Firm footing for the leap to incorporation

Tax Talk

Scott Taylor

Whenever I'm asked to explain what a corporation is, I start by drawing two circles on my notepad. In one circle I write the person's name, in the other I write "corp."

It's a simple way to illustrate the point that a corporation is a seperate legal entity from the individual. Incorporation builds a divide between your personal finances and your business, limiting your liability should the company go sour. For example, a corporation can claim bankruptcy without requiring the owner to do the same. Of course, the opposite is true as well: you can claim personal bankruptcy without affecting the corporation.

Incorporation isn't for everyone. Business taxes, contracts, lawsuits, and loans are for the corporation to deal with, but as the owner, you're responsible for making sure the business meets its obligations in addition to managing your personal finances. The corporation is your baby, and it requires extra attention in the form of paperwork, bookkeeping fees, and compliance with tax laws.

I bring this up now because lots of owner/operators see the start of a new year as the best time to move from sole proprietorship to incorporated entity. If you're laying the groundwork for a leap toward incorporation and need to know the basics, here are five points to put you on firm footing:

How do I incorporate?: Corporations are created by registering with either your provincial government or with the federal government (talk to your accountant or business advisor about which choice is best for you). The governing body will issue a certificate that says when the corporation officially takes on a life of its own. Think of it as your company's birth certificate. And no, you can't back-date it.

Name games: As a sole proprietor, you and your business are the same entity for tax and legal purposes. Incorporation separates the two. Sometimes I run into people who think that registering a trade name will accomplish the same thing. Not true. Unless the name has an Ltd., Inc., or Corp. on the end of it – meaning you've officially incorporated the business – you and your company are one and the same.

That said, the various endings all mean the same thing. Having one or the other is a matter of personal choice.

Formal processes: A corporation is controlled by its shareholders. You and possibly your spouse will be the shareholders of the company. Typically, with each share comes one vote. If your company has 100 common shares and you own 51 of them, then you have more voting power and can control the company.

Like Royal Bank of Canada or Magna International, your company should have formal processes to elect its leaders and review the performance and direction of the business. The shareholders elect directors and the directors hire the president, secretary, and treasurer. So as the majority shareholder, you can vote yourself director and then hire yourself as president.

Once a year, the shareholders are to have a meeting to review the performance and direction of the company. (Personally, I would have the meeting at a nice restaurant; the company can pick up the tab). Then they re-elect directors for the next year. So you get to have a meeting with yourself, decide whether or not you are doing a good job running the company, and then re-appoint yourself as director. Then of course comes the next tough decision on whether you should hire yourself again as president. Hey, maybe your spouse would do a better job.

Taxes: The corporation will get its own business number (BN) to file GST/HST returns, make payroll deductions to, and to use as an account number for filing its tax return. If you're a sole proprietor now and converting to a corporation, you would close your GST/HST account and if you have one, your payroll account as well.

The company's money: As a separate legal entity, the corporation will sign a contract with a carrier, load broker, or customers. It will show income from trucking and other services, as well as expenses incurred while running that business. Money made by the company belongs to the company, not to you. The company can reimburse you for business expenses you pay on its behalf, but when you take money for personal use it becomes your income.

When it comes right down to it, the act of incorporating is pretty simple. The hard part is maintaining the distinction between the corporation and you personally (remember those two circles?) So in the coming months I'll lay out strategies to help you manage the business side of your trucking business, including tax compliance, how to pay yourself, and what you should know about allocating shares in the company.

Until then, have a safe and happy Christmas. □

@ARTICLECATEGORY:3361;

– Scott Taylor is vice-president of TFS Group, a Waterloo, Ont., company that provides accounting, fuel tax reporting, and other business services for truck fleets and owner-operators. For information, visit www.tfsgroup.com or call 800-461-5970.