Canada Revenue Agency: 1 RRSP Mistake Will Leave You With a Huge Tax Bill

Description

When it comes to retirement savings, Canadians have several options to bolster their nest eggs. One of the most tax-advantaged ways to save a substantial sum of money for your retirement is the Registered Retirement Savings Plan (RRSP). This savings plan allows you to control how you invest your money, which you can use later on after your retirement.

As great as the RRSP is, some rules and regulations allow you to maximize the tax advantage offered by this savings plan. Canadians who are not aware of the RRSP regulations seem to be making a colossal mistake that ends up with them having to pay a substantial amount of tax.

Overcontribution

Canadian tax laws are generally lax when it comes to contributing to the RRSP. However, the RRSP does come with a maximum contribution limit. According to the tax laws in Canada, any contribution that exceeds $2,000 over an individual's limit in the RRSP is considered an overcontribution.

If you over contribute to your RRSP, you have less room (thanks to the $2,000 buffer) before you are penalized. The Canadian Retirement Agency counts any direct contributions to the RRSP. For those of you not sure about whether or not you have over contributed to your RRSP, you can check out your CRA account.

The CRA will give you an assessment that you have made too many contributions to your RRSP and that you owe taxes on the amount that exceeds your limit. The maximum amount you can contribute to your RRSP is 18% of the previous year's income up to a maximum of $26,500 in 2019.

For every month that your RRSP is over the limit, the Canadian government will tax you 1% until you correct the contribution level.

Making the most of your RRSP

The CRA only counts direct contributions to your RRSP as being liable for tax penalties if they exceed the limit. If you want to make the most of your RRSP and see your wealth grow, you should consider using your RRSP to hold dividend-paying stocks instead of cash or other assets. Buying and holding dividend-paying stocks like **Royal Bank of Canada** (TSX:RY)(NYSE:RY) in your RRSP will allow you to grow your wealth well beyond the limit without incurring taxes.

At writing, Royal Bank stock is trading for $104.99 — 12.14% higher than the value at the start of the year. The capital gains from your investment in Royal Bank are non-tax deductible in your RRSP. Additionally, the Royal Bank also pays shareholders dividend payments at a yield of 4%. Not only can you see your wealth grow due to capital gains, but the dividend payments will also be added to your account without you incurring taxes.

Foolish takeaway

Stocks like Royal Bank of Canada allow you to take full advantage of your RRSP. Dividend-paying stocks also add a substantial amount to your retirement savings account by the time you retire. Royal Bank is a reliable company with a strong history and a stable dividend income for shareholders. I think that buying and holding Royal Bank stock can help you grow your RRSP and make the most of it.

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