Canada Revenue Agency 101: 3 Ways to Legally Avoid Taxes in 2020

Description

Do you want to lower your tax burden, so you owe less to the CRA when you file in April?

Then you've got plenty of options available to you. Believe it or not, avoiding taxes doesn't require that you run afoul of the law. The Canada Revenue Agency actually offers a number of legal ways to lower your taxes, which you can take full advantage of. Most likely, you know about the obvious ones, like RRSP contributions and small-business tax deductions. However, there are other ways to avoid taxes that are less well known. The following are three that can save you big money when you file your taxes this year.

Buy a home for the first time

Everybody knows that RRSP contributions are tax deductible. What most people don't know is that under special circumstances, you can also *withdraw* funds from your RRSP tax-free. One of those is if you're buying a home for the first time. Under the *First Time Home Buyers' Plan*, you can withdraw up to $35,000 from your RRSP and pay no tax on it. The amount does have to be repaid, but you have 15 years to do it, so it shouldn't be too hard.

Take all the tax deductions you can get

Tax deductions are the "bread-and-butter" option for lowering your tax bill. The more deductions you claim, the lower your taxable income is, and the less tax you pay. One common tax deduction is RRSP contributions. Every dollar you contribute to an RRSP (up to a limit) lowers your taxable income up to a certain amount. If you contribute $10,000 to an RRSP in one tax year and have a marginal rate of 30%, you'll save $3,000 on your tax bill.

Invest in a TFSA

Investing in TFSAs is one of the most underrated ways to lower your tax bill. While TFSAs don't offer tax deductions like RRSPs do, they're truly tax-free, as opposed to merely tax-deferred. What this means is that you can invest in a TFSA and never pay any taxes on the holdings — not even after you've cashed them out and withdrawn the funds.

Consider an investor holding $20,000 worth of **Fortis** (TSX:FTS)(NYSE:FTS) shares. Fortis is a dividend stock, meaning that it pays cash income in addition to whatever capital gains it may provide. With a 3.3% dividend yield, FTS pays $660 a year on every $20,000 invested. Inside a TFSA, none of that cash is taxed — nor is any proceeds from selling stock. So, our hypothetical investor could get substantial tax benefits from holding FTS in a TFSA.

Outside a TFSA or RRSP, it's a different picture. An investor holding $20,000 worth of FTS in that context would have to pay taxes on any dividends or gains they realized. The dividends would be "grossed up" by 38%, and a 15% tax-credit applied to that gross up amount. That tax credit would then be taken off their dividend income, and the rest is taxed at their marginal rate. As for any capital gains realized on the shares, 50% of them would be taxed at the investor's marginal rate. When you look at both taxes combined, they can add up to quite a bit. So, if you have the contribution space available, it's a good idea to invest any leftover savings in a TFSA.

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Date
2025/09/18

Date Created
2020/02/18
Author
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