

Behind the Counter

Several ways for small businesses to save on taxes

If you are not incorporated, consider incorporating to take advantage of the tax deferrals available. The rule of thumb is that if you are a sole proprietorship and can make full contributions to your RRSP and still have income left over, it is probably time to incorporate. The main reason to incorporate is to take advantage of the lower corporate tax rates, especially if you are in a higher personal tax bracket. You can take income out of the corporation in the form of dividends, but be warned that dividends will not create any contribution room for RRSP contributions, nor will you be able to contribute to CPP.

Another reason to incorporate is if you are planning to sell your corporation in the near future. The shareholders can receive a tax free capital gain of up to \$750,000 if the shares of the corporation have been disposed of and the corporation is a Canadian controlled qualified small business corporation meaning that at least 90% of the income of the corporation is considered to be active business income (not investing).

If you decide to incorporate, a way to split income is to have your spouse purchase shares with her own money and then once the business is successful, dividends can be issued to your spouse as well. Your spouse will need to have a different class of shares to allow the payment of dividends only to that class. If your spouse works for the company on a part-time basis, you can add him/her to your payroll, but the income that you pay your spouse or any family member needs to be reasonable for the amount of work done. If a family member is on the payroll, they may be exempt from EI which may reduce the required monthly payroll remittances.

With the proper documentation, a spouse can loan the company money and receive interest on that loan which will be a deduction for the company, but income for the spouse. The interest rate needs to be reasonable, as defined by the Canada Revenue Agency, in order to be deductible.

If you are considering the purchase of a capital asset, time that purchase near the end of the year to take advantage of the full accelerated capital cost allowance in the following year. Only 50% is deductible in the first year of capitalization. However, you need to make sure that your property is 'available-for-use' before you can take advantage of the capital cost allowance.

Another way to save taxes is to be home based. If your business is run out of your home you can deduct a portion of your home expenses. If you have an office outside of the home, but meet most of your clients at your home, you can also deduct a portion of your home expenses. If your office in home

expenses exceed your income, you can carry the balance not deducted forward to offset income on next year's tax return.

Make sure all your returns are filed on time and that all your taxes are paid on time. This will save you late filing penalties and interest charges.

If you keep excellent records, you will be more likely to take advantage of all tax deductions available to you. You need to keep a mileage log to determine the percentages of business and personal use of your automobile and your meals and entertainment receipts should have the name of the business contact noted on the back of each. You should keep track of all your capital gains and losses that are carried forward so that they are properly offset in future years tax returns instead of expiring.

Finally, evaluate your spending habits and try to turn some of your personal expenditures into business related expenditures. Take advantage of the use of the home office, use your car more for business purposes by combining a personal trip with a business trip, make your business expenditures more business related by taking a client to a ball game, or perhaps taking a second mortgage on your home for business investment purposes. Be warned that membership fees, green fees and the meal after a golf game are not deductible expenses. If the meal expense at a golf course was incurred without conjunction with a recreational activity, such as a golf game, then the meal would still be deductible at 50%.

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