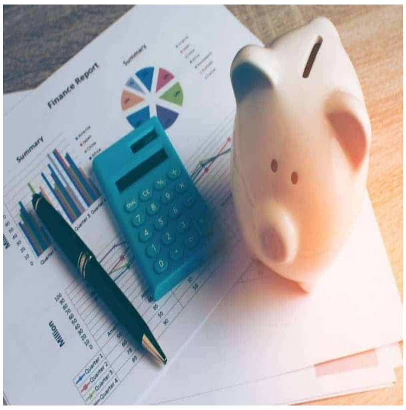

RRSP Investors: This Simple Rule Can Increase Your Dividend Income

Description

Do you want to maximize your RRSP income by investing in dividend stocks?

If so, you have plenty of options to choose from. There are thousands of stocks listed on Canadian and U.S. indices, many of which have high dividend yields. Your easiest and most obvious choice, of course, is to invest in Canadian stocks. They let you invest your money without having to worry about exchange rates, currency conversion, or withholding taxes.

However, by sticking to the "home field," you leave a lot of great options off the table. U.S. exchanges are home to some of the best stocks in the world, including ALL of the FAANG tech stocks that have been making investors wealthy recently.

Because of the great options available south of the border, you'd be wise to at least consider holding U.S. stocks in your RRSP. However, if you do so, there is one cardinal rule you have to abide by at all times:

Avoid Canadian ETFs that hold U.S. stocks

Generally, holding U.S. stocks in an RRSP exempts you from the 15% withholding tax that you pay on U.S. stocks. However, there is one exception: holding U.S. stocks through a *Canadian-listed ETF.*

If you hold U.S. stocks through a Canadian-listed ETF like **Vanguard S&P/TSX Index ETF**, you'll end up paying the 15% tax indirectly.

The reason is that Canadian ETFs have to pay the withholding tax on U.S. dividends, despite the usual RRSP exemption. So, if you hold U.S. equities through a fund like VFV, you'll be paying a 15% withholding tax. This is a tax imposed by the U.S. government and you can't get out of it as long as you hold VFV.

However, there is one way out of it: buy something completely different.

Holding U.S. stocks through a U.S. listed ETF

If you buy a U.S. ETF that holds U.S. stocks and hold the ETF in an RRSP, you won't have to pay the 15% withholding tax. The reason is that in an RRSP, you pay neither of the applicable withholding taxes (the tax to you as an individual investor, or the taxes the ETF pays before you receive the dividends).

In most "tax-free" accounts (e.g., RPSPs, TFSAs, RESPs) holding foreign stocks, at least one of these taxes are applicable. However, if you hold U.S.-listed ETFs of U.S. stocks, you pay neither.

You could earn more income

By holding U.S. ETFs of U.S. stocks, you could earn significantly more dividend income than you would holding a Canadian ETF of U.S. stocks.

To return to the Vanguard S&P/TSX Index ETF again, if you held that in an RRSP, you'd have to pay a 15% tax on dividends. So, if you had a 2% yield, you'd lose 0.3%.

But if you bought the U.S. version of the same fund, you'd pay no withholding tax, and get the full 2% yield. Especially if you're reinvesting your dividends, that can really add up over time, which shows the power of holding U.S. ETFs of U.S. stocks.

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