

CHAPTER 1: Taxation – Its Role in Decision Making

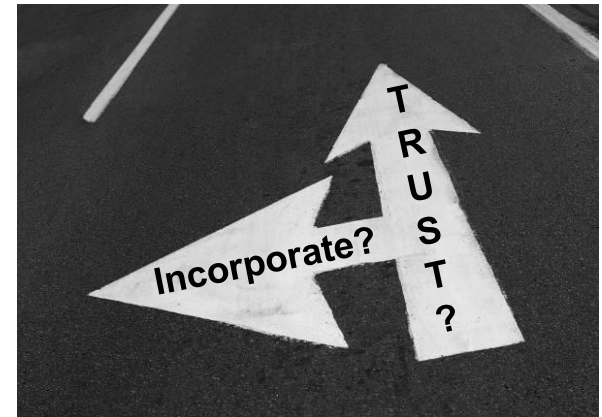
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CHAPTER ONE

Taxation – Its Role in Decision Making

- I. **Taxation and the Financial Decision Process**
 - A. Taxation – a Controllable Cost
 - B. Cash Flow after Tax
- II. **The Fundamental Income Tax Structure and its Complexity**
- III. **Conclusion**



I. Taxation and the Financial Decision Process

- Has an important effect on all financial decisions.
- **Business Decisions on:**
 - the form of business, (Corporation, Self-Employed, Trust, Partnership)
 - raising of capital, (investment in shares, loans)
 - wage and salary (deductible for company, taxable to individuals)
 - business acquisitions and divestitures. (buy assets, sell shares)

are all influenced by their tax treatments.

I. Taxation and the Financial Decision Process

- **Ultimate Goal** – Maximization of shareholder wealth – decisions that:



- Reduce, or
- postpone the payment of tax.

will increase overall shareholder wealth.

- **Return on Investment** measured by cash-flows.
 - Every decision has a tax impact,
 - That tax impact affects cash flows.

GIVE ME A NON-TAX ISSUE !!!!!



I. Taxation and the Financial Decision Process

Including taxation in the decision-making process leads to:

- improved cash flows, and
- the long-term maximization of shareholder wealth.



I. Taxation and the Financial Decision Process

Consider the cost of a 8% wage increase pre-tax value:

Employer:

25% tax rate

6% after tax cost

Employee:

45% tax rate

4.4% after tax value

The real cost to one party is different from the real benefit to the other.

II. Fundamental Income Tax Structure and its Complexity

Major variable in decision making:

1. Taxpayer – three entities:

- i. Individuals,
- ii. Corporations, and
- iii. Trusts.

2. Types of income:

- i. Business,
- ii. Property,
- iii. Employment, and
- iv. Capital Gains.



II. Fundamental Income Tax Structure and its Complexity

Major variable in decision making (cont'd):

3. Forms of Business Structures:

- i. Proprietorship,
- ii. Corporation,
- iii. Partnership,
- iv. Limited Partnership,
- v. Joint Venture, and
- vi. Income trusts.

4. Tax Jurisdictions:

- i. Provincial,
- ii. Federal, and
- iii. Foreign.



Conclusion

- Taxation is a major variable that must be included in all financial decisions
 - **Cannot be made in a vacuum.**
- Taxation as part of the formal decision making process will improve cash flows.

