



## Prepare for a CRA Tax Hike

### Description

Canadians are arguably the highest-taxed citizens of North America today. However, the Canada Revenue Agency (CRA) could still hike tax rates in the near future so as to cover the deep deficits created by economic stimulus packages and household income support programs during the COVID-19 pandemic. Its time investors start preparing for a CRA tax hike.

### Prepare for a CRA tax hike

Taxes are far too complex a topic for a one-size-fits all solution. However, there are broader strategies investors can employ to mitigate the impact of tax increases on their investment portfolio.

The truth is, taxes are a significant drag on the attainment of our financial freedom goals. While any strategies employed may not necessarily avoid higher taxes, they can improve tax efficiency in a portfolio and total estate. Tax planning will achieve much better results if done well beforehand.

But how best can we prepare for federal and provincial tax increases for which there's no date nor potential duration?

### Pay taxes upfront

The odds of a near-term tax hike keep increasing [with a widening fiscal deficit in Canada](#). Paying taxes now, instead of delaying or differing them, could be a marginally better option.

This could mean maximizing all Tax-Free Savings Accounts (TFSA's) if one has any contribution available. The cumulative TFSA contribution room for 2020 stands at \$69,500 for a qualifying Canadian who became an adult in 2009.

New contributions to the TFSA will be taxed at today's lower rates. Investors won't worry about higher taxes on income or capital gains in the tax-exempted account forever.

One may ask, what if I still have some unused contribution room, but no spare current income to throw into the TFSA account this year? It's simple: you can move your assets around.

## Move assets from an RRSP to a TFSA account

Moving your portfolio from an ordinary taxable account or from a tax-deferred account into a non-taxable account could be an option. You could pay lower taxes today and avoid future tax hikes.

Further, most withdrawals or liquidations from tax-deferred accounts like registered retirement savings plans (RRSPs) will trigger tax events, so the tax bill will be higher for 2020. One could liquidate just enough to fund any available TFSA contribution room — and the triggered taxes.

## Buy more tax-advantaged assets

Increases in general tax rates could hurt companies' bottom lines through higher income taxes. This could hurt equity investment valuations as profits and cash flows are eaten up by higher income taxes.

Generally, investors in taxable companies pay taxes at two levels. First, the company is taxed at the corporate level, and then investors pay taxes on dividends and capital gains at a personal level.

Buying more income tax-sheltered corporations could enhance portfolio tax efficiency. Tax-sheltered corporations include real estate investment trusts (REITs) and other dividend and royalty income trusts. These don't pay income taxes at the corporate level, but investors will incur taxes on distributions.

It follows that locating REITs in a TFSA will totally remove any future tax burden. One can therefore buy more tax-exempt assets and stash them into a tax-free account today. The challenge is that most tax-exempted assets, such as certain bonds and income trusts usually have very low expected annual rates of return. One has to live with this reality.

Perhaps it's time to reach out to your tax consultant for a discussion on how to achieve tax efficiency on your wealth before the CRA starts collecting more from you.

## Foolish bottom line

Political debates will continue raging on in the short term as to whether provinces and the federal government should raise taxes — and by what magnitudes. However, sooner or later, there will be a national consensus on the tax topic.

Truth be told, there are no free lunches. Budget deficits created in 2020 will need to be financed, and taxes are the major revenue source for any government. It's best to get prepared for a CRA tax hike right now [as you grow your wealth balance](#).

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