An Important Year-End Tax Tip for Dividend Investors

Description

Investors have a number of options available to them to minimize the taxes they have to pay on their various types of income. One way to reduce or even eliminate taxes on dividend income is to use a prescribed rate loan.

Here's how it works.

Let's say you want to invest in **Telus Corporation** (TSX: T)(NYSE: TU) because you like the dividend growth and stable stock price.

One way to keep most of the dividend income is to have your spouse, common-law partner, or children buy the stocks if they are in a lower tax bracket. Unfortunately, you can't just give them the money to buy the stocks because the government will attribute the income back to you.

Instead, family members who are in a high tax bracket can opt to shift investment income to other members of the family who are in a lower tax bracket by lending funds to the family members at the government's "prescribed rate".

That rate is just 1% until the end of 2014. By implementing the loan before the end of the year, you can lock in the 1% interest rate for the entire duration of the loan. This is important, because the prescribed rate could increase in 2015 or beyond.

The interest for the year has to be paid before January 30 of the following year to avoid the income from the investments being attributed back to the lending member of the family.

When the family member who has borrowed the money invests the funds in dividend-paying Canadian stocks, that low-income individual takes advantage of the dividend tax credit and can receive the dividends tax-free if the person receives no other annual income.

Depending on the province, the amount of dividends that could be received tax free is as high as $49,000.

Using a prescribed rate loan is a great way families can take advantage of income-splitting. To set it up, you would need to touch base with both your tax and legal advisors, but the benefits could be substantial given the current 1% rate and the size of the distributions that can be earned without paying any tax.

Investing in dividend-paying stocks is a good investment strategy, but you want to make sure you choose the best companies. The following free report analyzes three more dividend stocks that would be great choices for the plan.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:TU (TELUS)
2. TSX:T (TELUS)

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aswalker