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the newsletter of Prentice Yates & Clark

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Managing Debt

Debt is a reality in business operations. Indeed when properly managed, debt can be a fundamental building block for increasing inventory, expanding into new markets, or financing new equipment.

BUSINESS growth often requires the owner/manager to seek a bank loan, a line of credit, trade credit or some other form of financing. With the current interest rates the lowest they have been since the 1950s, owner/managers may be taking on new debt to boost their company's market presence, improve cash flow, enhance operations, or build a credit history for future borrowings.

How much debt should a company take on?
Before seeking a loan or other financing, take time to review the company's current financial situation and future prospects. You need to:

- ensure you are taking on debt for the right reasons, at the right time
- assess the impact of the new debt on the company's future cash flow
- determine whether you should opt for short-term or long-term financing, and
- in some instances, consider leasing rather than buying.

Vehicle Debt
With car dealers advertising 0% financing and other incentives, vehicle sales have soared. However, consider that when financing payments do not include interest repayment, purchasers are tempted to purchase a higher priced vehicle than they might otherwise choose.

When you purchase a vehicle for company use, you need to consider the impact on your tax planning in view of the restrictions on the capital cost allowance, your personal use of the vehicle and other variables. Determine the effect of the payments on the company's projected cash flow and compare the cost-benefits of purchasing versus leasing.

Leasing is sometimes the better option as it preserves the availability of working capital and credit.

Charge Card Debt
While credit cards with financial institutions may have interest rates as high as 18%, credit cards with specific businesses such as ABC hardware may charge even higher interest. The appeal of credit cards is not only the ease of purchase and broad acceptance, but also the ability to pay a monthly minimum when cash flow is tight. However, if you can't repay your credit card balance consistently and quickly, then this is a very expensive option for financing.

Tax Debt
Careful tax planning and regular payments of your instalments are critical to sound business operations. If your instalments are late, consider that not only do you incur interest and penalties, but also you cannot expense any interest charged on outstanding balances. Further, if a business fails to withhold at source or remit amounts withheld, it risks having its bank accounts frozen.

If your business owes taxes, it is best to have your chartered accountant speak directly to the CCRA to determine terms of repayment or changes that may affect the company's tax situation.

Line of Credit Debt
Most owner-managed businesses have a line of credit that moves up and down depending on the cash flow needs. A line of credit offers working capital on an as-needed basis, can be paid down without penalty when excess cash is available, and is usually provided at a reasonable rate of interest.

Ideally, a line of credit should be considered a current liability that will be repaid within the yearly operating cycle of the business. If you need to use the line of credit for a debt that cannot be paid within this time period, this financing source is too costly. It would be better to negotiate a term loan that provides for affordable payments and a fixed interest rate.

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New Employee Orientation

Orientation is the key to a better start and a happier, more productive employee. This is an opportune time to provide new employees with information that will ease the transition into the workplace and inspire them to have a good attitude towards the company and their new job.

GENERALLY the employee's orientation should cover three key areas:

- A general orientation — meet the company
- A departmental orientation — meet the team, and
- A specific job orientation — here is how you fit in.

When new employees are well informed at the outset, they are better prepared to take on their new responsibilities and are not as likely to take up valuable time of other personnel unnecessarily.

Starting Out Right

A well-planned orientation program avoids potential miscommunication and lost productivity and helps the new employee adapt to the new job and workplace faster.

- Plan and prepare an orientation schedule for the employee's first day.
- Indicate the time and locations of meetings with other staff, their titles, departments, local telephone numbers and the expected length of each visit.
- Provide each of these individuals with a copy of this schedule so they are well prepared to help the new employee learn about the company and its people.
- Schedule time for completing and signing documents for income tax purposes, health benefits and other employment matters. Make sure the employee's SIN, address, and résumé are on file.
- Make sure the new employee's work area is equipped with the tools needed to do the job.

The Company

- Provide a brief overview of the company, including the company's history, its products and services, the management structure, the competition, and the company's strategies and goals. If possible, have a chart available that shows how the company is set up and includes photographs of the key personnel and their titles.
- Provide information about the company's customers, suppliers and any other parties with which the company interacts.
- Consider matching the employee with a mentor in the workplace to turn for information or to discuss any difficulties.
- Discuss the daily operations and matters such as staff meetings, hours of work, time cards and lunch breaks.

The Tour

- Take the employee on a tour of the company to familiarize him or her with the various areas, staff, and equipment.
- Introduce the employee to co-workers and provide information about their positions, career background and personal interests.
- Point out any areas that are restricted for administrative, security or safety reasons.

Administrative

- Explain the administrative details of the employment, such as the pay period, company benefits, statutory holidays and vacation time.
- Explain the company's policies on staff development, advancement, salary/wage review and sick leave.
- Discuss the probationary period and clarify aspects of the job and expected performance.
- If it is a contract position, ensure that the employee signs the contract.
- If the employee is to receive salary plus commission, put the commission rate in writing.

Training

- Schedule the employee for any training that must be taken to meet business, production or safety requirements.
- Make sure the employee is aware of all safety regulations in the building and the procedures that must be followed in an emergency.
- Ensure the employee is aware of the safe and proper use of any equipment that is required for the job as well as any safety equipment that must be worn.

Most employees start a new job with some anxiety about meeting their new co-workers and measuring up to their new job duties and expectations. While a good orientation program takes time and effort, it is an important investment. A well planned orientation can ensure a smooth transition, avoid miscommunication, and ultimately reduce staff turnover. ∆

Managing Debt (continued from cover)

Long-term Debt

Next to an operating line of credit, a commercial term loan is an important and fundamental form of financing for many businesses. These loans are available to businesses to finance the acquisition of medium- or long-term assets, working capital or debt consolidation. Without term loans, most businesses would have difficulty growing.

When financing capital acquisitions, you need to evaluate this debt in relation to the profitability, impact on cash flow and product or service cycles. If the financing terms exceed the asset's useful life span or its capacity to produce profits, the burden of this liability could affect the company's future ability to obtain credit for additional property or equipment that is vital to business growth.

Accounts Payable Debt

Most businesses use the window of net 30 to 60 days that their suppliers provide to help their cash flow. After all, if ten suppliers are owed $5,000 each, a temporary positive cash flow of $50,000 is created - provided you do not miss the accounts payable date. Late payments risk interest charges and could damage your relationship, and credit arrangements, with your suppliers.

Before You Borrow

Before you borrow, analyze the capacity of your business. Your chartered accountant can help you prepare reliable forecasts outlining the required financing and prospective cash flow available for debt servicing as well as assess which sources of financing are the right solutions for your business needs. ∆

Investing for the Future

The punishing markets of recent times are causing many investors to take a more cautious approach to their investment strategy.

INVESTMENTS always involve risk. As an investor, you need to have a risk management plan in place to minimize losses when markets drop for extended periods of time. Solid research, a well thought-out plan and professional advice will help temper the risk to your principal so you can weather today's challenging market conditions and maximize the potential for long-term growth.

Diversify

Diversify your investments to spread the risk. Do not hang on too long to a losing investment. It is never easy to crystallize losses but sometimes rebalancing your portfolio may be the wisest thing to do. Your chartered accountant can assist you in weighing any tax advantages of realizing capital losses on investments that are outside of an RRSP.

Monitor the Market

Find out everything you can about the market, tax incentives, and the investment vehicle itself. Poor investment decisions happen when investors react too quickly on the promise of future profits without careful research. Others result from indecisiveness when investors fear the risks and make no changes in their investment strategies.

A dramatic example of the need to understand the market was the downfall of the Internet companies. Billions of dollars were lost because investors recognized too late that there were far too many Internet companies chasing a market that would not be sustainable. Changing needs, political pressures, demographic shifts, technology, climate changes and catastrophes all have an impact on market behaviour.

When considering equity investments, look at the company's technology, any contingent liabilities, forecasts, capital asset base, management team, controlling ownership and outstanding shares. Be wary of factors such as overly optimistic forecasts and underfunded pension plans due to over expectations of market returns. In addition to discussing your investments with your advisers, browse the Websites of these companies, subscribe to quality investment publications or join an investment club.

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PYC Briefs

ONPHA Trade Show

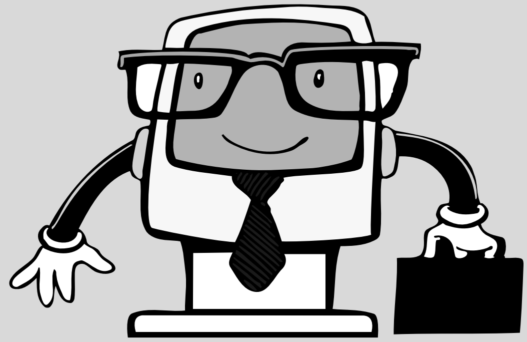
PYC will be exhibiting at the annual Ontario Non-profit Housing Association Conference and Trade Show on November 14, 2003 at the Toronto Sheraton Centre.

During the conference, John Torry and J.J Pauze will be facilitating a workshop for directors entitled *Balance Sheets for Boards*.

NV2

Q.W. Page is currently conducting several trial installations of the long-awaited NewViews for Windows.

PYC is involved in trouble shooting during this process. In addition, PYC staff are training on the new software. Look for an update in the next newsletter.



Investing for the Future (continued from page previous page)

Consider Government Incentives

The government often directs investment dollars with incentives in areas such as regional employment, research and development, and corporate/individual income tax. Whether you are considering domestic or foreign investments, reduce your risk by understanding these incentives before you invest. A quality long-term investment should provide an adequate return without its requiring a long-term dependency on government incentives or tax breaks. Your chartered accountant can assist you in understanding the impact of various tax incentives such as any tax credits that may be available.

Consider Leveraging Assets

While rates of returns on investments are at an all time low for both equity and income-generating investments such as bonds or GICs, interest rates for borrowing are also at an all time low. Now may be a good time to consider leveraging your assets to increase your investment portfolio before the next big upswing. With appropriate financial and tax planning, borrowing money to invest may make good sense.

One strategy is to leverage the equity you have built up in your home by using it as collateral to take out a loan or line of credit for long-term investment purposes. Because you are borrowing for investment purposes, the interest on the loan may be tax deductible provided the investment is outside of your RRSP portfolio. You cannot deduct the interest for loans to invest within your RRSP portfolio. However, contributions to an RRSP that you make early in the year will accrue tax-deferred earnings in your RRSP over a longer period as well as provide tax savings when you file your 2003 personal income tax return next year.

Of course before you leverage assets for investing, you should talk to your financial advisor. As the current interest rates may be short-term, you need to ensure you will be able to service the loan if the investment does not deliver the expected returns. You should have a cash reserve or alternate means of financing if you need to ride out an increase in interest rates.

Before borrowing, carefully assess your current debt management, ways you can control monthly expenses, and tax saving strategies that could improve your cash flow. Consider your comfort level, risk tolerance, and most important, your time horizons.

Get Professional Advice

Talk to your broker, financial planner and chartered accountant about the investments you are considering. Keep in mind that the profits that you make on your investments are subject to different tax treatments depending on the type of income that you receive from the particular investment and whether the investment is inside or outside of an RRSP.

While investment decisions are ultimately your own, the objective input from your professional advisers can help ensure you make decisions in line with your long-term financial goals, risk management plan and tax planning strategies. Δ

visit our web site

www.pyc.net

We would like to welcome the following recent additions to our professional staff.

Andy Butkovic
Nicole Zerva

You may have met them already or you will in the near future as they become an integrated part of our audit team.

September 2003

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We hope that you find *info@pyc.net* a useful source of information. If you should ever have any specific questions or concerns regarding your own business or personal finances, please call us. We will gladly help in any way that we can. If you would like to contact us by e-mail, we can be reached at info@pyc.net.

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