Randall J. Ladell, MBA

Chartered Accountant

Licensed Public Accountant

**1210 Sheppard Avenue East, Suite 405**
**Toronto, Ontario, M2K 1E3**
**Email: randall@rjladell.ca**
**Website: www.rjladell.ca**

**Business: (647) 436-8782**
**Mobile: (647) 280-4248**
**Fax: (647) 436-8742**


## Personal Canadian Taxes – Taxable income, rates and breaks

In 1972, the Government of Canada passed the first version of our "simplified" Income Tax Act (ITA). The 2005 CCH published Canadian Income Tax Act with Regulations is 2,580 pages. The ITA itself is supplemented by interpretation bulletins, information circulars, advance tax rulings and legal precedents, and to summarize even the basics in two pages is an impossible task. What this article attempts to do is provide a highly simplified overview of some very basic tax information.

### What is taxable

A Canadian resident is taxable on all of his or her income from all sources both inside and outside of Canada, that is, world income[1]. If some of the income is from sources outside of Canada, the taxpayer will receive full or part credit for any income taxes paid in the country in which the income was earned.

Individuals are taxed on income from an office or employment or self-employment, on income from any property he or she may own and on certain other receipts that are defined as taxable in the Income Tax Act (ITA). These items include scholarships, research grants and pensions. Income from property is most commonly rental income, interest, dividends and royalties.

A taxpayer must also declare as income 50% of any capital gains, i.e., any gain from an increase in value of any property that is realized on the sale of that property. A simple example would be an investment in a stock that was acquired for $10,000 and sold for $20,000. The realized gain of $10,000 is 50% taxable, i.e., you must add $5,000 to your income in the year the shares were sold. All capital properties are subject to capital gains taxation when sold with only two exceptions, the sale of personal use property with a value of less than $1,000 and the sale of your principal residence.

What is not taxable income? The Income Tax Act defines many items as not being income and some of the most common of these are loans and gifts, lottery and gambling winnings, proceeds from life and personal disability insurance, proceeds from personal legal actions, social assistance payments, workers compensation and Old Age Security Income Supplements.

### Tax deductions

After a taxpayer has calculated his or her total income on the T1 personal return he or she is then allowed to deduct certain amounts to arrive at net income and taxable income.

The basic deductions that taxpayers are allowed are for expenses and outlays such as child care, registered retirement plan contributions, union dues, carrying charges, moving expenses, allowable employment expenses, etc. Some of these claims are limited. RRSP contributions cannot exceed a deduction limit based on prior years' earned income and there is both an earned income limitation and maximum claimable amount for child care expenses. After deduction of these expenses the taxpayer arrives at net income which is the amount that the Federal and Ontario governments use to calculate entitlement to items such as the Ontario property tax credit, child tax credit or GST rebate.

After calculating net income, the taxpayer then is allowed to deduct more unusual items not generally applicable to most individuals such as any capital gains exemption and unutilized losses of prior years to arrive at taxable income, i.e., the amount upon which tax will be calculated.

---

[1] The rules relating to the taxation of foreign source income can be very complex and are impossible to summarize accurately in a short article. If you have foreign source income of any kind you should obtain competent professional tax advice.

**Tax credits**

Originally under the 1972 ITA, a taxpayer was allowed to deduct items such as personal exemptions, charitable donations or medical expenses directly from taxable income. This system was seen as unfairly benefiting high income earners who would receive a tax reduction of 50% or more for these personal amounts.

In 1988, items such as the personal exemption, a claim for a dependant spouse, medical expenses, education costs and a variety of other formerly tax deductible items were changed to tax credits and in 2005 these items have a constant tax credit value of approximately 22% of the claimable amount. Donations and political contributions are the only exceptions to this rule. In order to encourage charity, the government allows a tax credit of approximately of approximately 46% on total donations over $200. Similarly, to encourage the broadest possible political contributions, the government allows a credit of 75% on the first $100 in donations to a political party. (This rate declines as the political contribution increases.)

Although officially an individual begins paying tax when he or she has income in excess of approximately $9,600, effectively most taxpayers are tax exempt on their first $12,000 of income after giving consideration to tax credits for items such as CPP and EI contributions.

**Tax rates and taxes payable[2]**

Although, as noted above, personal tax credits may reduce your taxes to nil, you are taxed from your first dollar of income. We have graduated "ability to pay" tax rates that start from the first dollar of income at approximately 21% and rise to more than 46% for those with taxable income of more than $123,000.

Adding it all up a person with simple basic exemptions can expect to pay approximately $5,600 in tax on $36,000 in taxable income, $14,000 in tax on $63,000, $18,000 on $75,000 and $38,000 on $120,000 in income.

**Tax breaks on capital gains and dividends**

Not all income is taxed equally. Capital gains and dividends are considered "tax advantaged" income. As previously discussed a capital gain is only 50% taxable such that the maximum tax rate based on the "gross" gain is only 23%.

A company that is paying dividends does so from after from after tax income and the government gives a credit for the taxes paid to reduce double taxation. Without going into the details of the calculations the tax credit for company paid taxes reduces the taxes payable on eligible dividends[3] by approximately 22% and other dividends by approximately 15% for a taxpayer in the highest tax bracket.

**Conclusion**

This article has provided only the most basic tax information. It has not discussed even relatively simple items such capital losses, business losses, what is deductible if you have self-employment, employment or investment expenses or a myriad of more complex tax issues.

What it has hopefully done is provided a reader with little or no tax knowledge with a basic overview of our system. What is taxable or deductible? What is a tax credit? And what are the basic tax rates?

My advice to almost any taxpayer is that if you have questions about your tax return or are just not certain, go to a reputable tax preparer to ensure that you pay the lowest possible tax by ensuring that you claim all possible deductions and credits. If you have a more complex return with investment or self employment income, or more complex issues seek the advice of a tax professional.

As the old English expression goes do not be "penny wise and pound foolish." The dollars you pay to a tax preparer or professional may be the best investment you ever make.

---

[2] Based on rates in effect for Ontario for 2008

[3] Eligible dividends are generally those received from larger publicly traded companies. Other dividends are usually paid from smaller privately held companies.

*This report is presented as a source of general information only and has been prepared based on information from various sources. Every effort has been made to ensure the accuracy of the information but this article it is not intended as a substitute for competent professional advice tailored to the individual reader's particular circumstance.*

©2008 – Randall J. Ladell, Chartered Accountant