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Ontario Psychological Association

Accounting for your Private Practice

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Agenda

Taxation 101

- Employee vs. self-employed
- Incorporation

Accounting 101

- Record keeping
- Compliance
- Levels of assurance

Employee vs. Self-employed

Employee

Advantages:

- CPP, EI, Income tax and other benefits deducted at source (someone else does the calculations)
- No compliance record keeping requirement

Disadvantages

- Limited ability to claim professional expenses
- Minimal control over your work environment

Self-employed

Advantages

- Claim professional expenses
- Control your work environment, whom you work with, hours of work
- ability to earn more income

Disadvantages

- Requires more record keeping to track professional expenses
- practice management

Self-employed or running a business – record keeping

What records should you keep?

Make sure you keep orderly records of all income you receive. Also, keep all receipts, invoices, vouchers, and cancelled cheques indicating outlays of money. Such outlays include:

- salaries and wages;
- **operating expenses** such as rent, advertising, and capital expenditures; and
- miscellaneous items, such as charitable donations.

Your records must be permanent

Whichever accounting or record-keeping method you use, your records must be permanent. They must contain a systematic account of your income, deductions, credits, and other information you need to report on your income tax and GST/HST returns.

Incorporation

Health professionals regulated under the
Regulated Health Professions Act.



Who can incorporate?

Regulated Health Professionals in Ontario

Acupuncturist/Traditional Chinese Medicine

Chiropractors

Dental hygienists

Dental technologists

Dieticians

Massage therapists

Medical radiation technologists

Nurses

Opticians

Pharmacists

Physiotherapists

Respiratory therapists

Audiologists

Chiropodists and Podiatrists

Dental surgeons

Denturists

Kinesiologists

Medical laboratory technologists

Midwives

Occupational therapists

Optometrists

Physicians and surgeons

Psychologists

Speech language pathologists



Who can incorporate?

Regulated Health Professionals in Ontario

Professional Corporation shareholder restrictions

- All of the issued and outstanding shares of the corporation must be owned by one or more members of the same profession.
- All officers and directors must be shareholders.

Specific to **dentists and medical doctors**

- Are permitted to have family members own non-voting shares.
- Spouse must own shares directly.
- A trust for minor children may own shares.
- Adult children must own shares directly.



Who should incorporate?

Establish type of income first

- Fee for service income - qualifies
- Employment income – does not qualify

Factors to consider

- Age (how many more years will you be practicing?)
- Family dynamic (do you have a spouse and children?) Not as relevant to psychologists as cannot have family members own shareholders. However can be combined with family income levels and amount of earnings taken out of the corporation in a given year.
- Lifestyle (what are your personal consumption needs?)
- Resident status - are you and your fellow shareholders Canadian residents?

Why should you incorporate?

Key benefits

1. Tax-efficient income deferral;
2. Tax-efficient corporate distributions;
3. Limitation of liability (in certain circumstances);
and
4. Other benefits



Tax-efficient income deferral

Ontario Budget changes impacting 2014 planning

- Introduction of new personal tax brackets in Ontario
 - \$136,270 to \$150,000 (46.41%)
 - \$150,000 to \$220,000 (47.97%)
 - \$220,000 and above (49.52%)
- Previously:
 - \$136,270 to \$514,090 (46.41%)
 - \$514,090 and above (49.52%)

Example

- tax deferral through a corporation

Professional earning \$500,000 net per year

- Amount required for personal needs (pre-tax): \$300,000
- Tax deferral = \$67,836

	Self-employed Professional	Professional Corporation	Savings
Professional Income	\$ 500,000	\$ 500,000	
Corporate tax on \$200,000 (15.5%)		31,000	
Personal tax on \$300,000 salary		122,000	
Personal tax on self-employment income	221,000	-	
Net	279,000	347,000	
Tax on \$169,000 dividend (top marginal rate)		67,836	
	-		
Net after-tax cash	279,000	279,164	164
Tax deferral		67,836	

Tax- efficient corporate distributions

- Full discretion on future distributions
 - pay dividends in years where family income drops
 - Maternity/Paternity
 - Sickness
 - Fellowships
 - Retirement
 - on retirement - manage distributions with your other sources of retirement income including pensions and RRIF's.
- On retirement, the professional corporation would be deregistered and used as investment corporation. Can then be used as a vehicle for retirement income.

Dividend or Salary

All dividend strategy

Pros

- No CPP costs for the health care professional and the professional corporation
 - 2015 Maximum annual cost $\$2,479.95 \times 2 = \$4,959.90$
- EHT exposure (salaries $> \$450,000$)
- More cash available for corporate investing/insurance structures



Cons

- individual can no longer contribute to RRSP's
- Will reduce or eliminate the ability to collect CPP in the future

Limitation of Liability

Professional Liability

- No limited liability protection provided by the corporation
- Voting shareholder(s) and corporation are jointly and severally liable

Business liability

- Limited liability protection is provided by the corporation (assuming no personal guarantees).
- Examples of business liabilities include:
 - trade liabilities, employment contracts, lease liabilities and non-guaranteed loans.

Other Benefits

- Utilization of cheaper corporate dollars to pay
 - Club/golf memberships with a business purpose
 - Life insurance
 - Meals and entertainment
 - Non deductible penalties and interest
 - Repayment of debt
- Capital gains exemption (discussed later)
- Individual Pension Plans (IPP) and Retirement Compensation Arrangements



Costs of incorporation – initial set-up

- There are costs and complexity associated with incorporation.



On start-up consider:

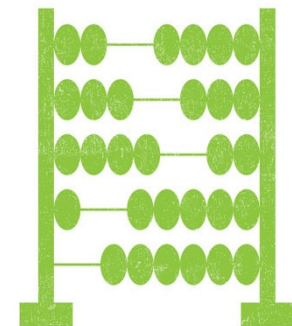
- legal costs to form the corporation
- application for a certificate of authorization for a Health Profession Corporation and annual renewal
- consultation with lawyer, accountant and financial advisor before incorporating

Costs of incorporation – ongoing

- ongoing legal and accounting fees
- additional administrative burden, for example:
 - corporation's record keeping and bookkeeping
 - corporate tax installments
 - annual corporate returns
 - need for separate bank accounts
 - corporate minute book upkeep, such as directors' resolutions, annual meetings, etc.

Accounting 101

- Choosing a trusted advisor/accountant
- Business registration with Canada Revenue Agency (CRA) and your business number(s)
- Record Keeping
 - Accrual accounting vs. cash basis accounting
 - Accounting Software
 - Compliance
 - Payroll
 - Tax



Choosing a trusted advisor

- Importance of having an accountant you feel comfortable with and trust
- Advisor should be familiar with and have experience with medical/professional practices
- depending upon your level of bookkeeping knowledge you may need a bookkeeper as well as an accountant

Business Registration with Canada Revenue Agency (CRA)

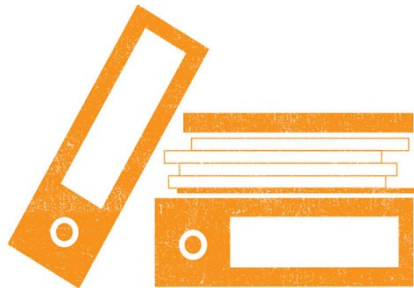
<http://www.cra-arc.gc.ca/bsnsss/menu-eng.html>

- Registration available by mail, phone or Internet
- Business numbers may be required for the following business accounts:
 - Payroll program account
 - Corporate income tax program account
 - GST/HST program account
 - Annual information returns (i.e. Return of Investment Income (T5))

Record Keeping

Cash basis accounting

- Sales are recorded when cash/payment is received.
- Expenses are recorded when payment is made.



Accrual accounting

- Sales and expenses are recorded when they occur, even if no cash changes hands.

Example:

- Sales are recorded when service is provided; payment for the services may not yet be received.

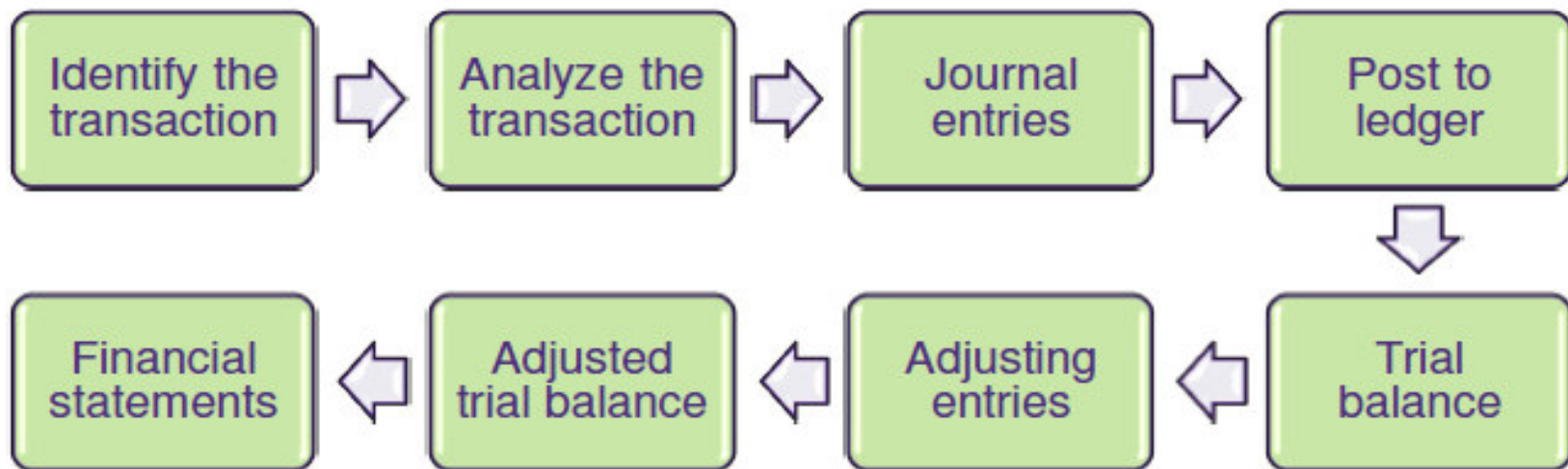
Record Keeping

Commonly used Software for record keeping:

- Excel spreadsheets
- QuickBooks
- Simply Accounting



Accounting cycle



Record Keeping – basic monthly processes

- Monthly reconciliations
 - Bank
 - Credit card(s)
 - Accounts receivable
 - Accounts payable
- Monthly reasonableness check
 - look for unusual balances in accounts
 - look for unusual amounts on the income statement and balance sheet

Record Keeping

Other considerations:

- Outsourcing bookkeeping functions
- Separate "business" bank account
- Separate "business" credit cards
- Corporations
 - Issues related to shareholder advances

Compliance

Payroll

- For yourself and your employees
- Payroll deductions – employer costs
 - CPP
 - Maximum pensionable earnings for 2015 is \$53,600
 - Maximum employee contribution for 2015 is \$2,479.95; employer required to match CPP contributions

Payroll (continued)

- Employment Insurance (EI)
 - Shareholder's with a percentage interest >40% are EI exempt
 - Employee maximum insurable earning for 2015 is \$49,500
 - Employee maximum annual premiums for 2015 are \$930.60; employer match is 1.4 times the employee's premiums

Federal and Provincial Tax

- Deduction based on employee completing form TD1 Form and CRA tax tables

Payroll (continued)

Remitting Payroll Deductions

- Based on average monthly withholding amounts (AMWA)
- Generally, where AMWA are < \$25,000 (starting in 2015); remittance are due on or before the 15th day of the month after the month the employees are paid.
- Accelerated remittances are required where the AMWA is >\$25,000
 - Threshold 1 - \$25,000 - \$99,999 – Payments due the 25th of the same month for amounts paid in the first 15 days and 10th of the following for payroll paid from the 16th to the end of the month
 - Threshold 2 - \$100,000 or more AMWA – payments due within 3 days of the payment based on 7th, 14th, 21st and through to the last day of the month

Payroll (Continued)

Employer Health Tax (EHT)

- Where annual payroll is >\$450,000; requirement to register and file annual return
- Monthly installments required where annual remuneration is > \$600,000

Workplace Safety and Insurance Board (WSIB)

- Registration required by most businesses
 - Recommend contacting WSIB to determine registration requirement
- Premiums are paid by the employer
 - Rates based on guidelines set by WSIB
 - 2014 rate for Office of Psychologists = 0.73/\$100 of remuneration paid

Payroll (continued)

Salary vs. Dividend

- Salary allows for RRSP contributions, whereas dividend payments do not
- Incorporated practices
 - May want to consider salary/dividend mix, depending on individual cash requirements
 - consult with your professional advisor

Compliance

Corporations:

- T2 Corporate Tax Return
 - due 6 months after your year end
 - where there is a balance due, amount to be paid within 3 months of the year-end to avoid non-deductible interest charges
 - Installment payments due quarterly or monthly

Compliance

Individuals:

- T1 Personal Tax Return
 - Employee – due April 30th
 - Limited deductions may include membership dues (where not reimbursed; otherwise Form T2200 may be required)
 - Tuition tax credits
 - Self-employed
 - Due June 15th
 - Where there is a balance due, amounts to be paid by April 30th to avoid non-deductible interest charges
 - There is a requirement to pay quarterly installments after the first year, based on the prior year taxes payable

Compliance

Harmonized Sales Tax (HST)

- Registration required where total taxable sales are > \$30,000
- Most health, medical, and dental services performed by licensed physicians or dentists for medical reasons are considered exempt services
 - No HST charged and no claim can be made for input tax credits (ITC's)
- Medical reports are excluded from the exempt supplies
 - Therefore, HST registration required where taxable supply is > \$30,000
 - ITC's claimed must only be related to the writing/producing medical reports; portion of overhead costs may be possible

Levels of assurance

- Auditor's report
- Review engagement report
- Compilation report (aka - Notice to Reader)

Levels of Assurance

Auditor's Report

- Based on Generally Accepted Auditing Standards (GAAS)
- Provides highest level of assurance, also the most expensive
 - statements must be prepared in accordance with generally accepted accounting principles.
 - Financial statements include Balance sheet, Income statement, Statement of cash flows and note disclosures
- Based on materiality
 - A misstatement in financial statements is considered to be material if the decision of a person who is relying on the financial statements would be changed
 - Auditor provides an opinion on whether the financial statements are presented fairly, in all material respects in accordance with the disclosed basis of accounting
 - Notes are included with CRA filings

Levels of Assurance

Review Engagement Report

- Negative assurance only – no opinion given
- States only that:
 - Based on my review, nothing has come to my attention that causes me to believe that these financial statements are not, in all material respects, in accordance with Canadian GAAP."
 - Procedures consist primarily of enquiry, analytical review and discussion.
- Still requires adherence to accounting standards and full financial statements, including notes.
- Notes are included with CRA filings
- Often the lowest level of assurance accepted by banks and other lenders

Levels of Assurance

Compilation Report (Notice to Reader)

- No assurance provided
- Readers are cautioned that these financial statements may not be appropriate for their purposes.
- Acceptable to CRA
- Can apply accounting standards or not, for example on a cash basis not accrual basis
- however may result in taxable adjustments if audited by the CRA

Can the practice be sold?

- Sale of Practice
 - More common in dental or other practices, with a large capital investment in equipment and building / leaseholds
 - However may be possible for an established practice, that has a good reputation and good referral sources
 - Sale can also be in whole or in stages as new practitioner shareholders or associates are brought in over time and other shareholders retire
- Consult with a professional tax advisor
- Can be selling the shares or the "assets" (i.e. goodwill/customer lists) of the professional practice. Vendors and purchasers are often at cross – purposes as to which

Sale of shares

- CRA has stated that shares of a professional corporation will be eligible for the \$800,000 exemption providing the small business corporation conditions are met, and the shares are qualifying small business corporation shares and they can be sold for value.
- Utilization of one individual's capital gains exemption can result in \$198,000 in tax savings. This saving is multiplied over the number of shareholders.

Sale of shares

- Capital gains exemption \$800,000 on QSBC
 - may qualify for sale of small business corporation
 - rules are complex
 - key is the assets held at time of sale
 - in order to be sure to qualify at the time of sale, practitioners are cautioned to deal with their professional tax advisor well in advance, at least a period of two years or more prior to sale.



Disclaimer

- This material deals with complex matters and may not apply to particular fact situations. As well, this material and the references contained therein reflects laws and practices which are subject to change. For these reasons, the material should not be relied upon as a substitute for specialized professional advice in connection with any particular matter.
- Although the material has been carefully prepared and reviewed, no persons involved in the preparation of the material accepts any legal responsibility for its contents or for any consequences arising from its use.

Thank you

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