TFSA Investors: Try This 3-Step Tax-Saving Trick Before the 2020 RRSP Deadline

Description

Do you want to save on taxes? With tax season approaching and the RRSP deadline coming up, most Canadians will have to make decisions regarding their investments. The choice you make could have a significant effect on how much you pay in taxes.

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Should you contribute to your TFSA, or maybe your RRSP? Invest in stocks, ETFs, bonds, or sit in cash? These are tough questions whose answers are specific to each person.

Here is one neat trick that some people have done that could save a lot of taxes in the future. It requires three simple steps:

1. TFSA first

If you're starting your career, you probably aren't making much money. You'll likely be in a lower tax bracket as a result. If you're only making $40,000 in Ontario, for example, you'll only be taxed a combined 20.05%.

If you invest in the RRSP at this time, the tax deferral or tax refund you will receive will be only 20.05% of every dollar you earn. By the time you retire and take out the money from the RRSP, your tax rate will likely be higher than that. It doesn't make sense to put your money in an RRSP at this point.

For the above reason, if you have room in your TFSA, invest in it first. The TFSA is also more flexible, transparent, and for beginner investors, it's easier to understand than the RRSP.

2. Invest in your TFSA

Now that you have some money in your TFSA, you'll have to grow it larger. There are several ways to do this, but dividend stocks that provide both income and growth are a favoured approach by many.

A company such as **Scotiabank** (TSX:BNS)(NYSE:BNS) is an excellent fit for most TFSA investors. Scotiabank is Canada's third-largest bank, with a market cap of $66.79 billion. Scotiabank has a broad international presence and is known to push into new territories to diversify its income streams.

The company has shown consistent income growth, from a net income of US$5.36 billion in 2015 to a net income of US$6.37 billion in 2019.

Had you invested $10,000 in your TFSA five years ago into Scotiabank, your investment would be worth $14,516 today with dividends reinvested. Not a bad return for such a short period!

Not only has the net income shown consistent growth and its stock price performed well, but Scotiabank's hefty 4.91% dividend yield can provide you with a steady income.

3. Transfer the TFSA to the RRSP

Here's where the exciting trick comes in. If you're in the later stages of your career and a higher tax bracket, you will be paying more in taxes.

If you're making $100,000 in Ontario, your tax bracket will have more than doubled to 43.41%. Your RRSP savings would be much more at this point, and you'll be closer to retirement also.

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If you don't have enough money to contribute to both the TFSA and RRSP, you can take money out from your now large TFSA and contribute it to the RRSP. You always have the option of putting money back in your TFSA the next year.

Conclusion

Everybody wants to save on taxes. Use this impressive technique to potentially save you thousands in taxes.

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