Canada Revenue Agency: How to Generate $422 in Extra Monthly Pension Income and Avoid OAS Clawbacks

Description

The Government of Canada provides retirees with a monthly pension income. It has a couple of pension programs, such as the Canada Pension Plan (CPP) and Old Age Security (OAS) to help residents lead a comfortable retired life.

The OAS is Canada's largest pension program. To apply for the OAS, you need to be over the age of 65 and a legal Canadian resident. Applicants should have resided in the country for a minimum of 10 years since the age of 18 to be eligible for the OAS.

When will the OAS by subject to CRA taxes?

According to the Canada Revenue Agency, the maximum monthly OAS payout for a 65-year-old Canadian is $613.53. This amounts to a maximum annual OAS payment of $7,362.36. But the Canada Revenue Agency can also tax your OAS if your net world income is over $79,054.

The CRA will levy a 15% tax on your OAS payments if your annual income exceeds the above-mentioned threshold limit. Further, if your net annual income is over $128,137, the CRA will recover your entire OAS pension.

So, how do Canadians eligible for the OAS avoid this CRA clawback? One way is by generating income under a Tax-Free Savings Account (TFSA). The TFSA is one of the most popular registered accounts due to its flexibility. Any contributions to the TFSA is not tax deductible. However, withdrawals from the TFSA in the form of capital gains or dividends are tax-free.

According to the CRA, Canadians over the age of 18 with a valid social security number can contribute up to $6,000 in 2020 toward their TFSA. The maximum total TFSA contribution limit is $69,500. So, retirees can limit or totally avoid CRA clawbacks on their OAS payments by investing in the TFSA.

The TFSA can also be used to allocate dividend-paying stocks to supplement your CPP and OAS pension payouts.

Canadian Natural Resources has a forward yield of 7.3%

Canadian Natural Resources (TSX:CNQ)(NYSE:CNQ) is one of the top dividend stocks that you can consider for your TFSA. Canadian Natural Resources is an exploration and production company with a market cap of $27.55 billion.

Due to the recent weakness in oil prices, CNQ stock fell from $42.57 at the start of this year to $9.8 in March 2020. It has since recovered to currently trade at $23.33 per share. Canadian Natural Resources stock has a forward yield of 7.3%, making it an attractive bet for income investors.

CNQ has a diversified asset base that generates significant free cash flow due to the low cost of maintaining production. In 2019, the company's net earnings stood at $5.4 billion, while its adjusted fund flow was a record $10.3 billion. This helped it return $2.7 billion to shareholders, including $940 million in share buybacks.

Canadian Natural Resources increases dividends by 12% in 2019 and has done so for 19 consecutive years. A dividend cut is unlikely in 2020 given CNQ's liquidity of $5 billion and a cash balance of $1.1 billion.

If you invest $69,500 in CNQ stock, you can generate $5,073 in annual dividend payments. This indicates a monthly dividend payout of $422. You can reinvest these payments to purchase additional shares or withdraw dividends from your TFSA without paying CRA taxes.

CNQ is just an example of a quality dividend-paying stock. You need to identify similar companies and diversify your TFSA portfolio to generate a predictable stream of tax-free passive income.

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