Canada Revenue Agency: 1 Quirky Reason to Avoid Dividend Stocks

Description

Investing is not just about income and growth. There are taxes to consider that could affect your overall returns. Newbie investors in general should know the tax implications when investing in registered (tax-free) and non-registered (taxable) accounts.

There is a funny rule where your dividend income will be grossed up by 138% before it is taxed, meaning it will be taxed more. Tax efficiency is the primary reason you should always buy dividend stocks within a tax-free account first. It's also the top priority when building a war chest for the foreseeable future.

Dividend investing

Secure Energy (TSX:SES) and **Wajax** (TSX:WJX) are two Canadian stocks that pay high dividends. It would be to your advantage to maximize contributions to your tax-free investment account, like the TFSA first, before considering investing in a taxable account.

Secure is a $691 million energy services company. The main line of business is to provide specialized solutions to upstream oil and natural gas companies operating mostly in the Western Canadian Sedimentary Basin and North Dakota.

Now that the stock is approaching its 52-week low, the current price of $4.40 is a good entry point. In return, you'll be partaking of the 6.44% yield. A $10,000 investment would deliver a $644 tax-free annual income.

The company is known as one-stop service partner to oil and natural gas companies. It provides comprehensive services throughout the energy life cycle. Secure does environmental planning, pipeline construction and maintenance drilling, and waste disposal, among other things.

While the service space has had a rough patch this year, environmental liabilities are becoming more and more critical. Secure is the go-to company in this area as well as in waste management. Low competition is also favourable for this company.

Wajax is a $293 million company based in Mississauga, Ontario. The company was founded in 1858 and is one of Canada’s longest-standing and most diversified industrial products and services providers.

The company caters to customers in various sectors including government, construction, forestry, industrial and commercial, oil sands, mining, metal processing, transportation, utilities, and oil and gas.

So far this year, the stock is down 7.51% although analysts are projecting a price appreciation of 50% ($14.65 to $22) in the next 12 months. Wajax pays a juicy 6.84% dividend. Again, all your earnings or dividends are tax-free, provided you invest within your TFSA.

Wajax lost revenue momentum in Q3 2019 primarily because market conditions declined during the period, especially in Western Canada. As a result, the company did not meet income expectations. Management will not alter its operational plans and still expects adjusted net earnings to increase versus 2018.

Zero-tax gains

The benefit of a tax-free account like the TFSA is the tax exemption on any earned income from high-yield dividend stocks like Secure Energy and Wajax. If you want to retain most of your earnings and not pay taxes to the CRA, invest in a non-taxable account.

Investing in a taxable account becomes an option if the contribution rooms in your registered accounts are full. In such a situation, you can’t ignore taxes and the dividend gross-up rule. As such, it makes sense to invest in dividend stocks that pay lower dividends to minimize the effects.

Some would rather pay off debts or mortgages before investing in a taxable account. Or you can seek the advice of tax consultants to know the proper course of action.

CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing

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2. TSX:WJX (Wajax Corporation)

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