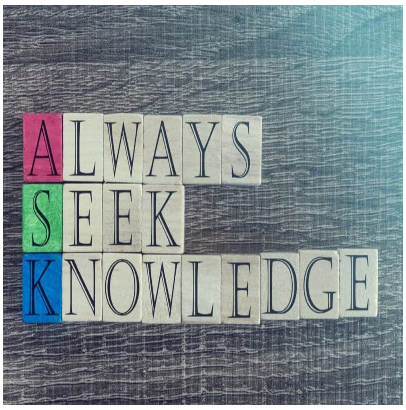

TFSA Investors: 3 Canada Revenue Agency Rules You Need to Know in 2020

Description

To maximize the returns on your investments, you need to do whatever you can to lower your tax rate. There are a number of legal ways you can do that, one of the most popular being holding investments in a TFSA. If you put your investments in a TFSA, you pay no taxes on gains or dividends, nor on withdrawals. This makes the TFSA the most flexible of the tax-savings account available to Canadian stock market investors.

However, if you're going to invest in a TFSA, it pays to be cautious. As you're about to see, there are three strict TFSA rules you need to be aware of that could get you hit with heavy taxes if you break them. We can start with one that may seem obvious but has deeper implications.

Rule #1: You need to be at least 18 to open an account

To open a TFSA in Canada, you need to be at least 18 years old. This is one of the first things your financial advisor will tell you if you're underage and try to open a TFSA.

So, why mention it?

Your age determines your contribution space. You don't start accumulating TFSA room until you turn 18, so the oft-cited $69,500 limit doesn't apply to anyone who was under that age between 2009 and today. If you turned 18 in 2010, you'd only miss out on one year of contribution room. If you turn 18 this year, then you'll miss out on the $63,500 that accumulated by 2019. If you're not aware of this fact, then you risk over-contributing and getting hit with a tax.

Rule #2: You can't hold investments you're personally connected to

Another TFSA rule you need to be aware of is that you can't hold instruments you're personally connected to in the account. That includes your personal debts, companies you own 10% or more of, and companies you directly influence.

This is one reason why it's great to hold ETFs like **iShares S&P/TSX Index Fund** (TSX:XIU) in your TFSA. As a diversified fund of TSX stocks, it gives you indirect ownership of a market-cap weighted replica of the TSX 60. This puts you a comfortable arm's length away from all the stocks in the portfolio, so you can't get dinged for owning investments you're personally connected to.

Rule #3: You can't contribute past your limit

A final TFSA rule you need to be aware of is that you can't contribute past your limit. If you do, you'll get hit with a 1% a month tax on the excess balance. While you might be tempted to run out and buy $69,500 worth of stocks in your TFSA, if you're young or have already made contributions, your remaining room may be far lower than that.

A TFSA isn't "tax free" if you over-contribute, so it's wise to consult the Canada Revenue Agency website to find out how much space you really have.

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