5 TAX TIPS EVERY RETIREE SHOULD KNOW

...BUT RARELY DO!

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The goal should be to pay the tax we owe, but not leave a tip.

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1. Age Credit Clawback

Individuals aged 65 and over are eligible for a non-refundable tax credit of up to $7,713 (for 2021) Calculated as $7,713 multiplied by 15%. Most people are aware that their Old Age Security (OAS) will be clawed back (recovery tax) when their income reaches a certain threshold. People are rarely aware that the same thing happens, be it on a smaller scale, with the age credit. This amount is clawed back (reduced) by 15% of your net income over $38,893 (for 2021) and is eliminated when your net income exceeds $90,313 (for 2021).

2. Dividend income is not the most tax efficient income option for Canadian retirees

Many people believe that dividend investing is the end all be all for retirees for a multitude of reasons. However, this broad thinking fails to consider several items including OAS and age credit claw backs, non-Canadian dividend income and the other potential forms of income creation.

While dividends paid by Canadian companies receive a tax credit, this form of income is also grossed up by 38% to determine your net income. It is your net income that determines your eligibility for other benefits such as Old Age Security and the Age Credit. The dividend tax credit is applied after the net income is calculated. Additionally, non-Canadian company dividend income is taxed at your top marginal tax rate. On top of that it is often subject to foreign withholding tax.

Focusing only on creating dividend income also neglects the opportunity for more tax advantageous income created through capital gains or even a return of capital. This is not to say you shouldn't invest in dividend paying companies and for now we will hold off the debate on whether dividend paying companies do a better job of keeping your principle intact.

3. Not All Income is Equal

When and where you take your income from in retirement can make a significant impact on how long your money lasts. Any income received from pensions, RRSP's, RRIFs and other retirement accounts, CPP and OAS are all fully taxable income. On the same hand RRIF and pension income can be split with your spouse where applicable to reduce the income of the higher income earner.

Income (withdrawals) taken from your Tax-Free Savings Account (TFSA) is completely tax-free and has no effect on any income tested benefits such as OAS or the Age Credit.

Income taken through non-registered investment accounts will vary based on the type of income such as dividends, capital gains, interest or return of capital.

It is important to consider all these variables when creating your sustainable retirement income withdrawal strategy to ensure you can minimize tax and maximize the longevity of your investment portfolio.

4. Claim up to $10,000 towards the Home Accessibility Tax Credit

We often find many of our retiring clients tackle the big home improvements they have been thinking about for years as soon as they retire. These often include accessibility improvements at the same time because, most often, their goal is to remain in their home as long as possible. This credit is designed to help with labour and material expenses incurred for an accessibility based renovation of a home. The credit is a maximum of $1,500 and is calculated as 15% of the qualifying expenses up to $10,000 per year.

Qualifying individuals are aged 65 and over or qualify for the Disability Tax Credit.

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5. Pension Tax Credit

We have many clients who do not require a regular stream of income from their Retirement accounts early on in retirement but will often want to take lump sums as needed. There is no requirement to setup a stream of income from your RRSP before it must be transferred to a Registered Retirement Income Fund (RRIF) at age 71. However, it often makes sense to transfer even a small portion of your RRSP to a RRIF if you are 65 or older and plan to take withdrawals from your RRSP. This is because the RRIF withdrawal will be considered pension income and the first $2,000 of pension income can be claimed towards the pension tax credit.

Learn more about how Matthews + Associates may be able to help you...

Matthews + Associates is a financial planning firm dedicated to helping those approaching or in retirement achieve & maintain financial freedom and create future opportunities for the ones they love.

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