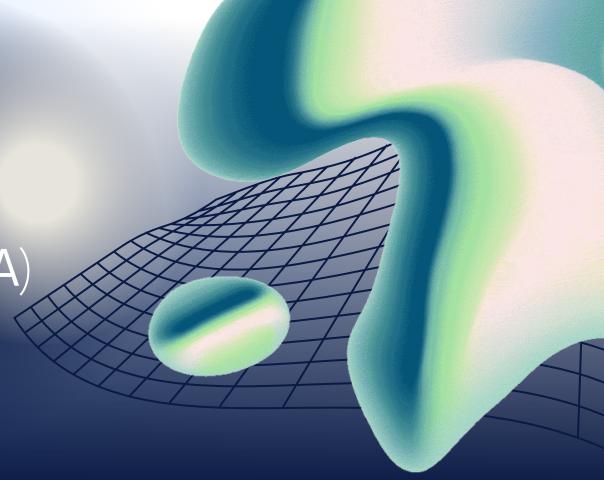


# SALARY vs DIVIDEND

## FOR SMALL BUSINESS OWNERS (CANADA)

How should you pay yourself as a Business owner?



### Paying Yourself: Salary vs. Dividend for Canadian Small Business Owners

As a Canadian small business owner, deciding how to pay yourself—through a salary or dividends—is an important financial and tax planning decision. Each method has its own advantages, disadvantages, and rules. Here's a clear overview to help you make an informed choice.

#### 1. Key Terms

- **Salary:** Regular employment income paid to you as an employee of your corporation. Subject to payroll deductions (CPP, EI, income tax).
- **Dividend:** Payment of after-tax corporate profits to shareholders. Not considered employment income; taxed differently on your personal tax return.
- **CPP:** Canada Pension Plan contributions, required on salary but not on dividends.
- **EI:** Employment Insurance, generally not required for owner-managers.
- **T4 Slip:** Issued for salary income.
- **T5 Slip:** Issued for dividend income.

#### 2. Paying Yourself a Salary

##### Pros:

- **CPP Contributions:** Builds your future CPP retirement benefits.
- **RRSP Contribution Room:** Salary increases your RRSP contribution limit.
- **Consistent Income:** Regular pay cheques can help with personal budgeting.
- **Deductible Expense:** Salary is a deductible expense for your corporation, reducing its taxable income.

##### Cons:

- **Payroll Administration:** Requires regular payroll remittances and filings.
- **CPP Costs:** Both you and your corporation must pay CPP contributions.
- **Immediate Tax Withholding:** Income tax is withheld at source, reducing your take-home pay.

## Important Rules:

- Must be reasonable for the work performed.
- Must remit payroll deductions (CPP, income tax) to CRA on time.
- Issue a T4 slip at year-end.

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## 3. Paying Yourself a Dividend

### Pros:

- **Simplicity:** No payroll remittances or CPP contributions required.
- **Flexible Timing:** Can be paid at any time, in any amount, as long as the corporation has after-tax profits.
- **Potential Tax Savings:** Eligible dividends benefit from the dividend tax credit, which can lower your personal tax rate.

### Cons:

- **No CPP Contributions:** Does not build CPP retirement benefits.
- **No RRSP Room:** Dividends do not create RRSP contribution room.
- **Irregular Income:** May make personal budgeting more challenging.
- **Not a Deductible Expense:** Dividends are paid from after-tax profits and do not reduce corporate taxable income.

## Important Rules:

- Must be declared by the corporation's board of directors.
- Issue a T5 slip at year-end.
- Only paid if the corporation has retained earnings (profits).

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## 4. Other Considerations

- **Mixing Salary and Dividends:** Many owners use a combination to balance tax efficiency and retirement planning.
- **Personal Tax Bracket:** The optimal mix depends on your total income and marginal tax rate.
- **Corporate Tax Rate:** Lower small business tax rates may make dividends more attractive.
- **Provincial Differences:** Tax rates and rules can vary by province.

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## 5. Summary Table

Factor	Salary	Dividend
CPP Contributions	Yes	No
RRSP Room	Yes	No

Payroll Admin	Required	Not required	
Tax Withholding	At source	On personal tax return	
Deductible Expense	Yes (for corporation)	No	
Flexibility	Less flexible	More flexible	

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## 6. Final Tips

- Consult with a qualified accountant or tax advisor to determine the best approach for your situation.
- Keep accurate records of all payments and issue the correct tax slips.
- Review your compensation strategy annually as tax laws and your business circumstances change.

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*This document provides general guidance and ideas. For personalized advice, always consult a Canadian tax professional.*

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