



Spring 2007 Quarterly

Dear Client,

I don't know about you, but I thought this last winter was extremely long. It seemed that way because I spent many weekends doing construction work on our new summer home in Point Roberts, which was not heated. I got a taste of Point Roberts winters and found out why people don't spend a lot of time there during the winter months.

We broke ground on April 14th of 2006 and as of April 15th 2007 the end of construction was in sight. I have a new found empathy for people who undertake being their own general contractor. I also have an appreciation for people who say they would never do it again and hire an architect from the onset. It's a once in a lifetime event, similar to having kids, lots of pain along the way but lots of learning and growth as the reward. Similar to having kids, you only really know what you're doing after you finished the job and it's too late to go back and change the way you actually did it. I was hoping to have construction completed by June 1st, however, we ran into a glitch that will extend that date out several weeks. In the meantime I will just whine about the aches and pains and keep in mind that it will only be a couple of more weeks until I can kiss my hammer good-bye.

Diabetes – A Modern Day Epidemic

When you hear the word epidemic, you probably think of something like the bird flu. But we're facing a different epidemic – diabetes. Here's what you need to know.

The World Health Organization (WHO) has predicted a 39% increase in the global incidence of diabetes, according to a study published in the medical journal, The Lancet in March 2007. This study of Ontario's population between 1995 and 2005 indicates that the rate of diabetes has increased even beyond the WHO's prediction. This means that you are more likely to know someone that will develop diabetes than ever before. In addition, we are seeing more diabetes in young adults. The younger a person is when diagnosed, the greater the chance of complications from the disease.

There are three types of diabetes:

- Juvenile or Type 1
- Adult Onset or Type 2
- Gestational diabetes

Type 2 is the most prevalent. The Lancet study indicates that in 2005, 17.1% of Ontario's population who were age 50 or older had diabetes and the majority had Type 2. Over the 10 years of the study, the number of people with diabetes increased by 113%, while the population increased by only 17%. The increase in diabetes is attributed to the aging population and obesity.

Most diabetes-related deaths are due to cardiovascular complications, kidney failure and stroke. The Government of Ontario has undertaken an education campaign to alert the public to these complications. According to this campaign, four out of every five diabetics die from heart disease because of the effects of high blood sugar on the heart and arteries.

The Ontario Ministry of Health predicts 300,000 Ontarians don't even know they have diabetes; some of these people will be diagnosed when they apply for insurance. Have you had a check up lately?

Copeman Healthcare Centre

I had been working on our Point Roberts house and put in some long days lifting and moving awkwardly. Several days later, I got pains in my chest. I rationalized that it must be muscle strain from working but in the back of my mind I felt uneasy in dismissing it without checking out to make sure it wasn't heart related.



I had been talking to Jackson Sayers, the VP of Business Development, at the Copeman Healthcare Centre about having Copeman provide my clients with insurance medicals in their beautiful downtown Vancouver facility. I inquired about the services they offered to determine whether or not it was something that would be of interest to me or my clients. They offer an annual membership which costs \$3,500 per year, per person, which provides the member with an annual Comprehensive Health Assessment and unlimited direct access to the many physicians and specialists. The doctors that work under the Copeman banner are salaried, and therefore there is no pressure on them to see many patients. The only obligation they have is to provide quality healthcare to their members, no matter how long it takes. They also offer a Comprehensive Health Assessment on a stand alone basis to allow prospective clients the opportunity to test their services before committing to an annual membership. The cost for the Comprehensive Health Assessment is \$1,200 which can be applied to the membership if you decide to join up.

I was planning to do the Comprehensive Health Assessment to test drive the centre and along came the chest pain. I decide that the assessment would be a good way to find out if the pain was heart related or not. I completed the three hour examination and consultation process, and the follow up session to review the findings. The chest pain I was experiencing was not heart related.

In preparation for my session I had to provide blood samples in advance and make a record of what I ate for the week prior. I arrived at the clinic at 8:30 AM, and after being interviewed and tested by a doctor, a physiotherapist and a dietician, I left at 12:00 PM feeling comforted that my health was excellent and that my chest pain was nothing to worry about. The feedback after each test was immediate which was great because there is no suspense. The final results of all tests along with health and lifestyle improvement recommendations will be provided in a written report when I return for the follow up. During the next two weeks the Copeman team will meet and discuss my results and provide their input in how I can improve my health, or simply how to maintain it. This report provides a base line for comparison for future years when I repeat the process, either annually or otherwise.

My only objection to my experience was the cost. How do you rationalize paying for something which we should be able to get for free? The truth is that you can't get the kind of service that Copeman Clinic gives anywhere else, let alone for free. I have to concede that the value received exceeds the price I paid and I am glad I did it. If you would like to get a comprehensive health assessment done I would encourage you to go to the Copeman Healthcare Centre to see what they have to offer.

TriAccess and the Copeman Healthcare Centre

By using the Copeman Healthcare Centre in combination with TriAccess health insurance coverage that I own I can optimize my healthcare. Please refer to the enclosed brochure for detailed information on TriAccess Insurance. If I were to uncover a health problem I can request a second opinion for diagnosis and treatment from Best Doctors through my TriAccess policy. If the treatment were not available in a timely manner or not available at all in Canada I could request treatment through an appropriate centre of excellence in the US. They would make all arrangements for my transportation and care on an immediate basis. Any procedures would be paid for by Royal Sun Alliance, up to \$3,000,000 over my lifetime except for the amount of my deductible which I would have to pay. Once the procedure was complete, all test results and follow up information would be forwarded to the Copeman Clinic to ensure that the appropriate care protocols were followed providing the best possible chance of complete recovery. I see the Copeman Clinic as being an ideal compliment to TriAccess Insurance.

TriAccess and Benefits Portfolio™

TriAccess Insurance can be wrapped in a new proprietary product that I am pleased to be able to offer my clients. The new offering is called Benefits Portfolio™. It is an exciting and revolutionary new way to provide benefits to employees that is fully web based and easy to manage. Benefits Portfolio is a platform that integrates health and risk management products such as Long Term Disability



Insurance, Critical Illness Insurance, Life Insurance, TriAccess Insurance, Health and Dental Benefits and a Health Spending Account for everything that is not insured that qualifies as a medical expense. It is available only within the context of an employer sponsored benefit plan and provides an in depth summary of features, benefit costs and taxation details to manage a leading edge employee benefits program for groups of 2 to 20,000 employees. Benefits Portfolio™ provides a highly sophisticated and flexible health care spending account engine for managing non-insured healthcare costs.

Portfolio Benefits™ enables an employer to allocate a dollar amount per employee that can be used to purchase insured benefits, as well as non-insured health care, on a tax effective basis. The management of the allocated funds is administered by a third party for a fee which can be a fraction of the cost of managing it in house. The web based portal allows employees access to their benefit information at any time, night or day, seven days a week.

TriAccess is available for employees through Benefits Portfolio. It has a lower dollar limit at a very affordable cost for employers that are looking to differentiate themselves when competing for skilled labour.

Executive Compensation Strategies

I recently attended a tax seminar that focused on the strategies available to business owners and companies relating to bonus incentive executive and employee compensation programs. One strategy in particular caught my attention as being a creative and tax effective method of providing employees with an incentive to grow the business. It uses Stock Options to reward employees for company growth without permanently transferring equity to the employee. This Stock Option has a Cash Out provision with some specific rights and restrictions attached to the options.

A requirement to use this strategy is that you must use an objective method to measure the value of the company. Valuing a private company is challenging but it is possible to develop a formula that reflects the success of the company. The formula must translate value into a share value that will change with the growth of the company. Once that formula is established, it is just a matter of determining the goal for the growth of the company that satisfies the owner's long term objectives.

A Stock Option is a right that entitles the owner of the Option to purchase company shares at a predetermined Exercise Price. Once the share price exceeds the Exercise Price stated on the Option, the Option is deemed to be "in the money". For example, an Option with an Exercise Price of \$100 would be in the money as soon as the shares of the company go over \$100. If the share price went to \$125, the owner of the Stock Option could buy shares for \$100 and sell them for \$125. It is usual that Options would not be exercised until such a time as the owner of the Option wanted to "cash out".

The Stock Option with Cash Out Rights works similarly to the above however, the Option requires that the holder must have the right to have the Options cashed out by the company upon request. In most cases once the options are exercised, the only value to the holder is the ability to convert them into cash, as private company shares are not tradable on any market. For Canadian Income Tax purposes, the employee is entitled to a 50% stock option deduction provided he has the right to ask for cash. The 50% stock option deduction is allowed whether the employee receives cash or exercises the options. The employer gets a deduction if cash is paid, but no deduction if stock is issued. The taxable amount of cash out of a \$100 stock option would be \$50, and after applying a 43.7% tax rate to that amount the tax payable would be \$21.85 versus \$43.70 if the \$100 were received as a cash bonus. This strategy provides the company with the same deduction as a cash bonus however, the tax cost to the employee is half of what a cash bonus would be.

The benefits of using a Stock Option with Cash Out Rights for compensating key employees are several. The Option gives the employee incentive to help grow the company's value, and allows them to realize a benefit by way of the stock option. The net tax payable on the income that is generated by



the “cash out” right is less for the employee than a cash bonus, and the employee gets a full deduction. This method gives the employers the ability to have the employee participate in the growth of the company, without giving up equity in the company.

GRIP Rules in a Nutshell

Bill C-28 creates a new tax regime for “eligible dividends”. It revises draft legislation that was released on June 29, 2006, to implement the 2006 budget proposal that was meant to level the playing field between corporations and Income Trusts. The explanation provided here is simplified to describe the potential practical applications of the new rules. The rules are complex and competent tax advice should be sought to determine how these new rules will affect your specific situation. What follows is a nutshell summary of the rules and how they will affect business owners.

There are two tax rates that are applied to business income in Canadian Controlled Private Corporations. The combined federal and provincial rate applied to the first \$400,000 of income is 17.3% in British Columbia. The tax rate on income over \$400,000 is currently 34.12% reducing to 31% by 2010. The tax rate on investment income earned by a BC corporation is 47.8% with half of the tax payable being credited to a Refundable Dividend Tax On Hand (RDTOH) account. Refundable Dividend Tax is refunded when taxable dividends are paid by the corporation. RDTOH is triggered by the payment of either an eligible or non-eligible dividend.

The common practice in prior years was to reduce business income to the Small Business Deduction Limit by paying bonuses to shareholders. Where capital was required by the business the after tax amount of the bonus was loaned back to the corporation as a shareholder loan. Under the new rules it makes more sense to leave the business income in the corporation and pay tax at 34.12%. This will result in a deferral of 9.58% in tax. Once the new rates have been fully implemented by 2010 the deferral will be 12.7%. Currently if a dividend is paid immediately out of the high rate corporate (eligible dividend) income, the effective flow through rate is 46.29%, assuming a personal tax rate of 43.7%. Flowing income through immediately will result in a higher effective rate than as if the income were paid out as a bonus.

So in summary one can conclude that:

- Income that is bonused out will be less common going forward
- Bonusing out corporate investment income still makes sense
- Leaving income in a corporation at the high rate creates a tax deferral of 9.5% to 12.7% verses bonusing down
- Leaving business income, tax at the low and high rate, in a corporation is still an excellent way to split income through dividend sprinkling

Creative Gift Planning

In the 2006 budget the Conservative government introduced legislation that eliminated the Capital Gains Tax on publicly traded shares that are gifted to a Public Charity. This has opened the door to significant opportunities for high income earners and business owners.

The 2007 budget proposes to eliminate the taxation of capital gains arising from donations of publicly listed securities to private foundations after March 18, 2007. Here is recap of the tax cost of making gifts to both public and private foundations:



Cost of Gifting Summary (Marginal Tax Rate of 43.7%)

\$10,000 Gift	Deduction Tax Savings	Donation Tax Savings	Capital Gains Tax Savings	CDA Tax Savings	Net Cost (Negative denotes profit)
Cash	NIL	(4,370)	NIL	NIL	5,630
Shares – Personal***	NIL	(4,370)	(1,092)	NIL	4,538
Shares – Corporate***	NIL	(4,370)	(1,092)	(582)	3,956
Flow Through Shares* - Personal	(4,370)	(4,370)	(2,184)	NIL	(924)
Flow Through Shares* - Corporate**	(4,370)	(4,370)	(2,184)	(4,490)	(5,414)

*Assumes no growth and no loss relating to the FTS.

**Assumes that if the donation wasn't made the funds would be subject to personal tax rate of 43.7% when paid out to shareholder as a bonus

***Assumes 50% of value is capital gains growth

Office Update

In March of this year my assistant Nicole Bedard left us to pursue her dream of becoming a psychologist. She was working on her master's degree during her time here and decided that it was time to focus solely on her passion of becoming a counselor. We wish her wellness and success on her journey.

If you have called the office recently you would have heard a new voice answering the phones. I would like to introduce you to Tara Forshaw. She is responsible for running the day to day functions of the office, and has taken to her role within our team with a welcome enthusiasm. Tara has begun courses to become educated in insurance and financial planning in order to better assist you.

On behalf of myself, Christie and the rest of my team here at Cove Financial, I would like to extend sincere wishes that you, your family and friends have a safe, happy and healthy summer.

Sincerely,

Cove Financial Planning Ltd.

Bernie Geiss
President