



# Business Losses / Treatment of Corporate Income in Personal Injury Cases

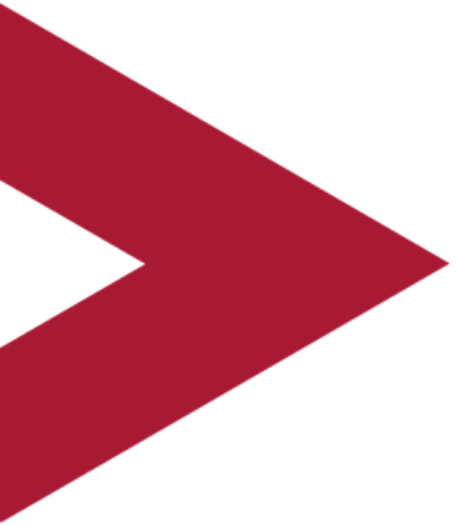
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MDD Forensic Accountants



# Agenda

- Overview of the self-employed
- Owner profit
- Business loss calculation methods
- Critique points
- Documentation needs



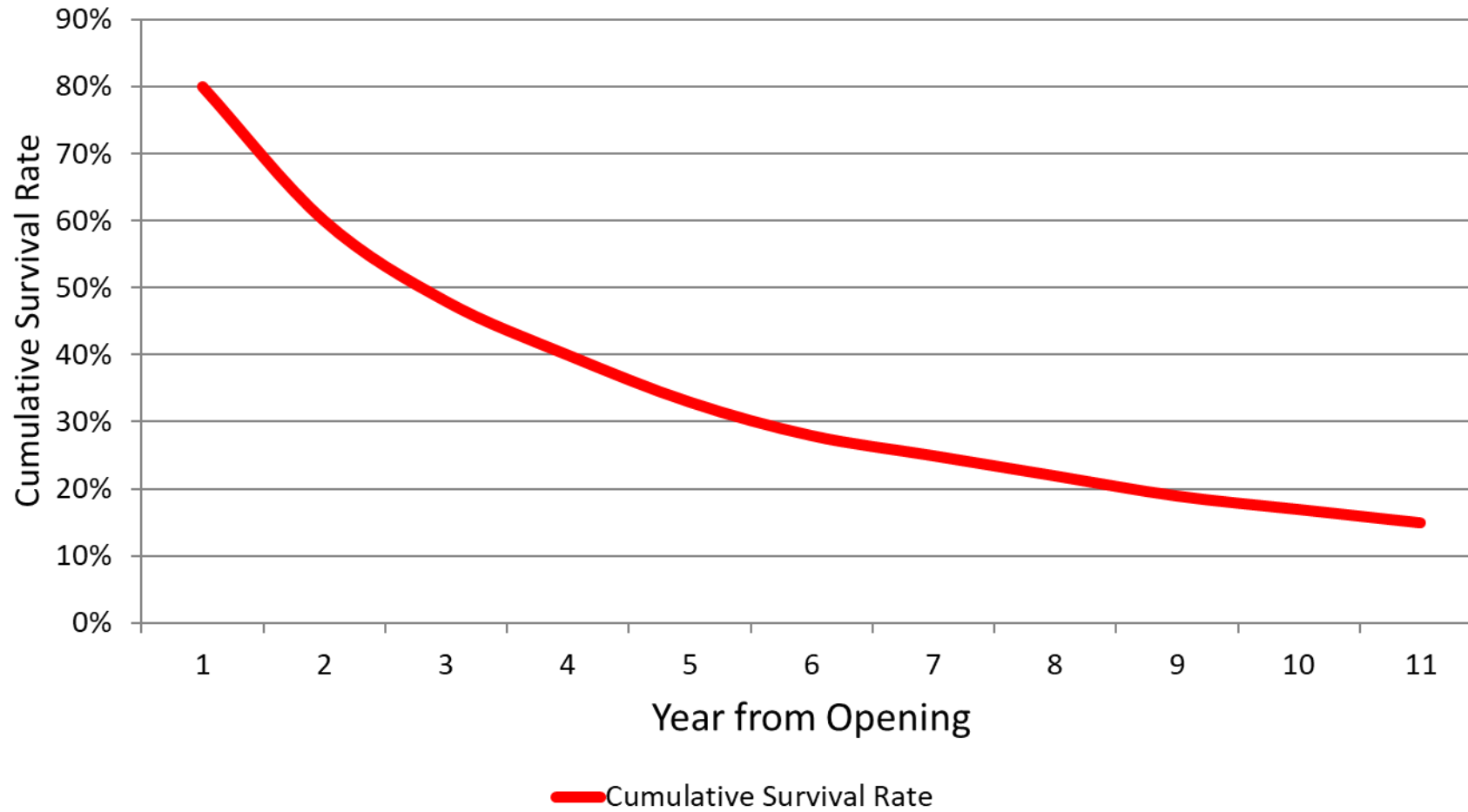
# Overview of the self-employed

# Facts & Figures

- 98% of all businesses in Canada are small businesses
- 20% of the workforce is self-employed
- 48% of the workforce is employed at a small business
- 42% of Canada's GDP is derived from small business
- Self-employed persons work, on average, 15% more than employed persons

*Source: Statistics Canada [2010]*

## Cumulative Survival Rate - Food and Beverage Industry



# Impact due to bodily injury

- Decline in sales?
- Increase in labour costs (e.g. replacement labour)?
- Both of the above?
- Can anything else be impacted?

# Personal attributes

- Technical know-how
- Negotiating ability
- Efficiency
- Reputation
- Relationships
- Ownership

# Legal form of business

- Sole proprietorship
- Partnership
- Corporation
- Does it matter?





Owner profit

# Measurement

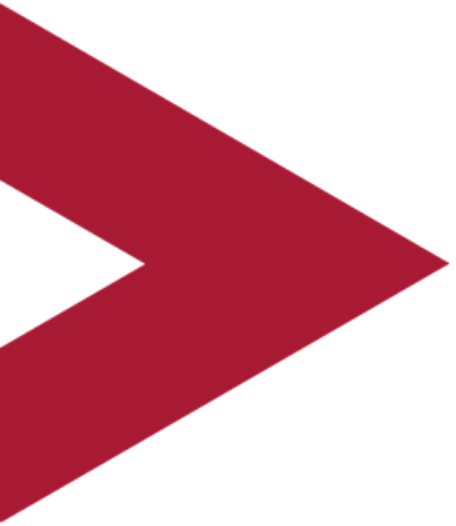
- Generally, owner profit is measured as business profits prior to owner salaries
- If a sole proprietor, owner profit = net income (assuming no discretionary expenses)
- If a corporation, owner profit = corporate net income + owner salary (assuming no discretionary expenses)
  - Dividends are not an expense!

# Discretionary expenses (examples)

- Wages to non-arm's length parties
- Rent
- Insurance
- Repairs & maintenance
- Motor vehicle

# Difficulties

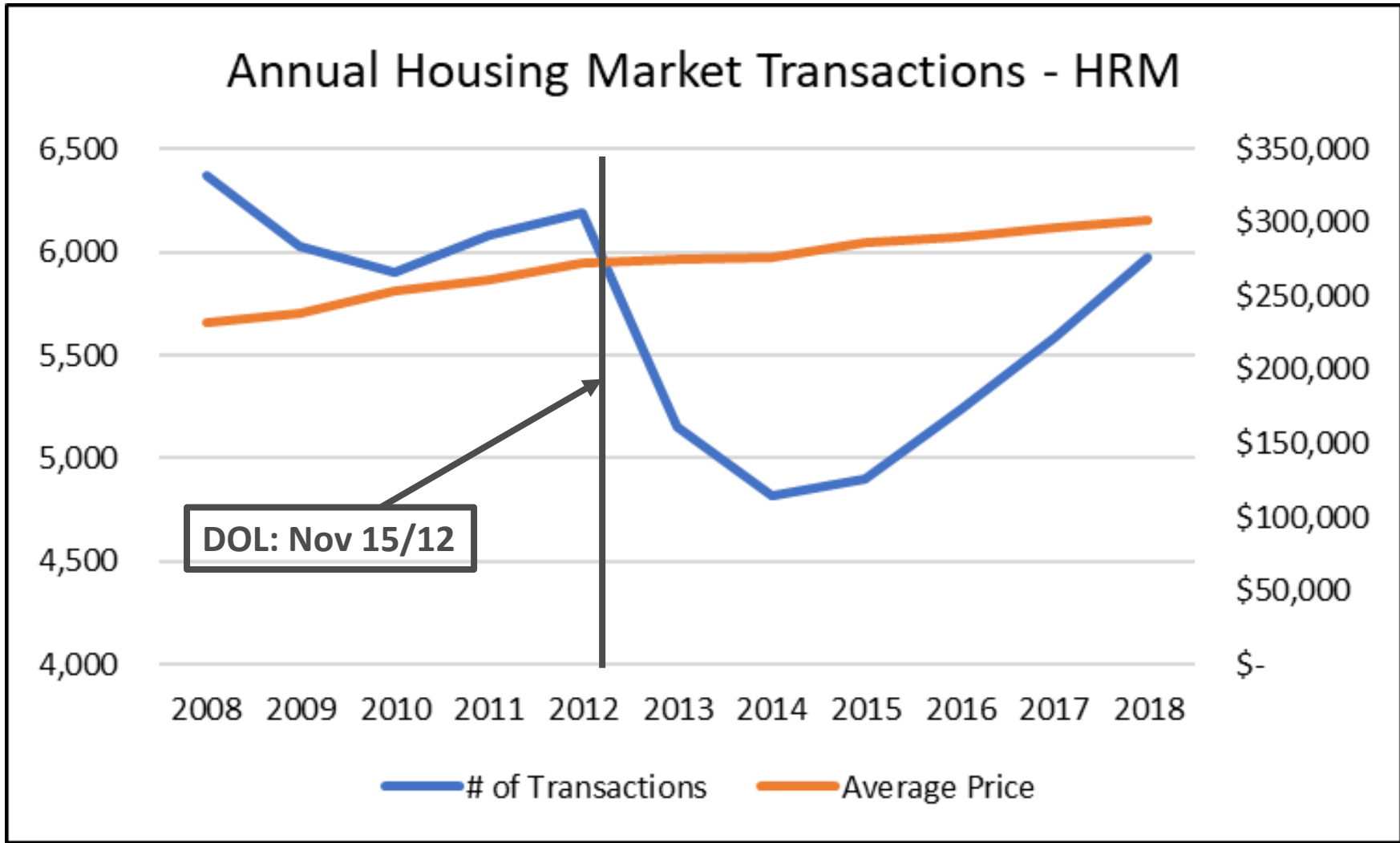
- Off-calendar yearends
- What is fair value (e.g. arm's length wage)?
- Who knew what, when? (e.g. "I don't know, my accountant prepared my taxes")
- Unreported income



# Business loss calculation methods

# Before-and-after method

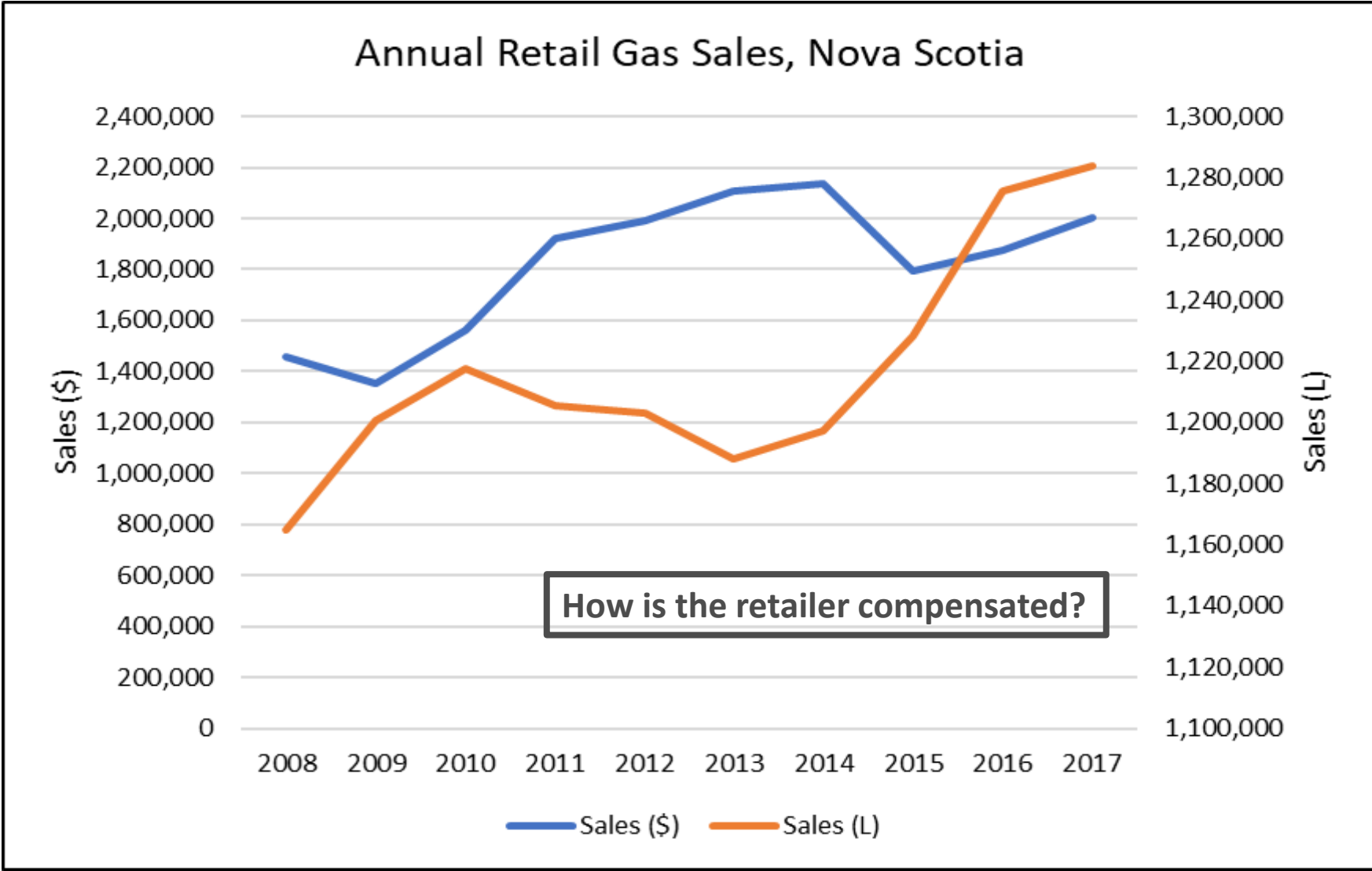
- Compares business results prior to the incident (“Before”) to those subsequent to the incident (“After”)
- Main advantage: easy to perform, easy to understand
- Main disadvantage: assumes any difference is due to the incident
- What may be appropriate for an employee may be inappropriate for a self-employed person



# Yardstick method

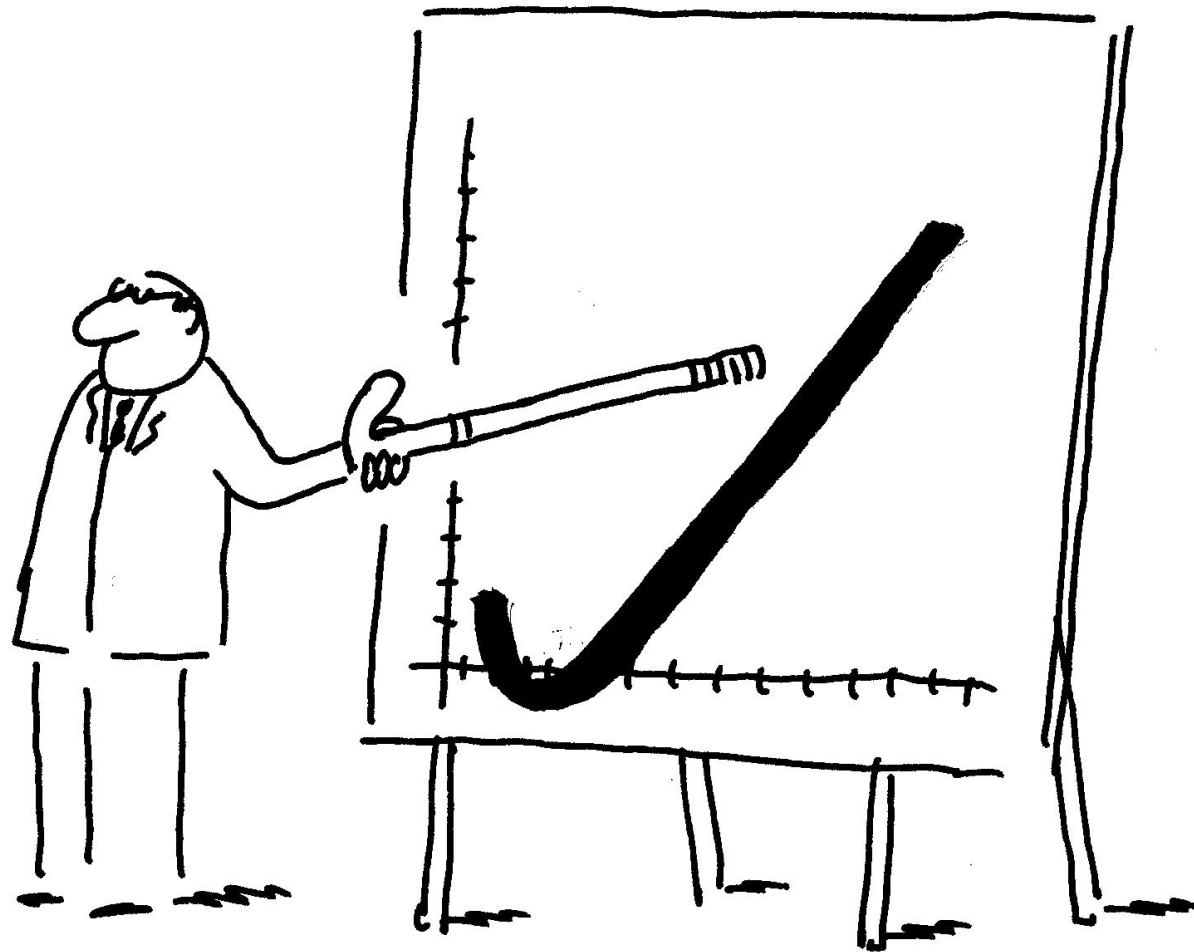
- Projects results using a “base period” combined with industry measures or comparable businesses
- Main advantage: can become scientific and precise
- Main disadvantage: not all businesses are created equally
- Most suitable for businesses where profits are mostly tied to external factors

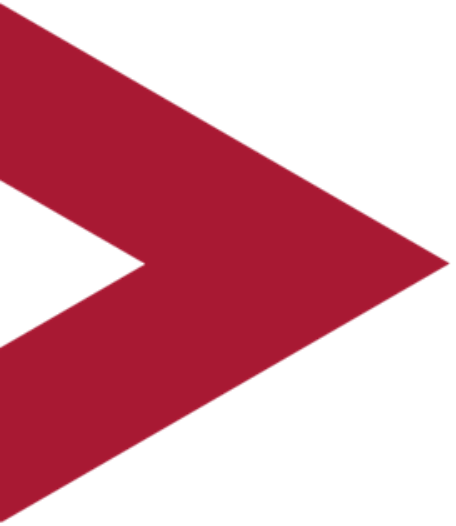




# Projection/forecast method

- Relies on company-specific forecasts (e.g. business plan), perhaps with adjustments
- Main advantage: emphasis on company specific factors
- Main disadvantage: it can be difficult to predict the future 😞
- When/why was the projection/forecast prepared, and how has the subject-business performed to date?





# Critique points

# Double counting

- “*During my time off work, my company lost \$100,000 in sales and I was unable to draw my usually salary of \$50,000... so, you owe me \$150,000!*”
  - Mr. Self-Employed
- What’s wrong with this statement?



# Valuation based on hours

- *“The Plaintiff advised that, on average, he works a combined 60 hours per week in his business. Job Bank ([www.jobbank.gc.ca](http://www.jobbank.gc.ca)) reports that HVAC technicians earn, on average, \$37 per hour and, therefore, we calculate projected normal income as \$115,440 per annum (\$37x60x52).”*
  - Ms. Plaintiff Expert
- What’s wrong with this analysis?

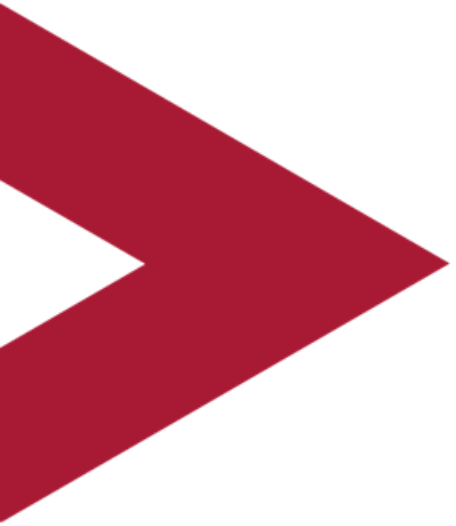
# Factors unrelated to the incident

- *“Comparing the Plaintiff’s average net income during the pre-MVA years 2011 to 2013 of approximately \$48,000 to her actual net during the post-MVA years of 2014 and 2015 of \$7,360 and \$670, respectively, we calculate an income loss of approximately \$88,000.”*
  - ABC Expert Firm
- What’s wrong with this analysis?



### Info from T2125s (Personal Tax Returns):

Description	Year				
	2011	2012	2013	2014	2015
Revenue	\$275,000	\$268,500	\$280,000	\$237,500	\$240,000
Cost of Sales	173,250	171,840	182,000	166,250	170,400
Gross Margin	101,750	96,660	98,000	71,250	69,600
	<i>37.00%</i>	<i>36.00%</i>	<i>35.00%</i>	<i>30.00%</i>	<i>29.00%</i>
Expenses:					
Wages	27,500	29,535	25,200	35,625	38,400
Professional Fees	5,000	5,000	5,000	5,000	5,000
Office	12,500	12,750	13,005	13,265	13,530
Interest	5,000	6,000	6,500	10,000	12,000
Total Expenses	50,000	53,285	49,705	63,890	68,930
Net Income	\$ 51,750	\$ 43,375	\$ 48,295	\$ 7,360	\$ 670



# Documentation needs

# Sole proprietor

- Complete personal income tax returns with form T2125
  - This is not what the CRA gives you
- Notices of Assessment or Income Tax Return Information-Regulares (ITRs)
  - ITRs tend to be more detailed and reliable



Income Tax Return Information-Regular

	NS	Social Insurance Number	Tax year
			2000
		Province of residence	Marital status
		N.S.	COMMON LAW
		Date of assessment	18NOV 2003

Line	Description	Reported	Processed
162	Gross business income	52,449	26,225
135	Net business income		26,225
150	Total income		26,225
235	Net income		26,225

Very limited

**Part 4 – Cost of goods sold and gross profit**

If you have business income, complete this part. Enter only the business part of the costs.

Gross business income from line 8299 in Part 3 on page 1 ..... I

Opening inventory (include raw materials, goods in process, and finished goods) .....	8300
Purchases during the year (net of returns, allowances, and discounts) .....	8300
Subcontracts .....	8360
Direct wage costs .....	8360
Other costs .....	8400
<b>Total of the above five lines</b> .....	<b>8500</b>
<b>Minus</b> Closing inventory (include raw materials, goods in process, and finished goods) .....	<b>8510</b>
<b>Cost of goods sold</b> .....	<b>8510</b>
<b>Gross profit (line I minus line J)</b> .....	<b>8519</b>

**Part 5 – Net income (loss) before adjustments**

Gross profit from line 8519 in Part 4 above, or gross income from line 8299 in Part 3 on page 1 ..... K

**Expenses (enter only the business part)**

Advertising .....	9001
Meals and entertainment (allowable part only) .....	9003
Bad debts .....	9006
Insurance .....	9000
Interest .....	9710
Business tax, fees, licences, dues, memberships, and subscriptions .....	9700
Office expense .....	9810
Supplies .....	9811
Legal, accounting, and other professional fees .....	9800
Management and administration fees .....	9871
Rent .....	9910
Maintenance and repairs .....	9900
Salaries, wages, and benefits (including employer's contributions) .....	9000
Property taxes .....	9100
Travel (including transportation fees, accommodations, and allowable part of meals) .....	9000
Telephone and utilities .....	9200
Fuel costs (except for motor vehicles) .....	9204
Delivery, freight, and express .....	9275
Motor vehicle expenses (not including CCA) (see Chart A on page 6) .....	9061
Allowance on eligible capital property .....	9000
Capital cost allowance (CCA) (from Area A on page 4) .....	9000
Other expenses .....	9270
<b>Total business expenses</b> .....	<b>9308</b>
<b>Net income (loss) before adjustments (line K minus line L)</b> .....	<b>9209</b>

**Part 6 – Your net income (loss)**

Your share of the amount on line 9309 in Part 5 above ..... M

**Minus** – Other amounts deductible from your share of net partnership income (loss) (from the chart on page 3) ..... N

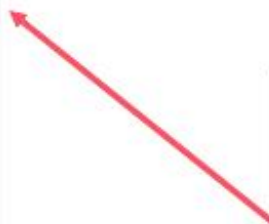
**Net income (loss) after adjustments (line M minus line N)** ..... O

**Minus** – Business-use-of-home expenses (from the chart on page 3) ..... P

**Your net income (loss) (line O minus line P)** ..... 9345

Enter this amount on the appropriate line of your income tax and benefit return: business on line 135, professional on line 137, or commission on line 139

Ask for this!  
 “T2125 Statement  
 of Business or  
 Professional  
 Activities”



# Corporation

- Same information for sole proprietor, plus:
- Complete corporate income tax returns with Schedules 9, 50, 100 and 125
- Corporation Notices of Assessment
- Owner's T4s



**RELATED AND ASSOCIATED CORPORATIONS**  
(2011 and later tax years)

Name of corporation	Business number	Tax year end		
		Year	Month	Day

- Complete this schedule if the corporation is related to or associated with at least one other corporation.
- For more information, see the *T2 Corporation Income Tax Guide*.

	Name <b>100</b>	Country of residence (other than Canada) <b>200</b>	Business number (see note 1) <b>300</b>	Relationship code (see note 2) <b>400</b>	Number of common shares you own <b>500</b>	% of common shares you own <b>550</b>	Number of preferred shares you own <b>600</b>	% of preferred shares you own <b>650</b>	Book value of capital stock <b>700</b>
1.									
2.									
3.									
4.									
5.									



SHAREHOLDER INFORMATION (2006 and later tax years)

Name of corporation	Business Number	Tax year-end		
		Year	Month	Day

All private corporations must complete this schedule for any shareholder who holds 10% or more of the corporation's common and/or preferred shares.

	Provide only one number per shareholder					
	Name of shareholder (after name, indicate in brackets if the shareholder is a corporation, partnership, individual, or trust)	Business Number (If a corporation is not registered, enter "NR")	Social insurance number	Trust number	Percentage common shares	Percentage preferred shares
	<b>100</b>	<b>200</b>	<b>300</b>	<b>350</b>	<b>400</b>	<b>500</b>
1.						
2.						
3.						
4.						
5.						



## GIFI Income Statement #1 - Schedule 125

Date: 2008/09/09

Account	Description	Amount (\$)
8299	<b>Total revenue</b>	139,237
8089	<b>Total sales of goods and services</b>	139,237
8000	Trade sales of goods and services	139,237
8518	<b>Cost of sales</b>	30,646
8300	Opening inventory	1,287
8320	Purchases / cost of materials	5,715
8360	Trades and sub-contracts	20,179
8450	Other direct costs	3,900
8500	Closing inventory	-430
8519	<b>Gross profit / loss</b>	108,591
9367	<b>Total operating expenses</b>	88,590
8520	Advertising and promotion	1,862
8522	Donations	40
8670	Amortization of tangible assets	3,353
8690	Insurance	1,266
8710	Interest and bank charges	160
8711	Interest on short term debt	2,132
8714	Interest on long term debt	5,008
8716	Credit card charges	1,592
8760	Business taxes, licences and memberships	5,104
8811	Office stationery and supplies	3,597
8812	Office utilities	4,817
8861	Legal fees	4,513
8862	Accounting fees	5,350
8871	Management and administration fees	818
8876	Training expense	295
8911	Real estate rental	30,800
9010	Other repairs and maintenance	504
9013	Security	135
9060	Salaries and wages	15,880
9180	Property taxes	493
9200	Travel expenses	518
9201	Meetings and conventions	353
9368	<b>Total expenses</b>	119,236
9369	<b>Net non-farming income</b>	20,061

Schedules 125  
(income  
statement) & 100  
(balance sheet)

# Any business

- Monthly sales
- Monthly payroll
- Projections/forecasts (and when/why prepared)
- Lending agreements



# Questions?



Buffet Lunch (12:00-12:15pm)

Food and Beverage Area

Keynote Speech with Peace by  
Chocolate Founder and CEO,  
Tareq Hadhad (12:15pm-1:05pm)

Argyle Suite



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