

## Business Advisory Letter

Does the phrase “May you live in interesting times” apply to accountants? Without a doubt, these times are anything but dull.

It appears the accountant, that bastion of public trust, that pillar of ethics, is destined to become the veritable goat of the new millennium. Already, reams of jokes, anecdotes, comics and unflattering metaphors have assailed our profession. For decades, surveys of public opinion regarding trusted advisors consistently ranked accountants at or near the top. Given the multitude of the people who are now poorer, allegedly from relying upon the opinion of an accountant, the next such survey may produce somewhat different results.

Accountants, or more appropriately auditors, are charged with the ominous responsibility of ensuring public companies fairly report their financial position and results of operations. By their unqualified opinion, the auditors represent that the financial statements contain enough information to enable the reader to discern whether the company is deserved of his hard earned investment dollar. The reported earnings should be credible evidence of the company's ability to produce a return on investment. The assets shown on the balance sheet should have tangible value and be of enduring future benefit to the company. If the information is complete, accurate and understandable, a reasonably sophisticated investor should be able to make an informed decision.

Accounting, however, is not an exact science. In its quest to balance the interests of the investor with those of business (read...management) the accounting profession has developed a somewhat subjective set of standards for the treatment of financial transactions.

The subjectivity of generally accepted accounting principles, however, has been tempered with the objective concept of “professional judgement”. It is this professional judgement that allows an auditor a certain degree of license as he considers accounting treatments that push the envelope of economic reality.

Regulators are speculating that the professional judgement of some auditors is subject to the pressures of the economic realities faced by the auditor themselves. Given that a company can lose billions of dollars of market value depending upon the choice of an accounting treatment, and given that an auditor can lose millions of fee dollars if it stands its professional ground, is it conceivable that the accounting treatment accorded certain transactions may favour the interests of management rather than the shareholder and general public?

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Perhaps the regulators are right. Perhaps an auditor cannot be completely objective when his livelihood depends upon the very company with which he may have a major professional disagreement. When a substantial portion of an auditor's annual revenue comes from one or two clients, can he truly be objective in the exercise of his professional judgement?

While we morally and ethically despise the corrupt corporate culture that could perpetrate a fraud as reprehensible as Worldcom or Enron, we cannot comment on the failings or negligence of their auditors. We do not know the circumstances that caused them to move the borders of their professional judgement. It does appear, however, that Arthur Anderson was well aware their position would not be defensible. By shredding evidence and obstructing justice they have put a blotch on our profession that will take many washings to remove. And given the number of voluntary earnings restatements hitting the pavement, it seems that the ramparts of more than one public company and their Big Five auditors are held up by flimsy logic rather than economic reality.

While we at VMSW do not audit any public companies, we do conduct audits of privately held businesses and various not-for-profit enterprises. None of these clients would themselves constitute any more than 2 or 3 percent of our total fees. We are, we believe, objective in the application of our professional judgement, and the financial statements on which we render an unqualified opinion do represent the financial position and results of operations of our clients. It seems to us that generally accepted accounting principles, properly applied, will provide a fair representation of the financial success or failure of a business enterprise.

Despite the media's portrayal otherwise, we are very proud of the ethics of our profession, and particularly those of our firm. We believe our relationships with our clients are based upon mutual trust. We also believe the users of our clients' financial statements take comfort when the VMSW name is attached. We adhere to the Rules of Professional Conduct of the Institute of Chartered Accountants of Ontario because they characterize the way we do business.

Well before Enron or Worldcom we began the process of codifying the values and mission that guide the operations of our firm. We have included the VMSW Core Values in this edition of the Business Advisory Letter to show our clients and others the enduring tenets by which we strive to live. These Core Values are embodied within our Mission Statement which gives our people a common cause and sense of direction. Through these documents we are accountable to our clients and to every other member of our team. Perhaps you will recognize some of these values as being your own. ♦

*Brent VanParys*

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## **In the Firm**

*VMSW continues its tradition of outstanding community service.*

Jean Shippey has accepted the appointment for another term as the Treasurer of the Woodstock Chamber of Commerce.

Bruce Schlitt is playing with the Woodstock Kelsey's fastball team again this summer; this will be his 8th year on the team. He will also be the new coach of the Woodstock Navy Vets midget hockey team.

Karen Raymond has been elected for another term as Treasurer for the Woodstock Minor Hockey Association Inc. This will be her fourth year on the board

The Norwich District High School 50th Anniversary Celebration raised \$17,000 which has been used to establish a bursary fund for NDHS students demonstrating a commitment to community service, inside and outside of the school. Brent VanParys was a member of the organizing committee.

*Education and professional development keeps our skills sharp and our service at its peak.*

Kim Cook returns to University of Ottawa to complete her second year of B. Comm. Honours Accounting Program.

## *In The Firm...continued*

Brad Bembridge, Systems Engineer with Oxford Technology Group, the Computer Network Design and Maintenance division of VMSW, successfully completed the Cisco Certified Network Associate course for 2002.

Big Congratulations Pam King who successfully passed the School of Accountancy and is now eligible to write the Uniform Final Examinations, the final step in her pursuit of the Chartered Accountant's designation.

Brent VanParys attended the Canadian Institute of Chartered Accountants National Conference which was focused this year on Business Advisory Services

In athletics, Captain Greg Bruce led a courageous group of accountants (supplemented with a few civilians) to a 42<sup>nd</sup> place finish in the Woodstock Community Challenge.

Congratulations to the VMSW team members: Greg Bruce, Kim Cook, Kim Hough, Pam King, Brent VanParys, Carol Stogrin and Jessica Losier

In keeping with our strong presence in the agricultural sector VMSW will be participating in another Outdoor Farm Show; September 10, 11, & 12. Greg Bruce, our Agricultural Team Leader, will be at the show promoting the latest technology with Settler "AgExpert Management Tools" software packages. Please drop by our booth and say hello to Greg. ♦

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## **Succession Planning** **The Human Side of Succession Planning - Part One**

Prepared for Managing Your Resources for 2003 by David Rose, Business Management Specialist, Ontario Ministry of Agriculture, Food & Rural Affairs.

Succession planning is not an easy process. Discussing succession with your family brings up difficult issues like aging, loss of control of your business and your financial affairs, and death. These selling features don't make succession planning very popular. However, if one of your life goals is to transfer a viable farm business to your child or children, then succession becomes an issue in much of how you do business and how you plan your life.

There are a number of factors that make within family transfers of farm businesses easier. Families that have a history of successful transfers have a family model that works for them. First generation farmers, or farmers that received their farms through the death of a farming parent don't have that historical family model to fall back on (well they do, but it's still not a preferred option...).

Family business skills like goal setting, open communication, planning for decision making, using outside advisors, wealth management, training successors, and retirement planning all help position the family and the business for successful transfer to the next generation.

### ***I Find This helpful***

Learn how to step back and take an objective overview of your situation. If you can't do this yourself, find some outside advisors who can help you. Use their advice to help you and your family to build a plan.

### ***Goal Setting***

Your long term vision feeds goal setting. Goals then provide direction. If you can't see where you're going how will you ever know if you get there?

### ***Start Early***

Build some off-farm investments to support you in retirement. These days, most within family transfers occur at prices well below fair market value. RRSP's or other investments help to ease the cash flow crisis at transfer.

### ***Business Viability***

Profitability is critical. It is pointless to talk about transferring an unprofitable farm to the next generation. Parents need income to support them in their retirement years. The money has to come from active business income (payments from your children), or from the sale of the business.

### ***Manage Farm Capital***

Invest farm profits in the right assets. It is difficult to get any money back out of high cost overhead items. Keep the farm lean and get some capital invested off the farm.

### ***Tools for Security and Estate Planning***

Take advantage of the legal tools that are available to give you some control of your assets in the event of incapacity or untimely death. Powers of attorney for property and for personal care allow you to put decisions you would normally make into the hands of a person you trust in the event you are incapacitated. An up to date will provides a backup transfer plan in the event of untimely death. Dying without a will (intestate succession) puts your assets into the control of the Provincial Trustee for distribution. Do you really want a stranger to decide how your assets and your family farm will be distributed?

### ***Changing Roles***

Sole proprietors are used to working independently. Having to share decision making, especially with one of your children is a real challenge for most sole proprietors. Once two people have to work together, the working relationship has changed. Partners are team members who have to talk, share decision making, and who have to learn how to fight without hurting each other. Family relationships add more complexity to the new "team" relationship. As a parent, you have to learn to see your child as an adult and then relate to the adult person you are now working with.

### ***Human Dynamics***

Human dynamics and variations in our behaviour add more challenges to the difficulties of working together effectively. People vary - some are natural born leaders and communicators, others make great team members but are less inclined to take the risks associated with leadership, while others just want to work alone. Learn to step back and assess your behaviour when human dynamics become a problem. Think before you act. Be diplomatic. Work it out, or get out. Hopefully you find this out during the time when you are testing your working relationship.

### ***Testing Period***

It is wise to set up a short testing period with your child who may become your farming partner. A testing period of two full years where your child works for a wage, or receives a profit share helps to test your working relationship. Can you work together? If it doesn't work out, your child can still go on to set up their own operation without your involvement. Using a testing period leaves doors open, and doesn't create the trap that the new barn and the new mortgage does. If the working relationship doesn't work out and you have left an escape route, you have protected the family relationship. The alternative usually means one less family to come over to your place at Christmas.

### ***Communication***

Communication skills are of critical importance for the successful transfer of a viable operation. Agricultural businesses are growing. Larger businesses require teamwork and coordination. People can't read minds, so they have to learn how to work together effectively. Regular business meetings where communication is open and decisions are made by consensus (as much as is practical) keep conflict to a minimum.

### ***Words***

Watch what you say and how you say it. If you are going to work as part of a team, don't hurt your team members with harsh words. Provide constructive criticism, not abuse. ♦

**Part Two of this article will be in our Fall 2002 Newsletter.**

*This article was written by the Ontario Ministry of Agriculture, Food & Rural Affairs. It is used here with the permission of the OMAFRA. All rights reserved.*

Convenience is without a doubt one of the major reasons why cell phones have been such a hit. Now businesses can use this technology to make the office network into a wire-free zone.

Although wireless networks have been available for some time, the high cost and the limitation of having to buy all of the equipment from the same manufacturer gave purchasers pause for thought. Now wireless standards have been developed that allow equipment from various manufacturers "to talk to each other". This inter-operability combined with improved speed and range, greater affordability, and simpler set ups makes the flexibility of the wireless network attractive to businesses of all sizes. However, the wireless network presents restrictions and risks that you need to assess carefully before you start installing those wireless network cards.

As this technology uses radio frequencies to communicate between computers, the ability to connect your PCs without the cost and inconvenience of installing cables is a very attractive feature.

### ***But is Wireless Secure?***

Security precautions for a wireless network are a very important consideration. After all, you wouldn't let someone with a laptop walk into your office and plug into your company's Ethernet hub. Since the wireless network's radio waves are similar to those used for radio stations and cordless phones, the transmissions could be potentially intercepted by anyone with the right kind of receiver, on the same bandwidth and close enough, say in your company's parking lot, to access your network.

While it may appear that the transmission distance is say just 60 feet, this limit is a result of the smaller antennas embedded within the computer cards. If you don't take the proper security measures, a snoop with a larger antenna may be able to pick up your network's signal from as far away as five city blocks.

### ***The WEP Standard***

As a first step for security, you need to ensure your wireless adapters adhere to the IEEE 802.11 wireless standard. This standard provides several mechanisms for ensuring a secure operating environment but does not in itself prevent all possible misuse of the network. In particular, its encryption ability called WEP (Wired Equivalent Privacy) protects the confidentiality of your network traffic using the wireless protocol.

Depending on the manufacturer and the model of the card, there are two levels of WEP available - one based on a 40-bit encryption key and 24-bit initialization (sometimes called the 64-bit encryption) and a 104-bit key plus the 24-bit IV (sometimes called the 128-bit encryption). The 64-bit is generally thought to be insecure so ensure the system you choose is 128-bit.

Keep in mind that for WEP to work, it has to be enabled at all of the access points of your wireless network. If WEP is not enabled, intruders could not only access your wireless network, but also your company's LAN.

### ***Tips for Protecting your Network***

Here are some strategies that can help you prevent unauthorized access and use of your network, and protect your business-critical information. Most of these tips are good network security practice no matter whether you have a wireless LAN or a hard-wired LAN.

1. Once you have installed hardware or software on any of your systems, always change the password from the manufacturer's default password to one of your own. Use passwords that combine letters and numbers and are at least eight characters long.
2. Locate the access point (AP) for the wireless network in the centre of the office and away from windows.
3. Make sure your wireless router or AP is secured with a password to prevent interlopers from accessing its administrative features.
4. Enable the WEP encryption on the AP and ensure it works.

5. Use a non-obvious encryption key for WEP. Avoid using simple numerical or letter sequences. Don't forget to change this key periodically.
6. Use WEP for data and authentication. By using the "shared key" method for authentication, you ensure that encryption is used to both authenticate the client and encrypt its data.
7. Practice safe sharing on the network. Only "share" those files and programs that you absolutely need to share. Do not share an entire hard drive.
8. Put password protection on everything that is shared. Change these passwords periodically. Of course, if an employee leaves, you should immediately change all access passwords.
9. Install a firewall on each PC to ensure that it isolates data from the Internet or other sources from the rest of the system. Since the firewall is designed to check each packet of data before it arrives or is transmitted through the rest of the system, this measure will help protect the network.
10. Keep your anti-virus software up-to-date and ensure employees are aware of company policies, and carry out proper procedures, to protect all systems against viruses.

### ***Before you Go Wireless***

While wireless adapters are more expensive than the standard kind, you will save on the cost of installing cable. Wireless also makes it easy to move computers around without the need for re-cabling.

Before you purchase, make sure that the wireless network is designed for business and meets the IEEE 802.11 standard. Also be aware that there are two types of wireless LANs and they cannot be mixed together. The 802.11b is suitable for small offices or home networks because it is less expensive. However, it is slower (11Mbps maximum) and its transmission distances average 60 to 100 feet. Just coming onto the market is equipment that meets the 802.11a standard that is suitable for larger offices. It is more expensive but faster (54Mbps maximum) and has shorter transmission distances (40 to 60 feet), which require more access points to cover a typical office.

Also consider that while the WEP protocol prevents immediate access, you will need to take additional security measures to protect your wireless network. Suffice to say that contracting an IT specialist at the outset of this upgrade could save you both money and headaches in the long run. ♦

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## **Taxation** **Smart Investing**

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.

Should you hold investments inside or outside of your RRSP? While there are tax advantages to holding investments that result in capital gains and dividends outside of your RRSP, interest-bearing investments may be best held in your RRSP as the interest income is 100% taxable either way.

If you are not aware of the tax treatment of the income from your various investments, you could be losing some tax advantages.

### ***Capital Gains***

At the current capital gains inclusion rate of 50%, only one-half of any capital gains you make outside of your RRSP is subject to tax. This portion of the gain is included in your income and taxed in the year of the sale. However, if you were to realize that capital gain within your RRSP, the entire gain would be taxable at the time that you withdraw it from your RRSP.

For example, say that you invested \$10,000 in the equity market outside of your RRSP and had the good fortune to later sell at \$15,000. At the current capital gains inclusion rate of 50%, only \$2,500 of this income (50% of \$5,000) would be subject to income tax in the year of sale.

If you sheltered the investment in your RRSP, you would defer the tax until such time that you made withdrawals from your plan. However, the full amount of \$5,000 would be subject to income tax at the time that you withdraw it. Of course, you must weigh the advantage of reinvesting the entire \$5,000 within your RRSP and continuing to defer the taxes on the further income and capital gains.

As you do not have to convert your RRSP until age 69, this tax disadvantage could be offset as the tax on this investment income is deferred until you start receiving it at age 70. Consider also that you may be in a lower tax bracket in your retirement years than you are now.

### ***Dividend Income***

Dividends are also subject to preferential tax rates so your after-tax return is increased when the dividends are received outside of your RRSP. Dividends that you receive from a Canadian corporation are taxed at a lower rate than interest income because of the dividend tax credit. The dividend tax credit is available to taxpayers since the corporation has already paid tax on the earnings that it has distributed as dividends to its investors.

Dividend income received from foreign companies is taxed at the same tax rates as interest income, but a foreign tax credit is available for any foreign taxes that have been withheld.

If the dividends from Canadian and foreign corporations are received within your RRSP, you will defer the tax on this income. However, at the time you withdraw this money, it will be fully taxable as income and you will not have the tax advantage of applying the dividend tax credit or the foreign tax credit.

### ***Mutual Funds***

If you purchase mutual funds outside of an RRSP, the taxation of this investment depends on whether you acquire a share of a mutual fund corporation or a unit of a mutual fund trust. With both, you may receive distributions during the year. With a mutual fund corporation, these distributions are either capital gains dividends, which are treated the same as capital gains with only 50% included in income, or taxable dividends.

A mutual fund trust allocates its income to the unit holders who then report the income, which may include capital gains, dividends, foreign income and other income.

When you sell the unit of a mutual fund trust or the shares of the mutual fund corporation, you may realize a capital gain on the disposition. Also, as discussed above, the beneficial tax treatment of capital gains and dividends is lost if they are received by an RRSP.

### ***Interest Income***

Interest income is fully taxable in the year in which it is received. For example, GICs and bonds produce interest income. Of course, if the GIC or bond is held within your RRSP, the tax on the interest earned is deferred until such time as you withdraw it.

### ***Investments in your RRSP***

Generally, your purpose for holding investments in your RRSP is to provide long-term returns so that you can augment your retirement income in the future. This allows the tax-deferred income to grow within the RRSP. Of course, your RRSP holdings must be invested in qualified investments, which fortunately include a wide range of investment vehicles. When you withdraw the funds, however, keep in mind this income is fully taxable at your marginal rate at that time.

Since various types of investment income receive different tax treatments, you should consider whether you or your RRSP should hold the different components of your asset mix. You should talk to your chartered accountant and your investment advisor about the potential impact of your investment strategies on your income tax position. Keep in mind that each investor's situation is unique as the after-tax return on investments varies according to the individual's income level and marginal tax rate as well as any other tax benefits that may be available. ♦

## VMSW - Mission Statement

We will strive for excellence in the practice of our profession, standing behind our services and our advice, with the best interests of our clients at the forefront.

We will seek out opportunities to serve our clients beyond the traditional scope of our profession, but always within the bounds of its ethics and principles.

We will employ the benefits of technology to improve our processes and add value to the services we render our clients.

Our strength is our people. We are committed to an environment that fosters personal growth, professional challenge and the opportunity to develop our team, and each member, to its fullest potential.

## VMSW - Core Values

### INTEGRITY

- To do what we say we will do...and more
- To do what is right
- To uphold the reputation of the firm, and each individual team member

### TRUST

- To put the interests of the client ahead of our own
- To admit our mistakes, and make them right
- To recognize that our clients rely upon us, and give them no cause for doubt

### INNOVATION

- To seek new services, new processes, new methods
- To constantly improve
- To give due consideration to new ideas

### SERVICE EXCELLENCE

- To deliver the best service of which we are capable
- To make it easier for our clients to run their business
- To deliver on time, complete and error free

### RESPECT

- To treat each member of the firm as you wish to be treated
- To have due regard for the self esteem of all members of the firm

### FRATERNITY

- To take pride in our association with the firm
- To support our fellow firm members in their professional and personal undertakings
- To seek, and to offer friendship with our fellow firm members

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*"The major reason for setting a goal is for what it makes of you to achieve it."*

*Jim Rohn*

