How the CRA Can Steal Your TFSA Money

Description

TFSA investors are smart. Using a tax-advantaged saving account is something every Canadian should do. But if you make a mistake or two, the CRA could *take back* some of your advantages. One mistake, for example, could force you to pay a 1% monthly fee to the government.

These errors are easy to avoid, but awareness is key. Despite their simplicity, thousands of Canadians fall victim to these mistakes every year. That likely results in millions of dollars reverting back to the Canadian government.

Want to protect your TFSA money from the CRA? Pay close attention.

Don't make this big mistake

The biggest issue that TFSA investors make is misunderstanding how their contribution limits work. This isn't the most exciting topic, but understanding the details below will help you avoid 90% of mistakes that lead to the CRA clawing back your money.

First, let's discuss the differences between *annual* contribution limits and *lifetime* contribution limits.

You likely know that the CRA sets annual limits on how much new capital you can contribute to your TFSA. In 2020, the figure is $6,000, but this sum has varied over the years. The annual limit was $5,000 from 2009 to 2012, increasing to $5,500 in 2013 and 2014. In 2015, it jumped to $10,000 but fell back to $5,500 from 2016 to 2018. The limit was $6,000 in 2019, the same as the current year.

Many TFSA investors think that the annual limit is a strict amount, but that's not so. The biggest number that matters to the CRA is your personal lifetime limit.

Canadians become eligible for the TFSA on their 18th birthday. This is when your lifetime limit begins accruing. If you turned 18 this year, for example, your lifetime limit would be $6,000. That's the maximum amount you can invest in your TFSA until next year, when a new annual limit will be *added*to your personal lifetime limit.

But what if you turned 18 in 2009? Then you would have accrued every individual year's annual limit. That sum totals $69,500. Here's the important part: if you never contributed in previous years, you're eligible to max out your lifetime limit today, even if that exceeds this year's particular limit.

Why is knowing your lifetime limit important? Many Canadian's *stop* contributing after they've hit the annual limit, even though they may still have additional room under their personal lifetime limit. Additionally, over-contributing will result in a 1% monthly tax to the CRA on any excess amount. Ouch.

Know your limit and contribute until you hit your lifetime maximum, but no further.

The CRA thinks long term

Here's a mistake that many TFSA investors make that can be *devastating* to your financial life.

When investing, always ensure that you maintain a long-term outlook. That means investing in stocks that you can buy and hold through age 50 and beyond.

But what happens if you do the opposite? If you day trade consistently, for example, the CRA could classify your trades as business transactions. This removes your TFSA protections, forcing you to pay traditional business taxes on your profits. This can reduce the value of your portfolio by thousands or even millions of dollars.

The solution is simple: buy stocks that can generate wealth over a lifetime, not just the next few hours or days.

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