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Should you incorporate your business?

Most people when starting a business encounter the first obstacle at set up time, whether to incorporate or not. From my experience most people tend not to understand the ramifications of incorporation and unincorporated business set up. There is a big difference between the two, net income of a sole proprietorship or a partnership (unincorporated business) is taxed directly in the hands of the owner on a T1. The incorporated business is a separate taxpayer (entity) with its own tax rates, and reporting style, this all should be considered at set up time. In short this means two sets of tax forms to be filled out (T2 & CT230NT) and strict reporting guidelines to be followed if you incorporate your business.

There are tax and non tax advantages to incorporating as follows:

Tax Advantages	Non Tax Advantages
<p>Tax deferral - corporation eligible for the small business deduction pays tax at about 25% on its first \$200,000 of taxable income. The remaining tax, which is paid by the shareholders upon receipt of dividends from the corporation, is deferred until dividends are paid. When dividends are paid the balance of the tax is levied on the Shareholder.</p>	<p>Limited Liability - liability protection is generally the main non-tax reason to incorporate, and is the main motivation for most incorporations to take place. While a sole proprietor or partner in a general partnership has unlimited liability to creditors of the business, shareholders of a corporation have no such risk. Without the protection of limited liability most entrepreneurs would not take the risks of going into business.</p>
<p>Capital Gains Exemption - the other main tax advantage to incorporation of a small business is the ability to claim the \$500,000 capital gains exemption on a sale of the business.</p>	<p>Directors Liability - while shareholders have limited liability, directors of a corporation are subject to various liabilities. These include liabilities for unremitted source deductions, unremitted P.S.T and G.S.T. and certain environmental liabilities. This means you as an owner of a small corporation will be responsible!</p>

Now really, do a lot of people understand this reasoning, or take it into consideration before deciding on what type of business format to set up? It is something to consider when you decide on what type of business you will be operating. Keep it simple talk to your tax advisor and get the right answers before you spend a lot of time and money setting up something that is not appropriate for your business.

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