The Worst Mistakes You Can Make in a TFSA

Description

Investing in TFSAs benefits investors. You can invest in a TFSA for tax-free income and growth. For a higher return, some investors take advantage of that by investing in stocks instead of putting their savings in interest-producing savings accounts such as GICs and bonds. However, these investors should be aware of the worst mistakes one can make in a TFSA.

Holding on to bad companies

Holding on to bad companies is devastating for a portfolio, especially if they're held in a TFSA (versus in a non-registered account). I'm not talking about holding a bad stock. If a bad stock is a good business, eventually the stock price will reflect the good business performance of the company. However, if it's a bad company with declining earnings, then it could take years for the company to turn around–if it does end up turning around.

To see what I mean, talk to **Teck Resources Ltd.** (TSX:TCK.B)(NYSE:TCK) shareholders who bought the stock at $40 in 2012. The stock has fallen 88% to below $5 today. Along with the price decline, its earnings per share have declined from $2.60 in 2012 to $0.28 in 2015.

Barrick Gold Corp. (TSX:ABX)(NYSE:ABX) shareholders who bought the stock at $49 in 2012 are in a similar situation. The stock has fallen 73% to $13 today. Along with the price decline, its earnings per share have declined from $3.81 in 2012 to $0.40 in 2015.

When you're holding on to bad companies in a TFSA, it's worse than holding them in a non-registered account because you can write off losses in a non-registered account. However, in a TFSA, selling at a loss means the amount is lost forever. That's why it's very important to make the right investments and pay the right prices for them when using a TFSA.

In my opinion, if investors must take on higher risk, they should do so in a non-registered account and invest more conservatively in a TFSA. For example, you might hold one or some of the Big Five Canadian banks in a TFSA, such as **Canadian Imperial Bank of Commerce** (TSX:CM)(NYSE:CM), which has paid dividends for over a century. The Canadian banks have pulled back to reasonable valuations and yield between 4% and 6%. Getting that kind of tax-free income is a good deal.

Compared with Teck Resources and Barrick Gold, Canadian Imperial Bank of Commerce’s share price rose 13% from $75 in 2012 to $85 today. In the same period its earnings per share increased 18.2%. That’s the kind of stable and conservative business I would invest in using a TFSA.

Transferring TFSAs yourself

Do not transfer TFSAs yourself! Some people withdraw funds from one TFSA to another, but this could lead to tax consequences because these transfers are treated as regular contributions and will reduce your TFSA contribution room.

If you overcontribute to your TFSA, you will be subject to a 1% tax on the highest excess amount for each month that the excess amount remains in the account. If you wish to make a transfer, make sure you get your issuer to do a direct transfer of your TFSA account for you.

Summary

Holding on to bad companies can be devastating to your portfolio and retirement plans. So, if you wish to take on higher risk for an investment, do so in a non-registered account. In a TFSA, invest more conservatively.

Transferring TFSAs yourself is a simple mistake to make. Instead, get your issuer to do it for you to ensure there are no tax consequences.

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TICKERS GLOBAL

1. NYSE:B (Barrick Mining)
2. NYSE:CM (Canadian Imperial Bank of Commerce)
3. NYSE:TECK (Teck Resources Limited)
4. TSX:ABX (Barrick Mining)
5. TSX:CM (Canadian Imperial Bank of Commerce)
6. TSX:TECK.B (Teck Resources Limited)

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