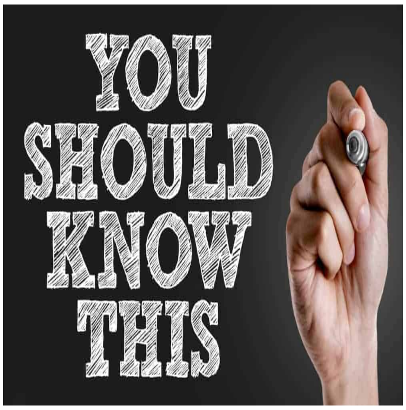

5 TFSA Investing Rules to Live By

Description

TFSAs are the most flexible tax-free accounts available in Canada. With tax-free gains, flexible withdrawals and carry-forward contribution room, they offer many great ways to grow your investments tax-free. Like RRSPs, TFSAs let you hold any conventional type of security, including stocks, bonds and mutual funds. Unlike RRSPs, however, TFSAs let you withdraw whenever you want without a tax penalty, making them more appropriate than RRSPs for short-term trading.

There's no doubt that opening a TFSA will be good for your financial future. However, once you've decided to open one, there are some important rules to live by in order to get the most out of your investments. The following are five of the most important principles to keep in mind when investing in a TFSA.

Know the contribution limit

TFSAs have a strict contribution limit that does not depend on your income level. In 2019, the limit is $6000. However, because TFSA contribution room carries forward, you can contribute as much as $63,000 if you open a new account today. For most middle class people, TFSA contribution room is not a major short-term concern; however it could become one eventually.

Never, ever exceed the contribution limit

If you do by chance go over your TFSA contribution limit, you'll be penalized heavily for it. There's a 1% a month fee that comes out for every dollar you go over the limit, and on top of that, gains on the above-limit contributions are taxed as they would be outside of the account.

Don't trade too much

Although you might be tempted to actively trade in your TFSA, it's important that you not reach the level where your trading becomes a full-time business. If the CRA finds that you've been day trading in your TFSA and living off nothing but the proceeds, then the earnings may be counted as income, at which point you'll lose your tax exemptions. In fact, you may suffer this penalty just by virtue of high trading volume, even if you're not earning a full-time income from it.

Invest aggressively

Thanks to their flexible withdrawal rules, TFSAs are more appropriate for aggressive investing than RRSPs are. If you think that **Shopify Inc** (TSX:SHOP)(NYSE:SHOP) will continue its dramatic rise and become a ten-bagger, then you can make that bet inside a TFSA and live off the proceeds should they materialize. Shopify is a particularly TFSA-friendly play, as its potential returns mean that you could earn a considerable amount of money off it even with the relatively small sums that TFSAs let you contribute.

Designate a beneficiary

If you want to leave your TFSA proceeds to somebody, it's important that you state your intent to do so before you pass away. As with RRSPs, you can name a TFSA successor or a beneficiary. There is a significant difference between the two: a successor actually receives the TFSA itself, whereas a beneficiary merely receives the holdings, which become taxable after being transferred. A successor must be a spouse or common-law partner, while a beneficiary could be anybody.

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