Ten Ways to Cut Your Tax Bill

By Neel Roberts

Are you one of the many Canadians who feel you're paying too much tax? If you grossed about $40,000 last year you could have paid almost 50% to the respective governments; yes almost $20,000! How can you do something about this sky high bill?

Use Your RRSP Deduction – Regardless of what you've heard out there, this is still a good tax deduction. Even if you do as little as $20 per week, you can still get as much as a $400 tax break at the end of the year while your money compounds "tax free". Also, you may be eligible to participate in spousal contributions depending on your marital status. If you haven't started a plan, today is a great day to do so.

Donations - In Canada, there are a wide variety of charities you can give to. This includes outreaches, churches and other worthy causes. As long as they have a Charity Number assigned by CRA (Revenue Canada), you qualify for a tax credit of up to 29% for all cash and goods donations which have receipts issued.

This can be a good opportunity to clean the house of things you don't want, but others could use. Depending on what you give away, you should get a receipt for the fair market value of the item. For example, your donation of $1,000 worth of old furniture to your church can give you a $290 tax break. As a bonus, you can save your receipts for up to five years.

Education – Have you thought of upgrading your skills or taking a course? Most educational institutions qualify for the tuition credit provided if is post-secondary, vocational or job-related. As a bonus, most also get the time credit, that is $200/$400 for each part/full time month they attended. Suppose you took a $500 part time evening course for three months, your tax break would be as much $286, or a 26% tax credit. Now suppose you went full time for that same semester and your tuition was $2,000. Your break is now $832. Tuition can also be carried forward to future tax years which are most beneficial or transferred between spouses and dependants.

Private Health Care Plans – Do you have a lot of medical expenses, dental work or prescription drugs? While many of these are tax deductible, it may still be cheaper to buy a health care plan rather than paying for these and deducting it. Supposing your medical expense is $2,000 for the year. Your tax break would be 26% $520, so your still out of pocket $1,480. If you buy a plan for $500 per year with a 20% deductible. Therefore you would pay for the premium of $500 plus $400 for the medical expenses for a total of $900. Not bad so far, as you are ahead $580. Now for the bonus; both the premium and deductible are tax credits of 26%, so you get a break of $234 for a net out of pocket of $666 or a saving of $814.

Start an Investment Portfolio - Outside your RRSP put your invested money into tax friendly vehicle. Specifically, dividend and capital gains oriented investments. CRA taxes these at a lower rates than ordinary investment income earned in your bank account, (T-Bills, Bonds, GIC's etc.). Also, as an investor, you are entitled to additional deductions such as interest on money borrowed to fund your investments, professional consultation/accounting fees, disposition costs and more over and above your personal deductions.

Start a Business – This is considered one of the most lucrative tax opportunities around. Not only is it tax smart to do this, but today it is the "in thing" to be running your own operation. In Canada, almost a million businesses get started each year and if you haven't done so already, you're missing the boat.

Consider Rental Income – More and more Canadians are adopting rental income as a side revenue opportunity. Why? Generally it's fairly easy for almost all folks to get into; there are tax advantages and several ways of doing it. If done right, within a few years it could become your main source of passive income. Generally speaking all expenses incurred to earn taxable rental income are deductible and any net losses can be used to offset your other income from jobs, etc. There are three main ways you can get started. First, you can sublet a portion of your home (depending on zoning laws). Even if you rent and don't own your home, you can still do this and qualify for the rental statement. Second, you can buy a property and do everything yourself. This can be a stretch for many people, especially when it comes to managing it, however once you're through the learning curve it can be lucrative. Last is to buy a managed rental property.

Check if Expenses on Your Job are Deductible – Do you earn commissions as part of your wages? Do you have expenses on the job which are not reimbursed and considered over and above normal? Driving to work is considered a normal, personal expense which is not deductible. However, if you use your vehicle on the job to travel between calls, meet clients, etc. this is considered deductible. Same is if you use part of your home, a cell phone, internet, office expenses, supplies, etc.

Consider Giving Assets to Lower Earning Dependants – Do you have substantial income earning assets and dependants with a low net income? Suppose you have a bond worth $10,000 face value and it earns 10% or $1,000 interest per year. You can pay as much as $390 tax.

Suppose you have $50,000 in bonds that pay 10% simple interest per year or $5,000. You are in the top tax bracket and would pay $1,950 in tax. Your 16 year old daughter is in high school and earns $2,500 per year from her part time job. You decide on giving her an endowment (sometimes called an early inheritance) and transfer it in her name therefore moving the taxable income to her. As her net income is under $7,600, she would have no tax liability and the net savings are $1,950 between the two of you for that year.

Now a few points to keep in mind here before considering this strategy. From CRA's point, the transfer must be reasonable regarding the amount and believable for the motive behind it. If they feel you are trying to hide your money, they'll come back to you with the attribution laws and tax you accordingly. The above example is fairly common and should be acceptable to CRA. Also, the giver and receiver must understand and trust each other as the onus is on the giver to prove their case and not the receiver.

Consult with Your Tax Professional - With the already complicated tax laws getting more complicated by the day, it's hard to stay on top of things unless you're practicing it daily. More and more Canadians are seeking the help of a professional to stay informed and maximize what's available to them.