



CESTNICK

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TAX MATTERS

## Use an RRSP to reduce tax on government benefits.

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In case you missed it, Groundhog Day was last week. Many places have their own furry prognosticator who crawls out of his hole each year on Feb. 2 in search of his shadow to determine whether we'll have an early spring. One such groundhog, Staten Island Chuck, confused residents in New York because, in his live-stream appearance, he crawled from his hole to absolutely no snow on the ground, despite the island being hit with a big storm that day. In addition, Chuck's handlers appeared in the video in short-sleeves, light jackets or sweatshirts. Turns out the video wasn't live. Looks like you can fool some of the people some of the time – but not everyone was fooled.

When it comes to pandemic support payments from the government – don't be fooled. Things aren't always as they appear. This "free money" is not actually free. If you've received government support, you'll have to pay tax on these amounts. Let me share an idea to deal with this issue.

### THE SUPPORT

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The government first offered support by way of the Canada Emergency Response Benefit (CERB), which you may recall provided \$500 a week for up to seven four-week periods (28 weeks in total) for those who qualify. Then, in September, the CERB transitioned into three different potential benefits which are available between Sept. 27, 2020, and Sept. 25, 2021:

- **Canada Recovery Benefit:** The CRB provides support to employed and self-employed individuals who are directly affected by COVID-19 and are not entitled to employment insurance (EI) benefits. The support is \$1,000 for a two-week period, for up to 13 of these periods, or 26 weeks in total. Those who are eligible for EI can receive similar benefits.
- **Canada Recovery Caregiving Benefit:** The CRCB is available to employees or self-employed individuals who are unable to

work because they're providing care for their child under the age of 12 or a family member who needs supervised care. The benefit is \$500 a week, for up to 26 weeks.

- **Canada Recovery Sickness Benefit:** The CRSB provides support to employed or self-employed folks who are unable to work because they are sick or need to self-isolate because of COVID-19 or have an underlying health condition that puts them at greater risk of getting COVID-19. You could receive \$500 a week for up to two weeks.

With each of these three new benefits, unlike the CERB, the government is now withholding 10 per cent of the payment as an income tax instalment since the amounts are taxable – but this might not satisfy the full taxes owing.

## **THE IDEA**

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You may be able to reduce or eliminate the tax owing on your pandemic support payments. How? By contributing to a registered retirement savings plan before the March 1 deadline, which creates an RRSP deduction to offset all or some of the taxable support you've received. You do need sufficient RRSP contribution room here.

Consider Wendy. She lives in Ontario and earned \$30,000 in 2020 – less than usual because the pandemic affected her work. She also collected the CERB for the full 28 weeks, providing her with \$14,000 in 2020. And she collected the CRB for six two-week periods (12 weeks in total) in 2020, for an additional \$6,000 of income. The government withheld 10 per cent, or \$600, from the CRB benefits she received.

So, Wendy's total income for 2020 was \$50,000 (\$30,000, plus \$14,000, plus \$6,000). She'll pay taxes of \$7,905 on this income. She had \$5,200 deducted from her pay in 2020, plus the \$600 deducted from her CRB benefits, for a total of \$5,800 in taxes remitted already. So, when she files her tax return for 2020, she'll owe an additional \$2,105 (\$7,905 less \$5,800).

Wendy could deal with this additional tax bill by paying the \$2,105 out of her savings, if she has any. Or she may be able to borrow the \$2,105 to pay the taxman. She could pay back a loan like this over 12 months at about \$180 a month if she were to borrow the funds at, say, 5-per-cent interest on an unsecured loan.

Alternatively, Wendy could accumulate wealth over time while paying the tax bill. How? She could contribute \$8,500 to her RRSP by borrowing to contribute. An \$8,500 RRSP contribution would reduce her total tax bill to \$5,755 from \$7,905. Since she's already remitted \$5,800 to the taxman, she'll be entitled to a small refund when she files her 2020 tax return.

If she were to take out an \$8,500 loan for this purpose, and paid 3 per cent on that loan, it would cost her \$188 a month for a four-year loan term. At the end of four years, these funds in her RRSP could be worth \$10,330 if she earns 5 per cent over that time. Her total interest cost over that time would be \$530.

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