TAXFILINGS
CANADA

FREE DECISION GUIDE, PLAIN LANGUAGE

Incorporation: Sole Proprietor or Corporation?

Whether to incorporate is half a math question and half a paperwork question — this book gives you both halves without the jargon.

Incorporating too early wastes money every single year — accounting fees, government filings and bank charges for a company that is not yet earning enough to use its advantages. Incorporating too late wastes tax you can never get back. The right moment is not a mystery: it shows up in two questions you can answer this week.

Five signs the corporation conversation is due — how many describe you?	
1	**Profit beyond what you live on.** Money the business earns but you do not spend can stay inside a corporation, taxed at a low business rate for now, and grow before you draw it out. If every dollar goes to rent and groceries, this advantage has nothing to work with.
2	**Someone could sue the business.** A corporation puts a legal wall between business trouble and your house. The wall has gaps — banks demand personal guarantees, and directors stay on the hook for some debts — but it is real.
3	**You might sell one day.** Selling the shares of a qualifying small business corporation can shelter a large slice of the gain from tax. That door only exists if there are shares to sell.
4	**Your income swings.** A corporation lets you pay yourself steadily through fat years and lean ones, smoothing what lands on your personal return.
5	**Contracts demand it.** Some clients and agencies will only engage incorporated suppliers. Sometimes the decision is made for you — but the tax homework still is not.

Fees, rates and limits in this area shift year to year. Treat this book as the map, canada.ca as the current rule book, and the free calculators at taxfilings.ca/tools as the arithmetic.

01 One business, two kinds of plumbing

Sole proprietor: one pipe

The business is you. Its profit lands on your personal return next to any other income, taxed at your personal rates, with both halves of CPP on top. Setup is nearly free, the books can be simple, and a losing year can offset your other income. You carry every risk personally, and a good year is taxed in full whether you needed the money or not.

Corporation: two pipes

The corporation is a separate taxpayer. It files its own T2 return and pays its own tax on profit; you are taxed a second time when money comes out to you as salary or dividends. The prize is what stays inside: profit left in the company has only paid the business rate so far, so more of it is working for you in the meantime.

SAVINGS

The small business deduction gives a Canadian-controlled private corporation a low tax rate on roughly its first $500,000 of active business profit each year — confirm the current limit at canada.ca. The gap between that rate and your personal rate only helps with money you leave inside. To see the effect on your own profit, run it through the corporate tax calculator at taxfilings.ca/tools.

02 The two-question test

Is there profit you do not spend?

Look at last year honestly. If meaningful money stayed in the business after you paid yourself, incorporation has raw material. If you drew out everything to live, the deferral advantage is theoretical — and the yearly costs are not.

Is there risk, or a sale, on the horizon?

Could a job gone wrong cost more than your insurance covers? Do you picture selling the business, or bringing in a partner or investor? Any yes here can justify incorporating even before the profit test is met.

PLANNING TIP

Two yes answers: book professional advice about incorporating this year — waiting has a price too. Two no answers: keep the simple structure, bank the fees, and rerun this test after every year-end. One yes: the details decide, and that is a one-hour conversation with an accountant, not a guess.

03 What a corporation obliges you to do

- [ ] File a T2 every year, even for a year with no activity at all
- [ ] Keep a corporate bank account, never mixed with your personal money
- [ ] Keep separate books — the company's records start clean and stay its own
- [ ] File the registry's annual return — a different filing from the tax return
- [ ] Run real payroll if you pay yourself a salary, with remittances on time
- [ ] Issue a T5 slip if you pay yourself dividends
- [ ] Maintain a minute book — shares, directors, resolutions
- [ ] Keep records six years (today's rule — check canada.ca for the current one)

THE EXPENSIVE MISTAKE

Treating the corporate account as a personal wallet. A draw that is not salary or a declared dividend becomes a shareholder loan, and a loan not repaid on the CRA's timetable is added straight back to your personal income — the costliest casual habit in the owner-manager world. Decide the two ways you pay yourself, and use only those.

04 What it costs, honestly

To set up

A government incorporation fee (federal or provincial), a name search, and — if you use a lawyer or notary — their time. Doing it yourself is cheaper up front, but a share structure drawn wrong is far more expensive to fix later than to draw right the first time. If family members or a future sale are in the picture, pay for the advice now.

Every year after

Accounting fees for the T2 and financial statements, the registry's annual return, and often payroll and GST/HST filings on top. These arrive whether or not the company earned a cent — this recurring bill is exactly what makes incorporating too early a slow leak.

To wind down

Closing costs money too: final returns, dissolution paperwork, sometimes professional help to get assets out cleanly. Corporations are easier to open than to close. Price all three stages before you decide, not just the first.

05 PRECs and professional corporations, in two paragraphs

Regulated professionals — physicians, dentists, lawyers, accountants, and in several provinces realtors through a personal real estate corporation (PREC) — can usually incorporate, but the professional body's rulebook sits on top of the tax one. It decides who may hold shares, what the company may be named, and what work it may do. Where family shareholding is restricted, some of the usual planning room disappears.

The tax machinery inside is the same as any corporation: the win is still profit left inside at the business rate. What incorporation never shields is professional negligence — insurance does that job, incorporated or not. If your regulator allows it and you reliably leave profit in the company, it is often worthwhile; check both rulebooks first, because the details differ by province and by profession.

06 The first ninety days, if you go ahead

- [ ] Incorporate and collect your business number from the CRA
- [ ] Open the corporate bank account before the first sale goes through
- [ ] Register CRA program accounts — corporate tax, GST/HST when required, payroll before any first paycheque
- [ ] Choose a year-end with your accountant — it does not have to be December 31
- [ ] Move contracts, invoices and insurance into the corporation's name
- [ ] Start the bookkeeping on day one — clean books are cheap; reconstructed ones are not
- [ ] Decide salary, dividends or a mix — the salary vs dividend calculator at taxfilings.ca/tools frames the choice
- [ ] Calendar every deadline — T2, registry return, GST/HST, payroll dates

07 Seven questions before you sign anything

Be honest — count the YES lines.

1. The business regularly earns more than I need to draw out and live on.	YES / NO
2. A bad day at work could cost more than my insurance would cover.	YES / NO
3. I can picture selling this business, or taking on a partner, someday.	YES / NO
4. I am willing to keep company money and my money strictly apart, forever.	YES / NO
5. I have priced the yearly accounting and filing bill, not just the setup fee.	YES / NO
6. I understand incorporation mostly defers tax rather than erasing it.	YES / NO
7. I already keep books I would be comfortable showing an accountant.	YES / NO

6–7 · Green
The structure fits. Get advice on share design, then move — delay has its own cost.

3–5 · Yellow
The case is forming but not made. Rerun this page with your next year-end numbers in hand.

0–2 · Red
Stay simple for now and bank the fees. Revisit the day the profit question turns to yes.

08 Your decision week

Day 1
Pull last year's numbers. Write down the profit, what you drew out, and what stayed behind.

Day 2–3
Answer the two questions from page 2 in writing. Show them to someone who will argue back.

Day 4–5
Run the profit through the corporate tax calculator at taxfilings.ca/tools and compare with staying unincorporated.

Day 6–7
Book a consultation and bring the numbers. One hour with facts beats five with feelings.

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Editorial policy. Every guide is researched against primary sources — the Income Tax Act, CRA publications and CPA Canada materials — fact-checked by Udit Gupta, and updated when the rules change.

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