over a period of time. This computed value is determined once a year. If the price that has been determined is higher than the current market price of the shares on the open market, Harvey may choose to pass on the opportunity he has been presented. He can obtain the same number of shares for a lesser cost. But if the opposite is true, he may exercise his right and purchase his shares through the plan. His out of pocket cost will be lower but he will be subject to a taxable benefit for the differential between his cost and say the market price of the shares on December 31 of the year. This will be taxed as employment income.

By participating in the plan Harvey may have to hold onto the shares for a certain period of time before he can sell them. But once that time has elapsed, he is free to dispose of them. At that time he will realize a capital gain or loss determined by comparing the proceeds he receives upon selling the shares and the

amounts he paid when he acquired the shares through the plan.

Employee stock option plans: These provide the employee the right to purchase shares of the company at a predetermined dollar amount at his option throughout a (usually) predetermined period of time.

For example, Rocco has been accorded the right to stock options. The agreement allows him the flexibility to choose when he will wish to exercise his option, which will typically be when he believes the differential between his "strike price", the dollar value that has been set as his cost at the time the option was granted, and the current market price of the shares on the public stock exchange is at its highest point. This is because, almost invariably, he will exercise his stock option and then immediately sell the shares on the open market to take advantage of the existing differential.

As can be seen in the accompanying example, Rocco will be taxed in a different manner than Harvey. Just as Harvey is accorded a "taxable benefit" and is taxed as employment income each time he exercises his right to purchase the shares, Rocco will be taxed when he decides to exercise his stock options.

Rocco is a salaried employee making \$200K at a public company. Over the years he has been offered the opportunity to participate in the company stock option plan which allows him to purchase company shares for \$7.00/share. He has accumulated 5000 stock options over the years and since the company's shares are currently selling for \$12/share on the Toronto Stock Exchange, he is contemplating exercising his options and buying the shares. He will then sell them on the public market. If he goes ahead with his plan, he can expect the following income tax treatment:

	\$	\$
Rocco's salary for the year		200,000
If stock option is exercised when shares are selling at \$12/share (5000 shares @ \$12/share)	60,000 (a)	
Less: 5000 stock options acquired at \$7.00/share	35,000 (b)	
Difference (a) - (b) is taxable benefit		(c) 25,000
Employment income for the year		225,000
Rocco is entitled to a "security deduction" calculated as (c) x 50%		(12,500)
Rocco will have a capital gain on the disposition of his shares:		
Capital gain is the same as the taxable benefit; taxable portion 50% thereof		12,500
Taxable income on personal income tax return		<u>225,000</u>

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