

THE Quarterly Dividend

Vol. 24 No. 4 Your guide to income tax & financial planning

FAST TRACK



Form T2200

Before an employee can claim expenses on his personal income tax return he must make sure that the employer concurs with his decision. This is done by having the employer sign Form T2200, the Declaration of Conditions of Employment. It need not be submitted with the return but must be available should it be requested by the Canada Revenue Agency.

The way the form is completed will influence the ability of the employee to claim employment expense deductions and their amount.

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Decision Making for Business Owners

We all make decisions each day. Some are as inconsequential as what flavour of ice cream to choose at Baskin-Robbins and some very important such as those involving personal matters and those of our families.

Business decision-making differs significantly from day-to-day personal decision-making and it is important to distinguish between the two.

Here are some things to think about during the decision making process. Making business decisions in an owner-managed business comes with the position of leadership that you assumed when you decided to hang out your shingle. The very act of going out on your own was an expression of confidence and strength. From then on, you were to assume responsibility for whatever outcomes resulted from these decisions.

- (a) remember the goals you set when you first started out. Although they included the often stated "to make tons of money" they also recognized your desire to contribute something of yourself to the world. Keep this in mind during good times and bad, it will keep you from being pulled "all over the place";
- (b) guide the business towards the goals you have set. Take action to achieve what you want, not necessarily what others may "want you to want". You can go along with your clients' and employees' demands only "so far". There will come a time when where you want to go will not fit in with what they want from you. You must have the courage of your convictions to stand up to them and go your own way, if necessary;
- (c) exhibit a mature character. This means having high moral qualities, being honest and

a person of high integrity. Do not give in on the things you know are wrong and rationalize your behavior as being in the best interests of the company. It is okay to be flexible and compromise when possible, but know when to say "no" politely and firmly;

- (d) take responsibility for what's going on, take charge, find solutions to problems. You create your own world by what you do and people respond accordingly. You cannot change others, only yourself. So if things are not the way you want them to be, it's up to you to fix them. It is you who must make things work. Become self-reliant. Do not let the fear of criticism hold you back. Never let it deprive you of your initiative to succeed;
- (e) when making a decision, consider its possible results and think about tomorrow as well as today. Obtain advice, sometimes it will keep you from acting rashly or make you aware of things that you hadn't thought about before. Having advisors is invaluable but that doesn't mean that every matter is one upon which you need their input. Hear them out, but do not automatically follow their advice without using your own judgement;
- (f) decisions don't make themselves. You can avoid making decisions by letting others decide or delaying the decision until it takes care of itself. But that is avoiding responsibility and prevents you from taking ownership of the problem and finding a solution. You should welcome the opportunity to make decisions in difficult situations while taking responsibility for their outcomes. These are your times to shine and make a difference;
- (g) what matters most is not what you do when

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The form is set up as a series of "Yes" or "No" questions so it is important to tick the correct response as they often build upon one another.

(a) this question establishes whether the employee was required to incur any expenses while fulfilling the duties of his employment. If the answer is "No" then the form need not be completed at all. A "Yes" answer is required even if the employer re-imburses the employee for some or all of his out-of-pocket expenses;

(b) this question concerns an employee's right to claim automobile or other travel expenses. If the employee goes to work each day and remains there the whole time, he will not be entitled to claim auto or travel expenses. This is because travel to and from one's primary place of work is not considered to be an allowable expense;

(c) this question inquires whether the employee was required to be away from his "normal" place of employment for at least twelve consecutive hours. This will establish whether he may claim his meals as an allowable expense;

(d) indicates the period of time the employee worked for his employer;

(e) this question focuses on whether the company paid a motor vehicle allowance to the employee and if such amounts were included in the employee's gross earnings for

everyone agrees with you, it's what you do when people do not agree with you. You can't please everyone all the time. Leadership means making choices that some people are going to disagree with. Everyone who makes decisions has to deal with people who don't like what was decided. Try to understand their feelings and explain them the rationale. Help them to see the good in the decisions they didn't like. But don't back down. If they cannot respect you or what you are trying to accomplish that will be "their problem";

(h) never be quick to anger and make decisions that you will ultimately regret. Look at the big picture and criticize only when necessary.

Control your temper. Before you do anything, stop and think about how you can handle things calmly. Don't just react and follow your emotions. Anticipate situations and plan accordingly.

Making decisions that affect your future at the "bat of an eye" on a daily basis is what makes entrepreneurship so exciting. Our culture admires individuals who have overcome hardship and become stronger and more self-reliant because of it. People who know what they want and take action to make their lives the way they want them to be. People who don't make excuses and blame others. This is the person you can become if that is what you decide.



Working Income Tax Benefit

My "favourite" part of the personal income tax return involves the taxpayer's claim for the Working Income Tax Benefit (WITB). Here are the details as well as a few situations where it can be applied.

WHAT: a refundable income tax credit for low-income Canadians who are working as an employee or are self-employed

WHO: taxpayers resident in Canada throughout the year, 19 years of age or older or married or living "common-law". The only exemption are students attending post-secondary schools for longer than 13 weeks during the year

WHEN: single taxpayers whose income is less than \$11434 or couples whose combined earnings are less than \$15790

HOW: see accompanying examples (using 2015 figures)

Example One: Self-employed, "using up" Basic Personal Amount

Sometimes when a taxpayer is just starting out in an owner-managed business, it takes awhile before he can start withdrawing funds and pay himself a "salary". But when it comes to filing his personal income tax he does not want to show his income as \$NIL and lose out on the over \$11000 per year that he can earn "tax free". See (a) below.

Example Two: Maximum refund for single taxpayer. Taxpayer contributes to the Canada Pension Plan, but not the maximum for the year. See (b) below.

Example Three: Maximum refund married/common-law taxpayers. Taxpayer contributes to the Canada Pension Plan, but not the maximum for the year. See (c) below.

	(a) \$	(b) \$	(c) \$
Self-employed income	12,502	7,028	10,316
Income taxes payable	893	NIL	NIL
Basic Personal Amount	(11,327)	(11,327)	(22,654)
CPP contribution credit	(446)	(175)	(337)
	(11,773)	(11,502)	(22,991)
Non refundable credits	(1,766)	(1,725)	(3,489)
Income taxes owing	43	NIL	NIL
CPP owing	892	350	674
	935	350	674
Less: WITB	(935)	(1,007)	(1,829)
Taxpayer refund	NIL	(657)	(1,155)



the year. These allowances are usually paid as a flat monthly amount or on a per kilometer basis. A secondary issue is whether the employee was supplied with a "company car" and to what extent did the company cover its operating costs;

(f) this question reports whether the employee was or will be re-imbursed for expenses incurred on behalf of his employer. It asks for the amounts and types of expenditures paid as well as whether these re-imbursments, if any, were already included in income. A supplementary question asks if perhaps the employee might have used the employer's credit card when incurring these expenditures and therefore might not be entitled to a re-imbursment at all!;

(g) this question centres on whether the employee might have received a re-imbursment for automobile expenses incurred rather than an allowance, as previously covered;

(h) this question asks the employer to report whether the employee was paid wholly or partly by commission. If so, how much did the employee earn as commission income and what services did he provide to earn these amounts;

(i) this question covers several areas of importance for employees who work under "employment contracts". They include whether he had to rent an office separate from that provided by his employer, hire

A Tale of Two Stations

It is not very often that we can see "behind the scenes" of large corporations, examine their behaviour and learn from their actions. Let me explain:

The date is Thursday, August 27, 2015 in Toronto, Ontario. Gas prices at the pump have been following an established pattern. The oil companies raise their prices for a few days and then gradually let them drop for a few days only to have them rise again. This has been going on for several years and the consuming public has learned to time their purchases accordingly.

It was announced on one of the websites that monitor gas prices in the city, that the price of regular gas was going to fall to 99.99 cents/litre on August 28, 2015 and increase to \$1.04.99/litre on August 29, 2015.

Once this became public knowledge, many customers topped up their cars on the Friday rather than waiting until Saturday when the price would be 5% higher. This was evident by the long lines of cars waiting at the pumps well into the late evening hours.

At Petro-Canada gas stations in the city, business was conducted as usual. They kept their pumps open as they normally do, notwithstanding the fact that the product already delivered to the station would be available for sale at a higher price the following morning.

Imperial Oil (Esso), in exactly the same situation as Petro-Canada, followed a different business model. They closed down all of their stations by 8:00 pm and were willing to forego Friday sales after that time. They were willing to risk antagonizing their customers by having them go elsewhere if they wanted cheaper gas. They knew the price was going up the next day and that they

would get higher margins the following morning.

So what do we learn from this story? Small and larger business owners must be cognizant of the big picture when making business decisions.

They have to know the market in which they operate. They must endeavour to satisfy their customers. But only so far. Most purchasers of gasoline look at Esso and Petro-Canada as selling identical products. Most purchasers fill up their cars when needed and will buy their product at whichever gas station happens to be nearby when they realize their car is getting low. The gasoline companies try to establish "brand loyalty" in their customers. But this is a losing battle. Customers will not go far out of their way to look for a particular company when the same product is being sold nearby.

The owners of Esso know this and can forego additional low margin sales for a few hours. There will be more customers tomorrow and they will pay the higher price because that will be the price charged everywhere else.

The owners of Petro-Canada do not understand this. To them higher sales figures are what matter. They do not consider the "bottom-line" in their decision making. Making low-margin sales is not profitable for most companies in the long-run. They should have tried to influence demand like Esso did. It would be interesting to learn how many "loyal" Esso customers filled up at Petro-Canada after eight o'clock that evening. And how many of these customers, in appreciation to Petro-Canada for selling them the cheaper gasoline that evening, took notice of how Esso treated their customers that day and switched their buying habits to Petro-Canada afterwards. My guess is "not very many".



The Going Concern Assumption

The business world is known for the rapidity in which things happen. A company may be profitable for a period of time but experience a reversal of fortune within a short period of time. There may be many reasons why this happens. Perhaps the company expanded too rapidly, assuming that ever-increasing revenues would automatically translate into ever-increasing profits. Or perhaps the company experienced a "bad debt" by selling on credit to a customer who promised to pay on time, then made excuse after excuse why their cheque was late and would always be issued "next week". Or perhaps the company's bankers

unexpectedly became nervous with the company's recent financial performance and balked in providing additional credit when requested by the company to meet payments to employees or suppliers.

Financial statements prepared by a business entity are based upon several beliefs, one of the most important being that the company will continue its operations into the foreseeable future. This is termed the "going concern" assumption. Without this understanding, users of the information contained in the financial statements would be hard-pressed to make long-term decisions about



staff in addition to those provided by his employer, and pay for his own supplies and telephone. To the extent that the answer is "yes", what portion of these amounts are to be re-imbursed;

(j) the issue here involves whether the employee is required as part of his employment to work from "home" and be re-imbursed for expenses incurred. The form asks for the percentage of time the employee is expected to work from his residence and the amounts and types of expenditures he has been asked to pay;

(k) was the employee a tradesperson and was he required to use his own tools in the performance of his duties?;

(l) was the employee a mechanic and was he required to use his own tools in the performance of his duties?;

(m) was the employee working in forestry and was he required to use his own tools in the performance of his duties?

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the company and would only concern themselves with the immediate time horizon. Management would lose its focus too, and concentrate on making plans whose outcomes would be determined only in the short term. Obviously paying attention only to the here and now will impair a company's long-term health and viability. And while past results are not predictive about what will occur "down the road", more often than not companies that have experienced strong, positive performances over the past while, will continue to do so. Unfortunately, companies in challenging times today are unlikely to reverse their

predicaments any time soon unless something dramatic has occurred.

Take a look at the condensed financial statements of ABC Incorporated over its past four years and the comments alongside them. Note the trends that appear to be developing and provide your own professional opinion whether you think its best days are behind it and whether it is likely to continue operations into the future. In other words, is it a "going concern" or a "dead company walking"? Your answer will be subjective as no one can say for sure what will happen tomorrow.



ABC Incorporated					
Financial Statements (in \$1000's)					
	2014	2013	2012	2011	
	\$	\$	\$	\$	comments/analysis
<u>Balance Sheet - Assets</u>					
Accts receivable	425	705	700	460	moving in right direction
Other assets	35	55	52	60	steady
Prop, Plant, Equip	860	1070	1070	1070	took amort first time 2014
	<u>1320</u>	<u>1830</u>	<u>1822</u>	<u>1590</u>	
<u>Liabilities</u>					
Bank indebtedness	525	590	550	560	remaining constant
Accts payable	1770	1154	880	470	dramatic increases
Loans payable	320	371			used to be \$NIL
Advances from sh	440	460	43	43	sh injected more \$
	<u>3055</u>	<u>2575</u>	<u>1473</u>	<u>1073</u>	
<u>Shareholders' Deficiency</u>					
Share capital	1000	1000	1000	1000	
Deficit	-2735	-1745	-651	-483	large accumulated losses
	<u>-1735</u>	<u>-745</u>	<u>349</u>	<u>517</u>	
	<u>1320</u>	<u>1830</u>	<u>1822</u>	<u>1590</u>	
<u>Statement of Operations and Deficit</u>					
Revenue	2860	3630	4230	5580	decreasing sales
Production costs	1200	2090	1800	3010	
Gross margin	1660	1540	2430	2570	up and down
Oper expenses	2440	2634	2598	2657	steady over time
Amortization	210				first time 2014
	<u>2650</u>	<u>2634</u>	<u>2598</u>	<u>2657</u>	
Net loss for year	-990	-1094	-168	-87	huge losses '13 and '14
Def, beg of year	-1745	-651	-483	-396	
Def, end of year	<u>-2735</u>	<u>-1745</u>	<u>-651</u>	<u>-483</u>	over \$2 m loss in 4 years
Note the trends. Is the company going in the right direction? Can it continue to operate at a loss much longer? Is it a "going concern" even today?					

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