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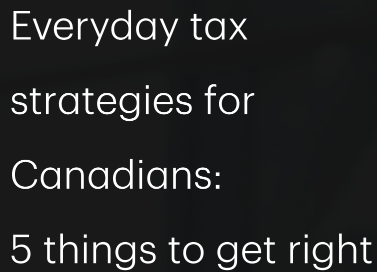


Everyday tax strategies for Canadians: 5 things to get right

In this tax primer, we offer five key strategies many Canadians can implement to help them feel confident in their financial plan.

It may be frustrating when you compare your gross versus net income: Are you really paying that much in taxes? Where does the money go? We all feel the same pain, right from the time we earn our first paycheque and knowing that our taxes keep our roads safe, our medical bills low and our society operating smoothly sometimes doesn't stop the anguish.

Geoff Chen, a High Net Worth Planner at TD Wealth, says that, besides paying for services we all use, the country also uses taxes to nudge our money into different areas. "Canada wants us to do certain activities by offering tax incentives and it also discourages us from other actions by the application of tax," he says.

He suggests these as the tax strategies everyone should look into.

Utilize RRSPs, TFSAs, RESPs to the max

Chen says one of the main components of tax strategy is to utilize tax-deferred or tax-friendly accounts: Registered Retirement Savings Plans (RRSPs), Registered Education Savings Plans (RESPs) and Tax-free Savings Accounts (TFSAs). Each plan defers or mitigates tax obligations in different ways.

Contributions to an RRSP lower your taxable income. You can generally contribute up to 18% of your previous year's earned income up to an annual maximum ($27,830 for 2021). The investments in the plan can grow tax-free until you withdraw the funds. As the funds are geared to providing retirement income, the key is to withdraw the funds in retirement when your income — and therefore your tax rate — is potentially lower.

"Depending on your financial situation, if you contribute to an RRSP, your taxable income shrinks, and your tax obligation may decrease. You may even receive a tax refund," Chen says.

The annual contribution limit for TFSAs is $6,000 for 2021. Contributions are made with after-tax dollars and no tax is applicable when amounts are withdrawn, meaning that investments can grow tax-free. TFSAs also offer some flexibility over RRSPs:

Savers can access their funds (depending on their investment type) and the amounts withdrawn can be recontributed in a following tax year.

RESPs offer a method to save toward funding a child's post-secondary education but also offer a tax saving opportunity. Like RRSPs, investments can grow tax-free within the plan and the growth is generally taxed in the hands of the recipient — the student whose tax rate is presumably less than the contributor. In addition, the federal government offers the Canada Education Savings Grant which can match 20% of up to $2,500 of the RESP contributions annually to a lifetime maximum of $7,200.

Split your income or pension with your spouse

"Just as contributing to RRSPs lowers your taxable income, so too may income splitting. It means another opportunity to save tax," Chen says. The following tax strategies only apply to spouses or common-law partners.

One goal of a spousal RRSP is to transfer funds from a higher income spouse to their lower income partner in order to provide them with more investment income.

"But the strategy also comes with tax benefits," he says.

Income splitting can occur before retirement, through spousal RRSPs, or in retirement through splitting a pension. In a spousal RRSP, the higher income earner would contribute to the RRSP of the lower income spouse, within their available contribution limit. This transaction can result in a lower overall tax rate for the couple as the higher income spouse would receive a deduction for tax purposes in the year of contribution. Later, when the funds are withdrawn from the lower income spouse's RRSP, the tax obligation on the RRSP withdrawal may be lower as it is taxed at the lower income spouse's tax rate.

Chen notes that the Income Tax Act in Canada requires that the spouse receiving the funds must keep the funds in the RRSP account for three years. Otherwise, attribution rules kick in and the funds will be taxed in the hands of the higher-earning spouse.

Income splitting can also apply to pension income: The concept is much the same although the higher income earner can share up to 50% of their pension income. The common types of pensions that can be shared include annuity payments from RRSPs, payments from RRIFs, life annuities from a superannuation or pension plan. Pensions that can't be split include Canada Pension Plan (CPP), Quebec Pension Plan (QPP) and Old Age Security (OAS).

Look into your principal residence exemption

This is a large part of financial planning when you sell your home. Usually, selling an asset such as an investment outside of a registered fund will result in a capital gain which is subject to tax. However, there is an exemption when you are selling your primary residence. Note, certain rules apply: In general, the home must be occupied by the homeowner and not be a rental property to claim the exemption. If the homeowner has a vacation property, a certain amount of planning may be needed to ensure that the largest gains are managed: If the vacation property has risen in value more than the home because it has been owned for a long period of time, it may be prudent to regard it as a principal residence in certain circumstances.

"Real estate that has been held for decades can generate enormous capital gains. The principal residence exemption is a powerful way to manage taxes and save money, especially for those who are using the sale of a home to fund retirement or healthcare needs," says Chen.

But he says that each person's situation is unique and consultation with a tax advisor on how to use the principal residence exemption is recommended.

Find the tax credit or deduction for your life situation

Here's a short list of some other areas to consider:

Moving expenses: If you have moved and established a new home for work or to run a business at a new location, you can deduct eligible moving expenses from the employment or self-employment income you earned at your new digs. Certain criteria must be met: For example the move must be within Canada and more than 40 kilometres away from your previous home. Other rules apply if you are involved in an international move.

The Canada caregiver credit: Many Canadians are actively supporting relatives or dependents who are infirm or have disabilities. These activities can include a wide range of support, from providing food and accommodations to transportation to medical appointments. You may qualify for the caregiver credit if you provide services involving the necessities of life to a close relative or dependent with an impairment, even if the relative does not live in Canada. Certain documentation is needed from a medical practitioner to support your claim. To see who may qualify, see the CRA website.[1]

First-time home buyers' amount: You can claim $5,000 if you or your spouse or common-law partner acquired a qualifying home (one existing or under construction). One qualification is that you must not have lived in another home owned by you or your spouse or common-law partner in the year of acquisition of the new home or in any of the four preceding years before the acquisition.

Medical expenses: There is a wide range of medical expenses that are eligible for the medical expense tax credit, but you can only claim an expense that you have not or will not be reimbursed for. Chen says to hold on to your receipts and submit the claim, even for small items because they do add up. You may also have to include supporting documents for your claim.

Make a heartfelt donation (and keep the receipt)

Chen says charities are one way the government offers incentives for generous acts. "Not only will you do a benevolent thing by giving to registered charity, but the government will give a tax credit for this action," he says. You may be eligible to receive a credit of up to 33% of your donation at the federal level if your income is in the highest tax bracket and further tax credits at the provincial level. You can claim up to 75% of your net income and donations can be carried forward for up to five years.

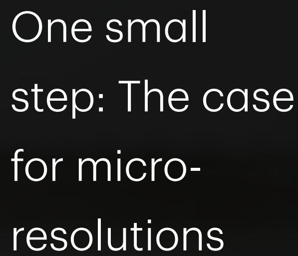
Chen says those people who have embarked on estate planning may wish to consider donating investments to their favourite cause. As well as a tax credit, donating investments can offer a separate benefit: It can potentially eliminate the capital gains tax on eligible securities. Eligible investments include investments trading on designated stock exchanges, segregated funds, mutual funds, and government bonds. Calculating the tax benefits is complex. However, depending on your situation, donating the investments, and receiving a tax credit may be more beneficial, tax-wise, than selling the investments and facing capital gains.

Chen says the best time for using tax strategies is in the spring when we do our taxes. At that time, we can make RRSP contributions or spousal contributions and search for tax credits and deductions.

"It also gives you a moment when you can consider how much you have given in charitable donations. If you haven't used your maximum, you can now begin to plan for next year."

— Don Sutton, *MoneyTalk Life*

[1] The Canada caregiver credit, Government of Canada, Updated Jan. 18, 2021, accessed Nov. 5, 2021, canada.ca/en/revenue-agency/services/tax/individuals/topics/about-your-tax-return/tax-return/completing-a-tax-return/deductions-credits-expenses/canada-caregiver-amount.html



One small step: The case for micro-resolutions

Change is hard. And resolutions can be quickly forgotten. Fortunately, scientists suggest smaller subgoals can be more achievable and have a big impact on our lives and finances. Here are some bite-sized resolutions almost anyone can keep.

You might be looking at a completely new career path or cleaning out the attic. You could be trying to lose 10 pounds or to eat more greens. But whatever commitments you make in life, if your goals are far away or difficult or just plain unclear, chances are that you might fail.

As anyone who has ever made a New Year's resolution knows, many people flunk at achieving their well-intentioned goals and scientific research backs this up. While we might fault ourselves for lack of commitment or discipline, research has also shown that by breaking our goals into small increments on the path to the finish line — what psychologists call subgoals — we may have a better chance of achieving the grander result we are planning for.[1]

"Subgoals are doable. You can perceive concrete steps whereas your larger goal may be more abstract," says Kristen Duke, assistant professor at Behavioural Economics in Action at Rotman (BEAR), at the University of Toronto. Duke studies the ways our decisions are influenced by emotions, work that relates to how our thoughts can motivate or deflate our approach to goals. She says it can be difficult to maintain motivation toward long-term goals but a technique that generates repeated jolts of motivation may help.

"Once people start to feel a sense of progress, it continues to be motivating. And as you get closer and closer to a goal, you get more and more motivated," Duke says. "So if you set up these more intermediate goals, you have more of these moments when you get that extra stimulation."

In one study, people exercising were able to burn 200 calories faster when their goal was broken down into smaller achievements.[2]

Taken out of the lab, this may mean that someone who wants to give up cigarettes may find a smaller subgoal — such as booking a doctor's appointment or learning about smoking cessation — more motivating and successful than trying to stop cold turkey.

If you want to conquer a goal, it may be better to chop it down to size. Here are some ideas on how to get started with subgoals.

Goal: Build a budget you can stick to
Subgoal: Review your grocery bill for 30 minutes

For those who want improved finances and are routinely buying the same standard items weekly, running your eye over your grocery bill receipt can give you instant ideas. It can be less intimidating than trying to redo your family's budget all at once. Groceries are regular expenses so tinkering with what you buy could have a larger impact over 52 weeks. For instance, if your goal is to save more money, there may be more discretionary items in your list that you can do without than you might think. Or you may simply decide house brands are a better bargain than national brands.

Goal: Eat better this year
Subgoal: Analyze one food craving

If you are trying to eat better, building new habits can be a frustrating challenge. Jumping out of auto-pilot mode is a proven behavioural science technique to develop a healthier diet. You can also

make it a subgoal.[3] The next time reach for a food craving, think deeply about why you are eating this particular snack right now: Are you bored? Stress eating? If so, what's the underlying cause of stress? Stepping back and examining your motivation may be the beginning of a new, better routine.

Goal: Get in better financial shape
Subgoal: Book an appointment with a financial advisor

Much like putting off a call to the dentist lest we hear bad news, a call to a financial advisor may provoke unnecessary trepidation. If you have a goal to get your finances in order but are not sure what is the first step, getting someone with financial know-how to weigh in on the state of your money affairs may be the path to some education around money. An advisor can examine your overall financial situation, help you make smart decisions about your money and suggest ways to help your investments grow. You may gain a lot through one simple phone call and it may lead to a better situation later.

Goal: Learn how to run for exercise
Subgoal: Take a regular walk around the block

Many of us want to become more active, but it can be hard to break from our sedentary lifestyle. Before you learn to jog or even run 10K, a subgoal might be just putting one foot ahead of the other, whether it's a walk around the block or taking the dog for an extra half-kilometre. Anything that gets the blood pumping is a benefit. Exercise can have a valuable impact on all kinds of health issues, and the great feeling you receive from all those endorphins will push you to conquer another subgoal in your fitness area.

Goal: Build a diverse portfolio
Subgoal: Make your first investment

Part of having a successful financial plan means owning a portfolio of investments that has the potential to grow over the years. Whether it's part of your Registered Retirement Savings Plan (RRSP) or Tax-Free Savings Plan (TFSA), your investments can mean you are working toward a financial goal, but it starts with making your first investment. It may not look like a subgoal — becoming an investor seems like a big step — but it is one step toward a well-rounded financial plan. A financial advisor can help you make that first investment and help support your decision on what sort of investment is right for you.

Duke equates subgoals to a teacher putting a jelly bean in a glass jar when a class is on good behaviour with the promise, when the jar is full, they get a pizza day. The visible reminder pushes everyone to work towards getting a slice.

"It's a clever incentive system that takes advantage of how motivation works to help keep us on track," says Duke.

"And then once you've reached the subgoal, it's motivating too because you say, 'Yay, I did it.'"

— Don Sutton, *MoneyTalk Life*

[1] Huang, S.-C., Jin, L., & Zhang, Y., Step by step: Sub-goals as a source of motivation. Organizational Behavior and Human Decision Processes, (2017). 141, 1–15, https://www.sciencedirect.com/science/article/abs/pii/S074959781730256X?via%3Dihub

[2] Huang, S.-C., Jin, L., & Zhang, Y., Step by step: Sub-goals as a source of motivation. Organizational Behavior and Human Decision Processes, (2017). 141, 1–15, https://www.sciencedirect.com/science/article/abs/pii/S074959781730256X?via%3Dihub

[3] Sairanen E, Tolvanen A, Karhunen L, Kolehmainen M, Järvelä E, Rantala S, Peuhkuri K, Korpela R, Lappalainen R. Psychological flexibility and mindfulness explain intuitive eating in overweight adults. Behav Modif. 2015 Jul;39(4):557-79. https://pubmed.ncbi.nlm.nih.gov/25810381/

Advanced tax strategies for wealthy Canadians

For many high-earning Canadians, there may be specialized tax strategies that help preserve and grow their wealth.

Just as your ambitions are uniquely your own, so too is your tax situation: No single tax strategy will fit all scenarios. Instead, your tax obligations may require a personalized guiding plan with annual tinkering and consultations with tax advisors as your wealth accumulates or your business evolves.

"Tax management can be important, particularly if you have worked hard to build up a business or a career. You want to be able to enjoy what you have earned and protect it," says Geoff Chen, a High Net Worth Planner with TD Wealth who works with wealthy families and business owners to help optimize their financial plans. He says tax planning is a subset of financial and business planning and not the other way around. "If you structure your life and corporation around tax issues, you may lose sight of your ultimate goals."

The first area executives or business owners should look to maximize, is their contributions to registered accounts, says Chen. That would include Registered Retirement Savings Plans (RRSPs), Registered Educational Savings Plans (RESPs) and Tax-Free Savings Accounts (TFSAs), assuming you qualify. These plans are the starting point since contributing can help mitigate tax exposure in various ways.

As well, Chen says most high net worth individuals should also consider utilizing RRSPs another way: income splitting through the use of spousal RRSPs which can potentially lower the couple's overall taxes. This is useful where one spouse is in a higher tax bracket and the situation is expected to continue at retirement.

"Everyone should consider making contributions to their favorite registered charities which can provide you with tax credits," says Chen.

There may be other strategies that can bring about a tax benefit that high net worth Canadians can employ to preserve their financial well-being. "Once these primary tax considerations are implemented, individuals may still wish to manage the tax implications of their wealth."

We talked to Chen who offered the following tax strategies for individuals who may have more complex situations and significant wealth. Read on to see if these may apply to you.

Incorporation

Who might consider this? A sole proprietor or someone starting a new business.

Owning an incorporated business can allow you to keep funds within the company structure where there is preferential tax treatment. The most obvious example is that the tax rate for small businesses is considerably less than the personal tax rate for individuals. This may provide certain tax deferral opportunities and, depending on the

nature of the business, a significant lifetime capital gains exemption may be available when the business is eventually disposed of.

If you privately hold real estate in the U.S., here's something to consider: If it's valued at more than US$60,000 and your worldwide assets exceed US$11.7 million as of 2021, then you may be subject to U.S. estate tax.[1] However, Chen says holding U.S. real estate through the corporation may be an effective strategy to mitigate U.S. estate tax concerns.

"With limited liability, incorporating your business also helps prevent the owner from risking their private wealth if the business is sued or fails," Chen says.

Business people and entrepreneurs should be aware of the legal and accounting charges that are associated with setting up a corporation: Shareholder agreements, articles of incorporation, annual financial statements and reports and filing tax returns are just some of the costs involved.

Prescribed rate loans

Who might consider this? High income family members with surplus funds.

Similar to income splitting, this strategy may lower the overall tax obligation for a family and may be suitable for higher income families with liquid assets. Briefly, it involves a higher income family member loaning a lower income member funds at the government prescribed rate of interest. The recipient can invest the money and earn income after interest is paid. In this way, taxable income may be shifted from an individual in a higher tax bracket to a lower tax bracket so that the overall tax impact may be less. The rate of the prescribed loan fluctuates, which is why this strategy may make most sense when the rate is low and the investment returns can help justify the cost of the arrangement, says Chen. Unlike pension income splitting and spousal RRSPs, you can make a prescribed rate loan to a minor child as well as a spouse.

Chen points out some other things to consider: For instance, the loan must be documented, and interest must be paid annually on or before the following January 30 each year or attribution rules kick in. For the plan to be effective, investment gains should be sufficient to offset the interest paid plus any expenses involved in structuring the loan. And because this strategy involves investments in the market, it comes with a certain amount of risk and should be done with the assistance of a financial professional.

Family Trusts

Who might consider this? Families who are sharing wealth and in need of tax and estate planning.

Chen says the tax benefits of a trust are the potential abilities to distribute wealth to family members and to lower the overall tax exposure of the family. A trust is a legal relationship between the person who sets up the trust (the settlor), the person who manages the assets in the trust (the trustee) and the individuals who benefit directly — the beneficiaries of the trust. For Canadian income tax purposes, it's regarded as a separate taxpayer. It can also be used to mitigate taxes in connection with claiming multiple lifetime capital gains exemptions.

"The trustees have flexibility to make decisions based on business conditions, impending tax events or the needs of the family," says Chen. "They have the discretion on when and how to make distributions to family members in a tax-efficient manner or whether to make any distributions at all in a given year. Due to business conditions, some years it may not be appropriate to make large payments at all."

Chen says family trusts can offer other benefits: A trust may protect family wealth from spousal or creditor claims and minimize probate fees. One thing to keep in mind is that every 21 years from the date of the creation of the trust, it is deemed to have disposed of its assets at fair market value. Further tax planning may be necessary as that date approaches.

Charitable donations

Who might consider this? Anyone who wants to make a sizable contribution or become more involved with their favourite charity.

The tax benefits of eligible charitable donations are available to all Canadians and you may earn tax credits which can lower the amount of tax you owe. Donations may be claimed in the year that they are made or carried forward for the next five years.

One charitable option available to high net worth individuals is a Donor Advised Fund. A Donor Advised Fund is a type of charitable giving vehicle that is created when a donor makes a contribution to a registered charitable foundation. The foundation in turn can gift all or part of the donation over to qualified donees (the receivers of the gifts), which can include any of the 86,000 registered charities in Canada. The donor is able to make recommendations to the fund concerning distributions of assets.

The individual making the donation — the donor-advisor — can set up their donor advised account and will receive the donation tax receipt up-front. The Private Giving Foundation, available through TD, has a minimum donation of $10,000 to get started (other foundations may vary), and a minimum subsequent donation of $1,000. The fund can provide flexibility if you are initially unsure which charity to donate to as there is no obligation to give immediately to a specific charity. In the meantime, you can continue to contribute to the fund and this money can continue to grow tax free.

As well as a tax credit, donating certain investments in-kind can potentially eliminate the capital gains tax on eligible securities. Eligible investments include investments trading on designated stock exchanges, segregated funds, mutual funds, and government bonds. Calculating the tax benefits is complex, says Chen, and depending on your situation, donating the investments, and receiving a tax credit may be more beneficial than selling the investments and facing capital gains.

Individual pension plans

Who might consider this? Executives with high incomes and small business owners.

High income earners may find at some point in their career that limiting their retirement plan to RRSPs may not be sufficient for their retirement objectives. An alternative solution, says Chen, is an Individual Pension Plan (IPP), a registered and defined benefit pension plan that a company can structure for its executives. A small business owner may also benefit from an IPP, although to qualify they must pay themselves a salary and meet certain other conditions.

An IPP can create more contribution room compared to an RRSP, and contribution room can rise significantly until age 65, says Chen, adding "the plans are based on the age and years of service of the recipient and usually become advantageous when the subscribers are in their middle 40s," says Chen.

Whichever tax measure you embark on, Chen recommends not doing it alone and getting the best advice available from your advisor or tax professional before you make a move. That's because tax legislation may be amended, business environments change, families grow, income sources evolve, and often unexpected problems occur. A plan that looks correct from a strictly financial point of view may not be what your personal situation needs.

"There are expenses involved with meeting experts in taxation, accountancy and finance. Working out a dedicated plan for your situation can be time-consuming," Chen says. "But you may get the best result and have a much better outlook on your whole situation and not just your taxes."

— Don Sutton, *MoneyTalk Life*

[1] Note that there are U.S. tax proposals to reduce this threshold to US$5.85 million.

Major Canadian Tax Deadlines and Dates

	2021	2022
Filing Income Tax Returns & Instalments:		
Individual	May 2, 2022	May 1, 2023
Self-employed individual	June 15, 2022[1]	June 15, 2023
Deceased — Final tax return[2]:		
Death occurred between January 1 and October 31	April 30 of the following year	
Death occurred between November 1 and December 31	Six months after the date of death	
If deceased was self-employed, death occurred between January 1 and December 15	June 15 of the following year	
If deceased was self-employed Death occurred between December 16 and December 31	Six months after the date of death	
Graduated Rate Estate	90 days after tax year end	
Trusts, including testamentary or spousal/common-law partner trusts	March 31, 2022	March 31, 2023
Quarterly tax instalments	15th of March, June, September and December	
Registered Retirement Savings Plan (RRSP):		
Contributions for the year	March 1, 2022	March 1, 2023
Contributions for the year an individual turns 71 years of age	December 31, 2021	December 31, 2022
Home Buyers' Plan (HBP):		
Withdrawal — Buy or build a home before October 1st of the following year	October 1, 2022	October 1, 2023
Repayment — Starts in the second calendar year after the withdrawal	March 1, 2023	February 29, 2024
Registered Education Savings Plan (RESP):		
Contributions to receive Canada Education Savings Grants (CESGs) for the year	December 31, 2021	December 31, 2022
Registered Disability Savings Plan (RDSP):		
Contributions to receive Canada disability savings grants and bonds for the year	December 31, 2021	December 31, 2022
Capital Loss Selling:		
Disposition of investments to realize accrued capital gains or losses for the year (last trading date for settlement to occur within the year)	December 29, 2021	December 28, 2022
Family Loans:		
Interest on family loans to avoid attribution rules	January 30th of the following year	
Charitable Donations	December 31, 2021	December 31, 2022

[1]Please note that if there is a balance owing for the 2021 tax year it must still be paid on or before May 2nd, 2022.
[2]The deceased's Will or a court order may set up a testamentary spousal/common-law partner trust. When testamentary debts of the deceased (or estate) are being handled through the trust, the due date for the final return is extended to 18 months after the date of death. However, any balance owing on the final return must be paid on the due date as determined by the date of death.

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