MITCHELL & PEARCE

PROFESSIONAL CORPORATION

Chartered Professional Accountants

TOP 10 REASONS TO INCORPORATE YOUR BUSINESS

1. **Tax Deferral Opportunities**
   For every $1,000 retained in an incorporated business, the corporation retains an additional $300 over what would have been paid in income taxes had they declared it personally.

2. **Income Splitting**
   Pay a reasonable salary and bonus to family members, including spouse and children for services they rendered to the business. Prepare a job description for the services they each render, and pay a dividend to family members. While the payment of a family salary must meet the "reasonable" test, this does not apply to dividends, which means you can pay a $100,000 dividend to a shareholder who does not provide any services to the company.

3. **Tax Advantage of Capital Gains Exemption**
   In Canada, we still have a wonderful tax break to reward successful entrepreneurship, the $800,000 lifetime capital gains exemption. It allows an incorporated business owner a tax-free capital gain, provided an individual holds the stock in a private company for at least two years.

4. **Paying Capital Gains instead of Salary**
   Clients who own incorporated businesses can structure their cash withdrawals as capital gains rather than salary or dividends. Capital gains are only taxed on half the income earned. So an individual who has fully used his or her lifetime capital gains exemption, who pays himself $300,000 in capital gains, who has an Ontario personal marginal tax rate of 46 per cent, will pay $69,000 in tax as compared to taking the same amount out as salary income. That would require paying the Canada Revenue Agency $138,000 in personal taxes.

5. **Individual Retirement Arrangements**
   If a business owner is over the age of 50, and employed by an incorporated business, they should consider creating a 'super-sized RRSP' – that is, an individual pension plan (IPP) or a retirement compensation arrangement (RCA). Contributions to these two vehicles will exceed maximum allowable registered retirement savings plan (RRSP) limits, meaning the business owner can save a great deal more money for his or her retirement in a tax-efficient way. Both are fully deductible by the sponsoring company and are non-taxable benefits for the individual. Increases in the total value of the assets held are tax-deferred until withdrawn.

6. **Universal Life Insurance**
   Universal life insurance allows tax-sheltered growth within the policy. A corporate-owned life insurance contract can tax shelter much of the corporation's retained earnings in the cash-value portion of the policy, provided the premiums are not deducted. As an incorporated business owner, you can access these funds for business or personal use by collateralizing the policy through loans from a bank. For example, you

might borrow funds annually in order to increase retirement cash flow. It is important that the appropriate documentation and guarantee fees are in place to avoid a personal benefit (which prompts significant unnecessary personal tax). Any related bank loan would be repaid automatically upon death from a portion of the policy proceeds. At the same time, a credit to the corporate capital dividend account (CDA) would be created equal to the full policy proceeds.

7. **Employee Profit Sharing Plan**
   An employee profit sharing plan (EPSP) is a special purpose trust that allows the beneficiaries of the plan to share in the profits of a company. The allocation to an EPSP is taxable in the hands of an employee, and a deductible expense for an employer. An EPSP is a non-registered savings plan in which the employer contributions are computed by reference to a company's profit.
   Advantages of an EPSP are:
   - They attract neither employer/employee Canada Pension Plan or EI contributions;
   - They allow for more control over retirement assets;
   - They are treated as pension and/or RRSP eligible earnings;
   - Source deductions and withholdings are not required by the EPSP trustee or employer;
   - They allow for income splitting opportunities;
   - All amounts paid from an EPSP to an employee are not subject to a reasonableness test, unlike salaries;
   - The 'kiddie tax' rules should not apply to income received by minor children from an allocation from an EPSP, if they are bona fide employees of the business; and
   - Contributions to the EPSP can be made up to 120 days after the corporate year end.

8. **Health Spending Accounts**
   A health spending account (HSA) is a corporate bank account with deposits available exclusively for health care expenses. Having an HSA allows you to convert health care expenses into 100 per cent business deductions equal to the annual deposits into the HSA. Payments of these expenses are treated as a non-taxable benefit to you. You will determine the contribution amount each year and also how to spend the benefit dollars. Unlike traditional medical and dental plans, if the deposits are not spent in the current year, the funds remain in the account, available for future use.

9. **Loan Money for Education and Succession**
   The basic principle behind the loan arrangement is to shift the income needed to pay for education from the parent to the low-income child. The child reports the loan as income when in the low tax bracket, and receives a deduction when in a high tax bracket. Suppose your corporation lends $60,000 to his daughter, including $40,000 for law school tuition. The daughter pays $7,000 tax. When the lawyer-daughter takes over the business and repays the $60,000, she can deduct the payments from the earnings, generating a total net savings of $24,000.

10. **Writing off your Mortgage**
    If you have a mortgage on your home and capital in the corporation, consider writing a cheque from the business to yourself, depleting this capital balance. After using this money to reduce or eliminate the home mortgage, go to the bank for a personal investment/business loan and invest the money back into the corporation. This strategy converts the non-tax deductible interest you pay for your mortgage into a tax deductible investment loan, plus it can also creditor-proof your money.

To discuss any of the above planning ideas or to determine if incorporation is right for your business please contact our office at 519-273-4145.