

An Introduction to Business Organization

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What business forms are available to me?

The most common forms of small business in Manitoba are a sole proprietorship, a partnership, and a corporation. Whether you are just starting out or looking to enhance your existing business model, you should give careful thought to the legal form your business takes.



Sound legal advice can guide you around the potential traps and pitfalls facing entrepreneurs, allowing you to focus on building your business. This article is meant to provide some basic information on the three main business structures available to you, highlighting some of the advantages and disadvantages of each business model.

What is a sole proprietorship?

A sole proprietorship is the simplest form of a business. A sole proprietorship is just you, and you alone carrying on a business. There is no legal distinction between the sole proprietor and the business.

What is a partnership?

Technically speaking, a partnership is “the relation which subsists between persons carrying on a business in common, with a view of profit”. This is a broad definition and it can be used to capture a number of enterprises as a partnership even if that was not the intention. When two or more people carry on business together, in the eyes of Canada Revenue Agency they may be considered partners.

If you are already carrying on business with one or more people, you might be deemed to be carrying on business as a partnership and be subject to the laws under The Partnership Act. You and your business associates could experience unintended consequences if your business is deemed a partnership, especially regarding your personal taxes.

What is a corporation?

A corporation is an entity that has the status of a person in law. Every business corporation must have at least one shareholder. Similar to how partners own a partnership, shareholders

own the corporation.

A corporation is more complex than a sole proprietorship or a partnership, however it provides a great deal of flexibility, especially with regard to succession planning.

What are the differences between these business structures?

Two of the main differences between the forms of business are the **tax treatment** of the business entity and the **liability** of the person or people involved in the business.

Liability in a sole proprietorship or partnership

Sole proprietors and partners are **personally liable** for the debts of the business. Everything that a proprietor or partner owns is at risk, including his or her house and financial assets. The assets of one partner can be seized to pay the debts of the partnership, even if a debt is a result of another partner's actions. A wayward partner can have a disastrous impact on the partnership's business and the other partners' personal finances.

Liability in a corporation

Due to the corporation having the legal status of a person, a shareholder's liability is usually limited to his or her investment in the corporation. This means that the personal assets of the shareholder are generally **protected**. However, if a personal guarantee has been given, a shareholder's personal assets can lose this protection.

How is tax calculated?

A sole proprietor's business profit is considered his or her personal income. For a partnership, profit is calculated for the partnership as a whole and then allocated to each individual partner based on his or her partnership interest. The partner's share of profit is considered his or her personal income.

A corporation is taxed as a legal entity separate from the individual shareholders. The taxation rate for a small business corporation is relatively low when compared to the personal rates that are assessed for the profit of sole proprietors and partners.

Following taxation at the corporate level, a corporation's directors can decide to retain the profit rather than pay it out to the shareholders personally. Keeping profit in the corporation avoids personal taxation at higher tax rates. Funds that are maintained in the corporation can be used to pay down debt or re-invest in tangible items such as equipment and machinery.

Is a corporation the best way to go?

A corporation has many advantages that don't exist for sole proprietorships and partnerships. The liability concerns and tax consequences alone are often enough of an incentive for many

to incorporate.

Canadian taxation policy is designed to give corporations an advantage and help incorporated small businesses thrive. A corporation is a great tax planning tool.

What paperwork must I file for my business?

If you want to create a corporation, you will need to file Articles of Incorporation for the corporation to come into existence. Additionally, corporations have a number of annual maintenance requirements.

No matter what form your business takes, you may need to register your business name if you carry on business using anything other than your legal name.

There are also registration and reporting requirements for tax schemes such as Retail Sales Tax and Goods and Services Tax.

What can TDS do for me?

No matter what stage you are at with your business, the lawyers at TDS would be happy to meet with you to discuss your options. There is no 'one size fits all' approach to business organization. Your specific situation and personal interests will determine what approach is right for you.

The lawyers at TDS can assist you in determining your best course of action for moving forward. We can outline the legal considerations you may face and prepare the legal documents to protect you now, and in the future.

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