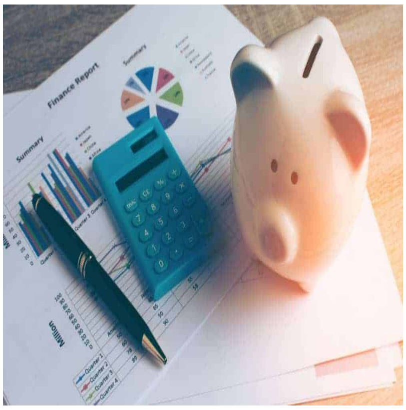

CPP Pensioners: Do This to Avoid the OAS Clawback!

Description

Did you know that if you earn too much money, your OAS benefits can be clawed back?

Known as the OAS Recovery Tax, the clawback takes 15% of any income you earn above a certain threshold.

For Canadians earning large amounts of employment or business income in old age, the clawback may be impossible to avoid. When it comes to investment income, the story is a little different. Thanks to the rules of a tax-free account introduced in 2009, you can earn dividend or interest that isn't considered taxable income. By making investments in this account, you can avoid triggering the OAS clawback through investment income.

The Tax-Free Savings Account (TFSA)

The TFSA is a tax-free account available to all Canadians 18 years of age or older. The account has limited contribution room, but new room is added every year. In 2020, you can contribute up to $69,500 to a TFSA if you were 18 or older in 2009.

At a 4% average portfolio yield, you'd earn $2,780 tax-free in in a TFSA with a $69,500 balance. That's a nice income supplement, and none of the income would lead to an OAS clawback, since TFSA withdrawals aren't considered taxable income by the Canada Revenue Agency.

What to buy

It's one thing to note that TFSAs are great tools for retirees to avoid OAS clawbacks, but quite another to know what to hold in them. TFSAs have no benefits if you don't invest in them, so you're going to need to hold approved investments to realize benefits in your TFSA.

If you're not sure what investments to buy, index ETFs can be great choices. Offering built-in diversification, low fees, and market-average returns, they're great assets to hold if you're not already an expert at picking stocks.

One Canadian ETF that I'm a big fan of is **iShares S&P/TSX 60 Index Fund** (TSX:XIU). The most popular fund in Canada, it tracks the TSX 60, the largest 60 publicly traded Canadian companies by market cap.

Why buy XIU?

There are several reasons.

First, the TSX 60 is a relatively high-yield index, with a 2.8% average yield compared to just 1.3% for the S&P 500.

Second, XIU has a historical tendency to outperform XIC, its sister fund, which tracks the entire TSX composite.

Third, the fund is highly liquid, so you can buy and sell units easily.

Finally, the fund has very low MER, so you won't see your returns eaten away at by the fees that some bank-promoted funds charge.

Although XIU isn't a high-growth fund that will make you rich overnight, it can provide a steady, stable income stream that will help you in retirement — and won't put you at risk of paying the OAS Recovery Tax.

What more could a retiree want than that?

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2. Investing

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1. Editor's Choice

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1. TSX:XIU (iShares S&P/TSX 60 Index ETF)

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