JUNE 2021

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FAST TRACK

Entrepreneurship in the 2020's

One of the many things that people going into business have to think about is how they will structure the entity they ara about to create. Is the budding entrepreneur going to "fly solo" either as a sole practitioner or in a corporation where he is the sole shareholder? Or is he going to spread the risks and rewards with another

In this Issue:

Repayment of Government Benefits

One of the cornerstones of the Canadian income tax system is that we "self-assess" and declare to the government our determination of the income we earned in the year and the deductions and/or expenses we incurred.

This does not mean that from time to time we are not asked by the Canada Revenue Agency to explain how we arrived at our conclusions and to show evidentiary support. This is why the government employs auditors and "fact-checkers" to determine if the income shown and the expenses incurred are "reasonable" and according to the Income Tax Act.

During the past year or so the government has been generous in its support of Canadians who have been hit hard by the COVID-19 pandemic. One of the most "popular" programs provided recipients $500 per week for up to fourteen weeks. Called the Canada Emergency Response Benefit or CERB, it was administered either by the Canada Revenue Agency itself or Service Canada under the auspices of Employment Insurance.

When if first came out, it appeared to many that there were few obstacles to be able to collect these benefits. The pandemic was just getting started and no one really knew (or even today still knows) how long the virus will continue to plague our country.

Now that we have had some time to adjust, some recipients may have come to believe that they never should have received the benefits in the first place.

This may have come about if (a) you returned to work earlier than you originally expected; (b) your employer paid "retroactive pay" to make up for the time you were away from work; (c) you applied for benefits but really did not fit into the category of those for whom it was intended; or (d) you received payments from both the CRA and Service Canada at the same time.

In these situations, the government has instituted provisions that will allow you to repay these benefits in a timely manner by returning the funds to the agency from which they were paid to you.

When the benefits were received in 2020, recipients received a T4A slip from the government showing the amount of benefits received under CERB and similar programs that was to be included as income on the 2020 personal income tax form. The amounts were taxable to be included as "other income" for the year.

Should a taxpayer decide that he was not eligible for the amounts he initially received, he should repay the amounts in question and then re-file his 2020 personal income tax return to allow an offsetting "other deduction" to effectively cancel the income inclusion recorded earlier on the form.

This is very different from what we may have expected. The usual CRA practice is to recognize transactions in the year that they occur. If the re-payment was made in February 2021. we would have thought it would be treated as a deduction on the 2021 tax form.

This is not the situation here. The government has expressed a desire to "align" the income inclusion and the deduction in the same

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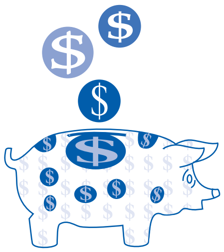


party under a corporate umbrella where two or more individuals come together as co-owners of the business that is about to open its doors.

A "true" entrepreneur is one who believes that he "works best" by being on his own and that his success or failure depends on him and him alone. It's not that he is a "loner" or "anti-social", it's just that he is fiercely "independent" with a streak of adventurism trying to show the world what he is made of. If things go well, he can take credit for all his accomplishments. And if things to do not work out exactly as he had hoped, he will learn from the experience and go on to another venture where where maybe he will have better luck.

In the past, and maybe in folklore, working on your own was always presented as the goal to which every businessperson should aspire. Success was all but

taxation year. The government will not penalize you if you return these amounts on your own volution. But if approached by an auditor or "fact checker" to justify your receipt of the funds, and you are found wanting for an explanation, you will be subject to penalties and interest for having received benefits to which you were not entitled.

CRA Error in the Taxpayer's Favour

In the original Monopoly boardgame, among the houses, utilities and railroads stands one spot where the player would be given $200 as a "bank error in your favour". This always came as a pleasant surprise in the game but even more so in "real life".

Here is an instance where we have "CRA error in the taxpayer's favour". Erin received $14000 in Canada Emergency Relief Benefits during 2020 and was happy to have the money during the early months of the pandemic when things were very much "up in the air" about the severity and duration of the virus.

As things progressed during the year, she was pleasantly surprised to receive a payment from a family investment in the amount of $50000.

Realizing that this "windfall" would be taxable, she made what she thought was a $7500 installment payment to the government on account of her income taxes for the year.

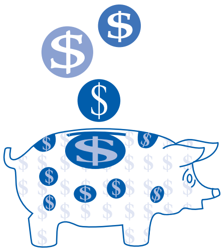
Perhaps through an error at the bank or maybe at the CRA, the $7500 payment was recorded as a partial "repayment" of the CERB that she had received, rather than as the tax installment that had been her intention. This meant that she received an income tax slip for $6500 from the government to be recorded on the form as opposed to the $14000 that she had expected to report all along.

It also meant that she had no longer paid $7500 in advance on what would ultimately be her tax bill.

The classification of this payment has very differing results. Scenario One looks at her income tax position as she had intended and Scenario Two reflects "what happened".

	Scenario One $	Scenario Two $
Employment income	17458	17458
Dividends from family investment (taxable portion)	57500	57500
CERB	14000	6500
	88958	81458
Can Pension Plan deduction	42	42
Taxable income	88916	81416
Income tax liability	12865	10605

The way things worked out, Erin was $2260 "better off" than she would otherwise had been. She had been awarded a "CRA error in her favour" and paid less taxes. The only drawback was that now she had to come up with the cash to pay off her liability (less the $1560 that had been paid through her employment). This amounted to $9045. Under her original plan, she would have only needed to pay the government $3805 on April 30 but her overall tax bill would have been higher.



guaranteed if one was willing to put in the necessary hours for his hard work to pay off.

No one thinks that way anymore.

Today's entrepreneur is more likely to "give it a go" for awhile but "throw in the towel" when problems appear. His "attention span" tends to be shorter and he will probably "go on to something else" if satisfactory results do not appear to be forthcoming within a foreseeable time horizon.

Today's folklore is that if you haven't made it by age thirty something, you probably never will.

Nothing could be further from the truth. Peoples' self-employment careers are starting later in life as they stay longer in school, work at a couple of jobs in their field to "learn the ropes" and gradually gain the confidence (and put away a few dollars) to go out on their own.

While It would be nice to have things work out great

Joint Ventures

Most people are familiar with the "usual" business arrangements in the marketplace. They know about sole proprietorships, partnerships and corporations. They are less likely to be knowledgeable about trusts and joint ventures, the latter of which is the subject of this article.

A joint venture is a business arrangement where two parties "come together" to work jointly on a business venture.

Each comes to the table with certain strengths, usually expertise or capital, in the hope that by working together with another business entity they will be able to accomplish more than what they might be able to achieve on their own.

The major difference between a partnership and a Joint Venture is that in most cases partners are seen to be jointly and severally responsible if the project upon which they are working runs into difficulties.

Let's say Partner A and Partner B are working together in residential construction. Six months after their project is completed, residents discover cracks in their foundations that have led to water damage in their basements. They naturally turn to the builders to fix the leaks in their houses.

Since the builders carried on business as a partnership, the residents would naturally look to the partnership entity as a whole to make things right in their homes. The builders are said to be jointly or collectively responsible for the problems that had developed.

If for some reason, the residents could not get satisfaction from the partnership entity as a whole, they could approach each of the partners individually to make good on the repairs.

The individual partners could not say that Partner A was responsible for roofing and Partner B was in charge of the foundation, so if problems developed in the basements the residents could only "go after" Partner B for satisfaction.

Residents have a claim against both partners individually to make good on their workmanship.

Since this is a partnership, the residents can approach Partner A individually or Partner B individually (termed "severally") to attend to their problems. Alternatively, they can seek a solution to their problem from the partnership as a whole (termed "jointly").

If the same scenario played out with Joint Venturer A and Joint Venturer B working together in residential construction, the disgruntled homebuyers would not have as many options to obtain the remedy to which they aspire.

Depending upon the wording of the Joint Venture agreement, it is likely that the residents would first approach the Joint Venture entity as a whole to make things right in their homes.

But if they were unable to get satisfaction at this stage, their only recourse is to "go after" Joint Venturer B because it was he who was responsible for the work on the foundations of the homes.

This was his contribution to the Joint Venture and the project. They are precluded from approaching Joint Venturer A to make repairs to their homes.

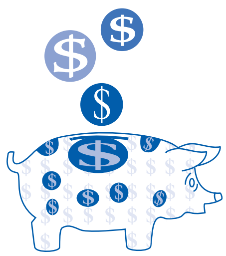
However, in the interest of maintaining a long-term favourable reputation in the industry, Joint Venturer A would probably be willing to assist the purchasers with the problems.

Risks and Rewards

Everyday the newspaper prints "the odds" on upcoming sporting events. It tells you how much you can expect to gain if one of the teams wins and how much you will realize if the other team prevails.

The reader makes a choice as to how much he will "put down" on the team that he favours.

For example, in a recent hockey game between the Toronto Maple Leafs and the Montreal Canadiens, the Toronto team was the "favourite" to win the game and the Montreal team was the "underdog".



from the "get go", turning a dream into reality is not easy and takes time. It also takes money. Fortunately, as you start off, your enthusiasm for the project will take you a long way and keep you going when obstacles start piling up. Here is where your ingenuity and resourcefulness will be tested and will ultimately define if you will "make it" or not. It will be your chance to see what you are "made of" and have what it takes to make it work.

Try to keep that passion for as long as you can. It will be what sets you apart from others who may have had similar dreams but never had the drive to pursue them.

Thanks for Your Referrals

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The newspaper showed Toronto as "minus 240" and Montreal as "plus 190". This means that a bettor would have to wager $240 and if the Leafs won, he would get back his original $240 plus $100.

Conversely, if the bettor chose the Canadiens, he would wager $100 and if the they won the match, he would get back his original $100 plus $190.

Armed with this information, the reader could choose to risk $240 and be rewarded with $100 or put up $100 and win $190. He could almost "double his money" if he selected the Canadiens or get a good payback, but not as much in percentage terms, if he elected to go with the Leafs.

He had only to decide by "game time" and the results would be known in about three hours.

Participation in this transaction would undoubtedly be termed "gambling", but does it differ that much from a transaction that involves the purchase of Bell Canada shares on the Toronto Stock Exchange?

Both participants have many choices as to how they can spend their money. Yet each of them deliberately decides to set aside some of those funds and put them in a vehicle that will hopefully get them back more than they had originally put in.

And, both participants undoubtedly weighed the "risks" and "rewards" associated with their particular choice against others that they may have considered.

Risk is the level of uncertainty that a particular outcome will occur. For the Bay Street buyer, this is his assessment as to whether the $20 stock of today will climb to $25 at some point in time and just how quickly it will get there. The same goes for the price of gold or any other asset about which he might be thinking.

For the participant in the "game of chance", risk is automatically factored in the price of "admission". Selections with the most "upside" are typically more costly. The bigger the payoff, the more expensive it will be to get involved (except for lottery tickets).

The reward for the Bay Street buyer is the $25 stock price that he anxiously awaits. For the "gamer" it is the "payout" that is associated with having a "winning ticket" when the numbers are drawn.

Here is a chart comparing the two activities.

	Gambling	**Investing**
Definition	staking money or something of value in the hope that a gain will result from an uncertain event	committing money or capital to an endeavour with the expectation of obtaining additional income or profit
Mindset	"...in the hope" (see above)	"...with the expectation" (see above)
Time Horizon	short-term	short or long-term
Ways of Participating	lotteries, bingo, sporting events. electronic gaming machines	purchase of property or financial assets
Timeline	have to commit very quickly, "you can't win unless you have a ticket"	no particular time to "get in" or "get out", depends on "gut feeling"
Risks	can sometimes be quantified	can sometimes be quantified
Rewards	that what he "lives for"	can be a "side line" or perhaps more

The differences between the two are in the mind of the participant. Is he "hoping" or is he "expecting"? They are not the same thing. At the moment, gambling is still illegal except in cases where the activity is being operated by the government. That never seems to stop anyone from participating if he so chooses.

There are some investing rules about "insider trading" and concerns about a "level playing field" for the "little guy" compared to the "big boys". But that never seems to deter anyone from participating if he so chooses.

How much do you want to bet that these activities are never going to change?