

not taxed on an annual basis. Both of these can provide significant tax savings and deferrals. However, RRSPs do not provide permanent tax relief. You are taxed on your RRSPs in the years that you withdraw funds from the plan (usually your retirement years).

Withdrawals from an RRSP are taxed similarly to employment income. That is, 100% of the withdrawal is included in your taxable income. This makes sense with the withdrawal of the original investments, but what about when it comes time to withdraw the accumulated earnings?

If your RRSP earned you interest income, the taxation of the withdrawal would be the same as if you earned the income in an unregistered account. That is, 100% of the withdrawal / income would be taxable. However, if your RRSP earned dividend income or capital gains, the taxation could be significantly different.

When you earn a capital gain in a regular investment account, you are only taxed on 50% of the actual gain. As noted earlier, when you earn a capital gain in your RRSP, it is not taxed immediately. However, when you withdraw these funds from your RRSP in the future, you will be taxed on 100% of the gain. Likewise, earning dividends in an RRSP will not allow you to take advantage of the dividend tax credit that may have been available if earned outside of your RRSP.

“How often do you consider the future taxation of the investments when making your RRSP contribution?”

Consider the following illustration. Assume you had \$10,000 to invest, and you have chosen to invest in a growth stock which you will sell in five years for a gain of \$7,500. Let's also assume your marginal tax rate each year is 35%, and you plan on retiring in 10 years. If you invested any immediate tax savings, you would earn 3% on those earnings.

If you were to invest this in an RRSP account, the following would occur.

1. In year one, you would make the RRSP contribution for \$10,000 and receive a \$3,500 tax refund.
2. You would invest this tax refund at 3% per annum, compounding annually. After the tax on the interest, this would be worth approximately \$4,160 at the end of 10 years.



3. In five years, when you sold the stock for a gain of \$7,500 you will not need to pay income tax on the gain.
4. At the end of the ten years, you will withdraw the \$17,500 from your RRSP. Your income tax on this would be approximately \$6,130, leaving you \$11,370.
5. When you add in your invested tax savings, your total balance available on retirement will be \$15,530. (Note – this does not include a calculation on any interest income that may be earned on the tax savings earned by not paying tax on the capital gain, since you have already invested the tax savings from the contribution).

Conversely, if you were to invest the funds in a non-registered account, the results would be as follows.

1. In year one, you would invest the \$10,000 with no immediate income tax consequences.
2. In five years, when you sell the stock, you will pay income tax of \$1,310 on the capital gain. Accordingly, after tax, you will have \$16,190 left.
3. You will invest this balance, again at 3% per annum, for the remaining five years before retirement. At the end of this period, you will have \$17,830 (net of annual income tax on the interest income).

As you can see, in this scenario, choosing the growth stock as your RRSP contribution cost you \$2,300 (\$17,830 - \$15,530), or 23% of your original investment.

Does this mean you should not use an RRSP to invest? The short answer is no. RRSPs will provide you many benefits. For example, due to the immediate income tax reduction generated from the RRSP contribution, your initial investment does not tie up as much of your capital. Theoretically, you could invest these tax savings to earn further returns. In the same way, since you are not paying income tax on capital gains earned in your RRSP until a point in time in the future, you could invest these tax savings to earn even further returns.

However, we do recommend that you consider the above when deciding what investments to

choose. This is particularly important if you invest both in registered and non-registered accounts. If you have the opportunity to purchase equity based investments where you expect significant growth in the share value, it may be more tax effective to do so in your regular account. Similarly, interest-bearing investments or income trusts may be good candidates for your RRSP account.

RRSPs continue to be one of the most effective mechanisms to defer income tax. With proper planning, you can structure your investments to ensure you end up in the most beneficial position for their withdrawal during your retirement.

What's in a Name?

Recently, the Institute of Chartered Accountants of British Columbia changed the rules for what public accounting firms can use as their name. Historically, firms have been restricted to using names of their partners, or retired partners. The new rules, while still providing guidelines on the professionalism of firm names, permit the use of non-personal names.

Over the past two years WKM has been exploring the option of using a non-personal name, to reflect the continued growth of the firm. We have invested many hours working with marketing consultants trying to identify terms and phrases that describe the key aspect of our firm. We have interviewed clients, referral sources and our team members. As a result of all of this we have identified a great new name that embodies what we strive to achieve.

“We have identified a great new name.”

We are planning to launch this new name and brand in early 2005. In the mean time, “mum's the word” on what we have chosen as the name.

We would, however, like to invite you to try to guess – just for fun. The name we chose is a one-word name describing an aspect of our client relationships. Send in your guess to

newname@wkm.ca. (To make it a bit easier for you we have, as a hint, used the word at least once in this newsletter.)

The winner will be chosen at random from all correct entries, and will receive a \$50 gift certificate to Felico's restaurant in Richmond.

Industry News

You have probably heard the buzz about the changes to the accounting rules in the USA recently. These changes,

partly in response to scandals such as WorldCom and Enron and the resulting Sarbanes-Oxley Act (“SOX”), have generated many news articles about all of the extra measures that accounting firms are now required to undertake.

Have you wondered how or if these changes will affect you?

The SOX is directed towards companies publicly traded on the USA Stock Markets. A Canadian equivalent, the Canadian Public Accountability Board has mandated parallel changes for companies listed on the TSE. Since WKM does not audit publicly traded companies, our clients will not be affected by this legislation.

The Canadian accounting industry, however, has recently adopted new professional guidelines to address some of the issues exposed by our American counterparts. Specifically, the CICA has adopted new guidelines for assurance engagements (reviews and audits) on the following.

- Independence requirements
- Quality Control
- Error and Fraud Detection
- Revenue Recognition
- Communicating with Audit Committees (or their equivalents)

“Your WKM accountants will also likely need to spend more time with you understanding more of the intricate details of your operations.”

Most of the “new” requirements are merely clarifications on the previous professional standards and guidelines. As such, there aren't the same onerous tasks for accountants as there are for those in the USA trying to comply with SOX.

These changes should not affect you directly. What they do mean to you though is that, where you have engaged us to review or audit your



financial statements, we will be spending more time on your file documenting our adherence to these guidelines. Your WKM accountants will also likely need to spend more time with you understanding more of the intricate details of your operations.

At WKM we have always kept up to date with changes in our industry, and in financial reporting requirements. We have always, and will continue to make every effort to ensure that this is seamless for our valued clients.

Please call your WKM accountant if you have any questions about any of the recent news and changes in the accounting industry. ☎

Closing Entries

Wootton King & Mulhern would like to extend holiday wishes to all of you, our valued clients. As in previous years, instead of sending out holiday cards we have chosen to make a cash donation to the Union Gospel Mission to support their work in helping the less fortunate. We hope you all have a very happy holiday and enjoy a safe, healthy, and prosperous New Year.

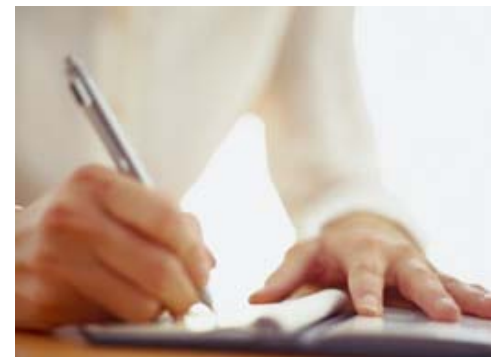


Doug Wootton, Ron Mulhern and Scott Armstrong at the TIAG conference in Madrid, Spain.

WKM continues to benefit from its international affiliation – The International Accounting Group™. Doug Wootton, Ron Mulhern and Scott

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Armstrong recently attended the TIAG conference in Madrid, Spain, where they met with their colleagues from around the globe. The conference featured excellent presentations on a variety of accounting, auditing, business and taxation issues. If you have questions about international issues, or if your business is looking to expand abroad, please contact us for a referral to an affiliated office in that area.



Taxation is confusing enough as it is, without having to wonder who you're paying your tax to. You may have noticed that, about a year ago, the Canadian taxation authority changed its name once again. It is now known as the Canada Revenue Agency (or CRA). This is of course after operating as the Canada Customs and Revenue Agency (CCRA) for several years, and previously as Revenue Canada.

Congratulations to Dr. Gary Albach, of Cogent Chipware Inc., on his recent appointment as Entrepreneur-In-Residence at the university-industry liaison office at UBC, the first such full-time position in Canada. ☎

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More Than Just Bean Counters

You've often heard us say that we are more than just your average bean-counters. Have you ever wondered what we meant by that?

At WKM we have experience in providing many different and unique value-added services to clients in a wide variety of industries. Our clients entrust us with much more than just preparing their financial statements and income tax returns. The following list, while not exhaustive, provides examples of such engagements where we have added value for our clients recently.

- Long-term financial / retirement planning.
- Cash flow projections and forecasts for business planning and banking.
- Business growth and expansion strategies.
- Corporate restructuring to facilitate asset and retained earnings protection.
- Operational realignment to facilitate further access to the Small Business Deduction.



- Due diligence and tax strategies for business acquisition.
- Business disposition strategies, including structuring for and multiplying access to the \$500,000 Enhanced Capital Gains Deduction.
- Business succession and operation planning.
- Shareholder Agreement suggestions.
- Estate planning.
- Remuneration and income allocation strategies.
- General business assistance and advice, including advisory boards.

"Our clients entrust us with much more than just preparing their financial statements and income tax returns."

Please call your WKM professional to discuss any of the above, or similar, services that may be useful to your business. ☎

Choosing Your RRSP Investments

By Scott Armstrong, CA

It's coming to the time of year when you once again will be looking at making or topping up your annual RRSP contribution. Each year you likely go through an analysis of the different investment options available and, in conjunction with your investment advisor, choose one that suits your investment needs. However, how often do you consider the future taxation of the investments when making your RRSP contribution?

We are all familiar with the primary taxation benefits of RRSPs. The contribution that you make reduces your taxable income, and therefore your current tax bill. Further, the income earned by the investments in your RRSP is