

Behind the Counter

Managing Risk

In smaller companies Directors and Officers are sometimes the same persons and they are accountable for their actions. Almost every Act that relates to business holds Directors and Officers responsible and **personally liable** for the debt or actions of the company. Examples of these are the Incorporation Act., The Employment Standards Act and the Income Tax Act. All legislation which may affect the company should be reviewed to identify any risks to the company, Directors, Officers and employees. The company then needs to decide whether they wish to retain, avoid, transfer or control those risks. After identifying the most significant risks, the business owner must choose the best method to manage each risk. Insurance is the most commonly used solution however, there are 4 common sense strategies that are less expensive and should be considered as alternatives.

1. Risk Avoidance means to avoid risk entirely. This is accomplished by only going after the 'sure thing' and eliminating any process or product or service that is thought to give only small profits. Some companies will implement education and training or retraining, modify their processes or institute new procedures to eliminate the risk.
2. Risk Control is the use of methods to reduce the risk and the likelihood of losses. This includes items such as reducing on the job accidents by requiring the use of safety equipment, increasing product quality by implementing quality control and inspection procedures. Installing alarm systems and restricting access to assets can guard against theft. Separating clerical duties, designing effective incentive systems and check points can guard against fraud. The purchasing or selling of foreign currency to match contract or investment flows can prevent foreign exchange loss. Installing sprinkler or alarm systems can protect against loss by fire.
3. Risk Transfer means that the sale contract should state who will be responsible for the loss and to transfer the loss to the other party whenever possible. For example, selling goods from point of origin transfers any transportation losses

over to the purchaser. Requiring that sub-contractors have their own WCB and liability coverage before they are considered as a supplier transfers the risk of loss over to the sub-contractors. Risks of cost delays may be transferred to a construction contractor at the time of negotiating the construction contract. The final example is to transfer the risk to your insurance company.

4. Risk Retention is the amount of risk that the company is willing to accept by self insuring, paying the deductible on a loss and setting the policy coverage limits.

Business risk addresses risk inherent in the structure of the business. A sole proprietorship will bear the financial risk personally. The personal assets, the house, the boat, the car, are all at risk in the business. An incorporated or limited company has limited risk. The shareholders of the company are only at risk to their level of investment, unless they have given a personal guarantee as a Director or an Officer of the company.

Business owners need to keep their personal affairs separate from their business affairs and insulate their personal assets from the possibility of business losses.

Here are some red flags that may indicate business failure. An excessive bad debt write off, rising inventory values, change in employee lifestyle, unexplained reduction in cash receipts, increase in accounts receivable, unread management reports, control logs poorly filled out and not reviewed, and conflicts of interest.

Market risk is a daily occurrence in business and may be due to some sales not materializing or being greater than the capacity of the company to produce. Customers may not pay; inventory may not move; quality control may have failed; technology may make the product obsolete and competition may take the market.

Exporting to foreign markets involves risk due to differences in culture, language, product liability, business practices and accounting practices. If exporting to a foreign country is part of the business, the business owner needs to understand the country, market and the kind of customer or partner. The idea of gigantic profits has lured more than one Canadian businessman to forget proper risk management and dive into a foreign market without proper study only to lose it all.

Even within Canada there are differences in business practices and legislation between the provinces.

Hot Tax Tip

December 31, 2007 is the deadline for most items that are deductible for personal tax filers. These items are moving expenses, childcare expenses, political and charitable donations, medical expenses, paid alimony, safety deposit boxes, paying of salary to a family member from a family corporation, sell property with a capital loss to offset property that was sold earlier that had a gain and RESP contributions. So the next 2 months is the time to make sure you have made all your expenditures so that these expenses will qualify for your 2007 tax return.