PROPEL CPA

Salary Vs Dividends

The Canadian Tax System is designed so that an individual should be indifferent between earning salaries versus dividends from a corporation. Below are examples of the after tax dollar to the individual when paying a Salary versus paying a Dividend

Corporation Eligible for Small Business Deduction in Ontario

	Salary	Other Than Eligible Dividends
Corporation Taxable Income (before tax)	10,000	10,000
Pay Salaries	(10,000)	-
Revised Corporate Taxable Income	-	10,000
Corporate Tax @12.2%	-	(1,220)
After Tax Funds in the Company	-	8,780
Personal		
Salary	10,000	-
Dividend - Other than Eligible	-	8,780
Taxes		
Salary (Highest marginal rate Ontario 53.53%)	(5,353)	-

Other than Eligible Dividend (Highest Marginal Rate 47.74%)	-	(4,192)
Net Cash to the Individual	4,647	4,588
Total Tax Paid (Corporate and Personal)	5,353	5,412

Corporation NOT Eligible for Small Business Deduction in Ontario

	Salary	Eligible Dividends (Paid from General Rate Income Pool, GRIP)
Corporation Taxable Income (before tax)	10,000	10,000
Pay Salaries	(10,000)	-
Revised Corporate Taxable Income	-	10,000
Corporate Tax @26.5%	-	(2,650)
After Tax Funds in the Company	-	7,350
Personal		
Salary	10,000	-
Dividend - Eligible	-	7,350

Taxes		
Salary (Highest marginal rate Ontario 53.53%)	(5,353)	-
Eligible Dividend (Highest Marginal Rate 39.34%)	-	(2,891)
Net Cash to the Individual	4,647	4,459
Total Tax Paid (Corporate and Personal)	5,353	5,541

Other Items to take into consideration when deciding whether to pay dividends or salaries:

DIVIDENDS

- With no other personal income, an individual can receive up to $33,733 tax free excluding the Ontario Health Premium for 2021
- Dividends are not based on work performed in the corporation therefore the shareholder does not need to be an employee and amount paid does not need to be reasonable. Although TOSI (Tax on Split Income) rules could apply to these Dividends
- May require quarterly personal tax installments depending on amount paid each year and the personal tax payable
- If income is too low may have unused tax credits (i.e. personal tax credits plus the dividend tax credit where as if you have salary only personal tax credits to be used)
- Dividends are simple and can be withdrawn at any time
- Potential for deferring tax to next calendar year
- Could be used to minimize cash flow as dividends are not subject to CPP or EI deductions and employer contributions
- Dividends do not affect taxable income of the corporation
- Dividends are not earned income therefore will not create RRSP contribution room
- There is no CPP contribution on dividends and this could affect the CPP pension amount when it is time to collect it.

SALARIES

- Potential to reduce corporate taxable income of a corporation if they exceed the Small Business Deduction Limit thus not paying tax at higher corporate tax rates
- Tax withholdings required in the corporation including potentially an employer portion of CPP and EI. The tax withholdings are required to be remitted regularly each month/quarter
- Can reduce tax payable if a portion of the salary is contributed to RRSP's
- Creates RRSP contribution room to plan for retirement
- Salaries are entitled to Canada Employment Amount (up to $1,245 for 2020)
- Child care expenses can be claimed only when there are salaries paid (earned income)

There are tax planning opportunities that may make dividends or salaries preferable in certain circumstances.

Please contact your Propel Advisor for advice about your situation.

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