Retirees: How to Earn $1,946 Tax-Free and Avoid the Canada Revenue Agency's OAS Clawbacks!

Description

In retirement, most Canadians rely on CPP and OAS payments to get by.

Unfortunately, OAS benefits can be all too easily taken away.

Every dollar you earn above a certain income threshold results in a 15% OAS clawback. It's a program called the OAS Recovery Tax, which is designed to ensure that OAS benefits go to those who really need them.

The problem is that earning a high income doesn't necessarily mean you have enough savings to retire on–particularly if you plan on retiring very soon.

Fortunately, there is one way to earn income that won't put you past the OAS income threshold — a simple investing strategy that can generate tax-free dividends that don't count toward taxable income.

Not only does this strategy help keep your OAS payments intact, but it's also a fantastic way to lower your overall tax burden. In addition, it can net you upwards of $1946 a year tax-free.

Invest in a TFSA

Investing in a TFSA is one of the best ways to avoid the OAS clawback. Investment income typically counts as personal income and can therefore put you over the OAS income threshold even if your salary is below it; this is a major risk to be aware of.

However, if you put a chunk of your investment portfolio into a TFSA, that won't count toward your taxable income, so you can earn investment income while avoiding the OAS clawback.

A great beginner TFSA investment for retirees

If you’re not sure what investments to hold in your TFSA, don’t worry.

You can start off by buying a low-fee index fund like the **iShares S&P/TSX 60 Index Fund** (TSX:XIU). That way, you’re virtually guaranteed market-average returns without needing to research individual stocks.

What makes XIU such a great fund for retirees is that it produces a significant amount of dividend income. With a yield of 2.8%, you’ll earn $1946 a year in payouts with $69,500 invested in it. That’s a nice income supplement to add to your CPP and OAS benefits. And of course, it’s all tax-free inside a TFSA.

Over the years, XIU has rewarded investors handsomely thanks to its combination of high dividend income and solid returns. Although Canadian markets haven’t done well over the past 10 years, the TSX 60–the index that XIU is based on–has done better than average. If this continues, then investors should see solid enough capital gains in addition to dividend income by holding XIU.

Of course, no single stock — or even a diversified fund — should make up your entire portfolio. A well-diversified TFSA portfolio should ideally consist of multiple stocks, ETFs, bond funds and other approved investments.

The example given here is for illustration purposes only. One thing is certain, however: With a $69,500 TFSA invested at an average yield of 2.8%, you’ll get nearly $2000 a year in tax-free income that won’t affect your OAS payments.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

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

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andrewbutton