

INDEX

MANAGEMENT

Tough Times

TECHNOLOGY

Is it Remotely Possible?

TAXATION

Are We Living Together?

MONEYSAVER

What Am I Going to Do?

MANAGEMENT

Tough Times

Fraud is a constant threat to any business whether times are good or, as they are now, bad.

In bad times employees who might not otherwise be tempted to commit fraud may become so worried about their jobs and personal finances they might be tempted to exploit weaknesses in internal controls to steal money or inventory. This is the time when the so-called "trusted employee", shielded by a reputation for reliability but performing duties, which in larger firms would be segregated, may cross the line into dishonesty. As a result, owner/managers who in the past paid little attention to accounting controls, are advised to pay closer attention to the various accounting cycles, especially the cash conversion cycle.

Every owner/manager should know what is going on day to day in areas remote from operations. Some things can be checked out quite easily and quickly. For example, are all suppliers and customers known? Do any have similar names such as "W. A. Smith" and "W. B. Smith" or unbusinesslike addresses such as P.O. Box numbers or private residences? Such simple reviews give a "feel" for company transactions that may raise questions when something seems amiss.



Each business has a unique accounting system for tracking its own types of transactions but some areas are common to all businesses and should be looked at regularly. Consider the following areas, which are vulnerable to fraud.

Accounts Receivable

Because the likelihood of collecting aged receivables decreases with time, aged receivables should be reviewed every two weeks. Any receivable older than 60 days needs to be examined to make sure it has not already been collected and applied to the incorrect

account. Payments in unusual amounts may indicate misappropriations or the presence of a “lapping” scheme. Lapping is a fraud in which funds received from one company are used to cover funds misappropriated from another company. Large accounts should be reviewed for unusual payment amounts and reconciled with the invoices.

Ensure that the accounts receivable control account in the general ledger agrees with the aggregate total of the accounts receivable sub ledger. Most integrated accounting systems ensure that the control account is updated when entries for sales, payment or adjustments are made to the specific customer file. Enterprising bookkeepers can, however, override the automatic link from the sub ledger to the general ledger thereby falsifying the overall accounts receivable.

During the accounts receivable review any unusual adjustments or accounts that take the form of credits, bad debt write offs, or other adjusting journal entries should be noted and followed up.

New clients should have assigned credit limits; credit checks should be run and the new customer’s place of business visited to establish authenticity. These simple precautions will reduce the possibility that your inventory will be “sold” to a new client who has set up shop solely to get product and dispose of it at a deep discount without paying your bill.

Personal Accounts

Owner/managers are notoriously casual about keeping track of their personal expenditures and withdrawals. Enterprising staff can cover up their own misappropriations by processing phoney expenses to your expense account or by charging missing funds to the draw account. Not only is your company out the funds but the owner may also end up paying personal income tax on the draw.

The “Till”

In any retail business the cash drawer must be reconciled daily. Cash, cheques, debit, charge card, and “out of till” disbursements should be recorded each day and the tape amounts reviewed and reconciled. Shortages and overages should be recorded on the reconciliation.

At the end of the month bank deposits should be reconciled to the daily tapes to ensure no funds have been removed between the till and the bank deposit. Discrepancies should be investigated and staff informed that shortages have been discovered.



All overrides should be reviewed to ensure that a dishonest manager with override authority is not selling deeply discounted merchandise to accomplices for a subsequent street sale or a return to get a refund at the full retail price.

Reconciling Bank Accounts, Term Deposits and Lines of Credit

Management must review all bank accounts monthly. Miniaturized photocopies of cheques now provided by most financial institutions make it possible to review quickly the payee, amount, and authorizing signature. Such an examination will catch cheques paid to unauthorized suppliers or approved with fraudulent authorization.

Kiting is a fraud that takes advantage of the time needed to clear a cheque. The fraudster deposits money in Bank A with a cheque written on Bank B then deposits money in Bank A with a cheque written on Bank B. The delay in clearing the cheques enables the fraudster to steal the cheque amount while no money is actually in either account. Although the use of electronic transfers make this fraud more difficult to commit, unscrupulous employees can still take advantage of the time delays between processing paper work for term deposits or lines of credit to cover shortages in bank balances. Statements for all the banks used in the business should be reviewed simultaneously to pick up on unusual deposits, transfers, or redemptions of GICs or other investments. The bank should be notified

immediately of any unauthorized purchases or redemptions of short-term investments.

It is also important to understand how the company's line of credit works and know the upper limit set by the bank. Lines of credit that are automatically accessed for a prearranged amount when your operating account goes into a negative balance provide an easy way for an employee to cover any theft from the company bank account, especially if management is not provided with the line of credit statement.

Transfers between all bank accounts should be reconciled. Many fraudulent transactions are intentionally committed near month end to enable the fraudster to cover the misappropriation by indicating that it is an outstanding deposit or cheque in transit. This usually leaves 30 days time for management to forget about the discrepancy or for the employee to cover the misappropriation.

Accounts Payable

In an accounts payable fraud the business honours fraudulent invoices for goods or services never ordered or for goods ordered but delivered to another site and subsequently sold. To guard against these possibilities owner/managers should consider the following:

1. Purchase and credit limits should be established for each approved supplier. This will discourage dishonest personnel from purchasing unauthorized material and selling it or taking it back for refund.
2. Follow up on invoices with names that are similar to actual suppliers or with unfamiliar addresses. Scam artists often mass mail invoices with logos and names similar to real suppliers but with different addresses. An accounts payable clerk may simply write out a cheque for the fictitious but similar invoice and the unsuspecting owner/manager signs it. This deception occurs frequently during the renewal of contracts for Internet, magazine, telephone, or newspaper advertising.
3. All statements from suppliers as well as the accounts payable sub ledger listing should be reviewed. Unusual purchases or returns should be queried as should any accounts not paid within 60

days. The account may be in dispute, but it is also possible that payment has been diverted to another account to cover up a misappropriation.

Expense Accounts

Padding of expense accounts for personal gain has been around since the beginning of time. Expense account and travel costs, including vehicle costs, should be closely reviewed.

Payroll

Payroll fraud is not normally an issue for smaller businesses because the boss normally knows everyone and it is virtually impossible to add ghost employees to the roster. Just the same, it pays to review payroll records and employee data stored in accounting programs to ensure the business is not paying for non-existent employees, unauthorized overtime or a raise.

Owner/managers should approve all hiring, dismissals and pay grade assignments or changes. Without this surveillance, the payroll system could easily be used to defraud a small business. Not only are the salaries and wages lost, but also the associated CPP, EI and workers compensation costs may have to be absorbed.

Review Your Financial Statements

Management should review the company income statement and balance sheet every month. Accounting software can now easily generate month-by-month and year-to-date comparisons, ratios, percentage changes and budgets; areas of concern can become visible sooner and follow up can be faster than ever before. Any issues of concern should be referred to a chartered accountant.

Owner/Managers Must be Proactive

An owner/managers' active involvement in all aspects of the business not only allows management to take the pulse of everyday business operations but also reduces the probability of employees taking advantage of lax protocols. Prevention of fraud is less expensive than the time and effort required to recoup lost assets, dismiss dishonest employees, file police reports, replace employees, and absorb any increase in insurance premiums. ■

Is it Remotely Possible?

The need to communicate has never been as important as it is now.

An increasing number of employees work from home or at remote jobsites and clients need immediate support. The development of remote-access software eliminates much of the need for face-to-face meetings, makes it possible to work with reduced staff, limits unnecessary travel, and advances the greening of business.

Any company providing client services such as accounting, reviewing documents or modifying plans or quotes should certainly consider providing its employees with remote accessibility. Remote desktop access allows a user to take over the remote computer and make instantaneous changes to data. Naturally, the host must be present to key the proper sequence to allow commencement of operations and can, at any time, with a simple keystroke or mouse-move, stop the process.

There are many questions a business owner should ask before deciding on the appropriate application or suite:

1. Is there support for different operating systems such as Mac OS, Linux, Unix or Windows?
2. Can the user easily synchronize files and folders between the remote and host computers?
3. Is the user-interface easy to use (such as the ability to transfer files back and forth using drag and drop)?
4. Can multiple monitors be used to view data from the remote computer on a secondary screen? (This effectively provides two large working areas, avoids confusion, and eliminates the need to work through a split screen or windowed application.)
5. Can the user print data from the remote computer to the host printer without installing the printer software?
6. Can the host computer view and control the remote computer?
7. Does the software support mobile devices, such as a Pocket PC, PDA or smartphone?
8. Does the software allow remote-guest access to view presentations or participate in online conference calls?



9. What is the cost per user and total cost of acquisition?
10. Can an administrator track and suspend users at any time?
11. Will users be able to gain access from anywhere in the world?

Security Should Not be an Issue

Does the software “play nice” with your firewall? Compromising security at either end of the connection could have detrimental consequences such as viral infection and increased vulnerability to attacks. Ensure that the application supports password protection and encryption and does not degrade the security of your network.

Pricing Your Needs is Tricky

Prices for remote-access software applications and suites can vary widely, from free to hundreds or thousands of dollars per year. Determining your needs first will enable you to make the most cost-effective choice for your business.

Trial by Fire

For those who may doubt the usefulness of such communication packages for their business, most companies offer a free trial period (usually 30 days) to demonstrate the ease of use, and overall usefulness of the product. Take the trial offer, as it will certainly provide assurances as to the value for your company.

Although the need for face-to-face human contact will never be replaced, the ability to remotely access a computer or network from anywhere in the world and communicate with coworkers is already widely available and will soon be ubiquitous. From reducing travel costs to increasing efficiency, remote-access software has its place in today's business environment. ■

Are We Living Together?

Head in the stars, feet off the ground – love is a beautiful thing!



It is indeed, but love also has some pretty banal earthly aspects that need to be looked into before that love becomes a living arrangement. Any two people contemplating marriage or merely living together for the long term should be aware that each type of relationship carries legal and tax implications. So, before getting too financially involved, the parties should pull together their respective financial information and meet with their lawyers and chartered accountants to discuss the implications of what they are contemplating.

Marriage, Common Law and the CRA

But how are these relationships defined in law? The term spouse has been reserved for a legally married couple; determining when two individuals are considered to be living together as common-law partners is a bit more complex.

For tax purposes the individuals in a common-law partnership (same or opposite sex) must have:

- lived together in a conjugal relationship for at least 12 consecutive months
- had a birth child together or adopted a child
- a child wholly dependent upon one of the individuals in the relationship and the other individual must have custody and control of the child.

Once married or determined to be common-law partners the Canada Revenue Agency does not differentiate for income tax purposes.

Partners in either type of relationship will see changes in many deductions and tax credits to which they were accustomed as single tax filers. Some changes are beneficial while others appear to penalize those whom love has brought together. Some common changes that each partner should review for their possible impact on the individual and the family unit are as follows:

Partners in both types of relationship may now make **RRSP contributions** to the other partner's RRSP. The result is a reduction in the contributor's taxable income and a consequent reduction in tax liability while the recipient is permitted to build a tax deferred RRSP nest egg. Couples should be aware of the rules concerning ownership of the plan and withdrawal from the plan before contributing to their partner's RRSP.

Individuals earning less than \$25,000 per annum are recipients of GST **rebates** approximating \$250 per annum. Once it is determined that individual taxpayers are married or in a common-law relationship, the GST calculation becomes based upon the combined income of the two partners; the GST benefit attributable to two "unmarried" individuals each earning \$25,000 is greater than the GST attributable to a "married" couple with combined earnings of \$50,000.

There are **tax credits**, including age credit, disability and tuition (to name but a few) that are transferrable to a spouse or common-law partner if one individual in the relationship cannot use them.

Many employers provide a \$10,000 tax-free **death benefit** payment to the surviving spouse, partner, or child of the deceased employee. If two friends living together do not meet any one of the conditions that define a common law partnership, the tax-free benefit may not be paid.

Medical expenses: are deductible once the aggregate of the expenses exceeds the lesser of 3% of net income or \$1,962. Those couples who meet the married or common-law criteria can transfer medical expenses to each other to attain an overall benefit. Similarly, **donations** made by individuals within a relationship can be transferred to the tax return of the other taxpayer if tax benefits accrue.

When an individual dies: the value of an RRSP and capital gains deemed realized upon death are taxed in the year of death. If the amount is large, it can create a hefty tax bill when added to any other income earned during the year of death. If the deceased is married or a common-law partner, RRSP amounts are transferred to the survivor's RRSP tax free. Capital items can, depending upon the decision made by the spouse or common-law partner, be transferred to the survivor without tax consequences.

Principal residence may be a pressing issue:

Whether married or in a partnership the Tax Act allows for only one principal residence. This means that, if each partner possessed a residence at the time of union, one residence will be subjected to tax on capital gain at the time of sale. This does not imply that one of the units should be sold just because of the union, but it does suggest that individuals should consider the tax implications of holding a second residence including a cottage.

A single parent who marries or enters into a common-law relationship will lose the *equivalent-to-spouse*

credit of \$10,100 for the 2009 taxation year. Further, if the single parent enters into a relationship, does not earn income, and circumstances permit the payment of child care by the major breadwinner, the child care payments will not give rise to a tax deduction for the individual paying tax on earnings because such payments must be deducted by the lower income "spouse".

For older individuals entering into a new relationship, the ability to *split pension income* with a partner who earns less can provide significant tax savings not permitted if the individuals were just friends.

Dispel Those Urban Myths

Meeting with your chartered accountant before entering into any kind of a long-term conjugal relationship is an excellent means of clearing up urban myths about the positive and negative aspects of splitting various items of income and deductions. Furthermore, the knowledge a chartered accountant gathers during the initial meeting will allow consideration of strategies that may prove beneficial to both partners as their lives together progress. ■

MONEYSAVER

What Am I Going to Do?

The death of a spouse is one of life's greatest stressors. Not only do you have to deal with the physical and emotional void, you must also deal with the details of winding up an estate.

In the midst of sudden grief, the banality of searching for the information needed to close the deceased's estate may be an intrusive and even offensive process. On the other hand, making the necessary phone calls may start you on your path through the stages of grief.

However the process of winding up the estate affects you, you will need to reach out for information and should call:

Your Accountant

Your accountant may have information concerning investments, RRSPs, and insurance that may lead



you to others you must call. You will also need your accountant's advice concerning the tax consequences of your spouse's death: the effect on the deceased's final return, and the potential impact on your own taxable liabilities. It is always advisable to discuss how the liquidation of assets, investments or government-sponsored savings vehicles, such as RRSPs or RESPs, and HBP's will impact the deceased's estate and perhaps even your own income taxes.

Your Lawyer

Your lawyer will probably have the original copy of the will and may even have been named executor. Your



lawyer can also provide insight into your responsibility for paying any outstanding debts incurred by the deceased. The will can be expected to provide details as to where assets, insurance policies or investments are held and name contacts.

The Funeral Home

Funeral arrangements can be expensive. Make sure you know the funeral costs in detail. The funeral director may allow you to defer payment until funds are available through the executor or the estate. Ask the funeral home for copies of at least twelve certificates of death since banks, insurance companies and government agencies will require proof of death.

The Bank

Notifying the bank of the death will freeze all accounts and access to any safety deposit box that might hold jewelry or evidence of investments. This action by the bank ensures the estate is intact for the executor and eliminates the possibility of unscrupulous individuals withdrawing funds or valuables.

The Financial Advisor

The company handling the deceased's investments must be contacted. The advisor will be able to provide the portfolio, its market value at the date of death, the

adjusted cost base and whether the assets are held solely or jointly. This information will enable your tax advisor to calculate the deceased's tax liability, if any, for submission of the final return. This information is also necessary for determining any effect on the survivor's tax position.

The Deceased's Employer

If the deceased was employed at the time of death, the employer will have to be notified. There may be accrued remuneration and vacation pay owing. For many, there may be insurance policies, pension plans, death benefits, that is, payments for built-up sick-leave credits owing, if the deceased had not yet retired, and payments acknowledging the deceased's service. You will also want to determine whether medical, drug and dental insurance continue for the immediate family. If the deceased had been a union member, the survivors might be entitled to union benefits.

Human Resources and Social Development Canada

The survivor should contact HRSDC as soon as possible after the loved one's death to claim the one-time lump sum death benefit of \$2,500 as well as the survivor's pension and children's benefits. The survivor's pension is based on the deceased's contribution to the

CPP. The monthly children's benefit for all children under the age of 18 continues while the children attend school full time.

A low-income survivor between 60 and 64 may apply for an allowance based on the previous year's income. Payments traditionally start six-to-12 weeks from the date of application. Early application is suggested as there may be difficulties receiving back payments exceeding 12 months. At age 65 the allowance changes to the Old Age Security pension. Once the survivor is receiving the OAS pension, application may be made for the Guaranteed Income Supplement.

Seek Objective Advice from Your Accountant

Emotional support and practical advice are much needed when a loved one dies. The emotional support can be garnered from family members or close friends, but it is best to speak with an independent and unbiased outsider such as your accountant for objective advice.

Your accountant can provide an informed opinion of the assets available and their liquidity, as well as the amount of income that you and your family will need to pay the continuing expenses. This information will enable you to judge which assets may have to be liquidated, the tax impact of any sale, or whether it would be better just to use short-term borrowing to bridge any period of low income.

Help and Understanding is There for You

Dealing with the death of a spouse is never easy. The help of loving family and friends together with the empathetic understanding and practical assistance of those who work in business and government will ensure that the slow return to normality is managed with care. ■

BUSINESS MATTERS deals with a number of complex issues in a concise manner; it is recommended that accounting, legal or other appropriate professional advice should be sought before acting upon any of the information contained therein.

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