20 Free Tax Secrets

for Canadians

Allan Madan

CPA, CA Tax Expert

20 FREE TAX SECRETS FOR CANADIANS

By Allan Madan

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TWENTY TAX SAVING TIPS: THREE BROAD CATEGORIES

Tax time is a painful process for all individuals. We all aim to save on taxes as much as possible, but unfortunately we always end up paying more. On average, one person misses several hundred dollars in deductions. Are you aware that you can receive deductions on rent payments, child care payments and automobile expenses amongst many others? So this year take on taxes like a professional and read on to find twenty tax saving secrets. Whether you are an individual, an investor, or a business owner, we have identified tax saving opportunities for you.

Three Broad Categories:
Individual
Investor
Businesses

INDIVIDUAL

1. Pay household expenses through the higher income spouse

If there is a difference in the income tax brackets that you and your spouse are in, then the mentioned tax saving strategy is ideal. This definitive and simple tactic calls for the higher income spouse to pay for majority of the household expenses. This way the lower income spouse will be able to use his or her income for investment purposes. Since the funds tied up in the investments belong to the lower income spouse, the marginal tax rate (lower) applied to those investments will correspond to the lower income spouse as well. Hence by using the lower income spouse to invest you are savings tons of money you would have originally given in the form of taxes.

2. If your dependant is ill, claim a higher deduction

Under the Income Tax Act, those paying taxes have the right to claim a higher deduction if their dependent is unwell in a manner specified under the act. A specific set of symptoms and ailments, including neurological diseases, certain disorders etc, specified, give way for this higher deduction claim. This deduction claim is raised further if the one suffering is a senior citizen.

A few further conditions apply; the patient is not allowed to claim deduction on a separate basis and has not, or will not be reimbursed for his illness by an employer, insurance company or a third party. Furthermore if the one paying the taxes has received only a certain amount as compensation, the balance can still be claimed.

3. Claim Child Care Expenses

Did you know that the money you spend on your young child can be reimbursed to a large extent? Luckily childcare expenses are tax deductible. However, the lower income spouse is entitled to these claims only.

Childcare expenses include the following:

•Babysitting fees

•PLASP fees

•Daycare

•After-school programs

There is a cap on the total deductible amount that can be claimed. For children born in 2004 and later, the maximum deductible amount for child care expenses is $7,000 per child. For children born between 1994 and 2003, the maximum deductible amount for child care expenses is $4,000 per child.

4. Pay your older (above 18) child wages for babysitting the younger ones

Paying your adult child money, for babysitting your under 16's, makes room for a tax saving opportunity. This tactic will allow you to claim a tax deduction for fees paid to your older child (16 or older) for babysitting your younger child. Childcare expenses, which include babysitting fees, are tax deductible.

Another advantage of this strategy is 'income splitting'. The payments you are making to your older child will be included in his/her income for tax purposes. There is a high probability that the tax he/she would be paying on this income would be a negligible amount. Another favorable aspect of this situation is that your child who is now earning income will be entitled to RRSP contribution room.

Hence, this minor form of income splitting results in a beneficial situation for the whole family, in terms of beating the tax man.

5. Claim deductions for your university going child's education and textbooks

Whether you are a college student or a university student, you can make some important claims. Full time students can claim around 65 dollars a month, just for text books and if you are part time student that number drops to 20 dollars a month. However text book amounts are not the only aspects of education that entitle you to a claim.

As a university or college student, you are also entitled to a 400 dollar amount (full time) monthly or a 120 dollar monthly amount (part time). Best of all, parents of university or college going students can receive these claimed amounts through a transfer. This transfer is applicable even if you are the spouse of a university or college student.

Hence, being aware of all the potential claims, that you and your family are entitled to, can prove to be surprisingly rewording.

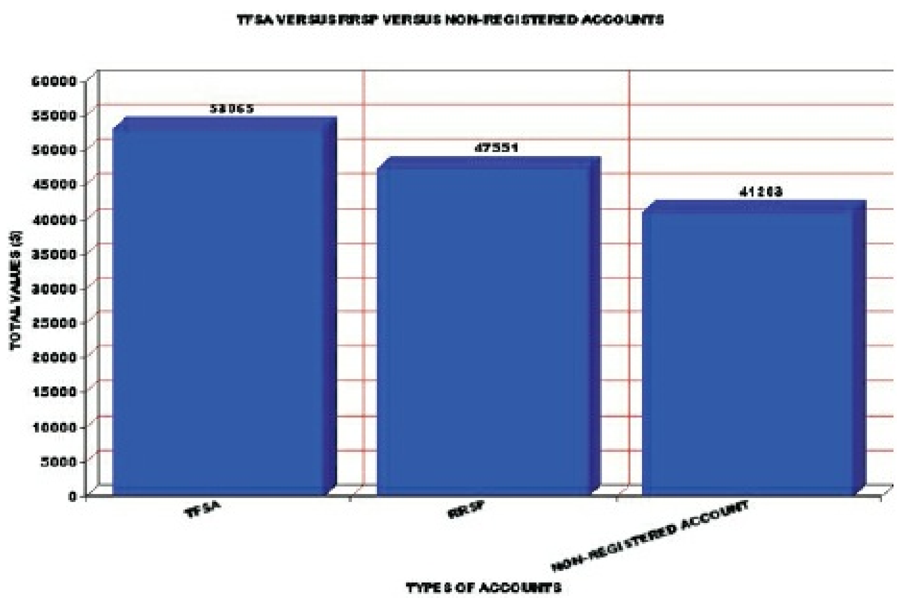
6. Make use of a Tax Free Savings Account

Since the last couple of years, Canadians were given the wonderful option of a Tax Free Savings Account. To open up a TFSA you must:

- •Be over 18.
- •Have a valid sin number.

You should consider contributing to a TFSA because:

- •Income earned inside a TFSA is not taxed
- •Withdrawals from a TFSA are not taxed



However, there is a limit on the amount you can deposit into a TFSA based on your “contribution room”.

This amount is the base amount picked for this account added to the withdrawals made in the previous year, added to the unused contribution room accumulated from before. The CRA monitors the limits. TFSA can also hold most eligible investments such as mutual funds, bonds etc. It is recommended to use a TSFA to save up for your child’s education.

7. Keep a hold on your stocks for at least a full year

Long-term Capital Gains are taxed at a lower rate, in comparison to short-term capital gains. If you hold your stocks for less than a year(short term), then you are likely to be taxed at a rate of almost 12% more, than you would if you had crossed the 12 month mark and converted it into a long-term capital gain.

In terms of taxes, paying a more than 10% difference can make a large difference in terms of the compounding effect on the lower income taxes today. In the bigger picture you will find, that holding on to your stocks for the sufficient period of twelve months will save you, a more than sufficient amount of money.

8. Protect income with an exempt life insurance policy

After deliberation with your financial advisor, consider using your life insurance policy as an investment strategy. Many life insurance policies today, follow the exemption rule. An exempt policy, allows a portion of the amount you pay as a premium to be deposited in a pool of investments that are increasing, to be free from tax. This amount, along with the face value of the insurance policy can then be handed to your offspring or successor upon death. However, in order to somehow be able to use this tax free pool of funds during your lifetime, you could potentially use it as collateral when borrowing funds.

9. Invest in Real Estate jointly with your Spouse

Investing in real estate collectively with your spouse is a form of effective income splitting. Purchasing a house and then renting the property out will generate profits. Splitting that purchase with your spouse will result in a fifty/fifty split of the profits as well. Hence the amount of profits will not increase the amount of income earned for just one partner. It will be evenly distributed amongst the two. Tax wise, it is smarter to split the amount as joint owners. It will cut down the amount of tax your family has to pay.

10. Invest in high risk flow-through shares and receive higher deductions

Flow through shares are designed in a way that they give investors a large amount of tax deductions, which are equal to, or almost as much as the original amount invested. The shares that you have invested in, allow tax deductions to be "flown" through the owner of the shares. The company issuing the flow through shares can renounce their expenses for the current in favor of the owner of the shares, so that the owner can claim those expenses on his/her tax return.

The deductions that have been issued to the investor are not used in the same year. Flow shares are also reduced by deductions the investor is able to claim.

In essence, by being able to deduct the full value of the initial investment (or close to it) on these special kinds of shares, investors are able to earn back what they initially invested.

11. Claim Deductions for Health & Dental Costs

Your business can pay health and dental premiums to your insurance company, for you and your employees. If your business is your primary source of income and you are actively involved in running it, then you are eligible to receive a deduction. A deduction is a claim that can be made to reduce your taxable income. It helps reduce your tax bill.

However as the owner of the business, you must provide your employees the same health and dental benefits that you and your family are currently receiving. However these benefits have to reasonable. In the case that you do not have any employees, you must make sure that the health and dental benefits are once again of a reasonable amount, an amount similar to what you would receive if working for a third party.

12.Hire a Co-op Student

If your business decides to hire a Co-op student or an apprentice, you can claim a tax credit.

A tax credit is different from a deduction. Receiving a tax credit will also reduce your tax bill but not by reducing your taxable income. It directly reduces your provincial and federal tax bill (dollar for dollar). As a business, you are entitled to receiving a tax credit of up to 25% on salaries paid to Co-op students. There is a cap on the actual amount you can receive annually per coop student, usually around 3000 Canadian dollars a year.

Through this tactic you can get reimbursed to a larger extent and benefit greatly as well, through the skills of the apprentice or co op student.

13. Pay your partner (spouse) a director's fee

A director of a corporation helps oversee the management of your company. A director's managerial activities include the following:

- Attending directors' meetings.
- Hiring officers for the company.
- Approving and overseeing Financial Statements.
- Declaring Dividends.
- Approving modifications to the share capital of the corporation.

There is a fee associated with the performance of these services. It is called the director's fee and is paid directly to the director by the corporation.

How is this relevant as tax saving strategy? Appoint your spouse as the director and ask him or her to perform the relevant services for your corporation. Then pay him or her, the appropriate fee that will be added to his or her income. If your spouse is in a lower income bracket, he or she will not be taxed heavily on the "fee" she received from the corporation. In terms of saving taxes from the corporation's side, the director's fee is tax deductible for your corporation as well, reducing the amount your company has to pay in tax.

14. Incorporate your business (Self-employed)

If you are self employed, running your own business, and want to reduce your never-ending outflow of money in the form of taxes, consider incorporation. By legally incorporating your business, you are automatically reducing your currently soaring tax rate.

An incorporated business's profits are only subject to a tax rate of 15.5 %, if the business is controlled / owned by a Canadian. However, in the event that you are a self employed owner without an incorporated business, the profits of your business are being added to your personal income. That important addition increases your taxable income by a significant amount, potentially landing you in the highest income bracket. The tax rate of the highest income bracket in Ontario, Canada is at a 49.53 %. So you can save up to 33% in taxes by incorporating, because of the difference in the rate of tax between an incorporated company and a business that has not been incorporated.

This is one of the most effective tax strategies to cut down on the amount you pay as taxes. If you haven't incorporated your business yet, speak to an experienced accountant immediately.

15. Use your corporation to buy a home

Instead of using your personal income to purchase a home, use your corporation to make the investment. How? Use an Employee Home Purchase Loan.

1. Obtain a loan from your corporation on a tax free basis. Ensure that the mortgage is defined and that the home can legally be used as collateral.
2. Pay a reasonable amount of interest, at least equal to the market rate of the interest.
3. Ensure the term for repayment of the loan, is of a reasonable amount. It is recommended you check

amortization periods to determine the appropriate time.

4. Employment- Ensure you are an employee of your own corporation, receiving regular payroll and under a valid employment agreement.

Hence after following the steps above you can easily use an Employee Home Purchase Loan and save!

As with any tax saving strategy, you should consult with your accountant before proceeding.

16. Home Office can be used to Maximize the Deductions

Following is the two taxable categories for home office:

1) Your home is where you conduct the principal portion of your business.

2) There is a specific location in your home (such as home office) that is exclusively used for your business.

If your self-employment meets one of these criteria or both, you are allowed to start deducting your home office expenses.

The following deductions can be made in respect of your home:

•Rent (if you are a tenant)

•Interest on a mortgage loan.

•Property tax.

•Utilities to run the space (electricity, gas, water).

•Home owners or renters insurance.

•Repairs and maintenance for the space to function.

Only a percentage of the above expenses can be claimed as a tax deduction. That percentage is equal to the size of your home office compared to the size of your home. For example, if your home office makes up 20% of the square footage of your home, then only 20% of your house costs can be claimed.

It is important to maximize your deductions as much as possible, so consider the following tip:

•Increase the amount of square footage your home office takes up in your home.

•Exclude square footage that is non-usable.

17. If your car is being used for business purposes, claim all deductions

Car expenses can be deducted to reduce your business income.
The following is a list of claimable Automobile Expenses:

•Lease costs (up to a maximum of $800 per month)
•Depreciation (calculated as 30% of the purchase price, to a maximum of $30,000)
•Parking fees and tolls your vehicle incurs while being used for business related tasks
•Car washes
•Insurance
•Auto loan interest
•Repairs
•Gas

You can only deduct the portion of your car expenses that relate to driving for business purposes. For example, if your business mileage is 80% of the total amount that you drove your car, then only 80% of your car expenses can be deducted.

Tip: In order to save more, keep your old car, you are more likely to have repair costs which will help in more deductions from annual taxes as compared to new car with minimal (if any) repairs.

Tip: Keep a log book to track your business mileage.

18. Income splitting through a family trust

A major source of tax savings can be done through a family trust. Follow the following steps to see how you can save your family thousands of dollars in tax with this tip.

Step 1: Set up a discretionary family trust.

This can be done through your bank or financial institutions. Include all family members above 18 years old to be eligible beneficiaries.

Step 2: Set up a limited company in Canada

Many self employed individuals (accountants, doctors, dentists, lawyers, etc) can create a limited company for their business. By doing so, your company will be taxed at lower rates than individuals. This means more of your business profit remains in the company.

Step 3: Buy company shares through family trust.

As your company earns revenue you will be required to pass the earnings along to the shareholders. Once the company has been taxed at the corporate rate it can then issue a dividend. Since the only shareholder is the family trust it will be passed down the dividend.

Step 4: “Flow through” dividend to family members.

When the dividend is paid to the family trust it will not be taxed as long as it does not remain in the family trust. The dividend would then be passed down the family members with the lowest income tax bracket. Since Canada works on a marginal tax system lower income earners will be taxed lower personal rates.

19. Quick Method for Accounting for HST

The Quick Method is available for small businesses, and is a simplified way of calculating net sales tax for HST purposes. The major advantage to small business owners is reduced paperwork and easier calculations. This method is available for a small business with annual revenue less than $400,000

How this method works is you will charge your clients 13% HST on sales. If your business meets CRA requirement of less than $400,000 annual revenue you are only required to remit 8.8%.

Example: John has business revenue of $100,000 during the year. He applies 13% HST to all orders. Thus John will have collected $13,000($100,000 x 13%) but only has to remit $9,944($113,000 x 8.8%).

CRA understands it's important for small business owners to have capital remain in their business. A major source of failures in new small businesses is they don't have enough cash remaining in the business. CRA is trying to help small business owners out by letting them keep a portion of tax collected.

20. Advantages of hiring your spouse if you are a medical practitioner

Medical Practitioners such as doctors, physicians, chiropractors, dentists, pharmacists can take advantage of many tax tips available to them. The most common form of tax savings is through income splitting. Medical practitioners can hire their spouses and/or children and pay them a salary. This will allow some of the income earned in your business to be taxed at a lower marginal tax rate if your spouse or children have no other or very little income. Important to note that the work must actually be performed and documentation must be kept. As well, pay should be an accurate representation of work your spouse or child actually performed.

Another form of Income splitting is making your spouse and/or Children partial owners in your Professional corporation. By doping this you can transfer down dividends to each member elevating some of the tax burden. When combined with tax tip 18 you can potentially pay no tax when the dividend is flowed through a family trust. Only the following Qualified Medical practitioners can become shareholders in Medical professional corporations:

-Orthodontists
-Chiropractors
-Surgeons
-Family doctors
-Pharmacists
-Physicians

For family members of physicians and dentists, they can become shareholders, as long as they own non-voting shares.

TIP: Dividends paid to children under the age of 18 will be subject to a “kiddie tax” and included in the owners taxable income at the highest marginal tax rate.

Other tax savings available to medical practitioners are spousal loan to obtain a return at a lower tax rate and Spousal RRSP Contributions.

About the Author

Allan

Madan

CPA, CA

Allan Madan is a Chartered Accountant, Chartered Professional Accountant and Tax Expert who enjoys working with business owners, individuals and entrepreneurs.

Allan has over 14 years of experience in public accounting. Prior to founding Madan Chartered Accountant in Mississauga, he worked for the prestigious firm Deloitte for six years, where he held the position of International Tax Manager. He has completed Parts 1 and 2 of the *Canadian In Depth Tax Course*, which is the most comprehensive tax training course in Canada. Allan has been involved in many complex, tax reorganization transactions for Canadian companies.

Allan Madan

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