Canada Revenue Agency: Top TFSA Mistakes for 2020

Description

TFSAs are your best chance at achieving [financial freedom]. There's simply no better tool.

With a TFSA, you can permanently shield your capital from taxes. It doesn't matter how long your money stays in the account, or how much it grows to, you'll keep 100% of the gains, with no slice taken out for the taxman.

Yet TFSAs aren't foolproof. Many investors don't use these accounts to their full potential. Others make critical mistakes that force them to *pay* money to the government, the opposite of a TFSA's intended effect.

If you invest with a TFSA, pay close attention to the following mistakes. Your net worth will thank you.

Actually invest

The biggest mistake Canadians with a TFSA make is that they don't invest regularly. It doesn't take a rocket scientist to figure out why this is a problem, but a little math can help clarify the situation.

Let's say you invest $2,000 every year and earn 10% annually. After 30 years, you'll wind up with $330,000. That's pretty good, but what if you invested more than once per year?

Now let's assume you have better investing habits and commit to depositing $170 per month, which works out to roughly $2,000 per year. By getting that money in early and investing consistently, you'll end up with $385,000. That's a $55,000 difference simply for splitting your payments into monthly sums, which gives each deposit a bit more time to grow.

Worried you won't be able to stick to a monthly investing schedule? Enable automatic contributions. Most TFSAs allow for this. For example, you can have $170 transferred automatically each month. This ensures you never miss a contribution date. Plus, it enables you to continue buying, even when the market drops, when it can be difficult to submit a manual transaction.

Want more money in your TFSA? Enable automatic contributions *today*. It's a simple trick, but it's a proven money maker.

Know your limit

It pays to know your limit. Literally. If you're lucky enough to max-out your TFSA contribution, be sure to avoid going over your personal contribution limit. If you breach this threshold, the CRA will charge you a 1% monthly fee on the excess until it's withdrawn. Ouch.

This is a straightforward mistake with a straightforward solution: always track your contribution levels.

The biggest mistake is made by investors that took withdrawals earlier in the year. Any TFSA withdrawal adds new contribution room for the *following* year. Note the emphasis on *following*. Many investors take withdrawals in the spring and mistakenly believe that they can re-contribute the sum in the fall. This is not so.

Contribute as much as possible to your TFSA; just be sure to stay within the limits.

Play the long game

TFSA investing shields you from pesky dividend and capital gains taxes. This protection sometimes encourages Canadians to trade more actively. That's a mistake.

Over time, famous investors like Warren Buffett and Prem Watsa have proven that long-term investing is the key to building wealth. If you want to grow your TFSA, stick with stocks that can compound capital through age 50 and beyond.

And besides, frequent trading can allow the CRA to classify your activity as a business, rather than an individual, which wipes away your tax protections. Stay safe (and wealthy) by maintaining a long-term outlook.

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