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Choose with confidence, get the CA and CFP advantage

Tax Tips

July, 2011

Whether or not to incorporate may be one of the most important decisions you will have to make for your business. There are reasons for and against incorporating and the more you know about them, the more informed your decision will be. This article covers the main types of discussions you should have in order to make the very best decision for your business.



*Should you incorporate?
What you really need to know before you decide!*

❖ Deciding to Incorporate your business?

We are often asked for advice relating to the incorporation of a small business, so we have prepared the following article to cover some of the most important aspects of incorporating.

❖ **What is Incorporation?** Incorporation is a business structure available to you to conduct your business activities. A corporation is a legal entity and is considered to be a separate person for tax purposes – it has to prepare its financial statements and file its own corporate tax returns with CRA.

❖ THE BENEFITS

✓ **Credit Proof your Assets:**

You are able to **creditor proof** your personal assets. You can limit your personal liability through incorporation by keeping your personal and corporate assets separate. Personal assets of the shareholders are not available to the creditors of the corporation. One exception would be where shareholders are required to give personal guarantees to banks, for instance.

✓ **Deferral of taxes.**

Most small Canadian corporations are taxed at a low rate of 15.5 % on the first \$ 500,000 of active business income, whereas individual tax rates can be as high as 46% .

The low rate of tax provides the business with the opportunity to defer taxes until the funds are withdrawn from the corporation. The corporation has the incentive to retain surplus funds, for growing its business.

A corporation can also deduct accrued salaries or bonuses in its fiscal year even though paid out after the year end provided that payment is made no later than 179 days after the year end – corporate taxes are thus deferred to the following year.

✓ **Capital Gains Exemption**

A \$750,000 **capital gains exemption** is available on the sale of the qualified small business corporation shares.

✓ **Income Splitting**

Different share classes may allow you to split



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income with family members thereby reducing your tax burden.

❖ THE DRAWBACKS

✓ **Cost of Incorporation**

The **costs** of setting up a corporation and of pre-paring financial statements and tax returns.

✓ **Losses not available for personal income**

Losses are **trapped** in the corporation and can only be used to offset future income from the corporation. They are not available for setoff against your personal income.

General Rule

The general rule is not to incorporate until the business is profitable. You should always seek professional advice before you incorporate.

The information presented is only of a general nature, may omit many details and special rules, is current only as of its published date, and accordingly cannot be regarded as legal or tax advice. Please contact our office for more information on this subject and how it pertains to your specific tax or financial situation.