

Marmer Penner Newsletter

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Corporate Year Ends and Income Determination for Child Support Guidelines Purposes

When preparing calculations of income for purposes of the *Child Support Guidelines*, the Chartered Business Valuator is required to consider the pre-tax income from corporate entities that an individual has access to and controls.

Personal income tax returns, which are by April 30 each year (June 15 for self-employed individuals) are prepared on a calendar basis. Corporations are permitted to have any fiscal year end that they choose. Accordingly, fiscal year ends other than December 31 are quite common. The following issue arises: How do you use corporate fiscal information, including pre-tax net income, prepared on a non-calendar basis with respect to the *Guidelines* calculation.

We have selected a corporate fiscal year-end of March 31, 2001 for illustrative purposes. The alternative methods of allocating the pre-tax income from a corporation with a March 31, 2001 year end for the determination of *Guidelines* income for the 2001 calendar year are as follows:

1. **Allocate all the income to calendar 2001**

This is the most simplistic approach, and it may reflect the timing of bonuses which are typically set up at fiscal year end and paid to individuals 180 days later. However, it may not reflect the economic activities or timing of actual cash flow and earnings.

2. Allocate all the income to calendar 2000, on the basis that nine months of the operating fiscal year overlap with calendar 2000

This approach maintains the simplicity as in the above calculation, and reflects the economic period when the majority of the corporate activity likely took place. However, in the majority of small businesses, bonuses are paid out to the individual at year end. Therefore, the individual's access to cash is not realized until calendar 2001, which may de-emphasize the most current income, which is most often at issue.

3. Prorate the income based on months with calendar 2001 receiving 3/12 and calendar 2000 being allocated 9/12

This approach may more accurately reflect the economic period when the corporate income is earned. This approach adds a level of complexity to the calculations, and makes the information a little more complex to disseminate.

4. Allocate all the income to the year where the significant economic activity occurred

For example, a Canadian farming business with a March 31 year end, would allocate all of the income to calendar 2000 because that year contained the growing season. This method does not require any complexity to the calculations. It places a higher level of relevance on the actual period of the corporate economic activity. The period when the activity occurred may also differ from when the corporation was paid, and accordingly was able to provide access to the funds to its owner.

5. Prorate the income based on sales or some other identifiable factor between the two years.

This method would require monthly or segregated information based on the December 31 year end. This specific information is not always available, or it may be prepared internally by management. Therefore, it provides a lower level of assurance than audited year-end financial statements. Similar to the other approaches requiring allocation, complexities arise as well as subjectivities with respect to the best method of allocation.

We do not recommend a single appropriate method for allocating the corporate fiscal income that should be applied in all cases. All of the above five methods may be applicable depending on the facts of the case. Of course, you should always look at available court cases for guidance and should consider the facts of the situation and available information when determining the appropriate allocation method.

This newsletter is intended to highlight areas where professional assistance may be required. It is not intended to substitute for proper professional planning. The professionals at Marmer Penner Inc. will be pleased to assist you with any matters that arise. Please feel free to visit our website at www.marmerpenner.com.