Retired Investors: How You Can Better Use Your TFSA Account

Description

Once upon a time, being retired meant withdrawing from a Retirement Savings Plan (RSP) and not having anywhere else to invest without attracting additional tax on profits and dividends. In today's environment, many younger investors are better using Tax-Free Savings Accounts (TFSA) to shield gains from attracting tax, but many retired investors are still not benefiting from this plan.

With many retired Canadians holding shares of Canada's banks for the long term, the benefit to doing so inside a registered account means that the gains of these securities will not be taxed. Instead, the money coming out of the account will be subject to tax regardless of how much profit was made. The potential benefit for retirees comes from what is done with the money once it has left the RSP.

At a current price of approximately $98 per share, **Royal Bank of Canada** (TSX:RY)(NYSE:RY) is a prime example of a company that many investors are not handling as best as possible. Once shares are removed from an RSP account, a total of 55 shares, representing $5,500, can be contributed to a TFSA account on an annual basis at current prices. Once the amount is in the TFSA, the dividends, which total close to 3.75% of the amount, invested will come completely tax free instead of subjecting the investor to a higher tax bill.

In addition to dividends coming in on a tax-deferred basis, the capital gains will also accrue on a completely tax-free basis. Down the road, things get better. The sale of shares and subsequent withdrawal of any money from a TFSA is not subject to tax. The tax has already been paid, and investors now have the entire value of their shares available for spending.

But why invest in Royal Bank of Canada?

After returning close to 8% on a year-to-date basis, shares of Canada's largest bank are one of the most sought after by investors, as the beta (a sign of volatility) is only 0.7. Since 2013, the company has increased the dividend at a rate of 8.4%, increasing the income paid to investors in every year. For retirees, what is better than an increasing stream of income?

The second way for shareholders to make money from the security is from capital appreciation. Looking back over the past five years, shares of Royal Bank of Canada have increased at a rate of 14.3%, creating a significant amount of profit for long-term shareholders.

When looking forward, there are a number of potential catalysts for the company. Currently, there is a clear buildup of shareholders' equity, which could lead to either a second dividend increase or (more likely) a major share buyback.

Bear in mind that the shareholders' equity ratio has increased drastically over the past four years. Investors holding shares of this institution in their RSP accounts may need to be diligent when dealing with RSP withdrawals and how to make the most of their gains in the future.

CATEGORY

1. Bank Stocks
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