

# Is a professional corporation right for you?

Incorporating allows a business to stand on its own as a legal entity, separate from its shareholders. A professional corporation has similar benefits but follows the additional rules and standards of its governing professional body or association, such as the Law Society of Upper Canada, Engineers and Geoscientists of British Columbia or the College of Physicians & Surgeons of Ontario. Professions that may incorporate include doctors, dentists, veterinarians, lawyers, accountants, engineers and architects. However, this list can vary depending on the province.

**There are many advantages to forming a professional corporation, though the benefits vary from situation to situation:**

## Deferred personal taxation

Businesses and individuals are taxed differently. Corporate tax rates, particularly those for small businesses, are significantly lower than the highest personal income tax rate.

However, new tax rules will limit access to the 'small business deduction' where a corporation (or associated corporations) earns significant passive investment income.

## Income splitting with family members

Another potential advantage of incorporation is the possibility to include family members, such as spouses, children or parents, as shareholders of the corporation. This can reduce the overall family tax bill by paying dividends to family members. However, recent tax changes will tax most dividends to 'inactive' family members at the highest marginal tax rate, thereby significantly limiting income splitting opportunities.

The main exception available to a professional corporation is for family member shareholders (aged 18 or over) who are actively engaged in the business for an average of 20 hours or more per week.

## Capital gains exemption

On the shareholder's death, or on the sale of shares, there may be a capital gains exemption for qualified shares of a small business corporation. In 2019, the lifetime exemption is \$866,912.

## Remuneration flexibility

A business owner can choose to be compensated by a company salary or by dividends, or other forms of remuneration. This offers a lot of flexibility in terms of personal financial planning options. Additionally, incorporated businesses can access the small business deduction on up to \$500,000 of professional income annually, which provides low corporate tax rates.

### Tax-effective borrowing

Business owners may be able to borrow funds from the corporation as a shareholder loan, thereby lowering personal financing costs. However, the tax rules preclude access to most shareholder loans, except for certain specific purposes or for funds borrowed on a short-term basis.

### Asset protection

Business owners may be protected from business creditors when claims are made against the professional corporation; however, this does not protect business owners from professional liability.

While there are many advantages to forming a professional corporation, it is important to weigh the pros and cons of each unique situation. Given recent tax changes, it is especially recommended for business owners to consult with their tax advisor to understand all implications of professional incorporation.



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