

The Basics of Starting Your Own Business

Are you looking to earn some money through self-employment or a side hustle? Here's what to know about the setup and tax implications before you get started.

With job insecurity on many of our minds during the COVID-19 pandemic—and an estimated 44% of Canadians already dealing with job layoffs or reduced income as of late March 2020, according to the polling firm Angus Reid — you might be thinking about starting your own business or side hustle as a way to earn extra money. Before you hang up a virtual shingle, take some time to understand your options:

- Should you incorporate your business?
- How to set up your business (will you need to collect GST?)
- What are the tax implications of being self-employed, even if it's only part-time?

Here's what you need to know.

THE CASE FOR NOT INCORPORATING

One of the biggest mistakes people make when becoming self-employed is jumping to incorporate their business. In many cases, it isn't necessary or beneficial. There are also additional expenses that can take a bite of a small business's slim profits; corporations can cost \$1,500 or more to set up a lawyer/annual bookkeeping, and corporate tax returns can cost \$1,500 or possibly much more with an accountant.

Incorporating does make sense in some circumstances. As a professional or more extensive operation, you might have a corporation if you have employees, an office lease and professional liability. If you have partners, if you expect to be able to leave savings in your corporation, or if you plan to sell your business, those may be reasons to incorporate.

As well, the tax benefits of incorporation can be attractive. Savings you leave in a corporation can be taxed at as little as 10% in Alberta. This tax rate is significantly less than personal income tax rates. If you sell qualified small business corporation shares, you may be eligible for a lifetime capital gains exemption of up to \$883,384 in 2020.

That said, a business can begin as a sole proprietorship or a partnership between two or more people, and subsequently, be converted into a corporation on a tax-deferred basis. In other words, not incorporating now doesn't mean you're locked into that decision forever.

REGISTERING YOUR BUSINESS NAME

If you are going to use a business or trade name other than your legal name, you may need to register the name to ensure it is not already in use. The Alberta Government fee to register a business is \$60.00. You can do it online with several registry businesses and pay them an additional fee to do the work for you.

DO YOU NEED TO COLLECT GST?

Canada Revenue Agency (CRA) is another good source. This link provides information as well as access to Business Registration Online, which you can register to charge and collect GST, to withhold and remit payroll tax for employees (you are not an employee), as well as other potentially pertinent programs.

Before registering, it is crucial to understand the way GST works. You may not need to register at all if your revenues do not exceed \$30,000 per year (technically over four consecutive calendar quarters). That said, you may choose to register to give the appearance of a more significant, more established business.

Once you register, you will need to charge GST on taxable goods and services you sell, provide your business number on invoices, and keep track of the sales tax you collect. GST paid on business expenses should also be tracked. When you file a GST return—a separate tax filing from your income tax filing—you will tally up your sales tax collected on income and sales tax paid on expenses (called input tax credits). The net difference is what you owe to CRA.

REPORTING AND FILING TAXES

An unincorporated business does not have a separate income tax filing. A sole proprietorship or your share of a partnership is reported on your personal tax return—generally on form T2125 Statement of Business or Professional Activities. The statement itself gives a good sense of the types of expenses that are eligible for business expenses, but CRA also provides a good summary here.

If you collect sales tax on your income, you generally report your income and expenses on your tax return exclusive of sales tax. There is an alternative approach called the Quick Method of Accounting for GST, which reduces record-keeping and calculates net sales tax payable on earnings based on a formula that depends on your industry.

A common misunderstanding when starting an unincorporated business is that if you do not take money out of your business bank account, it is not taxable to you. In fact, all net business income you earn is taxable, and is generally taxable on an accrual (as earned) basis—not necessarily when it is received.

Because business income does not have income tax withheld from it the same way as salary does, remember that it will generally result in tax liability at year-end. How much tax you will owe will depend on your other income sources, tax deductions and tax credits. If you owe more than \$3,000 of net tax in two consecutive years, the CRA will ask you to pay quarterly income tax installments. Installments are effectively a prepayment of expected tax owing for the coming year based on the net tax you owed over the past two years.

Record-keeping is particularly crucial for new small business owners as it can be difficult and frustrating to go back and to try to recreate records after the fact. Proper invoices are essential not only for tax purposes but also for optics for clients and customers. Income, expenses, and sales tax collected or paid should be tracked over the year. Consider out-sourcing the bookkeeping service from the very start.

BANKING, BOOKKEEPING AND INSURANCE

Using a separate business bank account is advisable, though not required for a sole proprietorship or partnership. Bookkeeping software is also a consideration, but records can be kept using other methods like a spreadsheet or some other summary or tally of income, expenses and sales tax for the year.

One important matter with self-employment is to ensure you have proper insurance in place if you are leaving a salaried role. This can include disability insurance, life insurance, critical illness insurance, or health insurance if a group plan from an employer no longer covers you. It can also include business-specific liability or other insurance.

There can be plenty of nuances when you are beginning self-employment, a consulting business or a side hustle, but hopefully, this guide is a good start. Speaking to an accountant or a lawyer may be advisable as well. It can be more comfortable and cheaper to do things right than to do them wrong and have to fix them after the fact.

HANNA RABC OFFICE (RURAL ALBERTA BUSINESS CENTRE)

Until June 30th, 2020, you have available to you a business advisory service locally in Hanna. This service is paid for by Alberta Economic Development, and there is no charge to you. Business plans, Financial plans or Marketing Plans or a discussion on the Viability of your business idea within the Hanna and area marketplace.

Contact Craig Berke at craig.berke@hannalearning.com or leave a message at 403-854-2099.

A portion of the above information was taken from Money Sense, Jason Heath writer. It has been adapted to fit Alberta. The information contained within is for guideline purposes only and details applicable to your individual needs should be discussed with your accountant or layer.