The Munro Letter

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MANAGEMENT

Age and the Workplace

Owner-managers need to plan for an aging workforce.

No wonder owner-managers have been noticing an increase in gray hair among their employees. According to the 2011 National Household Survey by Statistics Canada, 18.7% of the workers in the 18-million-strong Canadian workforce are 55 years of age or older. This is up from 15.5% in 2006 and 11.7% in 2001 of a slightly smaller workforce. By 2021, about 25% of the workforce is projected to be 55 years of age or older.

This trend is in place because the Baby Boomers (i.e., those born between 1946 and 1965) are aging. In 2011, the oldest Boomers turned 65; by the time all 9.6 million persons in that age group will have turned 65 by 2031, the proportion of seniors in the population could reach 23% from 15% in 2011.

Retirement May Be Out of Reach

However, retirement is becoming problematical for many of these workers. Of the 18 million people in the workforce, only about six million, or one third, are members of registered pension plans. Of these, only 48% are members of private-sector plans. Participation in private-sector pension plans has, in fact, been declining steadily since the early 1980s when membership was about 60%. Compounding the problem is the increasing unwillingness of employers to commit themselves to any kind of pension plan, especially defined-benefit plans. In addition, only about 24% of all tax filers contribute to Registered Retirement Savings Plans and, when they do, the amount is only around $2,800 per year or about 12% of the current maximum eligible amount.

If you put together the low participation rates in company pension plans and low savings rates in RRSPs, then add the fact that household debt is now at 163% of disposable income, it is easy to see that retirement without at least some earned income is going to be out of reach for many in the Boomer generation.

Owner-Managers Need to Adjust

These changes in demographics and retirement savings are putting owner-managers in a difficult position. On the one hand, they know that older, long-time employees may not want or be able to retire, but at the same time they recognize the future depends on hiring younger employees. Nevertheless, by embracing the realities of age-related differences, an organization should be able to continue to draw on the experience of the older workers and the energy and new skills of the younger ones while maintaining harmony and productivity within the workplace.

Owner-managers will have to learn to understand the needs of older workers.

Physical Considerations

Owner-managers should take into consideration the natural aging processes when developing health and safety policies. Constructing or retrofitting the workplace with age-friendly tools may be beneficial to the business because it could reduce downtime of essential employees and the associated costs of injuries and/or Workplace Safety Insurance Board (WSIB) claims. Minor changes that can make a positive impact on employee morale:

- larger display screens and better speakers for smart phones or other communication devices
- ergonomically designed chairs and seats
- better lighting to ensure improved visibility and reduce eye strain
- limited night travel for older employees
- better designed lifting equipment
- clear markings on items in excess of a standard "safe lifting weight"
- easy-to-hold tools that increase grip without more hand power
- lighter power tools with variable power shifts to reduce sudden torque impact.

Social Considerations

Reassure older employees that you respect their experience and abilities and that they are still making a valuable contribution to the success of your business. This can be accomplished by a few simple changes:

- Offer more flexible work schedules.
- Reduce overtime and reschedule shifts to allow longer rest time.
- Train the older worker to be a coach or mentor.
- Continue professional development of individual older employees to bring out latent competencies. For example, an experienced painter might refocus as an estimator.
- Revamp office, washroom, and work areas to ensure better functionality and accessibility with small enhancements such as levered handles on taps, graduated ramps and better air flow.
- Address any age-related bias head on with in-house presentations that look at not only the legal implications of age discrimination, but also the similarity of needs, concerns, and desires of employees regardless of age.

Older Workers Are Here to Stay

Older workers are going to be a part of the working world for a long, long time. With a little effort and minimum expense you can continue to benefit from their experience by a bit of rethinking of workloads and scheduling. Over the next 20 years as the Boomers retire, you will need to pay special attention to your management strategies to ensure a seamless transition between the generations of workers in your business. Providing assurances to older workers that their well-being is in the forefront of your planning will ensure the continued success of the company.

TECHNOLOGY

Password Security 2.0: Beyond the Password

Security technology is becoming more sophisticated but examine your options carefully before you upgrade.

With the release of the latest Apple iPhone – the 5s – a new security feature is now available, and the reviewers are all abuzz about this more convenient variant on privacy and data protection. But is all the hype really warranted?

There have been many great innovations and improvements in technology security and authentication over the years. Each type has its benefits and drawbacks. So, with all of these options, which is the best for your personal and business data? The basic forms of data security fall within one of three main categories: biometric, possession, and knowledge factors.

Biometric Factors

Biometrics (i.e., what the user is) are the unique physical traits of the user that can be measured and compared, such as a voiceprint, iris scan or, most commonly used in everyday technology, a fingerprint. While only you possess the originals, biometric factors are nevertheless vulnerable to being copied.

Fingerprint scanners – While not a new innovation, Apple's 'Touch ID' sensor on the iPhone 5s has once again brought mainstream attention to using fingerprints as a convenient way to let your phone know that you're, well, you. Early reviews suggest that the new sensor is convenient and effective and a considerable improvement over the older-style "swipe" sensors more common on business laptops. However, as with all biometric factors, this method can be defeated by a determined attacker if they have a sufficiently detailed copy of your fingerprint. Unfortunately, a copy of your fingerprint is not as difficult to come by as you might think. Just consider how many everyday items you touch casually, such as glass doors or windows, elevator buttons, cups or glasses, and any other non-porous surface.

Face recognition – Front-facing cameras have been included on mobile phones and computers for many years, thereby making this technology appear to have the prerequisites for a mass-market deployment. In fact, this feature is already available on many phones, such as recent models running Google's Android operating system. Unfortunately, the current consumer versions of facial recognition technology still have a lot of room to improve. In its current forms, the facial recognition security locks depend on lighting conditions and facial expressions for their effectiveness and can be fooled by a simple photograph.

Possession Factors

Possession factors (i.e., what the user has) essentially rely on a key-and-lock system. The 'key' may take many forms, such as a keychain token, smart card or a small device designed to interface with the machine, such as a USB or audio port token. Possession factors are relatively uncommon on their own for computing security, although they are frequently used as part of a multi-factor or two-step system (something we'll touch on a bit later). The primary weakness of using a physical object as an authentication mechanism is that it may be stolen or damaged. Think of someone who has the keys to your home, for example; they would have unrestricted access to everything inside!

Knowledge Factors

Knowledge factors (i.e., what the user knows) are very commonly used, such as a secret PIN, pattern or password. The main common advantage to knowledge factors is that the 'secret code' may be changed with relative ease and frequency. For example, in most applications, changing your PIN or password only requires a couple of clicks. Among other things, knowledge factors can be vulnerable to what is known in the computer security world as "brute force attacks." Simply put, a computer program attempts to 'guess' a passcode by systematically trying a large number of various combinations in a short amount of time. Of course, the greater the number of combinations, the harder it is to crack a password in this way. This is why, despite the inconvenience to the user, longer passwords that use a combination of numbers, symbols and both upper and lower case letters are considered to be more secure. Unfortunately, the longer and more complex a password becomes, the harder it is to remember!

A four-digit PIN has 10,000 potential combinations; a six-digit PIN has one million.

PINs and patterns, commonly used by financial institutions and Google's Android operating system respectively, have the advantage of being easier to remember. Depending on the number of digits in a PIN or dots in a pattern, there may be fewer potential combinations. A standard four-digit PIN, for instance, has only 10,000 potential combinations. On the other hand, a six-digit PIN has one million. Patterns, as implemented in Android, however, have fewer possible combinations than PINs, mainly due to the number of dots, and the inability to "re-use" the same dot twice.

Multiple Factors

Since biometric-, possession- and knowledge-based factors all have weaknesses of some sort or another, data security teams have devised what is known as Multi-Factor Authentication to try to decrease the possibility that a data thief or "hacker" will be able to breach your security. Multi-factor (also called two-step or two-factor) authentication is intended to make it more difficult for an attacker to have all the required factors, thereby improving security. An ATM is a classic example of a security system that requires two-step authentication in order to complete any transactions. First, you require a debit card (the possession factor) and second, you must know the PIN (the knowledge factor). Multi-factor authentication is often a requirement for highly secured IT systems, although it is becoming more commonly available in consumer applications. Google, Facebook, Twitter and other major online sites are now optionally offering some form of two-step authentication as well.

While Multi-Factor Authentication is arguably far more secure, the limitation is that the system itself must be set up to use two-step authentication. Unfortunately, since most software programs don't have the option to add a second step for authentication, a password is the only option available.

Balance Security with Convenience

Security and usability tend to have a direct relationship: as data security increases, it often becomes more difficult to access the data. The trick is to find the right balance between an acceptable level of inconvenience and the desired level of protection for your data and privacy. Keep in mind what you're trying to protect and the potential consequences if someone gains unauthorised access, and use an authentication method that strikes the best balance. For example, your fingerprint may be secure and convenient enough to keep prying eyes from your personal email or Twitter feed, but you might consider using something more secure for your financial accounts or sensitive client data.

Regardless of the kinds of authentication you're using, a little common sense can go a long way. Use a password that's sufficiently secure, never share your PINs or passwords, and don't write them down!

MONEYSAVER

Dad…Mom... I Need Your Help

If your son or daughter approaches you for a loan to start a business, make sure they have a solid business plan.

It has always been difficult for young people to start their working lives. The traditional route has been to apply along with hundreds or perhaps thousands of other equally well-educated people for advertised positions. But many young people, even those with post-secondary education, are unable to find work and believe the only course of action is to start their own business.

Even though they are well educated in their chosen field and perhaps have studied accounting, marketing and other subjects essential to running a business, they are not necessarily experienced with the pragmatics of a business venture.

Turning to the Parent

Your offspring has finished their formal training and has come to you with an idea for a business. You want to help but you are also an owner-manager who knows how hard it is to start and grow a successful business. You don't want to say "no" but you are not prepared to say "yes" yet either. So, maybe a little role playing would help get the two of you to a decision.

Get a Business Plan

Pretend you are the loans officer of a bank and have your son or daughter pretend they are the small-business person approaching the bank with an idea. Your question, of course, is the same as the bank's: "Will I get my money back if I risk it with you?" To find the answer, the bank would ask for a business plan. You should too. If your offspring hasn't already prepared a business plan, this is the time to get some experience. Tell them there's plenty of help available online from the Business Development Bank of Canada, the chartered banks and, of course, in the bookstores.

Check the Industry Canada website for important statistics.

A Reality Check

Make sure they read the latest edition of the Industry Canada annual publication *Key Small Business Statistics*. The *Key* defines a small business as an incorporated business with one-to-99 employees that has remitted payroll deductions for at least one employee, has sales revenue of $30,000 or more and has filed federal corporate tax at least once in the previous three years. This publication is a reality check on survival rates, education levels of owners and many other facts that define small business ownership. The Industry Canada website is also an important source of useful benchmarking statistics that will give your young entrepreneur an idea of the way industries actually perform as measured by revenue, expenses and net profit/loss.

From a Business Perspective

As a prudent investor, you will want to see the following in the business plan:

- What is the product or service?
- Is there a market for it and who are the competitors?
- Does your child have the relevant education and other competencies?
- What assumptions are made about the economy, the industry, the market and interest rates for the first five years of the business?
- Have sales, cash flow and profit projections been prepared for the next five years? Are the projections reasonable in light of the assumptions?
- Are there other partners or shareholders contributing capital?
  - Have their backgrounds been checked?
  - What will they do and do they have the requisite skills?
  - What are the terms of the shareholders' agreement?
  - Who has decision-making and signing authority?
- How long will it take for the company to break even?
- What is the anticipated rate of return compared to a risk-free investment?
- Will there be any lenders ahead of you?
- Is the loan insured against the death of the borrower(s)?

Your Investment Risks

a) What security is available for you in the event the business fails?
b) How long will it be before the principal amount is repaid?
c) Is the proposed return on investment from the business equal to or greater than the current rate of return on your existing portfolio?

Think of the Long-Term Impact

Don't make the loan for emotional reasons. Your offspring will have other opportunities; you may not. The older you are the less time and opportunity you have for financial recovery if your son's or daughter's company fails. You could end up with insufficient funds to live through your senior years. If the business fails and funds are lost are all parties aware of the emotional tsunami that may engulf the family? Have you discussed with other family members whether the outstanding loan will be deducted from the entrepreneurial child's share in the distribution of assets upon your death?

Have the business plan reviewed by professionals before committing your funds. Better to spend a couple of thousand dollars at the front end for professional guidance from myself, your lawyers, and possibly your investment advisor than it is to lose $200,000 when the business goes south for lack of due diligence.

And Finally…
Make it very clear to the adult child that business is business and family is family. When it comes to business, expect them to meet the conditions of agreements. If they do not, you will pursue available remedies in your own interest.

TAXATION

A Lesson in Record Keeping

The *Income Tax Act* requires you to keep all documents supporting your business activity; in an audit, the CRA will demand them.

Keep Everything

According to the *Income Tax Act*, taxpayers must keep "records and books of account ... together with every account and voucher necessary to verify the information contained therein" for a period of six years following the last taxation year to which they relate. For corporations, the start of the six-year period is the fiscal year; for individuals, the calendar year.

Show Us the Proof

The recent appeal ruling in *Tibilla v. The Queen* before the Tax Court of Canada, July 3, 2013, reinforces the need to maintain documentation. In summary here is what led to the ruling:

1. Mr. Tibilla (the taxpayer) acquired a rental property for $172,000 November 14, 2002, and sold it on December 18, 2007, for $285,000 but declared no capital gain in his 2007 tax return.
2. In 2010, the Canada Revenue Agency (CRA) advised the taxpayer that his return for 2007 was under review and that he was required to provide copies of the contract of purchase and sale, a statement of the capital cost allowance claimed over the years the property was owned, a list of any expenses related to the purchase and sale as well as the receipts for those expenses.
3. In a late filing of his 2008 tax return, the taxpayer declared a capital gain of $41,571.64 and a taxable capital gain of $20,785.82 (i.e., 50% of the capital gain). The taxpayer said he was declaring the capital gain in 2008 because, despite having signed the sale agreement in December 2007, disagreements with the new purchaser made the sale "uncertain and incomplete" until March 2008, when the disagreements were amicably settled.
4. Included in the taxpayer's capital gains calculation was $52,810 in renovation expenses claimed to have been incurred before he actually acquired possession of the property (i.e., between April and November 2002). (The addition of this amount to the adjusted cost base would have reduced the capital gain when the property was sold.)
5. The CRA rejected the renovation expenses because the taxpayer provided no vouchers. The taxpayer said he had stored the receipts in his basement but they had been lost in a flood in 2008. He was unable to explain why the existence and loss of these receipts had not been brought to the attention of the CRA during the audit, discovery or the appeal. The taxpayer said he had made no insurance claim for the loss because he did not want to increase his future insurance premiums. He therefore also had no documents from the insurance company attesting to his loss.
6. The appeals judge ruled that the sale had taken place in 2007 since it had taken place by deed of sale before a notary on December 18, 2007, and had been registered in the official land registry the next day.

7. The judge also ruled that the period between the date of purchase (November 14, 2002) and the date of sale (December 18, 2007) was not six years and, in any case, the *Income Tax Act* required the taxpayer to keep records of any claims until the expiry of the appeals process, which the taxpayer had not done.
8. The appeal was dismissed with costs to the taxpayer.

The burden of proof for deductions lies with the taxpayer.

Lessons

Referring to other cases, the judge emphasized that, since our tax system is based on personal self-monitoring, the burden of proof for deductions and claims lies with the taxpayer. Just keeping notes is not enough; documents are required. If Mr. Tibilla had been able to produce records of his renovation expenses (and if they had been accepted by the CRA), he would have saved himself a significant amount in taxable capital gains and legal costs. The addition of the claimed $52,810 in renovation expenses to the $172,000 purchase price would have given him an adjusted cost base of $224,810. His capital gain would have been $60,190 ($285,000 - $224,810) to give a taxable capital gain of only $30,095. Instead, he incurred a capital gain of $113,000 ($285,000 - $172,000) of which $56,500 was taxable. Mr. Tibilla's inability to produce his expense records cost him $26,405 ($56,500 - $30,095) in taxable capital gains.

What about Your Past?

Prior to February 22, 1994, there existed a cumulative capital gains exemption of $100,000. If this amount was not fully used by the February 22, 1994, deadline, taxpayers could use any unused amount to revalue capital property. Effectively, the taxable capital gain on any taxable capital property sold thereafter would be reduced by the election amount of 1994. Documentation to support 1994 valuations may be required.

Consider the following types of transactions that may need to be substantiated with adequate documentation years after they have occurred:

1. If you purchase shares of a corporation from a third party, the adjusted cost base (ACB) of those shares will not be the paid in capital on the balance sheet. Shares could be purchased at different times for different amounts.
2. If you have investments in income trusts, part of the monthly payments are usually return of capital which reduces the ACB of the investment.
3. When calculating the ACB of a partnership, you have to take into account the partners' taxable income, which is often different from the accounting income.
4. Corporations that incur a non-capital loss may apply to reduce all types of income in the three taxation years prior to, and the seven taxation years following, the loss (10 years for taxation years ending after March 22, 2005). It would appear from the Tax Court ruling that application of non-capital losses 10 years back would subject the applicant to another six years of record keeping in the event that CRA wished to audit the taxable years.

As a result of the 2013 Tax Court rulings, individual and corporate taxpayers should consider the following:

- Locate the original documentation pertaining to any capital property.
- Review the record destruction policy to ensure you are retaining pertinent records.
- Contact your lawyer, accountant, real estate advisor, appraiser or other professional to determine whether they have copies of any of your records that may be required. If possible, get the originals and leave them copies.

- Keep in mind that professionals change firms, die, or sell their business to others. If your professional is no longer available, review past tax returns and statements to determine whether there are any issues that may require documentation held by their predecessors.
- Consult with myself about losses and their applicability to prior years' taxable income to determine whether the time and cost of a potential CRA audit is worth the dollars that may be recovered.
- Maintain your relationship with your CA. Your CA will be attentive to maintaining historical information.
- Maintain originals of all documents. After all, as noted above, it is your responsibility to produce the necessary documents to support your claim(s).

Get It All Together

As you approach retirement and plan to sell the company or transfer ownership to others, you will need to have documentary evidence of past transactions to ensure any tax liability is kept to a minimum. Owner-managers should make reviewing the past and gathering the required information a priority.