Canada Revenue Agency: 3 Ways to Save $10,000 of Taxes

Description

The Canada Revenue Agency collects income taxes from us for the government every year. However, there are options and tools available that can allow us to save more than $10,000 of taxes.

Increase your investment income

We can earn income from working and from investing. However, your job's income will be subject to the highest tax rate versus capital gains and Canadian dividends that are taxed at much lower rates.

For example, if you live in Ontario and you earn $40,000 a year from your job, your 2021 tax rate will be 20.05%. And you'll pay CRA $8,020 in income tax. However, if you book an extra $5,000 of capital gains from your investments in 2021, you will only pay $501.50 in taxes, a rate of 10.03%.

Eligible Canadian dividends are taxed at even lower rates than capital gains (unless you are in higher tax brackets). The story is similar for Canadians working in other provinces or territories, too.

You can see how quickly the tax savings from your investments can add up. Therefore, Canadians should really take advantage of earning capital gains and eligible Canadian dividends in their non-registered or taxable accounts.

Use your TFSA wisely

A variety of investments are qualified for TFSAs, including money, GICs, government and corporate bonds, mutual funds, ETFs, and stocks. However, you should strive for the greatest risk-adjusted returns simply because what's earned inside a TFSA is tax free.

Consequently, compared to in taxable accounts, you should be able to save $10,000 of taxes much quicker. Be careful about earning foreign income in your TFSA though because foreign income can have foreign withholding taxes that are irrecoverable.

Stocks are the asset class that provides the greatest long-term returns. You may even land on multi-baggers that can 10 times your money. Alternatively, you can capitalize on beaten-down stocks like **Bank of Nova Scotia** that provide nice income and upside on a multi-year turnaround.

Be smart on using your RRSP

Qualified investments for TFSAs are also qualified for RRSPs. While the TFSA is suitable for those who are eligible and know what they're doing with their investments, the RRSP will be more effective for those with a high tax bracket.

Contributions to RRSPs will deduct your taxable income for the year. It follows that you can lower your tax bracket if you have a big enough RRSP room. Therefore, it's better to save your RRSP room for future years if you know you'll end up in a higher tax bracket later on.

Inside RRSPs, your investments will enjoy tax-deferred growth. RRSPs are ideal for saving and investing for retirement because in most cases, you'll be paying hefty tax bills when you withdraw in a year that you have full-time work.

The idea is that your RRSP investments will enjoy decades of tax-deferred growth. When you retire and withdraw the taxable income from your RRSP/RRIF, you'd be in a lower tax bracket and pay lower taxes.

There's a 15% foreign withholding tax deducted on U.S. dividends earned in TFSAs, but there's no such problem in RRSPs. Therefore, the RRSP is an excellent place to hold U.S. dividend stocks that provide decent yields.

For example, there are more dividend-paying healthcare and technology stock choices in the U.S., including AAA-rated companies like **Johnson & Johnson** and **Microsoft**.

The Foolish takeaway

By increasing your investment income via stock dividends and growth and using your TFSA and RRSP effectively, you can save many $10,000 of taxes over the next decades. Just ensure you've got a winning stock investing game plan that leads to overall satisfactory portfolio income/returns.

In the current market, it's not difficult to generate a safe yield of 3-5% and aim for price appreciation of 10-15% over the next three to five years. You just have to know where to look.

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