BUSINESS RECORDS AND OTHER BUSINESS PRACTICE SUGGESTIONS TO PROTECT AGAINST EXCESSIVE CHILD/SPOUSAL/PARTNER SUPPORT AWARDS

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INTRODUCTION

This document provides only general information. This guidance is subject to any advice that your lawyer has given you, any directions from accounting professionals, any agreements, and any court orders. These suggestions apply primarily to small Albertan private corporations. This document is not "legal advice" or "accounting advice". Laws as well as Canada Revenue Agency (CRA) practices change. You should speak to your lawyer and accountant about these matters, and speak to them prior to making any decisions which could significantly affect a family law dispute, taxes, or business disclosure requirements.

Would you be able to survive if your child/spousal/partner support payments tripled because of poor record keeping? In child and spousal/partner support disputes, business owners/controllers have the responsibility of proving that their expenses are reasonable, that not all profits are available for support purposes, and that payments and benefits to family and friends are reasonable. If your record-keeping is inadequate, you may not be able to prove these facts, and the court can set your income for support purposes at a much higher level than you actually earn, resulting in excessive support payments. It is not sufficient to rely on your accountant or bookkeeper, as they are probably not aware the requirements imposed by family courts, which is a much higher standard than what CRA requires. The more suggestions you follow, the more likely you will be to defend against an excessive claim for support.

In the summer of 2017, the Minister of Finance proposed several changes to the way that businesses are taxed. In particular, if the proposed changes to income sprinkling/splitting between family members are implemented, income distributions to family members will be reviewable by the CRA to test the reasonableness of compensating family members. Although this article focuses on what might be helpful in the context of a family law dispute, a lot of these steps may also help you survive an audit by CRA. It should also be noted that although your accountant/bookkeeper's record-keeping practices might change due to these tax changes, the family courts' ability to challenge compensation and benefits to family and friends is even broader; you should not rely on your accountant/bookkeeper's records alone.

ACCOUNTING AND BOOKKEEPING

Don't prepare your own financial documents. We strongly recommend that you hire an accountant to prepare Financial Statements in relation to your business. Not only are Financial Statements and Income Tax Returns open to attack by your former spouse, but documents not prepared by accountants can increase your legal cost and accounting expert cost in a future family law dispute. Using an accountant will also help to ensure that you're claiming all permissible deductions and credits, which could reduce your taxes.

Use a bookkeeper. Unless you only have a few expenses each year, you're confident in the quality of your own bookkeeping, and you're sure that you can remember the circumstances of each receipt and expense several years down the road, we strongly recommend using a bookkeeper to prepare ledgers setting out each of your receipts and expenses. That said, select your bookkeeper carefully, as they vary significantly in quality. You can ask them for references from other clients, and accountants to whom they've submitted their work, as the accountants will be able to compare their work to that of other bookkeepers.

Send this article to your accountant and bookkeeper. As accountants and bookkeepers usually aren't aware of the requirements imposed by family courts (which set much higher standards than what CRA requires), sending them this article may be beneficial. However, you should still also read this document yourself, as your bookkeeper/accountant won't be able to address all of these suggestions.

LEDGERS

Ledgers, or together, your General Ledger, track your revenues and expenses. It might look something like this (although much longer):

System:	**9/17/2015**	**8:08:41 AM**	**Page:**	**1**
User Date:	**4/12/2017**		**User ID:**	

DETAILED TRIAL BALANCE FOR 2016

General Ledger

Ranges:	**From:**	**To:**		
Date:	**1/1/2016**	**3/31/2016**	**Subtotal By:**	**No Subtotals**
Account:	**-6000-20**	**-6999-21**	**Sorted By:**	**Department**

Description: Consulting **Beginning Balance:**

Trx Date	Jrnl No.	Orig. Audit Trail	Reference	Debit	Credit
1/15/2016	3,570	PMTRX00000033	Purchases	$975.00	
2/15/2016	3,573	PMTRX00000034	Purchases	$975.00	
3/15/2016	3,576	PMTRX00000035	Purchases	$975.00	
Net Change		**Ending Balance**			
$2,925.00		**$2,925.00**		**$2,925.00**	**$0.00**

Use accounting software. Proper ledgers are usually much easier to read, look more legitimate to the courts and your former partner, and contain a better breakdown of each category, which will help prove each expense, and might reduce your legal cost and accounting expert cost in any family law dispute. We strongly recommend against hand-written ledgers. According to PC Magazine, the best small business accounting computer programs of 2017 were Intuit QuickBooks Online, Wave Accounting (Canadian), AccountEdge Pro, Sage 50c Premium Accounting (the successor to Simply Accounting), FreshBooks (Canadian), Xero, Zoho Books, GoDaddy Bookkeeping, Kashoo (Canadian), and OneUp. According to the article, all but Sage come with cell phone access. Some will handle time tracking. Some will even perform payroll (Sage, Quickbooks, Xero, KAshoo, Wave, AccountEdge). Except Sage and AccountEdge, most of these were under $50. See the full article for a comparison of further features and individual reviews: https://www.pcmag.com/article2/0,2817,2458748,00.asp

Ledger entries should be detailed. Don't write just "expense" or "purchase" or leave the description of each expense blank. Doing so will not be sufficient to protect you in a family law dispute. It's much better to write out a long enough description to enable anyone reading it to tell if the entry is an obvious business expense, or whether there might be some kind of personal benefit. Always record who the payment is to, who might have benefited, and which vehicle or phone the expense was in relation to, where applicable. For example, "Pens and paper for commercial office at Staples", "Business license from the city", "Invoice by John Smith for painting office", "Salary of employee Jane Smith", "Intact Insurance for 2007 Dodge Ram", "Meal out of town in Grande Prairie", "Fuel for 2007 Dodge Ram", "Meal with client John Smith", "Repairs to 2007 Dodge Ram", or "Flight to attend medical conference in Toronto". If you provide receipts to your bookkeeper or accountant, you can write notes on the back of the receipts, to help them to write proper descriptions.

Cash. Record cash transactions, and make sure that they're described as cash. If your ledgers don't show any cash receipts, and you're in a type of industry that many people would expect to earn some cash, then an absence of any cash transactions might not be believed. It's very common for former spouses to allege that the business owner received cash in the past, even without any evidence, and courts will often add some cash where it's possible that there might have been some undeclared cash income.

Tips. Along the same lines as cash, record any tips that you've received, and make sure that they're described as tips. If your ledgers don't show any tips, and you're in a type of industry where many people would expect you to earn some tips, then an absence of any tips in your records might not be believed.

Try to avoid claiming obviously-personal expenses. Even one obviously personal expense can make all of your record-keeping look suspicious. I often see liquor purchases, and even if it's for a client it still looks bad. Is a $10 write-off really worth risking higher support payments or an audit?

OTHER RECORDS

Keep track of any loan payments. Only interest can be deducted, but you should keep track of the principal portion of any business loan payments (i.e. the portion that isn't interest), because it might be relevant in relation to child support or spousal/partner support. You'll especially want to keep track of any loans between your business and family members or friends, including amounts borrowed and amounts repaid, along with what day the payment was made.

Keep receipts and invoices. You may need to produce these documents to prove that an expense occurred, or to provide a breakdown of what was purchased. For example, if your ledgers only state that you purchased something from Staples, your former partner could allege that you also purchased personal items at Staples in the past, which would make the receipt very relevant. The same goes for other categories, for example fuel, because your former partner could allege that you also purchased items other than fuel at the gas station, such as snacks or cigarettes. For small and medium sized businesses, it can be helpful to keep these expenses in envelopes, organized by month and year, or by year if there aren't many expenses. They could also be scanned, to reduce the risk of misplacing them.

Especially if you don't have a receipt or invoice for a payment, keep the statements that you do receive. For example, for many expenses that are the same each month won't issue a statement each month, and some loans won't issue a monthly statement either. That means you'll need to rely on whatever statements they do provide, whether that's one initial statement (eg many vehicle loans), annual statements, or another form of statement.

Keep copies of your business bank account and credit card statements. Banks don't keep records indefinitely. After a certain number of years they're not available online anymore, which sometimes means that you have to wait several months for them to be retrieved from archives, which may be too slow if you're suddenly in the midst of a family law dispute.

If you have many regular clients, keep a client list each year. This way if your revenues drop in any year, you can show that it's because you have fewer clients in any year compared to other years.

Records that you'll have to keep for future child support recalculation (as well as spousal/partner support, unless any further spousal/partner support is waived and there's no ability to vary, review, or recalculate). Among others, at a minimum you'll need to keep:

1. Your Income Tax Returns, including copies of all of the tax slips (eg T5) and Schedules;
2. Your Notices of Assessment;
3. Your bank account statements;
4. Your credit card statements;
5. Copies of business cheques written to yourself, family members, or friends;
6. Records of any other payments made to family members or friends;
7. Your business's Financial Statements (showing your revenues and expenses);
8. Your General Ledger (breakdown of each payment received and each expense);
9. The business's annual Amortization Schedule (often referred to as a Property, Plant, and Equipment Schedule);
10. For corporations: records of shareholder loan transactions; and
11. For partnerships: records of your income and draws from, as well as capital in, the partnership.

Keep separate business bank accounts and credit cards. Intermingling business and personal expenses looks bad, and can be difficult to sort through later. Separate business account statements also have the benefit of being another way to help prove that expenses were reasonable and all revenues were recorded.

PERSONAL BENEFITS

Keep summaries of personal benefits. Some accountants or bookkeepers will provide you with a form where you fill in your expenses for your cell phone, vehicle, internet, home office, and similar expenses. Or, you might send a summary to your accountant. If you fill this out or prepare this type of summary yourself, keep a copy, because it will help us determined how much your accountant actually deducted. It's especially important to know what proportion was deducted (eg if you only deduct 50% of your cell phone, or reimbursed yourself $50 each month for the use of your personal vehicle).

Keep mileage. We recommend that you track your mileage for any vehicles that you've ever used for any personal purposes, if you're deducting any expenses in relation to them. This is usually the most effective way to prove that vehicle deductions are reasonable, even if you claim a high per kilometre rate. It also helps to show that the vehicle was actually used for business purposes. As an example of what might be considered reasonable, the CRA's payroll automobile allowance rates for 2016 and 2017 were 54¢ per kilometre for the first 5000 kilometres driven, and 48¢ per kilometre after that. In your mileage log, keep track of the number of kms driven, and where you drove to and from. If you drive to the same location frequently and it's always the same distance, you probably only need to record that distance once in your mileage log. Usually you can't claim travel between your home and office. If in doubt, consult an accountant.

Keep track of who was present at meals. If you're deducting a meal, you can write who was present on the receipt. Briefly writing what business topics were discussed can also help.

COMPENSATION AND BENEFITS TO FAMILY OR FRIENDS

Courts often add compensation or other benefits (eg use of cell phone) paid to family members and friends to business owners' incomes for child support purposes (including salaries paid to your new partner and children). This also appears to be essentially what the CRA intends to start scrutinizing. You can help to protect against this by keeping evidence of their involvement.

Keep time sheets. Even if your family member or friend isn't paid per hour, we strongly recommend keeping track of their hours, in case your former spouse alleges that they didn't provide any services, or were paid excessively compared to the low number of hours worked. Even writing down the number of hours they worked each day is fine. You could also keep track of this on a calendar, although we recommend purchasing a physical calendar with all of the days pre-printed, so that it's more difficult for your former partner to allege that you only wrote it when they pursued you for support. Having the family member or friend fill out, sign, and date pre-printed forms can be helpful.

If they invested in the business, keep documentation proving that they did. For example, bank statements, incoming Interac e-Transfer notifications, gift letters signed for the bank to obtain financing, personal guarantees, or promissory notes evidencing prepayment.

Keep objective evidence of their involvement. It can be helpful to keep track of the projects/tasks they've been assigned. You could also list them on your company website, or keep copies of any forms that they've completed. Print out emails that they send. It can also be helpful to take pictures of them out at job sites several times per year. You might also want to list them on your company website or in social media, as there are services such as archive.org which sometimes archive historical website content, so that you can show that they were involved well before any family law dispute. You could also have them sign and date an employment agreement. Keep in mind the need to comply with privacy laws though.

The above is also important if anyone other than you owns any of the business. For example, if your parents, new partner, or children own all or part of a business, your former spouse might argue that it's actually a sham and you're in control of the business. In that case you will definitely want to keep track of the above. You'll also want to keep track of any evidence that they participated in decisions, for example emails where they made decisions or interacted with the business's lawyer or accountant, as well as any forms and contracts that they had to sign.

PROFITS

Keep yearly records of your plans for remaining cash. We recommend doing this after every year end, to minimize the risk of profit that you haven't even paid yourself being included in your income for support purposes (usually all of the profit will be added into your income unless you have a strong business reason for keeping it all in the business). This should include:

1. Whether the money is needed to keep the business viable (eg to build a float of cash);
2. Any plans or possibility of expansion and growth;
3. The possibility or existence of any economic downturn or uncertainty;
4. Any significant planned business purchases or expenses (or significant business purchases or expenses which occurred after the business's year end);
5. Whether the business or any of its products are still in the developmental stage;
6. The business's minimum monthly loan and expense payments;
7. Records of industry standard compensation (see http://occinfo.alis.alberta.ca/);
8. Any need to acquire or replace inventory;
9. Any receivables expected to be uncollectable; and
10. The business's monetary plans/needs generally.

CAPITAL GAINS, CAPITAL LOSSES, AND BUSINESS INVESTMENT LOSSES

Keep documentation relating to the sale of significant assets and investments. For example, a signed and dated bill of sale.

If the sale proceeds are reinvested into another asset or investment, keep records of that reinvestment. For example, bank account statements showing transfers in and out, and bills of sale for the new asset.

SIGNS OF IMPROPRIETY

If you're claiming poor earnings, try to avoid making significant purchases. Arguing for lower support after buying something like a flashy new vehicle or hot tub often angers former spouses, and makes them believe that you're earning more than you're reporting.

If your revenues drop, try to reduce your expenses. Although most people will do this anyways because it often makes good business sense, some will remain optimistic that the business will recover. It can look like a business isn't declaring all of their revenue when they're earning less but don't make any effort to reduce their expenses. When a client suspects that their former spouse is now working for cash, this is usually one of the first things that I look for.