TFSA Investors: 1 in 3 Canadians Are Making This Huge TFSA Mistake

Description

The Canadian government introduced the Tax-Free Savings Account (TFSA) in 2009. It was a strategic move designed to counteract the problem of minimal savings Canadians had by the time they retired.

The account type, of course, is more than a simple savings tool. Appropriately used as an investment vehicle, it can enable you to achieve several goals.

According to the Canada Revenue Agency (CRA), however, a significant number of Canadians are making a critical mistake with their TFSAs.

The account is relatively new, and many people don't understand the TFSA's intricacies. Yes, it's a flexible investment vehicle, but there are regulations that you should know.

The biggest mistake that one in every three Canadians make is not realizing that there's a contribution limit.

If you're not aware of this limit, you might end up doing one of two things: not contribute enough to maximize its benefits or contribute too much to your TFSA, resulting in tax penalties.

The maximum contribution limit

In order to make the most of your TFSA, you need first to understand the contribution limit. According to the updated figures, the 2020 contribution room limit of TFSAs is $69,500.

The government increases the maximum limit every year by $6,000 to adjust to inflation. The $69,500 is the total amount you can contribute to the account since it began.

If you haven't yet contributed to your TFSA, you have the option of investing in assets equivalent to $69,500. If you have contributed to your TFSA but haven't reached the contribution limit, you have the option of adding more to the account to bring it up to the maximum limit.

Exceeding the contribution limit will result in tax penalties. Make sure you keep track of your investments and avoid overcontributing so you can steer clear of tax penalties.

Investing in stocks

The TFSA allows you to hold assets and capitalize on any earnings in the account tax-free. If you use the contribution room to invest in stocks, you can turn that $69,500 into a lot more than its cash value.

Building a diverse portfolio of reliable stocks can help you substantially grow your wealth. Once stored in your TFSA, any investment vehicle will no longer be liable for taxation.

This means the shares can grow phenomenally in value, offering investors substantial income through dividends without having to pay the CRA any income tax on the earnings.

You can consider investing in a stock like **Canada National Railway** (TSX:CNR)(NYSE:CNI) to use the contribution room in your TFSA intelligently.

It is a stock that enjoys a wide competitive moat thanks to its unique railway network. It's the only railway company in continental North America that spans three coasts.

It operates in both Canada and the United States and its services are in heavy demand. CNR generates fantastic profits, and shareholders enjoy excellent returns through capital gains and increasing dividends.

Foolish takeaway

In the past 20 years, CNR stock has grown by a phenomenal 1,800% to trade for $126.85 per share at writing. It has the potential to appreciate further in the coming decades based on its historical performance.

Keeping your contribution limit in check and allocating some of the contribution room in your TFSA to a stock like CNR can help you maximize the benefit you can get from the account.

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