Canada Revenue Agency: Avoid These 2 TFSA Tax Traps

Description

The Tax-Free Savings Account (TFSA) is the supreme investment vehicle because it offers savings flexibility, tax-sheltered growth, and tax-free withdrawals. However, your money is 100% tax-free only if you can avoid two common TFSA tax traps.

Over-contribution

The most common error of TFSA users that could lead to unnecessary taxes and penalties is over contributing to the account. The Canada Revenue Agency (CRA) has been sending out letters yearly to those who have over contributed.

Let's assume your total contribution room ($63,500) as of 2019 is full, but you're interested in investing in **Canadian Natural Resources** (TSX:CNQ)(NYSE:CNQ) or CNR. You can purchase up to the extent of $6,000 worth of shares only. The amount is your 2020 TFSA annual contribution limit.

If you exceed the limit, you incur a tax of 1% of the over-contribution amount. The penalty will add up unless you withdraw the excess funds. Use up the $6,000 and wait for next year when the new contribution room is available.

CNR is an ideal choice for the TFSA because the company can generate consistent free cash flows amounting to billions of dollars. This $47 billion independent crude oil and natural gas exploration, development, and production company has a well-balanced and diversified product base.

CNR has recently been on a buying spree. The company has been acquiring buying up oil sands assets in Canada. The two significant purchases are Shell (2017) and Devon (2019). CNR is capitalizing on the weak economy and collecting assets, as it foresees an inevitable recovery of the industry.

Over the past year, the stock delivered gains of 21.06%. With robust growth and income prospects ahead, analysts are looking at a potential increase of 38.26% ($39.78 to $55) in the next 12 months. The 3.6% dividend yield today should be sustainable as the company continues to maintain a payout ratio of less than 50%.

Foreign assets

While your TFSA is the best tax shelter, you should think first before investing in foreign stocks. Dividends from abroad that you place in a TFSA are subject to withholding tax. To avoid the charge, you can instead invest in the top Canadian utility stock like **Fortis** (TSX:FTS)(NYSE:FTS).

Fortis is leading the way in power generation, electric transmission, and energy distribution across North America. About 60% of its regulated utility business comes from the U.S., and the remaining 40% is in the domestic market.

The biggest insurance that revenue, profit, and cash flow is consistent is that nearly 99% of Fortis' utility assets are regulated. The electric segment composes 80% of the asset mix, while the rest is in gas and non-regulated energy infrastructure.

The 10 utility companies it currently operates across North America serve two million electric utility customers and 1.3 million gas utility customers. North America. With a low-risk business model and a 3.33% dividend, you don't need to look elsewhere for the right TFSA stock.

Zero taxes forever

The TFSA, with dividend stocks such as CNR and Fortis, is the best route to reach your financial goals. You can guarantee zero taxes all the way if you can avoid the two tax traps.

CATEGORY

1. Dividend Stocks
2. Energy Stocks
3. Investing

TICKERS GLOBAL

1. NYSE:CNQ (Canadian Natural Resources)
2. NYSE:FTS (Fortis Inc.)
3. TSX:CNQ (Canadian Natural Resources Limited)
4. TSX:FTS (Fortis Inc.)

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