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A recent report showed that a surprising number of Canadians actually enjoy preparing their tax returns¹, perhaps because they know that there are a number of ways to realize significant tax savings through filing. Add to this some lesser-known government tax incentives and you can end up with extra cash in your pocket.

One of the best ways to get value from your tax return is to take advantage of all the tax deductions and tax credits that are available to you. If you make a mistake and fail to report some of your income, chances are you'll receive a letter from the Canada Revenue Agency (CRA) pointing out the error of your ways. On the other hand, if you fail to claim valuable deductions or credits, don't stand by your mailbox waiting for notification from the CRA. There's no automatic warning system in place to let you know that you could be getting more value from your tax return. So it pays (literally) to know how these deductions and credits can help you keep more of your money. You may also be interested to learn that some of the highest tax-driven benefits may be found beyond the pages of your return.

THE SYSTEM OF TAX DEDUCTIONS AND TAX CREDITS

Tax savings generally begin on page three of Form *T1 – Income Tax and Benefit Return* as this is where valuable tax deductions are claimed. These are amounts that you can deduct from your total income to arrive at your taxable income, which is the base for calculating the amount of tax that is payable. Additional savings can be found on *Schedule 1*, where you claim a number of non-refundable tax credits that directly reduce the tax you pay.

Income tax is levied at graduated, "progressive" rates, such that higher tax rates apply as your income level increases. Chart 1 shows the federal tax rates that apply to various levels of taxable income.

Chart 1: Federal tax rates for 2012

Taxable Income	Federal Tax Rate
To a maximum of \$42,707	15%
Above \$42,707 to a maximum of \$85,414	22%
Above \$85,414 to a maximum of \$132,406	26%
Above \$132,406	29%

Let's look at an example that shows how a tax deduction yields tax savings at the marginal tax rate² that varies with your income level, while a tax credit yields tax savings at a fixed rate. Suppose you have total income of \$50,000. Chart 2 shows how deductions and credits reduce the tax that you pay.

Chart 2: Value of a \$1,000 federal tax deduction and tax credit

	No deduction or credit	Tax Deduction	Tax Credit
Total income	\$50,000	\$50,000	\$50,000
Deductions	n/a	(1,000)	n/a
Taxable income	\$50,000	\$49,000	\$50,000
Tax @ 15% on first \$42,707	\$6,406	\$6,406	\$6,406
Tax @ 22% on remaining income	1,604	1,384	1,604
Total tax payable before credits	\$8,010	\$7,790	\$8,010
Tax credit (\$1,000 @ 15%)	n/a	n/a	(150)
Total tax payable	\$8,010	\$7,790	\$7,860
Value of deduction / credit		\$220	\$150

The amount of the deduction is subtracted from income, so that this amount of income is not taxed. In Chart 2 a \$1,000 tax deduction yields \$220 of tax savings, calculated as the \$1,000 deduction multiplied by the marginal tax rate that would have applied to the income (22%). Consequently, a deduction yields tax savings at your marginal tax rate.

With tax credits, a fixed rate is applied to eligible amounts and the resultant credit amount offsets taxes payable. Chart 2 shows that when the federal tax credit rate of 15% is applied to a \$1,000 amount, \$150 of tax savings results.

When you add provincial tax savings to the federal savings above, the total tax savings can range from 20% for the combined credits and up to 50% for a deduction.

THE VALUE OF SELECTED TAX DEDUCTIONS, CREDITS AND OTHER AMOUNTS

Since the value (tax savings) from a tax deduction is based on your marginal tax rate, a tax deduction can provide greater value for those who have higher levels of income. Since the value of a tax credit is based on a rate that is fixed for all taxpayers, a tax credit yields the same value regardless of income level or marginal tax rate.³

Chart 3 shows the hypothetical values you can realize from a variety of tax deductions, credits and other amounts. The tax rates used in the examples were chosen to approximate the average combined federal/provincial rates for an individual with \$50,000 of total income. You may be surprised to learn that many commonly-claimed items have relatively little value, while some lesser-known ones can produce up to a 300% tax-assisted benefit on your money. The assumptions used to come up with the savings are reviewed in detail below.

Chart 3: Hypothetical values of Selected Tax Deductions, Credits and Contributions at \$50,000 annual income level

Tax Deductions

RRSP deduction	\$1,500
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Tax Credits

Public transit amount	\$225
Children's fitness and arts amounts	\$300
Family caregiver amount	\$300
Charitable donations and gifts	\$360
Dividend tax credit for eligible dividends	\$590
Amount for children born in 1995 or later	\$660
Allowable medical expenses	\$700
Disability amount	\$1,510
Tuition, education and textbook amounts	\$1,965

Other amounts

Non-taxable portion of capital gains	\$750
RESP contributions	\$1,000
Pension income splitting	\$2,500
RDSP contributions	\$13,500



TAX DEDUCTIONS

RRSP Deduction – Value: \$1,500

One of the most commonly-known ways to save tax is to make a contribution to a Registered Retirement Savings Plan (RRSP). You can claim a deduction for contributions made up to 60 days after year end that do not exceed 18% of your previous year's earned income, with a maximum deduction of \$22,970 for 2012. If you have carried forward unused RRSP contribution room, you can claim a higher deduction. You may, however, choose to defer claiming your deduction until a later year, which can be advantageous if you expect your marginal tax rate to be materially higher in the future.

Suppose you made an RRSP contribution of \$5,000. At a marginal tax rate of 30%, this deduction would have a value of approximately \$1,500. Of course, this is merely deferring the tax owing on the \$5,000 until a later time, such as retirement, when the funds are withdrawn, hopefully at a lower marginal tax rate. In the interim, the investment income earned inside your RRSP is effectively tax-free.⁴

TAX CREDITS

Public Transit Amount – Value: \$225

You can claim a tax credit for the cost of public transit passes that entitle you to unlimited travel for an uninterrupted period of at least 5 days and at least 20 days in any 28-day period. Monthly and annual transit passes would generally meet these requirements, as would some weekly passes. A federal credit can be obtained at 15%. The provinces do not provide a credit for public transit.

Assuming you pay \$125 per month for transit passes for a total of \$1,500 annually, at a federal tax credit rate of 15%, the value of this credit is \$225.

Children's fitness and arts amounts – Total value: \$300

The children's fitness amount provides a tax credit for up to \$500 of fees you pay for your children to participate in programs requiring significant physical activity, such as sports and athletic programs. The children's arts amount provides another tax credit for up to \$500 of fees that you pay for children's programs related to artistic, cultural, recreational, or developmental activities, such as music, Scouts and Guides, or tutoring. Both the fitness and arts amounts can be claimed for each of your children who is under 16 years of age at the beginning of the year. Provincial credits are available for fitness and arts amounts only in B.C., Manitoba, and Ontario.

Suppose you have two children, with your first child enrolled in soccer and music lessons and your second child enrolled in dance and math tutoring. If you pay at least \$500 for each of these four programs, you could claim a \$1,000 (2 x \$500) children's fitness amount as well as a \$1,000 (2 x \$500) children's arts amount, for a total of \$2,000. At a federal credit rate of 15%, these credits would have a value of \$300.

Family caregiver amount – Value: \$300

Starting in 2012, you can claim a federal family caregiver amount of \$2,000 for each of your qualifying dependants who has an impairment in physical or mental functions. This is in addition to the caregiver amount that is available at the federal and provincial levels. Eligible dependants may include your spouse, children, or parents and grandparents who were at least 65 years of age. The \$2,000 amount is added to other amounts that you claim for dependants, such as the spouse or common-law partner amount, the amount for an eligible dependant, the amount for children born in 1995 or later, or the caregiver amount. Claiming the family caregiver amount of \$2,000 for one dependant provides a federal tax credit that, at rate of 15%, would yield tax savings of \$300.



Charitable donations and gifts – Value: \$360

A tax credit is provided for donations and gifts to qualified charitable organizations, including registered charities, and public or private foundations. For the amount of total charitable gifts that exceeds \$200 in a tax year, the credit is generally calculated at the highest combined federal/provincial tax rate.⁵ As with most other tax credits, the lowest tax rate generally applies to gifts below the \$200 threshold.

Suppose charitable gifts totalled \$1,000. An Ontario donor at the \$50,000 income level would realize a combined federal/provincial tax credit at a rate of 20.05% for the first \$200 and 40.16% on the remaining \$800, yielding a credit of about \$360.⁶

Dividend tax credit for eligible dividends – Value: \$590

In 2012, a federal dividend tax credit is provided that equals 20.7%⁷ of eligible dividend income; provincial credits range from 8.8% (in Ontario) to 16.6% (in Saskatchewan). Consequently, the combined federal/provincial credit is worth at least 29.5% of eligible dividends, and may be higher, depending on your province/territory of residence.

If you had eligible dividend income of \$2,000, the value of this credit would be approximately \$590 assuming a dividend tax credit rate of 29.5%.

Amount for children under 18 (born in 1995 or later) – Value: \$660

You can claim an amount of \$2,191 for each of your children who was under age 18 at the end of the year. For 2012, the amount can be claimed for children who were born in 1995 or later. The provinces do not provide a similar credit.

If you claimed this amount for each of two children, the total amount would be \$4,382 (2 x \$2,191). At a federal credit rate of 15%, the value of the tax credit would be about \$660.

Allowable medical expenses – Value: \$700

You can claim a credit for total medical expenses that exceed the lesser of 3% of your net income or \$2,109 in 2012. Common eligible medical expenses include fees for doctors, dentists, qualified therapists or other medical practitioners, prescription medication or eyewear, and hospital or medical laboratory services. One commonly-overlooked expense is out-of-pocket costs for medical and dental insurance plans. Beware, however, that qualifying medical expenses can differ from province to province. For example, fees for an acupuncturist can only be claimed in B.C., Alberta, Quebec and Newfoundland.⁸ Although amounts are not eligible if they have been reimbursed (such as by a health insurance plan), you can claim amounts paid within any 12-month period that ends in the tax year.

For example, the cost of putting braces on your children could easily be \$3,000 in a year. Coupled with medical insurance premiums, prescription medications and eyeglasses, and some visits to therapists for an aching back, you could find your expenses amount to over \$5,000. Assuming a threshold of \$1,500 (\$50,000 x 3%), you may have about \$3,500 in allowable expenses, which would yield \$700 of tax savings at a rate of 20%.

Disability amount – Value: \$1,510

You can claim the disability amount if a medical professional certifies on Form *T2201 – Disability Tax Credit Certificate* that you had a severe and prolonged impairment in physical or mental functions. For 2012, the federal disability amount is \$7,546 and provincial disability amounts range from \$5,558 (Newfoundland and Labrador) to \$13,331 (Alberta).⁹ You may also be able to claim a disability amount that would otherwise be claimed by another individual (such as your spouse, common-law partner, child or parent) to the extent that the individual does not need to claim the disability tax amount to reduce taxes payable to zero.

In 2012, an Ontario resident could claim a federal disability amount worth about \$1,130 (\$7,546 x 15%) and a provincial disability amount worth about \$380 (\$7,598 x 5.05%), for a combined value of about \$1,510.



Tuition, Education and Textbook Amounts – Value: \$1,965

Students enrolled in post-secondary education can claim a federal tax credit based on the amount of tuition that is paid. The federal education amount provides an additional \$400 per month of full-time attendance and \$120 per month of part-time attendance. The provinces also offer tuition amounts and all provinces except Quebec offer education amounts.¹⁰ Furthermore, the federal government offers a textbook amount of \$65 per month of full-time attendance and \$20 per month of part-time attendance.

If the student does not have sufficient income to use the credits in the year of attendance, up to \$5,000 can be claimed by the student's spouse or supporting parent or grandparent. Any remaining amount can be carried forward for use by the student in a future year.

Suppose your tuition was \$6,000 and you attended post-secondary school for eight months in the year. In Ontario, the value of the tax credit would be approximately \$1,965 in 2012.¹¹

OTHER AMOUNTS

When looking for tax savings, value doesn't only come in the form of deductions and credits and may even extend beyond your tax return.

Non-taxable portion of capital gains – Value \$750

Unlike interest income that is fully taxable, only 50% of capital gains (less capital losses) are included when calculating total income. The remaining 50% is excluded from income and tax is saved at your marginal rate on this excluded half of net capital gains.

Suppose you had net capital gains of \$5,000 from the sale of shares in 2012. Only half of this amount (\$2,500) would be taxed so you would pay tax of \$750 ($\$2,500 \times 30\%$) on the capital gain, assuming a 30% marginal tax rate. If instead you had earned interest income of \$5,000, you would have paid tax of \$1,500 ($\$5,000 \times 30\%$). The tax savings from earning capital gains in comparison to interest income would, therefore, be \$750 ($\$1,500 - \750).

Registered Education Savings Plan (RESP) – Value: \$1,000

RESPs allow for tax-efficient savings for children's post-secondary education. Up to \$50,000 can be contributed for each child who is a beneficiary of an RESP. The government provides Canada Education Savings Grants (CESGs) equal to 20% of the first \$2,500 of annual RESP contributions per child or \$500 for each year. If a contribution is not made in a particular year, unused CESG room is carried forward and beneficiaries up to age 17 can receive up to \$1,000 of CESGs in any one year, with a \$7,200 lifetime limit. Consequently, a catch-up contribution of \$5,000 will garner the maximum CESG of \$1,000 in one year.

While contributions to an RESP are not tax deductible, earnings accrue on a tax-deferred basis. Funds that are withdrawn for post-secondary education are taxable to the student, who often will pay little or no tax.

If an RESP is first opened in April 2013 and a contribution of \$5,000 is made, provided there are at least two years of unused RESP and CESG room, the government would contribute an additional 20% in CESGs. The value from a \$5,000 contribution is, therefore, \$1,000 ($\$5,000 \times 20\%$).

Pension income splitting – Value: \$2,500

Spouses and common-law partners can jointly elect to split pension income. Up to 50% of income that qualifies for the pension amount can be deducted by the recipient, provided this same amount is added to income by the individual's spouse or common-law partner. This pension income splitting technique has value when the pension recipient has a higher marginal tax rate than the spouse.

Pension income splitting may also prevent the loss of income-tested benefits by lowering the income of the pension recipient below the clawback threshold. Old Age Security (OAS) benefits, which had a maximum of about \$6,510 in 2012, are clawed back at a rate of 15% with net income exceeding \$69,562. The Age Amount, which provides federal/provincial tax credits



ranging from about \$1,200 to \$1,500 for 2012 depending on the province, is reduced at a rate of 15% when net income exceeds about \$33,000.¹²

Suppose you have a marginal tax rate of 45% while your spouse's rate is 20%. The net tax savings on split pension income would be 25% (the difference between your 45% marginal rate on the pension deduction and your spouse's 20% marginal rate on pension income). The value of splitting \$10,000 of pension income would, therefore, be \$2,500 ($\$10,000 \times 25\%$), plus possible savings of OAS benefits and preservation of some or all of the Age Amount.

Registered Disability Savings Plan (RDSP) – Value: \$13,500

RDSPs are tax-deferred savings plans that can benefit Canadians who are eligible for the Disability Tax Credit. Up to \$200,000 can be contributed to the plan until the beneficiary turns 59, with no annual contribution limits. Canada Disability Savings Grants (CDSGs) and Canada Disability Savings Bonds (CDSBs) may be received from the government until the beneficiary turns 49. Depending on family income, CDSGs may be up to 300% of your contributions, with a maximum of \$3,500 per year, while no contributions are needed to receive the maximum CDSB of \$1,000 per year. If maximum CDSGs and CDSBs are not claimed in a year, unused CDSG and CDSB room can be carried forward for up to ten years. Up to \$10,500 of CDSGs and \$11,000 of CDSBs will be awarded in a year that catch-up contributions are made.

As with an RESP, contributions to an RDSP are not deductible; however, taxes are deferred until withdrawal, when funds are taxable to the plan beneficiary who may have little or no tax to pay.

Suppose an individual first became eligible for the disability tax credit in 2011 and continued to be eligible in 2013. If an RDSP were first opened for the individual in April 2013, contributions could be made for each of the three years of eligibility (2011, 2012 and 2013). A \$1,500 contribution would yield \$3,500 of CDSGs for each year, so three years' worth of contributions (\$4,500) would net \$10,500 of CDSGs.¹³ \$3,000 of CDSBs would also be paid into the plan¹⁴, regardless of contributions, for total value of \$13,500 ($\$10,500 + \$3,000$).

CLAIMING DEDUCTIONS AND CREDITS FOR PREVIOUS YEARS

We can see that valuable tax savings can be realized by claiming tax deductions and credits. But what if you didn't know about these savings or forgot to make claims in previous years? You can still remedy the situation by filing Form *T1-ADJ – T1 Adjustment Request* for any of the ten previous tax years. In this form you report the amount of the deduction or credit that you originally claimed (zero if no claim was made), along with the revised amount that you are claiming. CRA will process your request and, assuming the deduction or credit is allowed, will issue you a refund for the tax overpaid.

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- ¹ Survey commissioned by Thomson Reuters in February 2013. See http://www.drtax.ca/en/ufile/news/tax-news/13-02-25/Survey_says_41_per_cent_of_Canadians_actually_LIKE_filing_their_tax_return.aspx.
- ² This report considers statutory income tax rates and does not consider the impact of low-income tax reductions or the loss of various income-tested benefits, such as Old Age Security or the Age Amount, that are "clawed back" once income reaches various annually-indexed, legislated thresholds. For more details, see "Know your marginal effective tax rate" at <http://www.nationalpost.com/related/topics/Know+your+marginal+effective+rate/2528406/story.html>.
- ³ Note that provincial surtaxes, where applicable, can increase the value of a credit. For example, in Ontario the provincial tax credit rate for most non-refundable credits is 5.05% when the surtax does not apply and effectively increases to 7.88% when the maximum high-income surtax of 56% applies.
- ⁴ For a full discussion of the benefits of RRSP investing, please see our Report "Just do it: The case for tax-free investing" at <https://www.cibc.com/ca/pdf/case-for-taxfree-en.pdf>.
- ⁵ In 2012, for donations over \$200, the combined federal and provincial donation tax credit in Alberta, Ontario and New Brunswick differs from the top marginal tax rate and is 50%, 40.16% (46.41% for Ontario taxpayers subject to the high income surtaxes) and 46.95% respectively.
- ⁶ The 2013 Federal Budget proposed a temporary First-Time Donor's Super Credit, which would provide an additional 25% tax credit for a "first-time donor" on up to \$1,000 of donations made after March 21, 2013 and claimed in tax years up to 2017. For a qualifying charitable gift of \$1,000, this would increase the value of the federal credit by \$250.
- ⁷ $6/11 \times 38\%$.
- ⁸ A list of authorized medical practitioners by province is available from CRA at <http://www.cra-arc.gc.ca/tx/ndvdl/tpcs/ncm-tx/rtrn/cmpltng/ddctns/Ins300-350/330/ampp-eng.html>.
- ⁹ The disability amount is allowed federally and in all provinces except Quebec, where an "amount for a severe and prolonged impairment in mental or physical functions" of \$2,485 can be claimed.
- ¹⁰ The provincial education amount equals the federal amount in Saskatchewan, Manitoba, New Brunswick and P.E.I. In B.C., Nova Scotia and Newfoundland and Labrador, the provincial amount is 50% of the federal amount. The provincial education amount exceeds the federal amount in Alberta and Ontario.
- ¹¹ The federal amounts total \$9,720 (\$6,000 education amount + 8 x \$400 education amount + 8 x \$65 textbook amount) and the federal credit is \$1,458 ($\$9,720 \times 15\%$). The Ontario amounts total \$10,048 (\$6,000 education amount + 8 x \$506 education amount) and the provincial credit is \$507 ($\$10,048 \times 5.05\%$). The combined federal/provincial tax credit is, therefore, \$1,965 ($\$1,458 + \507).
- ¹² In 2012, the federal age amount of \$6,720 yields a tax credit of about \$1,000, which is clawed back at a rate of 15% when net income exceeds \$33,884. In provinces other than Quebec, the age amount ranges from about \$3,700 to \$6,700, with tax credits ranging from about \$200 to \$500 and clawback of 15% with a net income threshold of about \$27,000 to \$36,000. In Quebec, the amount for individuals born before January 1, 1948 is \$2,350 and yields a credit of \$470 at a rate of 20%.
- ¹³ This assumes that family income did not exceed thresholds for receiving the maximum amount of CDSGs and CDSBs in each of those years.
- ¹⁴ Ibid.

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