THE GLOBE AND MAIL

TAX MATTERS

Year-end tax strategies that business owners need to consider

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So, you're a business owner. Two of the biggest challenges you likely face are succession planning (who is going to take over the business) and tax planning. As for succession planning, it's common in Japan to find talented sons taking over for their fathers. The reason? According to a Freakonomics report a few years ago, the family patriarch usually recruits an "ideal son" to run the business and then adopts him or encourages a daughter to marry him. Hey, you could just as easily recruit the right woman for the job, adopt her, or have her marry your son. Sounds like a great plan to me.

To be honest, tax planning is a little easier. As we near year-end, let me share some tax strategies that business owners need to consider.

Review your compensation mix. Consider what mix of salary and dividends makes the most sense for you for 2019. Generally, our tax law is designed to leave you indifferent between paying salary or dividends (you should have about the same money in your pocket after taxes either way). But the system is not perfect, so do the math – or have a tax pro do it for you. Also, keep in mind the following: If your only source of income is ineligible dividends (those paid out of corporate earnings taxed at the small business rate), you can receive up to $50,000 in 2019 and pay an average tax bill of just 9.7 per cent across the country. Also, dividends don't require tax withholdings or Canada Pension Plan (CPP) and Employment Insurance (EI) contributions. On the flip-side, salaries will provide you with RRSP contribution room (salaries of $151,278 in 2019 will provide the maximum in RRSP room of $27,230 for 2020), and if your company's taxable income is more than $500,000 in 2019, salaries can reduce your corporate tax bill.

Pay salaries to family members. If a family member has provided services to your business in 2019, consider paying them reasonable salaries, wages, or bonuses before year-end if they'll pay less tax than you or your company. An individual can earn up to $12,069 and pay no federal tax, so your business may be entitled to a deduction with little or no tax paid by your family member personally if they have a low income. This idea also provides RRSP contribution room to your family member, can allow for child-care deductions, and contributions to the CPP if the hope is to collect CPP later.

Pay tax-free amounts if you can. If you own a corporation, you may be able make tax-free withdrawals from your company in a few ways: Paying yourself capital dividends if your company has a balance in its “capital dividend account” (which is the case most commonly when the company has realized capital gains in the past or has collected life insurance benefits), returning “paid-up capital” that you have invested in the company, or paying yourself rent if the company occupies space in your home (this income can be offset by deductions against that income such as mortgage interest, property taxes, utilities or repairs).

Manage shareholder loans properly. Have you lent money to your corporation? Consider taking a repayment of those loans if you need cash personally since these will be tax-free payments to you. Further, taking repayment could reduce the passive income you’re earning inside your corporation and reduce the company’s tax bill. On the other hand, if you’ve borrowed money from your corporation, be aware that those loans will be taxable to you unless you repay the amounts by the end of the year following the year you borrow the money. So, consider whether repaying loans before year-end is necessary.

Time the purchase and sale of capital assets. If you’re planning to purchase capital assets, consider buying those assets and putting them to use before your business year-end to begin claiming capital cost allowance, or CCA, sooner. If you’re selling capital assets, you might want to delay the sale until after your year-end to claim CCA for one additional year.

Consider a corporate reorganization. Given the changes to the tax rules that apply to private corporations, it’s time to revisit your planning if you haven’t already. It could make sense, for example, to change your share ownership so that different family members own different classes of shares. Why? So that you can pay dividends on certain classes of shares to certain individuals and not others. You’ll have more control over how you distribute dividend income, which can allow you to avoid the Tax on Split Income rules. It can also make sense to issue shares to certain individuals in the family who may not be subject to TOSI rules and do not own any shares today.

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