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Advice that counts

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Quick Facts: Should You Incorporate?

- A self-employed individual can operate one of three ways: as a proprietorship, a partnership, or through a corporation.
- Whichever way you choose to operate, your ability to claim expenses and deductions are the same.
- If you are operating as a proprietor or a partnership, you are taxed on the profits you make – not what you put into your pocket.

A common issue for proprietors and partnerships is the requirement to pay tax when all the annual funds have been spent or allocated. This is usually due to the following:

- The business used current year income to purchase capital assets (assets with a life of more than 1 year and costing more than $500) such as office equipment. The equipment may have cost $3,000 but your deduction for tax purposes is only $300 in the first year.
- A build up of accounts receivable. You may have earned the income, but you have not been paid. For tax purposes you are taxed on the amount you billed, not what you receive.

Many find it beneficial to incorporate because the individual is taxed only on what they receive and the corporation pays tax on the excess. In BC the corporate tax rate is about 13.5% of the first $500,000 of profit; an individual can pay anywhere up to 47.7%.

- As an example, if corporate earnings were $100,000 and a person pays him/herself $60,000 salary per year, the tax savings of operating through a corporation would be just under $12,000.

Common issues for corporations:

- To operate as a corporation, you need to have several sources of income and employees that are unrelated to you.
- There are legal and accounting fees associated with setting up and maintaining a corporation. These costs must be weighed against the tax savings.

Every situation is unique. Please make sure you consult your tax professional so that you get the advice that's right for you.