TAXATION

Convention Expenses

Many owner/managers, employees and self-employed individuals are now planning their attendance at conventions throughout 2005.

If you are planning to attend a convention this year, be sure to consider the tax implications of the costs in view of the applicable taxation rules. Some convention expenses are deductible in whole and some in part. Other expenses may be considered personal and not eligible to be deducted as business expenses.

Under the *Income Tax Act*, reasonable expenses incurred for an individual's attendance at professional or business conventions and conferences are tax deductible for corporate businesses, self-employed individuals and partnerships if attendance is for a business purpose. However, some restrictions apply for meals and entertainment and the additional costs of your spouse or partner accompanying you. Employees who attend a conference for business purposes may or may not have a tax liability for convention expenses covered by their employer, depending on the circumstances.

Convention Fees

While generally you may deduct convention fees and all travel and accommodation costs in their entirety, you may only deduct the costs of two conventions in any one year. A corporation is generally subject to the same two conventions per year in connection with its business but it may send more than one representative to each convention. However, the CRA's administrative position is that the limit is applied to each business interest of the corporation. For example, the limit of two conventions for a large corporation would apply to its various business interests of personnel, accounting, production, etc.

For tax purposes, the conventions must:

- Relate to your business or professional activity; and
- Be held by a business or professional organization within the geographical limits of where the sponsor of the convention usually carries on business.

This second limit means that a convention sponsored by a Canadian business or professional organization must be held in Canada where the organization is national in character or in the particular province, municipality or area if the organization's activities are limited to such an area.

Expenses incurred attending a convention held outside the geographical limits of the Canadian organization will normally not be an allowable deduction. However, under the Canada-United States Tax Convention, expenses incurred by a Canadian resident or citizen attending a convention sponsored by a Canadian organization and held in the U.S. are treated as if the convention were held in Canada if the convention is held by a national organization. A provincial organization holding a convention in the U.S. would be outside of the territorial limits of the organization and the expenses therefore would not be deductible.

In addition, you can deduct reasonable expenses incurred for attending a convention in another area or country if the convention is sponsored by an organization of that area or country and it is related to your business or professional practice.

If your spouse or children accompany you to a convention, these expenses are normally considered to be personal and, as such, are not deductible. Similarly, the incremental costs of a vacation, which are combined with the convention, would not be deductible.

Meals and Entertainment

The registration fees for a convention will sometimes include the cost of food, beverages, or entertainment. If these amounts are not shown separately on your bill, you must subtract $50 from the total convention fee for each day the organizer provides meals and entertainment. You can then claim this amount as an expense under meals and entertainment, of which 50% is deductible. (Note that incidental items such as coffee and doughnuts that the organizer provides at meetings or receptions at the convention are not considered to be meals and entertainment.)

You can also claim the costs of meals and entertainment that are not included in the convention fees, subject to the 50% deduction.

Employee Attendees

If your employer requires you to attend a convention and you are reimbursed for your costs, the reimbursement is normally not taxed in your hands. You are not entitled to deduct any of the costs of attending a convention in computing your own personal income. However, some portion of the amount paid by the employer could be considered a taxable benefit in some circumstances, for example, if the employer covers any of the costs of your combining a holiday with the conference.

If your spouse or partner accompanies you to the conference and your employer pays, or reimburses you for this additional cost, the amount is considered a taxable benefit in computing your personal income. The exception is where your employer has requested that your spouse accompany you to help you achieve the business objectives of the trip. In that instance, the amount paid for your spouse's travel and accommodation would not be considered to be a taxable benefit.

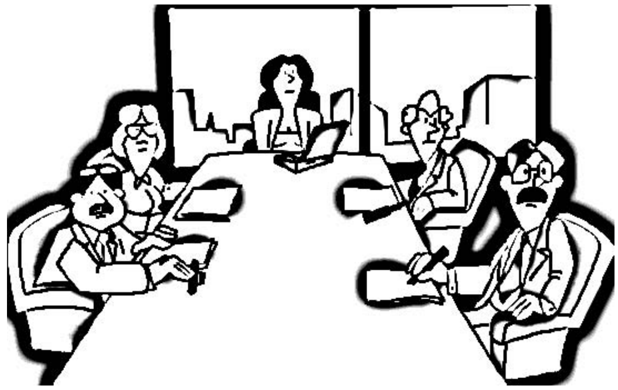
Some Tax Tips

Make sure you can back up your convention expense claims.

- Keep your convention registration form and receipt, session outline and receipts for travel, accommodation and other expenses.
- If the registration fee will include meals and entertainment, ask if these costs are shown as separate items on the receipt. Otherwise, the $50 a day rule applies.
- If you attend a conference outside of North America, make sure you can show the relevance of the convention to your business.
- If you combine a vacation with a conference, be sure to keep separate records of your personal versus business expenses. While the business expenses are deductible, the personal expenses for the vacation portion of your trip are not. If you are an employee, the personal portion is considered a taxable benefit and taxed in your hands.
- If you are an employee and your employer requests that your spouse accompany you to the conference, ask that this request be provided in writing and keep this with your other conference documentation.

Conventions can be revitalizing and can help boost your productivity. They not only help you find practical strategies and solutions that can be applied to your business but also offer valuable opportunities to learn about new materials and products as well as share ideas with others in your sector. Since the rules limit the deductibility to just two conventions each year, carefully research the many offerings to ensure you maximize the investment of your time and money. ■

Company Shares



Owner/managers of incorporated businesses know that they own the company, but at times may not be as familiar with some of the concepts regarding shares.

Under the *Canada Business Corporations Act* (CBCA) a corporation will have shares. The corporation is not required to have common shares, special shares or preferred shares, but rather it is only required to maintain shares. Most of the provinces' provincial legislation regarding share capital is very similar to the CBCA; however, there are differences. It is important to ensure that the corporation properly complies with the laws of the jurisdiction under which it is incorporated.

In many private companies, the owner/manager controls the corporation and may be the only shareholder. However, as the corporation is considered to be an entity unto itself, the shareholder must not treat the business as if all the assets were the assets of the shareholder.

Generally there are two types of shares issued from a corporation, common shares and preferred or special shares.

Common Shares

Where a corporation maintains only one class of shares, these shares must be entitled to vote at meetings of shareholders and must be entitled to the residual value of the corporation on liquidation. These shares are common shares. If there is more than one class of shares, it is possible to separate these attributes.

Common shares represent the residual capital in the assets and earnings of a business. Traditionally each common share has one vote. In most owner-managed businesses, the original common shares issued would have nominal value, say $1 per share.

Common shareholders have the final say in the operations of a company. Normally a 51% majority is required to approve major events in a company, such as electing directors, liquidating the company or selling major assets.

Rights of Common Shareholders

There are certain rights or advantages to being a common shareholder. These rights or advantages can be modified within the bylaws or within the shareholders' agreement but generally include:

- The ability to dispose of share holdings.
- The right to vote.
- The right to elect directors.
- The right to attend company meetings.
- The right to receive copies of the company's annual report and financial statements.
- The right to share in the company's growth, earnings or assets of the company.
- The expectation of limited liability.

These rights are not without a cost. Common shareholders can have no expectation in the profits of the company unless the dividends are declared by the directors. If a company is doing well, dividends are usually paid out of profits. Conversely, if profits do not exist, the company will not declare a dividend, and in some instances, may be prohibited from doing so. Add to this risk that should the company not be successful, common shareholders have little hope of recouping any of their original investment.

Many start-up entrepreneurs issue common shares to family members. This may be done, for example, to provide the ability to declare dividends to more than one person.

When considering the share structure of the company, the owner/manager should consider the rights of all common shareholders. Regardless of the number of shares held, common shareholders have rights that, if exercised, could create operational headaches for the majority shareholder.

Preferred Shares

Preferred or special shares have a differentiating factor in the special right or rights attached to these shares. For example, if a share is entitled to priority on liquidation, this share would be viewed as having preference over other shares. There are many attributes that can be attached to preferred shares, such as they may not be entitled to vote at a meeting of the shareholders or be restricted in the dividends that can be received.

Preferred shares are usually designed to be more secure than common shares that carry no guarantees as to their worth or the return on investment. For instance, it may be that the preferred shares must be paid a return of 5% before common share dividends could be paid out.

For most owner/managers, the use of preferred shares is not considered in the original incorporation of the company. Later, as a company becomes more successful and starts to accumulate value, preferred shares along with common shares may be used to create holding companies to protect the assets of the operating company and therefore the shareholder (owner/manager). This reorganization is often referred to as a Section 85 rollover as it utilizes that section of the *Income Tax Act.*

The Shareholders' Agreement

The shareholders' agreement governs the rights and obligations of the shareholders and as such, is a very important document. Among the many provisions specific to the corporation that are contained in this agreement, some rights and obligations arise due to the governing legislation. If the corporation is provincially incorporated, the applicable provincial legislation will apply. If the corporation is federally incorporated, the federal legislation will apply.

The agreement usually covers such matters as the amount of issued stock, names of shareholders and the amount and class of shares that they own. Other matters include necessary approvals by shareholders, nominees of shareholders and buy/sell provisions as well as organizational matters such as number of directors, name of chartered accountant, location of books and records and the cap on indebtedness that the corporation can incur.

Regardless of whom the shareholders are, whether your spouse, friends or business colleagues, it is imperative to have your lawyer draft a comprehensive shareholders' agreement. Areas that may be addressed include matters such as the amount of capital invested, the ability to sell shares to outside parties, distribution in the event of the death of a shareholder, and operational responsibilities such as signing authorities, debt and capital purchases. Formalizing these issues in the agreement will reduce the likelihood of conflict points during operations and will provide guidance in the event of the death of one of the shareholders.

Be sure to get advice from your lawyer and chartered accountant to determine the best means of protecting the rights and privileges of the company's shareholders now and in the future. ■

TECHNOLOGY

The Phish E-mail Trap

The latest means of scamming the unsuspecting e-mail recipient is an old boiler room tactic that has been "slicked up" from a telephone con and applied to e-mail.

Unscrupulous e-mail transmissions are being sent that are designed to fool the individual into believing that they have received a legitimate offer or information request and elicit a response. Known as phishing, these devious e-mails are used to lure victims into revealing their personal financial data. Basically, these online criminals use these e-mail transmissions as the bait when "fishing" for ways to steal your money, credit and even your identity.

The Scam

By disguising the e-mail message to look like a legitimate communication from a well-known company, the sender seeks out personal information such as your social insurance number, your address, bank account numbers, passwords or credit card numbers. The e-mail might ask you to review your account with a warning that failure to do so will result in future problems or even cancellation of services. Sometimes the e-mail will promote an attractive contest for which you must complete an online form.

To ensure that the offer looks credible, the thieves have gone so far as to include an e-mail link to "look alike" websites that imitate the real organization's logo and format. The phony site may look credible but, in reality, the site is controlled by criminals.

Sometimes the scam is in the form of an e-mail that masquerades as a request from your financial institution. To motivate a response, the e-mail may caution that your credit line is going to be cut or services terminated if the requested information is not provided immediately by clicking on the link and completing an online form. Given today's busy schedules, many times the victims will quickly fill in the electronic form simply to get rid of the problem without further investigation of the legitimacy of the e-mail request.

How Can You Protect Yourself?

Since you would not reveal personal, financial and private information to just anyone who asks, do not provide this information online.

To protect your privacy, money and identity:

- Be wary of any e-mail that looks suspicious or out of character.
- Do not respond to e-mailed requests for personal and financial information.
- Do not use the link provided in a suspicious e-mail or complete an online electronic file.
- Call the company or the financial institution to verify that the information request was sent by e-mail. Do not use the telephone number provided on the e-mail as it too could be phony.
- If the request is legitimate, go directly to the company or institution's website and log on there. Type in the website in your browser. Do not use a link that has been provided in an e-mail.
- If an e-mail request for personal information appears to be sent from a representative that you know, send a separate e-mail to that person confirming that the request is legitimate. Do not click on reply. Better still, call that person directly.
- If you must transmit sensitive information online, make sure the website is secure.
- Do not send e-mails containing sensitive personal, financial or private information unless you know it is safe, e.g., use encryption.

If you have responded to an e-mail request for personal information that turns out to be phony, take immediate action:

- Report the crime to your local police immediately.
- Contact your financial institution and change all your PINs, access codes and passwords.
- Contact the credit bureaus. Call directly or go to their websites:
  – Equifax Canada at www.equifax.com
  – TransUnion Canada at www.tuc.ca.

Phishing is yet another spin on fraud and identity theft. Take extra precautions before responding to any e-mail that requests sensitive financial and personal information. ■

MONEYSAVER

A Better Bottom Line

February is the ideal time to review the lessons learned from the past year and set strategies in place to improve this year's results.

An excellent starting point for finding ways to improve the bottom line is to compare your current income statement with those of the previous year. Just as the balance sheet gives you a snapshot picture of the financial condition of your company at a point in time, the income statement shows you the results of your financial operations over a month or quarter, half, or a full year. The income statement is sometimes referred to as the profit and loss statement.

In addition to the income statement, you should also generate a report showing the ratios of expenses to sales and/or ratios of change of sales and expenses on a line-by-line basis and do a comprehensive review of the changes that have occurred.

When reviewing your sales and expenses, focus on any variations, whether they are positive or negative. Past experience will likely direct you to the following high dollar areas.

Sales/Revenue

A review of sales is an integral part of any financial statement analysis. Separate sales into the various categories or services to determine which product lines or services are moving forward and which are lagging behind. This will help you determine if certain product lines or services require more marketing and sales efforts or whether they should be modified or dropped.

Cost of Goods

The cost of goods section is another useful area to review. The proper allocation of expenses, including wages and other costs directly associated with manufacturing a product or providing a service, lets you determine whether the mark-up on goods of services is adequate. If you have several lines of products or services, review each line separately in view of the revenue earned. This will provide additional support in determining whether to invest more money and effort or drop a product or service.

Wages and Benefits

Analyze significant changes in wages and benefits. Are increases created by increased costs for overtime, hourly rates or WSIB, EI or health benefits? Are decreases a result of sub-contracting work? It may be necessary to complete a more in-depth analysis by examining the component parts of the actual account.

Review your past expenses for temporary and seasonal staffing. Have your staffing requirements changed and it is time to bring more people on board?

Office

Review recurring costs such as general supplies, subscriptions and software updates. If you are leasing equipment, determine if it would now be more cost-effective to purchase new or used equipment.

Travel

Travel expenses warrant careful attention. Review travel expenses in view of the amount of business the travel actually generated. To determine areas where travel expenses could be reduced, look at the specific components of these expenses. There may be opportunities for trimming some expenses and modifying any caps, such as daily expenses for meals. Be alert to significant increases in any category as this may indicate misallocation or expense abuses.

Analysis is more difficult if an account includes too many categories. This may be an ideal time to set up additional accounts within the general ledger to allow a more comprehensive analysis of specific expense categories in the future.

Vehicles

If repairs and maintenance expenses are low, consider whether you need to budget for increases in these expenses. Could some vehicle expenses be reduced by changing routes or reducing or combining routes to see specific customers?

If vehicle leases are close to renewal, consider whether you should buy-out the lease, renegotiate, or change leasing companies. Is automotive insurance posted to the account and is the coverage adequate? If vehicle expenses are an essential part of production costs, should the allocation be moved to the cost of goods sold?

Management Salaries

Review your salary, bonuses and any dividends received and the remuneration of family members who are involved in the business. If you expect the cash flow or profits may be tight this year, consider reducing your outlays. Review your remuneration planning with your chartered accountant as changes may have an impact on your personal income taxes for the calendar year.

Communications

If your communications expenses, such as Internet and telephone services, have been increasing, can you reduce or renegotiate your rates and services? A package deal or bundle of features may be less expensive as well as better meet the specific needs of your business.

If long distance charges have been allocated to specific customers, projects or business functions, this breakdown will help you identify potential ways of reducing costs. For example, long distance faxes and certain calls can be completed after peak hours or the information can be transmitted by e-mail. If cell phone expenses are greater than anticipated, purchase blocks of time. Alternatively, consider replacing some cell phones with pagers.

Interest

When interest costs are appropriately allocated, you can determine the sources and make adjustments. If, for example, most of the interest expense comes from carrying balances on credit cards, are the cards being used to finance operations? Consider using a line of credit, which can be obtained at a lower interest rate, and pay the credit card balances in full each month.

Track, Control and Manage

For owner/managers, a financial analysis of the past year's results aimed at reducing costs or improving services is a worthwhile management exercise. This comparison and analysis can help you identify trends, determine those revenues/expenses that are not consistent with expectations and highlight areas that need attention in your budget planning. ■

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