



The Top 5 reasons that business owners should pay themselves a salary and have RRSPs

In my experience, business owners dislike RRSPs. They don't understand them, and they don't like taking the money out of their corporation. So, most business owners build up cash and even investments in their business corporation. While understandable, it's terrible planning and here are the top 5 reasons business owners should pay themselves a salary (around \$100,000) every year, and contribute the most they can to a RRSP:

1. **They're creditor exempt.** In Saskatchewan, RRSPs, RRIFs, and pensions are creditor exempt. Creditors can't touch them. When times are good, business owners can't fathom that things could ever get so bad that they might need creditor protection. But when times are bad – there isn't the cash available to take out of the corporation, and if you did, a creditor might attack it as a "fraudulent conveyance".
2. **They're creditor exempt.** Same as above. You might think it would be impossible for things to get so bad that all of your accumulated wealth in the corporation would evaporate. You might think "there's no way I would let that happen – I'd sell out first". Famous last words. In my experience, most small businesses can weather one serious negative occurrence, and maybe even two. Business owners being the resilient, hard-working people they are, they will go the extra length to turn their business around when times are tough. Some succeed. Usually, the first negative occurrence is solvable and can be weathered with hard work and diligence. But the second one might put them on the ropes – cash flow becomes a challenge, and they have to scramble to make payments. Hard work, good management and a good year can turn that around. The problem is that when the third one happens, it's a knock out punch and it's not pretty. Most of these are unpredictable and beyond your control – it might be a terrible weather event, terrorists crashing a plane into a skyscraper, a downturn of the US dollar, a stock market crash, a fraudulent employee, or a global pandemic...
3. **They're creditor exempt.** A RRSP, RRIF or pension is just a special type of tax account. It simply means that the money inside it has never paid tax. You can invest in nearly anything you want with your RRSP. I don't care what you invest in (you can invest in shares, mutual funds, GICs, even mortgages), I just want you to have a creditor-exempt, protected nest-egg. That being said, a small business is a high-risk investment and probably makes up the majority of your wealth – so perhaps something a little safer would be a good idea for your RRSP.
4. **They're creditor exempt.** Perhaps you haven't been paying attention... I cannot emphasize enough how important this is.
5. **They're creditor exempt.** Hopefully, at this point you can see why this is necessary, not optional.

There are some other reasons why it can be helpful to have RRSPs if you're a business owner:

At some point, you're probably going to want to retire. Maybe you have a child or children who want to carry on the business, and a child or children who aren't involved in the business. In that case, having liquid assets like **RRSPs can help with dividing the estate** between your children when you die. Otherwise, your choice might be to force a business-involved child to buy the business from you so that there is cash for their siblings, or to leave a very unequal and low amount to the uninvolved children.

Another reason was hinted at above – good financial planners always recommend that you **diversify your risk**. Don't have everything in one type of investment (like stocks), one market (like Canada), one sector (like banking or energy), one city, or one business (including yours). Having a RRSP allows you to diversify your wealth and risk, instead of having all your eggs in one basket.

RRSPs are another way to have **tax-sheltered growth** of your investment. It's one of the biggest gifts the government has allowed. It's crazy not to use it.

Taking money out of your corporation makes sure you **get your money working for you**. Lots of small business owners sit on cash – it makes them feel good and safe. They remember when things were harder, and having this cash reserve gives them a feeling of security. On top of that, they know that if they take the money out, they'll have to pay tax and they hate doing that. But having cash sitting there means that money isn't working for you. Any money that you pay out as salary and then put into an RRSP means the tax is deferred to a later date (when you take the money out of the RRSP). So the RRSP enables you to continue to put off paying the tax but also having your money work for you.

Finally, **leaving cash in your corporation might cost your family a lot of tax!** When you sell your business or if you should die (you're deemed to sell), there will likely be a big capital gain on your business. The government has given you another big gift – the capital gains exemption. That means that your first million dollars of capital gains could be tax-free. But it's only available for the shares of a *qualified small-business corporation*. If you have too much cash in your corporation, your business won't qualify. That's why lawyers and accountants will recommend creating a holding corporation once you start to build up cash. But if you pay the money out to yourself, and put it in a RRSP, you can keep your business eligible for the capital gains exemption and delay the costs of setting up another corporation.