

Stock options and the independent consultant

By PETER MERRICK

During the late 1990s there was a lot written on the value of employees receiving stock options as an employee benefit and the favourable tax treatment this form of compensation received from the Canada Revenue Agency.

However there has been very little discussion on the benefits of using stock options as a way that skilled independent consultants can be paid in lieu of money. Independent consultants may want to explore this alternative during lean economic times.

It was not long ago that we heard daily news about Gen Xers who had just graduated university and had begun working for start-up companies that suddenly went public on some stock exchange. Overnight these 20-something-year-olds would find themselves with more than enough money in the bank to retire comfortably for life.

This was, and still is, the lure of company stock option programs. It seems like a lifetime ago since Jan. 14, 2000, when the Dow Jones peaked at 11,722.98 points and March 10, 2000, when the Nasdaq reached its all-time high of 5048.

Staying positive

The lessons that history has taught us over the last century

about the movement of stock prices can be summed up in eight words: "The downs are temporary; the ups are permanent!"

Stock options might be out of favor as today's preferred form of compensation, but those with vision and faith in our economy know that experience has proven that what most people describe as a bear market is actually a really big sale.

Further, those professionals who embrace stock options as a portion of their employment financial compensation have deep down within them an intrinsic belief that their stock options will be very valuable in the future because the companies they are working with will be successful.

They want to share in that financial success. In the end true optimism is realism. Fear of the future is counterintuitive to the nature of human progress. The Internet, to date, is humanity's greatest invention and it is only 37 years old; just imagine what innovation the next 37 years will bring.

Top talent

When the job market was tight in the late '90s for hi-tech professionals, paying in stock options allowed companies to get access to top talent at below-market prices. This same logic applies when some sectors of the Cana-



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dian economy are soft.

Companies that trade their potential future stock value in options are able to barter for the skills of highly paid consultants today. Including stock options as compensation will, from the employers' point of view, solidify their relationship with their contractors. Also, if structured properly, stock options have no financial risk. There are no tax consequences to either the employer or the independent consultant as long as the options are not exercised. And when the stock options are exercised, the consultant will receive favorable tax treatment on the proceeds of the sale.

If independent consultants are considering receiving stock options as part of the payment, they should be particularly cautious that their relationship is structured contractually so that

CRA will view them as independent, not as employees. The CRA tests individuals on four criteria to determine their status as independent consultants:

Test 1. To what extent does the independent consultant control how the work is done?

Test 2. Does the independent consultant own the tools?

Test 3. Does the independent consultant pass the integration test?

Test 4. What are the chances of profit and loss for the independent consultant?

To help create safeguards from having an employer/employee relationship deemed by CRA, stock options issued to independent consultants should be in the name of their incorporated companies, not to them personally.

All stock option documentation specific to the independent

consultant should be excluded from stock option plans and documents for the company's full-time employees.

Over the last few years the legislation regulating stock options as compensation for employment in Canada have been in constant flux.

It would be highly recommended before considering receiving this type of compensation to seek the advice of a labour and employment lawyer to make sure all bases are covered.

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Free up your time for tax planning



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suggest you go out and buy *The World Is Flat* by Thomas L. Friedman. You may find some of the answers to your time dilemma in that excellent book.

In life, when you do not have time to do everything you want to, you have to prioritize. When it comes to business, your priority should be the core benefit that your firm provides.

Take this one step further and ask yourself, what is the core benefit you provide to clients? Is your core benefit a completed tax return?

All practical problems have multiple solutions.

Ask your clients and I think you will find them saying that the core benefit you provide is the proactive searching for and implementation of tax minimization and deferral strategies.

The problem that arises here is a little like the chicken and the egg. You need to have tax returns completed to have an idea of possible tax planning strategies that you can implement for your clients. And to run a successful

business you need many clients. Many clients equal many tax returns. Preparing many tax returns requires vast amounts of time spent on a task, though important, not accountants' core benefit.

So what is the solution? All practical problems have multiple solutions, but the solution that I want to focus on is outsourcing.

There is a good reason why Nike outsourced the making of their shoes, but kept their marketing department in North America.

They have outsourced activities that are not central to their business to minimize costs and maximize efficiency. They can easily train others to make their shoes, but not to perform their core benefit of customer contact. They are now able to focus more of their time on what they are really selling, image.

Their success speaks for itself, but what of the world of accounting? Accounting is not made of shoes and image you may say!

Here is why it makes strategic sense to outsource the completion of tax returns.

Allowing someone else to complete the forms will mean you may be able to lower your

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