



## Professional Corporations Fact Sheet

### STRATEGIES FOR PROFESSIONAL CORPORATIONS (PC's)

- Can save taxes by retaining income in corporation
- Can Invest Surplus Retained Earnings into:  
**Real Estate, Equities, Bonds, Mutual Funds etc.**
- Potential \$500,000 Capital Gains Exemption on sale of business
- Can Set Up Additional Retirement Benefits:  
**Individual Pension Plan**  
**Retirement Compensation Arrangement**  
**Employee Profit Sharing Plan**
- Estate Planning Tool to simplify Taxes at Death
- Can own life Insurance through corporation

### WHO IS CONSIDERED A PROFESSIONAL?

- Accountant
- Architect
- Chiropractor
- Chiropracist
- Doctor
- Dentist
- Engineer
- Lawyer
- Midwives
- Optometrist
- Pharmacist
- Physiotherapist

### KEY DIFFERENCES BETWEEN A REGULAR CORPORATION AND A PROFESSIONAL CORPORATION

- PC's must be legally and beneficially owned by members of the profession.
- Every shareholder of the PC must be a member of the profession (current exception: architects, engineers and pharmacist where majority must be members of profession.)
- All officers and directors of the PC must be members of the PC.
- Name of PC Must include "Professional Corporation".
- Professional remains personally liable for professional liability claims.

## TAX SAVINGS EXAMPLE

- In 2003 first \$225,000 of Annual Business Income, is taxed at 18.60% (Ontario) This increase to \$250,000 in 2004, \$275,000 in 2005 and \$300,000 in 2006.

<b>Example - Ontario</b>	<b>2003</b>	<b>2005</b>
Active Business Income (ABI)	\$100,000	\$100,000
Tax Rate on ABI	18.60%	17.12%
Corporate Tax	\$18,600	\$17,120
After Tax Earnings	\$81,400	\$82,880
Tax Rate on Personal Income <small>*assumes top marginal tax bracket</small>	46.41%	46.41%
Personal Tax	\$46,410	\$46,410
<b>Tax Savings</b>	<b>\$27,810</b>	<b>\$29,290</b>

\*taxes would catch up if paid out personally as dividends, salary or bonus.

## INDIVIDUAL PENSION PLAN (IPP)

- Alternative to RRSP with higher contribution limits
- Contributions by employer and employee are tax deductible.
- The contributions to an IPP are graduated by age, and as such as the individual grows older, their contributions increases by a rate of 7.5% per year (RRSP's has fixed maximum regardless of age - \$14,500 for 2004.)
- Unlike an RRSP, IPP has an ongoing actuarial valuation requirement of 7.5% growth per year which may require additional contributions if the portfolio has underperformed those mandated requirements leading to a further corporate tax deductible expenses,
- Potential intergenerational rollover for family business.

## IPP ALLOWABLE CONTRIBUTION LIMITS

Amounts certified by actuary to fund defined benefits. Sample of maximum year 2003 tax deductibility.

<b>Age</b>	<b>Pension Contribution Limits</b>
45	\$18,600
50	\$20,400
55	\$22,400
60	\$24,600
65	\$25,900

## INVESTING SURPLUS OF RETAINED EARNINGS

- Owning Investment Property or more liquid investments (stocks, bonds, mutual funds etc.) In PC's (excluding primary residence).
- Can build up investments or pay off mortgage faster since more dollars left in PC than would be available if taken as personal income.

- In Case of real estate, mortgage may be assumed by PC.

### **OWNING INSURANCE IN PROFESSIONAL CORPORATION**

- Can purchase Insurance with corporation (life, sickness and income maintenance) policies in PC.
- Can pay premiums with dollars taxed at lower corporate tax rate.  
Ex. If insurance premiums are \$10,000/year
- To pay personally you would need appx. \$18,500 before tax
- To pay through PC-you need to earn appx. \$12,500
- Insurance proceeds may be paid out tax free through the capital dividend account.

### **CAPITAL GAINS EXEMPTION**

- May be able to sell business under \$500,000 capital gains exemption.
- This is still available for private company shares that can result in first \$500,000 of profit from sale being tax free.

### **ESTATE PLANNING TOOL TO SIMPLIFY TAXES ON DEATH**

- Shareholders are deemed to have sold shares owned, not all the assets of the business in the case of proprietorship.
- Shareholders have capital gains to pay, whereas a proprietorship may have to recapture depreciated assets.

### **SETTING UP A RETIREMENT COMPENSATION ARRANGEMENT (RCA)**

- Additional retirement benefit that can allow you to supplement your existing retirement plans while also permitting the corporation to make tax-deductible contributions well in excess of traditional RRSP or pension limits.
- RCA's can also allow some interesting tax savings opportunities.

### **SETTING UP AN EMPLOYEE PROFIT SHARING PLAN (EPSP)**

- Allows you to contribute appx. \$4000 per year per person into plan allowing you to bypass required payments to CPP.
- No withholding tax required.
- Contributions to ESP can be delayed by 120 days for additional tax deferral.

### **DISADVANTAGES OF INCORPORATION**

- Cost of setting up and maintaining corporation (ex. Additional legal and accounting fees.)
- Loss of 10 year 1995 Reserve (this ends 2005.)

- Less flexibility with income splitting and personal expenses.
- As an employee personal deductions reduced.