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7 Tax Saving Strategies for Pharmacy Owners

The #1 question we get from pharmacy owners is:

“How can I save money on taxes?”

There are over 250 tax strategies available to pharmacy owners in Canada. However, most do not take advantage of these savings because their accountants don’t know about them. Most pharmacy owners think their accountant is helping them save money on taxes but the truth is, they are just getting their tax return filed.

Our professional pharmacy accountants have heard this complaint time and time again from thousands of pharmacists across the country. Many of you are frustrated that you aren’t getting the advice you are looking for to pay fewer taxes, grow your pharmacy, and build your wealth.

Don’t rely on general accountants to save your money, our pharmacy-focused accountants know how to help you save on taxes. Every pharmacy owner should use our top 7 tax savings strategies - they promise tax savings ranging from $6,872 per year to over $238,802 when you sell your pharmacy.

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1. Pharmacy Specific Corporate Structures

Many pharmacy owners are the sole shareholders of their corporation, meaning that they will overpay in taxes when it comes time to sell their pharmacy. Instead of overpaying on taxes, take advantage of your spouse or family member's capital gains exemption.

Every Canadian gets a lifetime capital gains exemption, a tax incentive to encourage people to start or buy a business in Canada. For each spouse or other family member that you add as a shareholder, you can save up to $238,801 in taxes at the time of sale.

Here's an example showing how much tax you would pay if you started your pharmacy from scratch and sold it for $2 million. Let's consider two scenarios, how much would you receive after-tax if:

Scenario 1: you were the only shareholder in your pharmacy
Scenario 2: you and your spouse are shareholders in your pharmacy

	1 Shareholder	2 Shareholders	
Pharmacy Sale	$ 2,000,000	$ 2,000,000	
Less: Capital Gains Exemption	$ 892,218	$ 1,784,436	1
Capital Gain	$ 1,107,782	$ 215,564	
Tax Payable	$ 296,498	$ 57,696	2
After-Tax Proceeds	**$ 1,703,502**	**$ 1,942,304**	
TAX SAVINGS	**$238,802**		

(1) 2021 Lifetime capital gains exemption = $892,218 per person
(2) Capital Gain Tax = 50%; assume highest marginal tax rate in ON (2021) = 53.53%

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As you can see, each lifetime capital gains exemption is worth up to $238,802 in tax savings. Thus, the goal is to multiply this exemption so that you can sell your pharmacy in the future for little to no taxes.

There are many options as to who can be shareholders. Your spouse, adult family members, and minor children can be included as shareholders. No matter who you choose to be shareholders in your pharmacy, they do not have to be a pharmacist or have any decision-making power in your business. You can simply take advantage of their lifetime capital gains exemption to grow your business and save on taxes.

Now, you can't just add a shareholder at a snap of a finger. There needs to be a completed valuation, then a reorganization of the corporation to add shareholders. This comes with valuation, accounting, and legal fees, so a cost-benefit analysis should always be done first before moving forward. Each province also has different college rules as to who can be a shareholder.

It is incredibly important to choose an accountant that specializes in pharmacy and understands these rules. Pharma Tax can help you assess if this strategy is right for you and help you avoid mistakes.

2. Split Income With Family Members

If you are in a higher tax bracket than other adult family members, you are overpaying in taxes as a family. You can easily lower your family income taxes by shifting some of your income - which is taxed at a higher tax rate - to a lower-income family member who is taxed at a lower tax rate.

In 2018, the federal government stopped service-based businesses from participating in tax splitting. This barred dentists, doctors and other service-based healthcare professionals from saving on their taxes through income splitting. Many pharmacy owners also miss out on these savings because most accounting firms paint pharmacies with the same brush as other healthcare professionals when, in actuality, pharmacy is a product-based business.

Even in today's era of Tax on Split Income (TOSI), pharmacy owners can still split income with family members whether they work at the pharmacy or not.

Take our clients Neil and Nicole for example:

Neil is the pharmacist and his wife, Nicole, is not. Nicole works in the front shop of Neil's store helping customers. There was a large difference between Neil's tax bracket and Nicole's tax bracket and, after consulting with Pharma Tax, they implemented the income splitting strategy.

	No Income Split	Income Splitting	
Pharmacy Owner Salary	$ 180,000	$ 114,000	
Spouse Salary	$ 48,000	$ 114,000	
Family Gross Income	$ 228,000	$ 228,000	
Tax Payable	$ 70,427	$ 63,555	1
Family Net Income	**$ 157,573**	**$ 164,445**	
TAX SAVINGS	**$6,872**		

(1) Using 2021 ON marginal tax rates and assuming no other deductions

Now, Neil and Nicole are saving $6,872 per year in taxes this year and every year going forward. Over 5 years, that is $34,360 that would have been wasted on taxes instead of keeping that money for themselves.

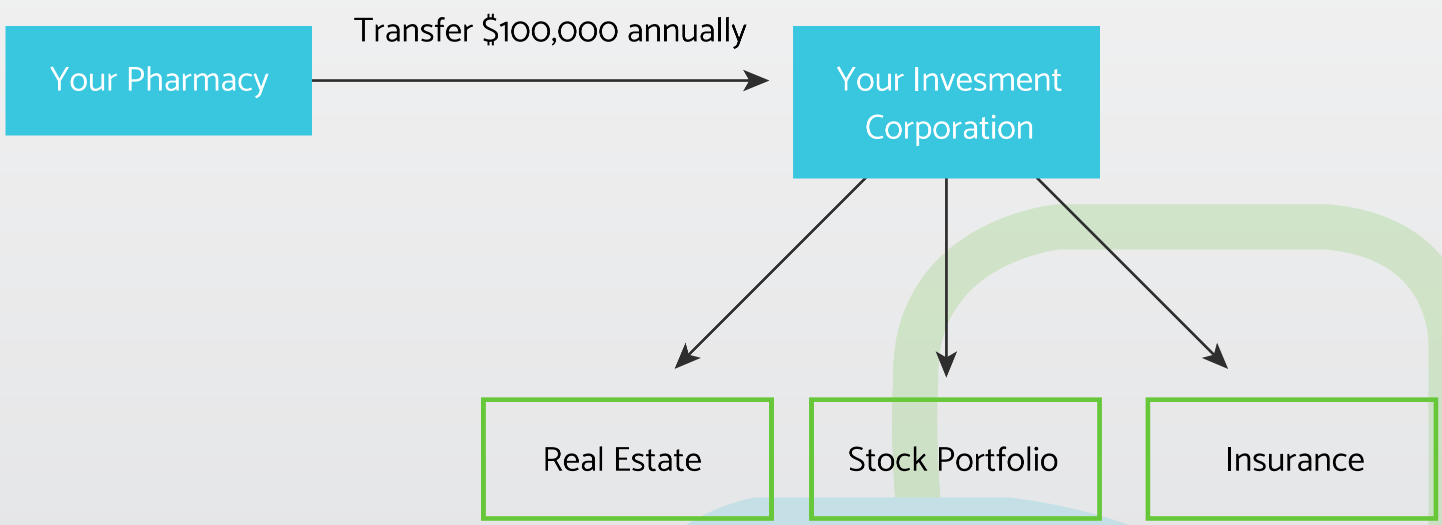
What would you do with an extra $34,360?

3. Pharmacy Cash Flow Strategies

Many pharmacy owners ask us, “I have extra cash in my business bank account, what should I do with it?” It’s a great question, and the answer is it depends on what your goals are. Typically we recommend two things:

1. Reinvesting into your pharmacy to help grow your store and/or start another pharmacy
2. Keep enough cash to cover 2-3 months worth of expenses

If you still have idle cash, it is time to set up a separate corporation, often called a holding company or investment corporation. Any excess cash can be transferred to this holding company and used to build your retirement fund. You can invest in real estate, start an investment portfolio, or hold any permanent insurance retirement strategies.



A common mistake that pharmacy owners make is that they place these investments inside their pharmacy corporation. This is a mistake because when you sell your pharmacy in the future, you are selling the pharmacy itself, not the investment portfolio and/or real estate properties. That’s why it’s important to set up a holding company and have these investments grow inside there; you will never sell this holding company and it will serve as your retirement income for the rest of your life.

A holding company is also useful when you own multiple pharmacies. You can use this corporation and centralize income to this corporation for a variety of reasons including:

1. Charge as a relief pharmacist to each of your pharmacies
2. Charge a management fee to run your pharmacy
3. Extract your share of the profits from each pharmacy

Once the income is inside this holding company, you can withdraw your salary from this corporation, charge car mileage driving to/from each pharmacy, and invest any leftover money.

There are multiple ways to get money from your pharmacy or pharmacies into a holding company or investment corporation. Having a pharmacy accountant that understands these strategies can help you determine what the best option is going forward and how to make your money work for you.

4. Maximizing Tax Deductions

As a business owner, the tax law is filled with breaks to help you save more of your money. You simply need to take the time to understand the rules to know what you can claim as a deductible. Essentially, the more deductions you make, the lower your taxable income is. This helps save a great deal of money on your pharmacy's taxes.

Here are some great examples of what you may be able to claim as taxable deductions:

- Travel expenses
- Professional development
- Child care
- Mileage & auto expenses
- Moving expenses
- Start-up or expansion expenses
- Charitable donations

A very common mistake that we see is paying for medical expenses personally. Generally, your corporation cannot pay for your medical expenses directly unless it is done through a health insurance plan. However, you do not need a group benefits plan. A health spending account is a great way to save on medical expenses.

For example, our client Sandy has a daughter who needed braces. Sandy was going to pay for her daughter's braces personally until she spoke to us. We helped her set up a health spending account and she used this to pay for her daughter's braces. Doing so saved her $2,793 in taxes!

	Paid Personally	Paid with HSA	
Cost of Braces	$ 7,500	$ 7,500	
Claim Admin Fee & Tax	$ -	$ 1,612	1
Personal Income tax	$ 4,405	$ -	2
Income Required To Pay For Braces	**$ 11,905**	**$ 9,112**	
TAX SAVINGS	**$2,793**		

(1) Admin Fee 10% and Tax (HST and Premium Tax for Ontario)

(2) Marginal tax rate of 43.41% on annual income $125,000 in Ontario less Medical Expense Tax Credit

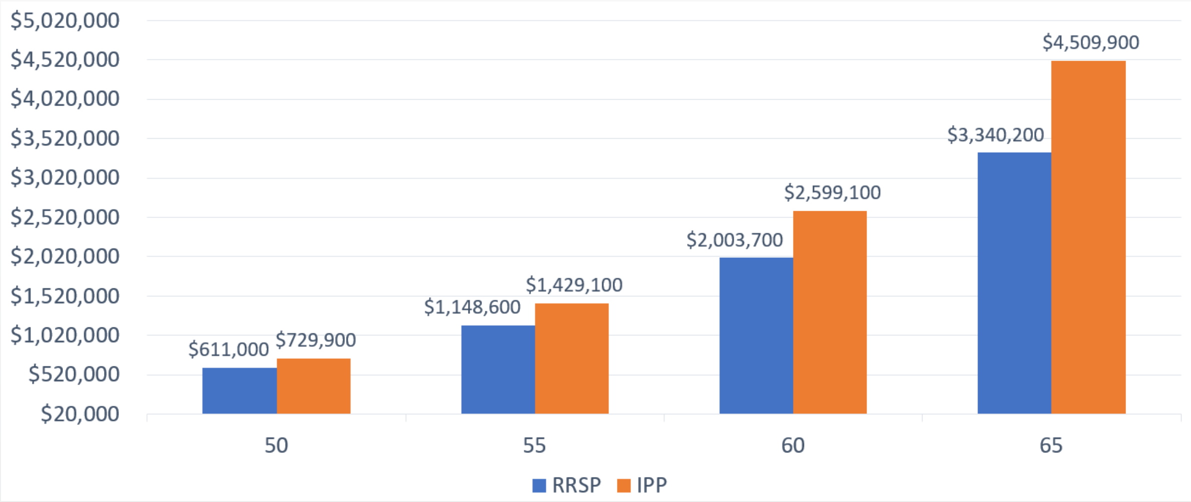
5. Wealth Building Strategies

A lot of our clients dream of semi-retiring around age 60, still owning their store, and working 1-2 days a week. Others want to sell their pharmacies and retire completely. No matter what your retirement goals are, you will need to start building a retirement fund to last you the rest of your life. Pharma Tax can help provide clarity and build a plan for your retirement.

- There's a variety of options to build your retirement fund including:
- Registered Retirement Savings Plan (RRSP)
- Spousal RRSP
- Tax-Free Savings Account (TFSA)
- Individual Pension Plan (IPP)
- Corporate Insured Retirement Plan
- Real Estate Investments
- Permanent Life Insurance
- Flow-Through Shares

Our best piece of advice for pharmacy owners looking to retire is to stop RRSP contributions and instead start an Individual Pension Plan (IPP). An IPP is like an RRSP on steroids. Your future retirement fund can be up to 65% more with an IPP than you can with an RRSP, and all the contributions are tax deductions for your business.

Portfolio Value Over Time



Not only will your retirement fund grow larger with an IPP, but you are also promised a specific amount of income that is payable for the rest of your life at retirement.

For instance, we set up an IPP for a client who wanted to retire at age 60. Here's what his projected annual pension will be for life.

Pension Payable For Life

With RRSPs, there is no promise of how much you will receive and how long that will last.

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6. Insurance Tax Strategies

When pharmacy owners want to withdraw money tax-free from their corporation, they should use a corporate-insured retirement plan, a permanent life insurance strategy. A corporate-insured retirement plan is funded by your corporation and is meant to provide you with a tax-free source of retirement income. It is also meant to leave your family a large sum of money tax-free after your death.

A lot of people hate the word insurance but what many don't know is that this is one of the best ways, if not the best way, to save money in taxes. No other investment vehicle in the world gives you the opportunity for your investment to grow tax-free but also to withdraw your investment completely tax-free.

Let's look at an example. Assume that a 40-year-old pharmacy owner that wants to invest $50,000 per year for 20 years. There are two scenarios to consider:

1. Start an investment portfolio (stocks, bonds, ETFs, etc.) inside your corporation where all growth of the portfolio is taxed.
2. Start a corporate preferred retirement plan inside your corporation where all growth of the portfolio is completely tax-free.

You can start withdrawing funds at any time in retirement but for simplicity's sake, let's say you didn't make any withdrawals. Let's also assume that both portfolios earn the same rate of return of 5% per year. If you pass away at age 86, your family would receive vastly different earnings:

1. Corporate Investment Portfolio = $2,796,129
2. Corporate Preferred Retirement Plan = $4,358,517

Tax savings = $1,562,388!

With the Corporate Preferred Retirement Plan, your family could receive 56% more than the traditional corporate investment portfolio, all because of taxes!

This strategy is appropriate for any pharmacy owner who has leftover cash in their pharmacy and wants to invest. There are no minimum or maximum amounts that can be contributed, and plans can be customized to suit your needs.

7. Estate Planning Strategies

We will never forget the story of a pharmacy owner passing away suddenly at the young age of 40 due to a heart attack. His death took everyone by surprise, even his wife who is also a pharmacist. This family was not an official Pharma Tax client yet, but they were in the process of coming on board.

Visiting the pharmacy, his wife turned to us and said, “This is a disaster. Dave and I never really talked about how he runs his store, his staff doesn’t like me, and, ever since his death, patients are leaving and revenues are way down. We were not prepared for this.”

Unfortunately, many pharmacy owners are not prepared for something like this until it is too late. No one ever wants to think about death, sickness, or illness, let alone imagine it happening to you. It’s a difficult conversation to have but is incredibly important.

Estate planning involves preparing you, your family, and your pharmacy in case disaster strikes, such as but not limited to:

- Pharmacy owner dies, what happens to your pharmacy or pharmacies?
- The pharmacy owner gets sick or injured and cannot work, is there a backup designated pharmacy manager that can run the store?
- Marriage breakdown with a spouse that owns shares, what happens to their shares?
- Relationship with business partner(s) breaks down, does the pharmacy get sold?

Let’s use one of our clients as an example:

Rob owns 4 pharmacies and has accumulated significant wealth inside his holding company. When planning for his death, Rob drafted a Primary Will. This was a big mistake that could cost his family greatly.

What Rob and many pharmacy owners don’t know is that, at death, there is a tax that is charged called Estate Administration Tax. This tax is charged at death and before your executor can start distributing the assets of your estate. The Estate Administration Tax is only charged on assets that fall under a Primary Will.

Instead of leaving his heir to pay more taxes on his pharmacy businesses, Rob could separate his Will into a Primary Will and Secondary Will. Primary Wills cover everything you own in your personal name (e.g., house, car) whereas Secondary Wills cover your corporation(s) like your pharmacy.

By dividing his personal property and corporate assets into different Wills, he saved his family a great deal of money.

	Primary Will		Primary Will	Secondary Will
House	$ 1,400,000		$ 1,400,000	$ -
RRSPs	$ 459,000	1	$ 459,000	$ -
Value of Pharmacies	$ 4,395,000			$ 4,395,000
Holding Company Investments	$ 8,320,000			$ 8,320,000
Less: Debts	($4,005,000)		($440,000)	($3,565,000)
Gross Estate	$ 10,569,000		$ 1,419,000	$ 9,150,000
Estate Administration Tax	**$ 150,900**		**$ 13,650**	**$ -**
TAX SAVINGS	**$137,250**			

(1) RRSP are not subject to Estate Adminitration Tax with an assigned beneficiary

Thanks to his Secondary Will, Rob is leaving his family $137,250 more in the future. Not only does planning his estate help save his family money, but it also gives Rob peace of mind knowing that his family and his pharmacies will be taken care of should something happen to him.

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You can spend days, weeks, and even years trying to figure out how to maximize your tax savings. Instead of spending your time trying to save money, let a professional accountant help.

Knowing which strategies apply to you first requires an understanding of you, your family, and your pharmacy. Unfortunately, a lot of pharmacy owners think that their accountant is doing this for them but most do not - most accountants file your taxes and that's it.

Pharma Tax is a team of accountants and advisors who specialize in pharmacy. Our mission is to help you pay less tax, grow your pharmacy, and build wealth with expert accounting and financial solutions.

Click here to schedule a free consultation! We can help you pay fewer taxes with our tax-saving strategies.

Ask yourself, "Is it worth spending 30 to 45 minutes of my time if they can help me save $6,872 to $238,802 in taxes?"

Ricardo Ardiles

Co-Founder & Partner

Ricardo works with you to help you save tax, grow your pharmacy, and implement wealth-building strategies. He lives in Etobicoke with his spouse, Maribel, and daughter, Valentina. Together, they enjoy travelling to tropical destinations, dining out, and burning off the calories by dancing to salsa music. Ricardo also loves to play soccer, squash, and golf.